

**Speech for Michael Roberts at Managing out of the Recession conference – 19  
Nov 2009**

**Introduction**

Good morning, and thank you to Anna and Chris for their invaluable contribution to this crucial debate. I welcome the opportunity to take part and set out the views of the Association of Train Operating Companies and our member companies about how the railways can help manage Britain out of recession.

The railways are part of the bedrock of this nation. They provide a professional, public service, helping millions of people every day to go about their business. And in these challenging times, the railways, including train operating companies, have a dual role to play.

On the one hand, our sector must keep attracting passengers, preferably in growing numbers, to help keep Britain moving.

So that someone who is unemployed can travel to the other side of the country, for example, to look for work. Or so that an entrepreneur can keep in touch with clients, investors and new markets.

To help day tripping families to visit – and spend money – at heritage or tourist centres. And of course to enable commuters to travel into work and home again.

With people, rather than trains, at the heart of our business, passenger rail underpins all this economic activity, while also helping to sustain social bonds and contributing to the nation's well being.

On the other hand, rail must respond to the pressure on public finances. Focusing on how best to get the most out of every taxpayer's penny. Innovating to generate new ways of winning fare-paying customers. Attracting new sources of money to plough into better services for today and major projects for tomorrow.

It is very much in this context that I want to talk today about the case for a smarter approach to the system of franchising passenger rail services.

The railways today are essentially a partnership between the public and private sectors. Franchising is very much at the heart of this and, while it has evolved over time, train companies believe further evolution is necessary to get the best out of that partnership.

By moving towards franchises which respond more quickly to the ups and downs of economic activity, concentrate more on what passengers want rather than detailed over-specification of operations, and encourage long term investment – we think train operators can play their part in delivering a better railway for passengers and taxpayers alike.

### **Train companies at the forefront of rail renaissance**

But it is important to add that the reform we seek is not a call for change because the system is fundamentally broken. Far from it. Instead we are looking to improve and build on the progress which the railways have made since privatisation.

Passengers have been flocking onto trains in numbers not witnessed since the late 1940s. There has been a sixty per cent jump in the number of journeys since 1996, with people using our trains 3.5 million times a day – and passenger numbers are expected to double over the next 30 years.

Train companies have played a big part in this resurgence in rail travel. They have invested £4.5 billion in new trains since 1995 and have made a substantial contribution to reducing delay minutes. The result is record levels in train performance and passenger satisfaction, up over recent years to 81%.

And maybe just one factor behind that growth in demand is that while fares have gone up 5% in real terms since 1996, the growth in disposable income has outstripped that, increasing by more than 20%.

Of course, to make their points, critics can pick out individual examples from the 100 million fares in the system which are needed to provide 3 basic types of ticket, as well as seasons, for all possible journeys between the 2,500-odd stations on the network.

But let's get a sense of proportion here. When you consider that the average price of a single rail journey will still not be much over a fiver come the January fares changes; and that train companies in a good year overall make a modest margin of 3-5% - all against a context of continued, growing investment – I think it is reasonable to say that there is much to be positive about in the recent record of rail in this country.

### **The need for reform**

And yet - and yet - train operators are passionate about going beyond past success. Which brings me on to the case for focused, sensible franchise reform.

We want to increase the positive part which rail plays in our lives, by increasing its attraction and winning people from the car and the plane. And, of course, there is much to do.

There must be continued focus on improving customer service, as well as tackling the perception that rail does not offer the value for money which people expect in a modern economy. We must provide additional capacity, to deal with today's overcrowding and tomorrow's growth. Only this week, we have heard about the need to deliver a more consistently good-quality experience at stations.

Tackling these challenges effectively will depend on many things:

- Sustaining commitment to the current five-year programme of network maintenance and enhancement, as well as additional rolling stock, albeit in tight economic circumstances
- Within that programme, improving the delivery of major and minor projects
- Planning ahead for the longer term development of rail, as we at ATOC are currently doing with our Network Rail and freight partners
- Reaching strategic decisions within Government about the balance of funding for rail between taxpayers and passengers – and about wider transport policy, including the relative pricing of different modes.

On to this broad canvas we would add franchise reform. Not radical overhaul of the institutional framework, which would distract attention from the key job of delivering for customers, but a package of evolutionary reform focused on six aspects of franchising.

