

18 May 2005

Jon Clyne
Head of Financial Economics
Office of Rail Regulation
1 Waterhouse Square
138-142 Holborn
London
EC1N 2TQ

Dear Jon

**POLICY FRAMEWORK FOR INVESTMENTS: AN INITIAL CONSULTATION,
FEBRUARY 2005**

Once again PTEG thanks the ORR for its workshop in Leeds and welcomes the opportunity to comment on the Consultation paper. You will have separately received comments from Merseytravel, PTEG endorses those comments.

In general the Policy Framework is positive and addresses the issues and associated problems faced in delivering investment in PTE areas. We welcome the principle that the ORR will secure Network Rail's obligations in respect to investments and, in particular, the project risk allocation and the proposal of a default position.

In regard to the specific question regarding the Framework for which we have the following comments/answers in addition to the points made by Merseytravel. These do not contradict that response and in general reinforce the points made.

- **With ORR's proposed approach to securing Network Rail's obligations in respect of investment.**

PTEG agree with the ORR's approach but remain concerned that Network Rail will be able to fulfil its obligations in resourcing the activities on which they are expected to deliver.

Although Network Rail have become more customer focused, with the emphasis on better route plans integrating third party proposals and involvement in the SRA's Route Utilisation Strategy process, investment in new infrastructure still through of as an 'add-on' in terms of resourcing. Network Rail is rightly resourced to fulfil their primary role of maintaining and renewing the current network but experience has shown that when additional work to facilitate new investment they struggle to deliver to agreed/reasonable timescales.

- **That Network Rail has an appropriate set of incentives to facilitate and deliver investments.**

Apart from the incentive to deliver schemes at a lower price than the fixed or target price (a change which is welcomed by PTEG and will be dealt with latter in the response) and the rate of return on the RAB, incentives differ little from

those that the ORR had to manage Network Rail, through the SRA, in the current arrangements.

Could the ORR identify how they intend to police Network Rail to ensure that they fulfil their obligations?

- **With ORR's proposal that, in most cases, it is appropriate for Network Rail to offer the customer a fixed price or a target price for delivery of the require outputs.**

PTEG welcomes and fully supports with this proposal. Previous arrangements, based on emerging costs, have made it difficult to plan projects and therefore a severe barrier to progressing rail schemes in general. Many PTEs face particular difficulty in achieving confidence in rail scheme costs relative to those for other modal schemes which work on a fixed cost basis.

However, it is yet to emerge whether Network Rail's offers on this revised basis will provide value for money.

Could the ORR describe how they intend to 'market test' Network Rail's offers to ensure that the fixed or target costs provide the funder with value for money and are consistent across the Network?

This raises the wider continuing concern that the costs associated with investments, although transparent, remain high for reasons which are opaque, and the implications of the consistent application of costs upon 'low-cost' community railways. We need to understand why it is that costs associated with rail-based projects are disproportionately high by comparison with other utilities or transport modes. Although we know with a greater degree of certainty that a shelter on a station platform will cost three times more to install than in a lay-by, we don't know much more about why this should be so. The ORR's proposals appear to have more to do with consistency of approach and risk-spreading than with overall cost reduction.

- **With the ORR's proposed default allocation of risk.**

Both Railtrack and subsequently Network Rail have been 'risk averse' in their dealing with third party investment schemes. The proposals recognising that Network Rail have a part to play in the responsibility and management of risk is a great step forward.

The principle of a default risk allocation is fully supported by PTEG. However, the effect on Network Rail's price offers is yet to emerge and should be monitored as part of the on-going compliance with this framework.

- **With ORR's proposal to reflect differing levels of scheme risk through the contingency, and also for their views on the appropriate level of contingency, given the discussion above.**

The proposal to reflect risk through the scheme contingency is a practice which is already used by PTEG and therefore acceptable. The range of contingency appears to be appropriate, however, in PTEG's view this is secondary to having an agreed and transparent process through which risks/contingencies can be assessed and agreed between Network Rail and the funder.

Consultees are asked to comment on:

- **ORR's proposal to make additions to the RAB for expenditure that has been efficiently incurred and adds to the economic value of the rail network.**

This proposal is fully supported by PTEG as it offers an improved incentive to Network Rail and other funders of network capacity schemes to plan for the future with greater confidence.

The recently published West Midlands Route Utilisation Strategy (RUS) consultation document has identified measures (including platform extensions) which do not add to the economic value of Network Rail's assets but are essential to the rail network in dealing with growth and to represent an efficient whole-industry solution. The expansion of the criteria will assist in the delivery of these measures.

- **The proposals for logging up investments to the RAB**

No comment.

- **The conditions which the ORR believes should be met to achieve an efficient outcome.**

PTEG agrees with the conditions proposed, however, in the light of the Railways Bill 2005, an indication of future governance arrangements between the DfT and Network Rail for delivery of enhancements would be welcome and how third parties, in particular PTE's, would be engaged.

- **ORR's proposals to assess the efficiency of schemes on an *ex ante* basis.**

The approach is noted, however, PTEG feel that there is a place for efficiency assessment both before and after the delivery of major investment schemes. The *ex post* approach maintains the incentive on Network Rail to deliver what is submitted for the initial *ex ante* assessment, identify any variations and to feed into future *ex ante* assessments on a lesson learned basis.

- **Consultees are asked for their views on ORR's proposal to allow efficient written-off development costs incurred by Network Rail on schemes required by Government to be added to the RAB.**

PTEG recognises that Network Rail need to be funded to develop schemes whether they progress or not. Any vehicle identified by the ORR to do this is welcomed.

- **ORR would welcome consultees' views on any of the issues discussed above or other issues in relation to Network Rail's proposals not covered here.**

Investment sponsored by third parties

Centro are a key funding source for improvements to rail network in the West Midlands and as such an important stakeholder for Network Rail. Any improvement in understanding Network Rail's processes and procedures and transparency on risk allocation, payments to Network Rail and their obligations and accountability is welcome.

Centro appreciates that there is still work to be done in assessing some of Network Rail's proposals, in particular the implications of the Network Rail Fee and Industry Risk Funds and the risks this fund is proposed to cover.

Whatever the way forward, Centro will be looking to the ORR to establish a fair and amicable solution which lifts the barrier to Centro investing in the rail network.

Nexus have also raised the need for the proposals to have greater flexibility when applied to community railways. The ethos of the concept is that such lines will flourish through a combination of community ownership, entrepreneurial marketing and operation, and a lower level of costs arising from differential maintenance standards and other relaxations. The proposed levels of costs and charges seem unduly onerous where community railways are concerned relative to their cost base, and could scupper the prospects of investment-led improvements. A separate risk pool or a lower level of fees should be considered for these routes, in recognition of their different roles and functions.

I hope the above is self explanatory, however, should you need any clarification or further information, please do not hesitate to contact me.

Yours sincerely

R WICKS
DIRECTOR GENERAL

RW/KM
PTEG RESPONSE TO ORR (POLICY FRAMEWORK)