



OFFICE *of the*
RAIL REGULATOR

REGULATORY OBJECTIVES FOR RAILTRACK

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Regulatory Objectives for Railtrack

Railway privatisation has involved a major process of industry restructuring. Railtrack, passenger and freight train operating companies, rolling stock leasing companies and infrastructure maintenance and renewal companies have been created and the process of transferring them to the private sector is nearly complete. All of these companies are affected in different ways by regulation and I believe that an effectively regulated railway requires to be told by its Regulator what are the Regulator's expectations about its future conduct and performance. Throughout 1997 I intend to continue to monitor activity in rail markets to ensure that they are functioning effectively, and in the public interest, and supplement my statutory Annual Report with Bulletins or longer Policy Statements. *This is the first Bulletin, addressing my expectations of Railtrack, described by its Chairman as being "at the heart of Britain's railway industry"*

Railtrack has been responsible for the management, operation and development of the national rail network for almost three years and has been in the private sector for almost a year. It benefits from a level and security of income, as a result of my decisions on its access charges two years ago, which give it an historically unique opportunity to make a major contribution to the public interest and bring about improvement in the rail network for the benefit of all rail users, the taxpayers (who indirectly pay Railtrack to invest in a more efficient network) and the nation. The primary expectation is that this opportunity must be grasped and the contribution must be achieved.

Railtrack has made progress on improving performance and increasing expenditure on the infrastructure. I have said, publicly, that the improved performance of the passenger railway in 1996 is attributable, in part, to Railtrack. Passenger complaints are falling. Most representations made to me by passenger and freight users, Rail User Consultative Committees, MPs and train operators are more positive than they were two years ago. I am also encouraged by changes in the organisation of Railtrack which suggest stronger commitment to working with customers. Nevertheless, in certain important areas, progress has not been, in my view, satisfactory. I have decided, therefore, that I should supplement the Statement which I included in Railtrack's Prospectus ¹ and to set out publicly what I expect Railtrack to achieve in the period between now and the next review of its charges (to take effect in 2001), and in particular over the next 12 months. I will be taking steps to ensure that it has every regulatory incentive to do so.

¹ "Railtrack's access charges for franchised passenger services: the future level of charges: a policy statement" Office of the Rail Regulator, January 1995

Next month Railtrack will publish its Network Management Statement. I have agreed with Railtrack the form which this Statement must take. I will attach great importance to the commitments made in the Statement and moreover to their achievement.

Objectives for the regulation of Railtrack

My primary aim, publicly stated in my Annual Report, is to work together with the industry to achieve a better railway for passengers and other users. Railtrack is in a central position in the railway industry, and its performance is critical to the achievement of that aim. Therefore, I expect Railtrack to act as a responsible and efficient steward of the national rail network and to do so at all times in a manner which promotes the public interest in the achievement of an improved railway.

Stewardship of the national rail network

In my decisions on the level of its access charges, in January 1995, I provided Railtrack with a substantial degree of certainty in respect of its income and thereby placed it under an obligation to take action to ensure that, as I said in my Policy Statement², "the network is effectively and efficiently maintained and is renewed in modern equivalent form". In addition to ongoing maintenance provided for as part of operating costs, I included an allowance of £3.5 billion (at 1995-96 prices) for investment in the renewal of the network over the period of the review, together with an additional allowance to allow for accelerated investment, in particular to deal with backlog of expenditure on property.

To date, Railtrack's record, in terms of its stewardship responsibilities, is disappointing in important aspects. It has taken speedy action to improve current operational performance, which is clearly very welcome to rail users, but this has not been matched by equally prompt action to renew the infrastructure in modern equivalent form, for which Railtrack is also being paid.

When Railtrack published its interim accounts in November, these showed some increase in spending on the infrastructure in the first half of the financial year. But even with growth in spending in the remainder of the year, I estimate that it will be carrying forward significant unspent accruals in respect of renewal of the infrastructure and backlog of expenditure on property, largely stations and maintenance depots. As I said in December 1996, the current level of underspend is wholly unacceptable. Railtrack must demonstrate that it has credible plans to deal with that backlog and should deliver on those plans, now that it is free from public sector financing limits.

² "Rail Regulator's statement of the Railtrack Prospectus" Office of the Rail Regulator, April 1996

Thus, I expect Railtrack to deliver an effective infrastructure renewal and investment programme which follows four key regulatory principles:

- (a) Railtrack should, in a timely fashion, renew the railway infrastructure in the appropriate modern equivalent form;
- (b) Railtrack should take a proactive and positive approach to the development of the railway network in a way which reflects the needs of its customers and of rail users;
- (c) Railtrack should make good the current shortfall in expenditure in an efficient and effective way; and
- (d) Railtrack's plans and investment approval processes should ensure delivery of these objectives.

