

1 September 2011

Richard Gusanie
Office of Rail Regulation
1 Kemble Street
London WC2B 4AN

Dear Richard,

Periodic Review 2013 First Consultation

This letter sets out TfL's response to the PR13 First Consultation as a series of responses to the questions asked in the consultation document.

Chapter 3 (our objective for PR13)

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

TfL agrees with ORR's objectives but there is a need to ensure that the review takes account of changes in the industry following the McNulty review and other changes such as introduction of long term station leases.

Chapter 5 (high-level timetable)

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

We are content with the timetable

Chapter 6 and annex B

Price control separation and Network Rail devolution

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

TfL agrees with disaggregation of Network Rail data to operating route level which will enable benchmarking within Network Rail. It may take time to build up a consistent set of train operator data but TfL agrees with the ORR/ATOC view that it is best to publish some information in 2012 and then improve on it over time.

Performance measures should be disaggregated to service group level.

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

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

TfL agrees that there should be a further separation of the price control to route level subject to not introducing too much complexity into the charging regime and not introducing excessive costs into the regime. It should be noted that train operators do not always map closely to routes and a London Overground train may travel on three routes. Charging different rates for each route would increase complexity.

For third parties such as TfL dealing with Network Rail teams across different routes, the process needs to be streamlined to avoid excessive workload.

Chapter 6 and annex C

Outputs

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?

Outputs is generally the best approach to definition of obligations but it needs to be sufficiently detailed to incentivise the desired behaviours. In some cases, such as specific infrastructure enhancements, inputs may be a more appropriate measure. Network Rail should be measured against what government is buying through HLOS and this may mean disaggregating measures eg increased capacity should be disaggregated to route level or service group level if appropriate rather than to terminal level.

TfL does not favour a move towards outcomes e.g. customer satisfaction unless the outcomes selected are reasonably within Network Rail's control, otherwise Network Rail could be expected to charge a risk premium for being measured against outcomes which are dependent on external factors.

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

TfL has no views on this issue.

Q8 Should we make more use of 'whole system' outputs over which Network

Rail does not have full control, or focus on more narrowly defined outputs which the company is fully responsible for?

In line with TfL's response to Q6, it is generally better to focus on the outputs for which Network Rail is responsible. However, it is important to incentivise Network Rail and operators to consider whole system costs in their planning and incentives could include an element of whole system costs.

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

Some outputs should be route specific e.g. performance targets and capacity whereas other may be better managed at aggregate level.

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

Output obligations need to be sufficiently detailed to be meaningful but at the same time need to be sufficiently clear to be achieved and monitored. Where services operate across routes, thought should be given to how outputs should be defined.

Q11 Should Network Rail's output obligations include a specific safety requirement, different from its legal obligations?

Targets or measures based upon lagging indicators such as the number of accidents can encourage under-reporting, i.e. accidents are not reported or are explained away in order to keep below the measure. This means that lessons cannot be learned and true levels of safety are not known. Targets or measures based upon leading indicators, e.g. the good things that are done to improve safety, are effective but are much more difficult to derive and quantify.

Chapter 6 and annex D

Incentives

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

Variable charges account for a very small proportion of operators' costs and provide weak incentives to make efficient use of the network. TfL recommends that variable charges are increased as a proportion of total charges to provide adequate incentives for operators to change their behaviour. Replacement of network grant with access charges would improve transparency.

Q13 Do you have views on how the effectiveness of Network Rail's incentives to make best use of capacity could be improved?

The McNulty report recommends that better use of existing capacity should be made, reducing a bias towards capital investment. This could include making better use of existing paths by, for example reducing the volume of freight paths which are often unused from congested parts of the network in peak periods. Although Part J of the Network Code includes a use it or lose it provision, operating capacity on some routes remains underutilised at peak times.

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

TfL has concerns that such a mechanism could introduce too much complexity into the incentive regime. It could also have the effect of disadvantaging minor operators who are unable to influence overall efficiency on a route and who could receive less favourable treatment than larger operators. There could also be a conflict between provision of higher service quality on a route and the case for reduced costs with different operators having different views.

Q15 What are your views on exposing franchised passenger train operators to changes in Network Rail's costs at a periodic review?

This could increase the risk premia charged by train operators who would see Network Rail costs as outside their control. The impact would depend on the length of franchise remaining at the Periodic Review date such that a franchise let towards the end of a control period could be seen to have higher risks than a franchise let early in a control period.

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

TfL does not agree with revenue sharing as Network Rail's behaviour has limited impact on train operators' revenue other than during periods of disruption or poor performance which are already compensated through Schedule 4 and Schedule 8. Revenue sharing could lead Network Rail to favour high revenue, long distance operators at the expense of urban or regional operators.

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

Enhancement efficiency benefit sharing could be appropriate where operators have an influence on enhancement costs and would need to be considered on a case by case basis.

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

TfL proposes no further incentives.

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

Network Rail and operators may have conflicting objectives and will be driven by commercial incentives and not by economic factors. There is a risk that in entering into efficiency sharing arrangements, Network Rail and operators may reward behaviour that creates commercial returns but which creates disbenefit for other operators. ORR needs to ensure that incentives do not create social or economic disbenefit and that non-financial impacts are taken into account in decision making.

Chapter 6 and annex E

Financial framework

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

5 years is the right duration.

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

TfL is content with 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?

TfL believes the approach was generally appropriate.

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?

TfL believes that Network Rail should be protected against inflation risk over which it has no control but that indexation to CPI would be preferable to RPI.

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

TfL has no comments.

Chapter 6 and annex F

Structure of charges

Q25 Do you consider that our charging objectives remain appropriate?

ORR's charging objectives remain appropriate.

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

Geographical disaggregation is supported as it would align charges more closely with costs. However the charging mechanism would need to be transparent and excessive complexity should be avoided.

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

TfL supports a charge to reflect network scarcity.

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

TfL supports a reservation charge to make best use of the network.

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

Open access operators should pay charges that reflect the costs of their use of the network and that incentivise efficient use of paths. However, open access operators do not receive the same level of government support as franchised operators.

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

TfL supports the need to incentivise reduced traction current usage and recommends that ORR through the charging regime incentivises the use of AC and DC metering for new and existing stock in CP5.

TfL recommends, in support of the objective on transmission losses that ORR provides clarification on what constitutes efficient system loss and how it will work out shared responsibility with unmetered operators and that Network Rail is required to produce a clear plan for delivery of improvements.

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

TfL does not believe that ORR should cap freight charges in advance of the determination. More efficient use of capacity is required and charges for passenger and freight operators should be considered at the same time.

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'?

TfL has no comments.

Yours sincerely

Carol Smales

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