Such reform would aim to strengthen the role of train operators, as the most commercial and customer-facing part of the industry – but still within a framework determined and overseen by government – with three purposes in mind.

The first is to increase the focus on improving quality for passengers. By moving to more output-based franchises, we think Government could more productively encourage train operators to find the best ways of giving passengers what they want.

The second is to speed up the delivery of improvements. One way would be to encourage operators to take on more responsibilities. With more streamlined decision-making when it comes to, say, upgrading stations, we believe that train companies could deliver enhancements faster than Network Rail.

The third purpose is to give taxpayers a better deal. Longer franchises, for example, would improve the prospects for attracting more private finance into rail because this would give operators more time to benefit from any investment they might make to improve service quality.

### **Our six point plan for smarter franchising**

What does this mean in detail? Let me run through in turn each of the six areas I mentioned earlier.

#### *More flexibility for TOCs*

First of all, we want to see less over-regulation and micro-management of franchises by the Department for Transport. A more output-based approach would be consistent with advice on Government procurement and has been used before in delivering rail improvements.

The current approach sees government specifying things like timetables, frequency of trains and rolling stock. We believe the government must continue to monitor franchises closely, but by concentrating less on telling train operators in detail how to do things, and more on setting outputs for TOCs to deliver in the most effective way.

In practice, this might mean setting goals for things such as levels of overall passenger perception about quality of service, performance and carbon reduction – together with specifying things like commuter capacity in peak hours, times of first and last trains, minimum standards by station category and in some cases minimum service frequencies.

The detail would be down to the train companies to determine, leaving them freer to find the best solutions. This freedom would speed up delivery, by not requiring TOCs to seek permission as often as now from the DfT to make changes. It might even have the added benefit of enabling a reduction of perhaps a third in the overall running costs of DfT Rail, including consultancy costs.

### *Longer franchises*

We also want to see longer franchises adopted as the norm. Such franchises are already used successfully in Britain: the three TOCs with the highest scores today on performance and on passenger satisfaction today have franchises of 15 years or more.

We think the norm should be 15 years, and possibly 20 years in some cases, as opposed to the current typical length of seven years. We feel this would strengthen TOC managerial focus on improving services for passengers, rather than planning for the next make-or-break bid. It would also provide stronger incentives for operators to bring additional money into the railway, by allowing them more time to benefit from the returns on any investment they make in improvements.

Longer franchises, though, would need to be introduced on the right terms. To protect passengers and taxpayers, existing mechanisms to deal with poor delivery against clearly defined targets need to be retained so that terminating a franchise which runs into trouble is no more difficult for a longer franchise than for a shorter one.

### *Quality as well as price*

The third change we feel is necessary is a greater commitment to the principles of best value procurement, in line with official advice.

This would mean DfT giving more weight, when considering bids, to proposals which commit to higher service quality at an acceptable price, and not just the size of premium or subsidy due to be paid.

To be fair, the DfT's approach in recent years has helped drive down the cost to taxpayers of procuring rail services. We fear, however, that bidders who might want to offer more than the minimum sought by DfT are less likely to do so as they know they will get insufficient credit for them when it comes to deciding on the award of a franchise.

We think passengers are losing out as a result of this. We would prefer to see instead a system where quality is weighted at least as highly as price in the final bid award. Franchising authorities in mainland Europe seem to be able to do it – our members' experience is that typically the price bid counts for about 40-60% of the final score – so why not try it here in Britain?

### *Improve financial stability*

A further vital area for attention is the need to put in place better risk-sharing between operators and others, in the interests of promoting stability in the industry.

The worst recession since the 1930s has led to revenue growth significantly below projections made in franchise bids. Yet a lack of flexibility means operators pay the same costs at a time when revenue is falling.

The fundamental principle that the franchisee takes risks which it is best placed to manage should remain, but we would like to see new features built into new franchises to address the level of risk which long term franchises in particular should be subject.

One option would be to link franchise payments to GDP (whether it goes up or down), for example, to provide more ability for operators to ride the impacts of a major economic downturn. Another would be to allow revenue support to begin earlier in the franchise. Harmonising the different indexation processes currently used for determining fares, access charges and franchise payments provides a further opportunity.

By better risk sharing in these and possibly other ways, TOCs can devote more attention to delivering for passengers – and the taxpayer benefits as well, as the resulting improved stability of franchises would enable DfT to plan ahead financially for the long term with greater confidence.

