National Union of Rail, Maritime & Transport Workers

RMT response to joint ORR and Department for Transport consultation on a greater role for ORR regulating passenger franchisees in England and Wales

Introduction

The National Union of Rail, Maritime and Transport Workers (RMT) welcomes the opportunity to respond to Rail 2014.

The RMT is the largest of the rail unions and organises 80,000 members across all sectors of the transport industry. We negotiate on behalf of our members with some 150 employers. RMT is the only trade union to represent all grades in the rail industry.

RMT strongly objects to all proposals to further remove the operation of Britain's railways from democratic accountability. It is the view of the Union that such proposals are designed to facilitate greater fragmentation and the drive for profit, pushing through the proposals of the McNulty Rail Value for Money report, and to limit Ministerial responsibility and accountability. The proposals would be a significantly regressive development for Britain's rail industry, passenger services and railway staff and we note that there is an ever-growing consensus across the industry that opposes the proposals in this consultation.

Publication

1. May we publish your response?

Yes.

General principles

2. Please comment on the general principles against which changes in responsibility for regulation of passenger franchises should be assessed.

Due to the high levels of public subsidy and fares paid by passengers RMT believes that democratic accountability should be the primary principle against which changes to the regulation of rail passenger services should be assessed. We are concerned that by switching the focus of the regulatory framework from passenger services on to the content of rail passenger franchises, the government risks undermining essential, generic regulatory standards in the industry. We are concerned that the negotiations between TOCs and a less accountable regulator over the content of individual franchises will lead to regulatory standards being eroded. The unacceptable levels of political pressure that this and the last government have placed on regulatory standards in the transport and every other industry indicates the context of this proposal: de-regulation. This will undoubtedly lead to democratic accountability, key to an effective and transparent regulatory regime, being seriously compromised.

3. Do you see any potential benefits or drawbacks in moving towards giving ORR an enhanced role in respect of franchise change?

See response to Question 2 above.

Additionally, RMT is opposed to the system of rail passenger franchises and supports renationalisation. Until that happens, all regulatory functions should remain within the Department for Transport under a single transport regulatory system. In theory, we agree with the Rail Value for Money Study's conclusion that the rail industry should move toward a single regulatory body but we believe that the Department for Transport should be that regulatory body, not the ORR as the McNulty Review recommends, as it was jointly commissioned by ORR

4. Are there any representations you would like to make concerning ORR's role in holding Network Rail to account?

ORR's existing role in setting Network Rail's budget for the control periods inevitably raises concerns. We understand that for the next control periods the ORR intends to reduce Network Rail's funding, thereby risking safety standards. Additionally, it is unclear as to whether or not the ORR is acting independently, as it is supposed to, or simply implementing the recommendations of the McNulty Rail Value for Money report.

In January 2011 RMT wrote to the National Audit Office in relation to the RMT's assessment of how well the Office of Rail Regulation promotes efficiency within Network Rail. The following is an excerpt from that letter, and we have also attached two documents which outline our assessment of the ORR's approach to promoting efficiency in Network Rail and which are referred to in the excerpt below:

"The first document is a recent analysis we have submitted to the current McNulty value for money review into the railways. The RMT assessed the ORR's international cost efficiency benchmarking of Network Rail which purported that Network Rail is 34-40 per cent less efficient than other European infrastructure managers.

You will see that RMT believes that the ORR analysis was fundamentally flawed not only because of the methodology and data sources but also because of basic omissions. These included not taking into account whether other European infrastructure managers may have additional factors which impact on overall efficiency, such as fewer interfaces with other parts of the railway, different forms of ownership, funding streams and methods of raising finance.

It is also not clear whether ORR in its international cost efficiency benchmarking report or indeed at anytime, has made an assessment of whether taking renewals and some enhancements back in-house would improve the efficiency of Network Rail. This is a serious omission when, according to the scoping study of the McNulty report, renewals and enhancements account for three quarters of Network Rail's expenditure.

We also know from McNulty that the decision by Network Rail to bring its maintenance function in-house from 2004 has delivered maintenance cost savings of over £400m per annum, of which at least £100m is reported to be a direct result of reduced interface costs. In our main submission to McNulty, based on calculations undertaken by Professor Jean Shaol of Manchester University, RMT argued that taking renewals back in house would also save £400m per annum.