I believe that Railtrack accepts those regulatory principles. They are consistent with the purposes of the Railways Act, with the content of Railtrack's licence and with Railtrack's published commitments in statements to shareholders. They are more than merely carrying out a set of commercial agreements without being in default.

Railtrack's Network Management Statement

When Railtrack publishes its Network Management Statement next month, I expect it to demonstrate - publicly - its commitment and capability to deliver an infrastructure investment programme which meets the objectives I have set out above. The Statement must demonstrate to Railtrack's customers, to others funding its operation, and to the taxpayer, that money which they have committed is being spent on the railway, and spent well. Therefore, I expect Railtrack to set out in detail its plans for maintaining, renewing and developing the network, both in terms of its expected level of expenditure, and details of the work actually to be undertaken including the relevant timescales. There must be a clear and unequivocal commitment to deliver these plans, with significant progress being made during 1997.

Wider regulatory objectives for Railtrack

During 1997, in addition to my focus on Railtrack's stewardship, and its plans for maintaining, renewing and developing the infrastructure, I will expect Railtrack to achieve other regulatory objectives including:

- (a) *promoting services to passengers*: I expect to see the development and promulgation by Railtrack of a consolidated plan setting out its role and objectives in the provision of network benefits to passengers and the action it is taking, with TOCs, to secure the

delivery of such benefits as improved timetabling and train running information and improved services for the disabled;

- (b) *ensuring efficient train timetabling and operation*: I expect to review the contractual timetabling and access planning processes to ensure the network is timetabled and operated in a way which meets the needs of customers and encourages use and development of the network;
- (c) *delivering better performance*: I expect to review the operation of the contractual performance regimes, focusing on whether they are operating in the public interest, including the securing of opportunities for passengers to connect between train services;
- (d) *promoting rail freight*: I expect Railtrack to promote the use and development of the network for freight, to the greatest extent economically practicable, through its contractual arrangements and customer relationships, its operation and planning of the network, and investment in infrastructure;
- (e) *improving railway group standards change processes*: I expect to review the effectiveness of the Railway Group Standards Code and underlying consultation and change procedures, with the aim of ensuring that they fully meet the requirements of Railtrack's Network Licence;
- (f) *encouraging flexibility in charging and preparing the way for the next periodic review of Railtrack's charges (to be completed by 2000)*: the charging arrangements for track access involve very high fixed charges which give little information on how the network might be more efficiently used. Thus, I expect to see the development of greater variability in access charges under existing contractual mechanisms and in response to changes in the access requirements of passenger franchises. I also expect to begin preparation for the next periodic review of charges.

Railtrack is already taking a number of important initiatives in these areas, which I welcome, and I look forward to seeing substantial progress on these fronts.

Monitoring and publishing information

During 1997 I shall be closely monitoring Railtrack against the objectives set out in this statement and taking steps to satisfy myself that my Office has available to it all the information about Railtrack necessary to do so. I expect Railtrack to publish information about its plans for the network in the Network Management Statement, information on the performance and capability of the network in its half-yearly Network Maintenance and

Renewal Quality Indicators, and also regulatory accounting information which Railtrack has agreed to publish.

Conclusion

In summary I expect continued regulatory scrutiny of key aspects of Railtrack's business to ensure Railtrack operates in the public interest and meets the regulatory expectations underlying the current access charging and contractual framework (and which are reflected in a long term commitment ultimately funded by the taxpayer).

I expect to continue to develop a view of what Railtrack should be achieving in terms of operational performance, maintenance, renewal and development of the network, and in terms of efficiency and return on assets. I will wish to understand how Railtrack is performing against these benchmarks, and the proactive steps Railtrack is taking to improve its performance and meet my expectations, both in terms of the stewardship of the network and the wider regulatory objectives.

In Railtrack's Prospectus I said *'the first seven years of the Railways Act 1993 will be the proving ground for the railways of the twenty-first century, and ... the more Railtrack recognises the public interest in its conduct during these years, running up to the next periodic review of Railtrack's charges, the less likely that they will be followed by a substantially different regulatory approach'*. I further said *"I will in particular want to be satisfied that the amounts included in Railtrack's plans for bringing the network up to standard, and for maintaining and renewing it, are properly spent for the benefit of all rail users"* and *"where Railtrack's performance is better than expected for reasons other than greater efficiency, I would not consider it appropriate for the entirety of such benefits to be passed on to shareholders to the exclusion of Railtrack's direct and indirect customers"*. This approach will continue to be the basis underlying my objectives and expectations of Railtrack, and I expect to take further appropriate and timely regulatory action if Railtrack cannot demonstrate that these expectations are being met.

JOHN SWIFT QC

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