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Dear Richard

Keolis welcomes the opportunity to contribute to the PR13 review. Attached is our detailed response to each of your questions which we hope reflects our view that:

- If train operators work closely with Network Rail the immediate cost concerns facing the industry can be overcome
- Train Operators are Network Rails customers but the payment of Network grants direct from DfT has muddied this relationship, and;
- Devolving profit and loss accountability to as low as possible within an organisation makes good business sense provided this is done within a framework of good corporate governance.

Hence, we are very supportive of the approach to disaggregate Network Rails financial (and other) data and of the introduction of a route level benefit sharing mechanism. We also support the approach to use market mechanisms to promote competition as we see this as developing a more even playing field in terms of pricing and when competing for scarce capacity.

Where we have concerns are around the suggested removal of the variation provisions at Control Periods and train operators sharing Network Rails cost risk. Our detailed response covers these issues.

If any of our answers are unclear or you would like us to explain them in more detail we would be more than happy to meet with your team to discuss them face to face.

Yours sincerely

David Franks
UK Rail Director

PR13 FIRST CONSULTATION DOCUMENT

We would like to make the following points:

Q1. Do you agree with our proposed objective for the review? If not, what issues would you add or subtract?

- That when comparing UK efficiency with the best railways in the world it is important to bear in mind the outputs expected from each of the railways used in the benchmarking process. An exact like for like comparison will be difficult to achieve.
- Keolis supports the proposed output approach and our answers to subsequent questions attempt to expand our thinking in this area.
- Whilst we support competition on the railway it is important to ensure that in terms of pricing there is an even playing field for all operators. From a franchisee perspective franchise length and the degree of specification are also relevant factors to be considered.
- The language used around the design of incentives ‘to promote NRs delivery *and outperformance* of outputs’ could be interpreted that the targets set should be beaten and therefore when they are established are not quite as challenging as they could be.
- We support the view that to strengthen the customer/supplier relationship between Train Operators and NR it would be better for Network grants to be channelled through access charges Train Operators pay NR.

Q2. Do you have any views on our proposed timetable for the review? Do you need further information to plan your involvement with PR13?

- The nature of Keolis’ involvement, as a minor shareholder with TOCs in the UK, has unfortunately excluded us from key working groups. We have not been involved in the preparation of the initial industry plan and have little knowledge of its content. Going forward we would like to bring the Keolis and SNCF experience to the UK and wish to contribute more fully to the development of UKs railways.
- The consultation timescales look very challenging and we note that there has been a short delay in publishing the ‘Establishing NRs efficient expenditure’ document.

Q3. Do you think our approach to the disaggregation of NRs financial (and other) data to operating route is appropriate? Is the information we are requiring NR to produce set at the right level? Do you have views on the information train operators should produce?

- The move to disaggregate NRs financial (and other) data is appropriate and necessary to support the industry changes proposed by Sir Roy McNulty, it will also bring greater transparency in the use of public funds.

- We firmly believe that how NR choose to organise their activities is a matter for their Board but the consequences of route based costs need to be considered. For example if NR establish the network wide 'system operator' the costs of this need to be transparent particularly, if these costs are passed back to the routes in the form of a management charge.
- TOCs provide DfT with financial (and other) data, if ORR is given access to this information there should be no need for additional reports.

Q4. Which aspects of the price control should be separated for England & Wales and Scotland, e.g. should the efficiency assumption be separate?

- Retaining the separation of the RAB for Scotland continues to make sense. Efficiency targets should be set for Scotland for the reasons outlined in our answer to question 5.

Q5. Do you think there should be further separation of the price control for NR's operating routes and, if so, which aspects of the price control should be separated?

- Outputs and revenue requirements need to be established for each NR operating route if TOCs are to be able to have a meaningful role in driving industry efficiencies, this will be imperative should TOCs share risk and/or rewards. Such separation will also allow operating routes to be benchmarked against one another.
- Disaggregating NR costs is likely to require several iterations to ensure the correct costs fall in the right places. British Rail experienced this when setting up Railtrack and the Train Operating Units shortly before privatisation and a period of 'wooden dollars' was used to get things right. A similar approach may be appropriate in any move to devolve NRs financial and (other data). It may be possible to achieve this in the current control period.
- A GB wide variable usage charge price list is an appropriate start point but should be subject to challenge as route lead efficiencies are achieved.
- It is probably not necessary to disaggregate the RAB other than for Scotland and possibly Wales.

Q6. Is the current approach to defining obligations in terms of outputs the best approach? What outputs should be defined? Should there be a move to more use of outcome based obligations? Would another approach be appropriate such as specifying inputs or intermediate measures?