The RMT also has concerns that the impartiality and objectiveness of the ORR report could be open to challenge. The report was largely written by Railconsult, a subsidiary of Balfour Beatty Rail, which was one of a number of companies which lost contracts when Network Rail bought rail maintenance work back in-house. In examining future options for the structure of the railway both the McNulty review and the Government are considering whether there would be merit in breaking up and selling off Network Rail. It is clear that Balfour Beatty would benefit *from such a move and would also not have an interest in examining options for the railway which would impact adversely on their own business, such as taking renewals back in - house.*

The second attached document has also been submitted to the McNulty review which is our analysis of the 2008 ORR Network Rail Employment Cost Efficiency Review. This review was undertaken by Inbucon consultants for the ORR and claimed that employment costs at Network Rail were between 15%-20% greater than external marker benchmarks.

Again we found that the methodology and data were flawed and that Inbcon calculations on total average pay were inaccurate by as much as 41%. It is of utmost concern that this review was used to influence the ORR determination for funding to Network Rail for Control Period 4 (CP4), which in turn required Network Rail to seek to introduce 21% efficiency savings for CP4. This in turn has resulted in a 'feast and famine' approach of renewals" with a significant amount of work being deferred and also the loss of thousands of maintenance and renewals jobs.

No assessment has been made of the consequences of the haemorrhaging of thousands of skilled railway jobs will have on the rail industry's skills and knowledge base. In this respect it is our contention that cuts of this scale will prove to be a false economy. We would also ask the NAO to note that unlike other industry stakeholders the trade unions were not invited by the ORR to be involved in the discussions which led to the draft determination of Network Rail funding for Control Period 4.

In conclusion we believe the ORR's approach to Network Rail efficiency is far from thorough, narrow in scope and has been compromised by its relations with vested interests. The McNulty review into the future efficiency and structure of the railways is jointly sponsored by the ORR which means the Rail Regulator's shortcomings, which have already seriously damaged the rail industry, will also lead to a poor deal for the taxpayer and passengers".

5. Should ORR consider any revisions to its enforcement and penalties policies if it takes on a wider role? In particular, should ORR consider how and whether it could accept commitments to make improvements for passengers as an alternative to levying a penalty?

Whilst we oppose the ORR being equipped with more regulatory powers and responsibilities, if this were to go ahead the suggestion that the ORR should consider whether to downgrade the use of the financial penalties available to them is deeply worrying. In the event of unacceptably poor performance, the franchisee would obviously want to make improvements otherwise, we presume, they would lose the franchise. This would appear to be another example of the farcical 'nudge theory' favoured by the Prime Minister and the threat it represents to democratically accountable public transport. Financial penalties should surely be separate from any commitment to improve performance; this 'either or' position is a false choice.

6. Are there any specific points on which DfT and ORR should set out their proposed approach during the transition period?

RMT believes that there should be no transfer of powers from the Department for Transport to the Office of Rail Regulation. Therefore, there should be no transition and subsequently no transition period.

Should there be any transfer of powers in should be done with a view to strengthening the integration of the Britain's transport network and so should see the Department for Transport assume responsibilities previously held by the Office for Rail Regulation.

7. Should ORR review its funding arrangements in the light of the changes proposed in this consultation?

As stated previously, RMT rejects the proposals in the consultation. It is obvious that were the Government to pursue these proposals then the ORR, due to a massively increased workload, would have to review its funding arrangements.

<u>Specific proposals</u>

8. Do you have any comments on the proposals for regulating complaints handling procedures?

RMT believes that the Secretary of State, or devolved governments as appropriate, should remain ultimately responsible for the handling of complaints because democratic accountability is essential in any complaints procedure. The Secretary of State should also remain responsible for approving the complaints procedure. The view of RMT is that there should be a uniform complaints procedure, for which the Secretary of State is responsible, across the transport industry.

9. Do you have any comments on any of the proposals for regulating DPPPs?

RMT believes that transport policies affecting disabled passengers should of course be regulated but that this function should be carried out by the relevant government department which should be the Department for Transport. Policies on protecting and promoting the needs of disabled passengers should be standardized across all rail passenger services, and not the subject for debate between TOCs and the ORR. We also noted with concern that the Public Bodies Act 2011 abolished the Disabled Persons Transport Advisory Committee (DPTAC), the expert independent advisory body which had previously advised the Department for Transport on the impact on people with disabilities of rail and other transport policies. We do not believe that the ORR will have sufficient expert knowledge or resources to ensure that the interests of passengers with disabilities will be protected or promoted under these proposals.