#### *Greater responsibility for TOCs*

We believe that allowing train companies to take on more responsibility for stations, depots and rolling stock would also work better for passengers and taxpayers.

On stations and depots, our experience suggests that, were operators to take on more of a role from Network Rail in delivering improvements, then with their lower overheads and approach in scoping projects, savings of £250m and maybe more might be possible, compared with Network Rail's prospective spend in this area over the next 5 years. This is money which could be re-invested in further station improvements or other priorities.

On rolling stock, we have seen DfT progressively take over the role of procurer. Yet TOCs previously have built up a positive record of working with ROSCOs to lead the ordering of £4.5billion worth of new trains. Giving TOCs the responsibility of managing procurement would lead in our view to faster delivery of rolling stock and better cost efficiency in the commissioning of new trains.

## *Franchise mix*

Finally, we would like to see a mixed range of franchise sizes sustained. There has been a general move towards larger franchises in recent years, but we think there should be no automatic presumption in favour of further merging of franchises.

Changes in franchise boundaries can be costly and having a number of smaller franchises can help make the UK market more attractive to bidders than a market dominated by larger franchises might otherwise be.

### **What underpins our proposals**

The six areas which I have just described together represent the package of reform to franchising which we would like to see adopted. Perhaps it would be worthwhile just saying a few words about the philosophy which underpins our approach, before I wrap up.

Fundamentally, our views on franchising are driven by a belief that giving train companies a greater stake in the railways, on the right terms, works for passengers and taxpayers on a number of levels.

Increasing the length of tenure and range of responsibilities for train companies has the potential to strengthen the cultural and commercial drivers in support of the best instincts of operators. It gives them yet further incentive to nurture their customer base – and supports their development as equal partners with Network Rail in thinking about the long-term development of the railways.

Our approach also frees up other key players in the industry to do what they do best. Network Rail has a major task, not just in terms of network management but also in delivering a big enhancement programme. Transferring some of its current role on station upgrades and depots would allow it to focus more on its core tasks and expertise.

Similarly with our proposals for a more output-based approach to setting requirements. This would allow Government, as guardian of the public purse, to focus on its key job of setting high-level expectations for rail, committing the necessary funds and monitoring delivery – while providing the space for train

companies to play to their core strength, which is to run operations and work with customers.

Our approach is also one which together we should have confidence would work. It has worked before. Before 2003, when the DfT began to take tighter control in franchise agreements, operators were making dramatic service improvements, with the frequency of train journeys on many long distance routes almost doubling, and the significant investment in rolling stock which I mentioned earlier.

Our sector is also a mature one, populated by major public transport players with a strong track record, and managerial resources, at home and abroad.

And by final way of underlining why we should be confident of such an approach, I repeat my earlier point: this is about giving operators a greater stake in the railways *on the right terms*. This is not about giving TOCs unfettered freedom to do what they want, it is about a stronger partnership between the public and private sectors.

Government would still set the framework in terms of setting requirements. We are looking for better sharing of risk, but not total transfer of risk away from operators. The existing mechanisms to deal with poor delivery would remain. At the end of the day, those operators who can grow the market, manage costs successfully and deliver a high level of service would prosper: those who cannot would lose their franchise.

### **Conclusion: a future full of opportunity**

So, to conclude, why are we so focussed on these ideas now?

One very simple reason is that there is a window of opportunity in which to adopt a new approach in time for the next round of franchises. The forthcoming relet of the East Coast would be a perfect starting point for reform and the programme could then be rolled out to other franchises as experience builds.

But the political climate is also right. The main political parties remain committed to franchising, with the Government making clear its intention to return the East Coast franchise to the private sector in the next 18 months or so. We know DfT is

actively thinking about the future of franchising, and the Conservatives and the Lib Dems have both expressed keen interest in our ideas on reform which we published last month.

Our journey began 16 years ago. There have been many challenging moments along the way, as there are today and as there will be in the future.

Today's conference is focused on how we deal with the challenges in CP5 and beyond. The prospectus I have set out addresses one part of the response we need to make as an industry to those challenges.

It is about a further evolution in the journey on which the public and private sectors are fellow travellers. And it is a reform programme whose time we believe has come.

Thank you.