Q7. What are your views on how we should compile and present 'scorecards' of Network Rails performance in CP5?

The following comments relate to both Questions 6 and 7

- In principle the approach to using output measures is correct but if the definition of outcomes includes passenger satisfaction then this is not an appropriate measure as this is a TOC responsibility. We observe that obligations at major stations have confused NRs role in this respect but even at these locations it should be for TOCs to hold NR to account. Consequently,

we do not support the establishment of regulatory targets for NR with regard to passenger satisfaction.

- If the definition of outcomes also includes NR customers' satisfaction (TOC and FOCs) and Stakeholder satisfaction then these are appropriate measures although internally NR may need to use input measures at operating route level in order to drive change.
- An easily understood efficiency measure is needed, something akin to PPM. The success of the National Task Force, as highlighted by Sir Roy McNulty, has been achieved by the focus on one measure that all industry parties can contribute to. Work to create an appropriate efficiency measure is seen as essential by Keolis. The cost reduction per passenger km KPI proposed in the McNulty report is a good start point but may need refining to ensure consistency of use throughout the rail network and to eliminate perverse impacts.
- Other measures should include PPM (supported by NR delay minute targets), passenger and employee safety targets and employee satisfaction levels.

Q8. Should we make more use of 'whole system' outputs over which NR does not have full control, or focus on more narrowly defined outputs which the company is fully responsible for?

- We support the findings in the McNulty report that there are circumstances where it would be appropriate to make use of whole system outputs particularly where trade-offs can deliver better value for money, for example at the wheel/rail interface.
- A whole system approach is also appropriate in the creation of resource efficient and robust timetables and to improve operational decisions at times of disruption. We would support the retention and possible development of the delay per incident KPI.

Q9. How should output obligations be defined in the context of devolved Network Rail routes with separate price controls?

- They should be disaggregated wherever possible.

Q10. How should the balance between the number of output obligations and their individual significance be struck?

- The balance should relate to the priority set for each of the PR13 objectives.

Q11. Should NR's output obligations include a specific safety requirement different from its legal requirement?

- A safety obligation should be established but something different to the PR08 industry safety metric which has proven to be very difficult to disaggregate across the industry.

- Please also note our response to Q6/7.

Q12. Do you have views on how the effectiveness of the existing financial incentives can be improved?

- NR should not be lead into in a mind-set that they have to outperform financial targets. Targets need to be easily understood, challenging but deliverable. They should then be cascaded to managers and their teams to incentivise delivery.
- Indices used to determine the levels of inflation throughout the control period should be closely linked to the relevant commodity index, rather than the generic use of RPI.

Q13. Do you have views on how the effectiveness of the existing incentives to make best use of capacity could be improved?

- This is an area constrained by franchise specifications and limited train planning resources within NR. The upside opportunity from the existing incentives is often outweighed by alternative incentives e.g. Schedule 8 costs reflecting the compromise sometimes necessary between performance and capacity. If the scarcity regime is to be introduced these issues should be explored in some depth.
- ORR has an important role in approving Access Rights, however, it lacks the ability to validate timetable solutions when there is a dispute over whether paths exist or not. If this ability did exist it would in itself provide an incentive on NR to be more rigorous in its approach.

Q14. Do you agree that we include a regional efficiency benefit sharing mechanism calculated at the NR route level? Are there further issues about how a regional efficiency benefit sharing mechanism should be introduced which you want to highlight?

- We support the approach to include a regional efficiency benefit sharing mechanism at operating route level which is completely in line with the NR devolution plans. Such a mechanism will facilitate real and meaningful dialogue between NR and its customers and lead to local efficiency gains provided the power shift from the centre to the routes is real.
- We do not agree that train operators should pay part of the impact of NR costs being higher than expected as these would be completely outside of Train Operators control. The difference in size between NR and Train Operators cost bases, which for Train Operators are only reviewed at franchise renewal, together with their respective operating margins are also important considerations.

Q15. What are your views on exposing franchised passenger train operators to changes in NRs costs at a periodic review?

- In principle we do not support such an approach but if it was to be implemented it would only work if TOC financing was also subject to the Periodic Review process.

Q16. Do you believe that NR should share in train operator revenue and/or costs? Are there further issues about introducing a revenue/cost sharing mechanism which you would highlight?

- NR should not be able to share in train operator revenue and/or costs.
- In an economic downturn train operators ought to be free to negotiate lower Access Charges by agreeing to defer certain NR spend areas. This would help offset revenue shortfalls, particularly relevant if the franchise cap and collar regime is removed and alternative revenue protection mechanisms are limited.