10. Do you agree that the regulation of punctuality and reliability performance should be brought together in one place? Could this proposal work and what refinements could be made? Are there any alternative ways of doing this?

RMT believes that the regulation of punctuality and reliability performance should be brought together in one place, and that that one place should be the Department for Transport, in order to have a fully integrated railway system of a universal standard, there should only be one performance regime on one system for each franchising authority.

11. What are the key areas that should be covered by service quality measures and commitments? How should Government decide what to include in each franchise? Is there merit in having a core set of requirements that apply to all?

RMT believes that in order to have a fully integrated railway system of a universal standard, there should only be one performance regime on one system for the whole of England and Wales.

12. Please comment on the specific benefits and disbenefits of the requirements on service quality measurement and commitments being enforced by licence rather than by contract.

RMT favours the use of a contract as a contract is more robust, prescriptive and enforceable than a license.

13. Do you believe that the proposed license condition would provide effective and proportionate accountability for delivery of service quality standards? Would a transparency obligation, relying on reputational incentives, be adequate? Or should it be supplemented by a compliance obligation? Should the compliance obligation be subject to doing what is reasonably practicable to deliver it, for instance through a purposive approach similar to that being considered for performance?

RMT believes that a combination of compliance obligations and a contract would be much more robust in providing guarantees of service quality standards for passengers than reputational incentives would be.

14. What would need to be set out in guidelines to ensure credibility and consistency of reporting against service quality measures and transparency for passengers? How do we ensure that we give sufficient clarity and flexibility for franchisees in guidelines?

RMT believes that passengers and staff should be at the heart of any proposals to ensure credibility and consistency of reporting against service quality measures and transparency for passengers. For this reason, the Union believes that guidelines are insufficient and that flexibility for franchisees should not be a priority. It is the view of the Union that flexibility for franchisees will only result in avoidance of, or evasive reporting against service quality measures.

RMT maintains that a single set of requirements should for the reporting against service quality measures and transparency for passengers should apply to all franchises in each franchising authority and should be regulated by the Department for Transport. Clarity would be ensured by including obligations in the contract between the DfT and the franchisee.

As is implied in the consultation document question, any lack of credibility identified in relation to a franchisee should result in that franchisee being stripped of their franchise, and barred from the bidding process for future franchises.

15. Do you agree with the approach set out on monitoring of compliance with the service quality commitments? In particular do you think that an adapted safety management maturity model could be applied in this context?

RMT does not agree with the approach set out as we believe it to be insufficiently robust.

16. Do you agree with ORR's proposed approach for service quality commitments of requiring improvement plans as a prelude to formal enforcement action?

No. RMT believes that any commitments such be contractual. If such commitments are not met, enforcement action should be taken as opposed to requesting further commitments from a franchisee with a record of breaching their commitments.

RMT National Policy Department briefing

Extract from RMT submission to the McNulty Review: Analysis of the 2008 ORR Network Rail Employment Cost Efficiency Review

The cost efficiency review for the Office of Rail Regulation was undertaken by Inbucon consultants for the ORR. Inbucon investigated the issue of Network Rail's employment costs by broad category of employee against a range of external pay benchmarks. The determination indicated that Inbucon found employment costs at Network Rail are between 15%-20% greater than external marker benchmarks.

RMT found fundamental flaws in the methodology used, these included

- No direct comparisons were available for benchmarking.
- Analysis of the employment market in the UK included regional differentials which are irrelevant given the fact that there is a national bargaining unit.
- Inbucon did not work from a complete and comprehensive employment cost dataset. Information relating to allowances, a significant component of pay, was not made available by Network Rail.
- Despite this, Inbucon insisted that "allowances at Network Rail are excessive in comparison with the market". Inbucon did not have the data for allowances and so could not possibly compare the allowances with the market.
- Inbucon acknowledged that their analysis "was not intended to be completely accurate" and state that this would have been impossible given "the information, budget and time available".
- Inbucon used "estimates for all allowance and bonus data". These estimates were been added to the base salary and clearly distorted the data.
- Inbucon used annualised salaries for part-timers and acknowledge this "may have had an impact" on the integrity of the data.
- Inbucon calculated total average pay as being:

TOTAL AVERAGE PAY

Basic Salary **+**	Average Total Allowance **+**	Bonus **+**	Overtime **+**	Rest Day **+**	Sunday
	(estimate)	**(estimate)**	**(estimate)**	**(estimate)**	**(estimate)**

Inbucon <u>estimated</u> average total allowance, plus bonus, plus overtime, plus rest day working and Sunday to be equal to 70% of basic salary. **The lack of concrete data for these components of employment costs indicate that the total average pay calculated may be inaccurate by up to 41%.**

It is of utmost concern that this flawed review was used to influence funding to Network Rail for Control Period 4 (CP4).

> "...determine Network Rail's revenue for next review period (CP4) which will run from 2009/10 to 2013/14....As part of this work ORR needs to make an assessment of Network Rail's proposed costs in CP4. The review of Employment costs at Network Rail is part of this wider project"[1]

This in turn led directly to Network Rail's decision to seek to introduce 21% efficiency savings for CP4. That process resulted in the deferral of renewals work and a review of maintenance functions, which in turn led to the loss of thousands of maintenance and renewals jobs, including the scandalous and brutal immediate sacking of 1000 railway engineers following the collapse of Jarvis.

Discussions with Network Rail and the tabling of parliamentary questions have provided no evidence whatsoever to demonstrate what proportion of 21% efficiency savings should be derived from staff costs or how changes to employment levels, standards and conditions would achieve efficiencies.

No assessment either was undertaken which can provide assurance that the haemorrhaging of thousands of skilled railway jobs has will not adversely affect the industries skills and knowledge base.

What we do know is that the mass redundancies in the railway industry are directly linked to Network Rail Bonuses. In June of 2010 ORR told Network Rail that

> "... you claim an overall efficiency improvement for...maintenance and renewals... it includes assumed significant renewals efficiency even though there is real uncertainty over your calculation... In these circumstances we would suggest that you and your colleagues on your remuneration committee exercise real caution in the award of annual and long term bonuses related to efficiencies until you are confident that real economic efficiencies have been achieved."[2]

In other words the payment of bonuses is directly linked to cutting jobs and attacking terms and conditions. The ORR approach to efficiency means Network Rail Executives are *incentivized* to make huge job losses. This is fundamentally iniquitous and therefore detrimental to morale and productivity and efficiency. It also another glaring example of the irrational alignment of incentives in the industry where strategically important decisions on staffing levels and our skills base are made on the basis of financial reward rather than improving its performance or efficiency.

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[1] Network Rail Employment Costs Efficiency Review, Inbucon, March 2008
[2] ORR letter to Network Rail, 2nd June 2010

RMT National Policy Department briefing – International cost efficiency

RailKonsult/ORR report: International cost efficiency benchmarking of Network Rail

Overview

There are a large number of inadequacies in the information used by the ORR and their consultant in putting together their report and also serious questions as to whether which raises real concerns as to whether the

Non impartiality and lack of transparency of Report

In outlining the history of Network Rail, and Railtrack, the document highlights the Hatfield disaster which led to an increase in "operating, maintenance and renewals" costs. It is ironic that this document has relied significantly and perhaps wholly on information provided by RailKonsult, a subsidiary of Balfour Beatty Rail who held the maintenance contract for the line on which the disaster occurred. It should be remembered that Balfour Beatty was one of a number of companies which lost work when maintenance work was brought back in-house. Balfour Beatty would have a clear interest in any break-up, further commercialisation or privatisation of Network Rail. Simarly Balfour Beatty would not have interest in taking steps to reduce costs which may affect their business, for example taking renewals back in house.

The dataset used for the study was provided by the International Railways Union (UIC) which not only represents railway infrastructure managers (including Network Rail) but also employers organisations with no responsibility for infrastructure such as the Association of Train Operating Companies. The information used was, therefore, not independent and potentially subject to competing interests. Our concerns are raised by the fact that ORR has also not published the dataset and so its impartiality and authenticity cannot be verified.