Q17. We would welcome your views on possible bespoke arrangements for enhancement efficiency benefit sharing and whether there is the need for additional measures to increase the contestability of expenditure?

- We support the approach of bespoke arrangements for enhancement efficiency.
- Consideration should be given to amending the Network Code to establish an appropriate process to achieve this with Train Operators becoming involved at an early stage in the planning process to examine the options being considered.
- NR project management costs should be a key area for challenge.

Q18. Are there further new incentives which you believe should be introduced and what would the benefits be?

- An incentive on NR to reduce the level of electricity losses that occur in the overhead power supply system would assist the industries carbon footprint and deliver significant cost savings.

Q19. Are there other interactions between incentives (and the wider regulatory framework) which we need to take into account?

- Where relevant we have tried to address interactions in our answers to questions above.

Q20. What are your views on the duration of the control period?

- 5 years seems about right, although given the scale of change envisaged with the devolution of NR activities it may be appropriate to establish a period of 'wooden dollars' (see answer to question5). This may require a mini review to adjust Regional finances in light of experienced gained, say over 1 – 2 years.

Q21. Do you think we should retain the single till approach rather than moving to a dual till approach?

- We support the ORR position to retain the single till approach.

Q22. Do you think that our overall approach to risk and uncertainty in PR08 was appropriate and are there any improvements that could be made for PR13.

- It would be preferable to establish Industry governance arrangements to manage funds set aside for schemes that are not properly developed at the time of the PR13 determination rather than passing the monies to NR to control as happened with the performance fund, for example .

Q23. Network Rail faces a number of risks. At this stage, do you have any views on how general inflation risk and input price risk should be addressed?

- As far as possible these should be back to back with the arrangements in franchise agreements including where indices such as RPI are used the relevant month adopted.

Q24. We plan to retain the same high-level approach to amortisation in CP5 that we introduced in CP4. What are your views?

- We are happy to support your position.

Q25. Do you consider that our charging objectives remain appropriate?

- Please note our answer to question 5 regarding variable charges and their disaggregation. Our view is that disaggregation does not need to create complexity and it makes sense for a number of reasons including:
 - It supports the new NR devolved structure and accountability at route level
 - It permits benchmarking between routes
 - It facilitates appropriate challenge between Train Operators and NR
- We support the review of whether a scarcity charge is appropriate and look forward to offering comment in due course. The relationship with the current capacity charge, schedule 8 and fixed access charges needs to be included in this review.
- Consideration should be given to expanding the reservation charge to passenger train operators. For example passenger operators may want the ability to reserve seasonal slots.
- We support the review of charges paid by passenger open access operators and support the greater use of market forces to decide who is allocated paths. We agree that Open Access operators should be required to pay their fair share of fixed track access charges with compensating reductions passed onto the other operators. We also support the review of the 'not primarily abstractive' test using actual experience gained from the existing and past open access activity.

- We note your concern to protect the value of franchises where Open Access operators are in direct competition but believe this to be an impossible task. We would cite the West Coast competition as a case in point where Alliance Rail proposals that have just been made public will inevitably be reflected in the price the successful franchisee is prepared to pay.

Q26. What are your views on the geographical disaggregation of variable access charges?

- See answer to question 25.

Q27. What are your views on introducing a charge levied to reflect network scarcity?

- See answer to question 25.

Q28. What are your views on a reservation charge (assuming it would be set to be financially neutral for freight operators)?

- See answer to question 25.

Q29. Should passenger open access operators pay charges that exceed variable costs? How should charges be calculated?

- See answer to question 25.

Q30. What are your views on the proposals to improve incentives to reduce traction electricity consumption?

- We support the move to electricity metering for traction electricity but there is a need to avoid a winners and losers situation occurring where savings to one operator lead to increased costs for another.
- Please also note our answer to question 18

Q31. Should we put a cap on certain freight charges in advance of our determination and should these be linked to other changes?

- It is unclear to us why freight charges should be the subject of such a cap.

Q32. Do you have views on the interactions between these possible changes and when they should be implemented – for example whether some changes should only be introduced after other changes have bedded in?

- As indicated throughout this response one of the most important changes is the NR devolution plan and the potential to disaggregate the PR13 determination to route level. This will almost certainly need iteration over a period of time. Until this has been achieved it is difficult to see how TOCs and FOCs can fully engage in efficiency initiatives at route level.
- Please also note our comments in answer to question 5 regarding the GB wide variable usage charge price list.