It should be noted that the document attacks the cost efficiency of Network Rail, and also advocates establishing a connection between cost efficiency and access charges, which implies that access charges would be reduced for private train operators if efficiency targets were not met by Network Rail. There is no mention of the self-interest of ATOC and other representatives of train operating companies in this matter.

Low quality benchmarking

The document "only reports on Network Rail's cost efficiency and does not disclose the relative efficiency of other infrastructure managers" ie. there is no real comparison with any real infrastructure manager in Europe. This raises serious questions as to the quality of the benchmarking and the integrity of the results. As indicated above the treatment of the actual benchmarking data as confidential does not provide scope for verification.

Although the dataset provided information for 14 infrastructure managers, only 12 were used. Data incompatibilities are offered as the reason for this. However, it is not clarified as to whether or not information relating to the selected infrastructure managers was compiled in a standardised manner or if other discrepancies exist.

RMT has a number of specific concerns relating to the quality of the benchmarking including:

- **The use of sub-national/regional information from other countries to benchmark against a national organisation**

  This is not appropriate in establishing comparators for a national body such as Network Rail. Furthermore, no explanation is provided as to criteria for selecting sub-national/regional units for examination and comparison and raises questions of cherry-picking.

- **The use of an efficiency frontier**

  This does not allow for a genuine comparison and does not directly benchmark Network Rail against an existing infrastructure manager(s). It is another form of cherry-picking. It is essentially selecting the most efficient piece (eg. renewals) of a number of infrastructure providers in Europe and creating a fictional railway to compare Network Rail to. The creation of this efficiency frontier is a process similar to selecting the best players from a number of football teams and creating a “fantasy football” team to draw comparisons of an existing team against.

Establishing real cost

It is a major concern that that the report does not include a number of significant aspects which will affect the relative cost of infrastructure provision. For example no mention is made of infrastructure costs being higher due to

- Whether comparator infrastructure managers carry out more work “in house”. There is this omission despite the fact that the Scoping Study for the McNulty Review has recognised bringing maintenance in House produced significant savings. .The omission is all the more glaring when we know that renewals and enhancements constitute almost three quarters of Network Rail expenditure.

- Whether comparator infrastructure managers have less interface costs than Network Rail. This is likely as the UK railways have far more interfaces than other railways. Again the omission is surprising when the scoping study identified savings through reduced interface costs.

- Whether comparator infrastructure managers can borrow at a relatively cheaper rate because they are wholly state owned.

In addition the report takes no account of any relative differences between rail-specific and whole-economy (or other sectors’) price level. Therefore, many factors affecting the costs of national infrastructure managers have not been taken into account in relation to their national economy (ie. priorities in state investment).

Furthermore, paragraph 4.36 of the report states that the "updated models show in their totality that the cost inefficiency range for Network Rail in 2008 could be as high as 70% and as low as 20%. However, from a methodological standpoint, this would be a very simplistic way of looking at our results, because the models show very high values for efficiency or inefficiency had to be immediately discarded due to statistical inconsistencies. Therefore, we consider the credible range for the efficiency gap is 34-40%". There is no explanation of the statistical inconsistencies, or the "methodological standpoint", and although some of the translog models show a gap of zero this is also not explained.

Highlighting areas of particularly high costs

The document notes that the highest cost impacts include "assets being operated beyond design life". RMT believes that is a problem of lack of investment which would be compounded were the infrastructure to be managed by a private sector company, as opposed to the current not-for-profit infrastructure manager. Additionally, the document states that Network Rail's expenditure rates are higher than other European infrastructure managers due to "renewing assets at a rate greater than the steady rate". The rate of renewal of assets by Network Rail is one of the primary reasons for the high safety levels of the railway in Britain.

Furthermore, no attempt is made to benchmark safety despite the obvious connection between maintenance and renewals "efficiency" and safety levels.

Not comprehensive

The document highlights the most inefficient areas of Network Rail as being the possessions strategy and the contracting strategy. The contracting strategy is a feature of marketisation and one which has been consistently opposed by the RMT. RMT believes that any further privatisation or disintegration of the national infrastructure manager will create another tier of sub-contracting which will compound this problem. Additionally, the possessions strategy of Network Rail is currently under review and as such the data used is no longer relevant.