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**Subject:** HS1 Ltd response to ORR system operator consultation

**Date:** 16 October 2015

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## 1. Context & overview

HS1 Ltd is pleased to respond to the ORR consultation in relation to *System operation: making better use of the railway network*. No aspect of our response is confidential. System operation is clearly an important aspect of delivering great railways for customers and we support ORR's work to investigate this issue in advance of the Periodic Review for Network Rail (PR18). HS1 Ltd's interest in this matter is as a(n):

- adjacent IM with an obviously keen interest in the efficient and customer focussed operation of the railway network; and
- purchaser of certain services from NRIL such as timetable planning which are considered to be system operator functions.

The remainder of our response first makes some general comments about the coverage of the consultation and some suggestions for additional points of focus. We then answer each of the specific consultation questions in turn.

## 2. General remarks

ORR sets out the purpose of the document, including to:

*Test what we mean by system operation, including the functions involved and what good system operation looks like*

The focus of the document is on the functions that comprise system operator activity and how they are regulated, because other issues such as industry structure and organisation of functions are wider policy issues for Government.

ORR sets out a useful schematic showing system operator functions, related activities, and then the range of parties that input at each stage. The schematic is set up in terms of long-, medium-, and short-term functions.

The consultation document then sets out the link between 'good' system operation and the outcomes for the railway.

We think that the consultation starts at too high a level by stating what the system operation functions and activities are. Instead, the debate should start with a definition of system operation, and criteria that can be used to determine whether something is or is not 'system operation'. System operation is often used to mean those functions that have natural monopoly properties and which should therefore be provided by a single entity in a centralised way. Such discussion is missing from the consultation document – instead the functions listed are acknowledged to have the input of a range of parties at a range of levels. This confuses the debate and makes it unclear what the outcomes / implications of any findings are.

In addition there appears to have been no assessment or consideration of system operators from first, other rail systems globally, and secondly, other similar sectors such as the UK electricity industry where the concept of system operation has been well understood and applied for 20+ years. We recognise there are unique properties within rail that add complexity but there are valuable lessons to learn from other sectors.

We recognise that the ORR consultation is necessarily partial in nature – ORR does not have authority to implement policy changes. But if we want to optimise the whole system

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then there needs to be a way to at least raise the relevant issues and identify any important constraints so that they can be addressed elsewhere. For example, options for the ownership structure of a system operator are important because amongst other things this impacts on incentives to balance efficiency and effectiveness. If we start with the criteria about what constitutes system operation we can use this to identify:

- what can be changed / improved within the current framework and context; and
- major constraints that prevent optimising the system operator function which need to be reviewed by policy-making bodies.

To answer the first of these questions the consultation document could usefully:

- outline what each of the parties actually do and what the options for change are; and
- develop a means of assessing the benefits and costs of different ways of providing the functions even within the current system.

### **3. Consultation Question 1**

*As discussed in section 2, to deliver good system operation, we think system operation involves these functions:*

- *Developing proposals for changes to the network;*
- *Choosing projects for changes to the network;*
- *Determining capacity from the physical network;*
- *Allocating capacity (including to possessions) and performance; and*
- *Operating the system (including at the route level) enabling services to run.*

*What are your views on the functions we have mapped out, and their ability to facilitate delivery of the system operation outcomes? Do you think we have missed any key functions of system operation?*

As set out in our general remarks above, we consider that the functional descriptions are too high-level, and the level of detail within each section (e.g. the role of the system operator during perturbations within the ‘operating the system’ function) too limited. This is particularly the case given an acknowledged driver for the debate is devolution. A ‘system operator’ suggests a single entity, whereas the categorisation adopted has multiple parties involved in each function.

While more analysis is required overall to investigate exactly what is or is not included in system operation, we don’t agree that system operation should determine what projects are done to change the network. This should sit with those who are willing to pay for the changes.

As a more specific comment, while we agree that the ‘Infrastructure Manager’ functions are not part of the system operation, some of these functions also impact on the same outcomes as those performed by the system operator. For example, the efficiency of the possessions regime adopted by the IM impacts on available capacity.

### **4. Consultation question 2**

*As discussed in section 3, through our work on system operation we want to improve how the railway meets the current and future needs of passengers, freight customers and funders. We think a greater focus on system operation can improve outcomes in six areas:*

- *Continued safe operation;*

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- *Choosing the right investment;*
  - *Making the right trade-offs;*
  - *The right services using the network;*
  - *Helping train operators to deliver; and*
  - *Choosing the right investment.*

*What are your views on the outcomes of good system operation that we have set out in this consultation?*

We agree that these are the outcomes of good system operation at the high-level, indeed these are the good outcomes of railway industry services generally. Further work would helpfully focus on:

- outlining what we mean by a great system operator and where we are looking to go – what is the target for 2020 say to give a more tangible impetus to the consultation;
- identifying the outcomes in more detail, including the link between specific system operator functions and these outcomes so that a targeted approach can be adopted;
- improving the line of sight between the system operator and the end customer experience. Rightly the train operators deliver the end experience but at HS1 we have gained a huge amount of understanding on how we operate our system from better realisation of what end customers want now and in the future. This avoids the historic top down system approach to rail delivery and encourages a bottom up feedback that delivers a system that customers actually want; and
- developing measures to allow us to quantify these outcomes. This is challenging as other workstreams have identified, but would allow the assessment of different approaches to system operation. This will help optimise the approach which is the intent of the work.

### **5. Consultation question 3**

*Can you give us any examples, based on your experience, where these functions improve outcomes?*

*This could include examples of when system operation has helped you in running your business and delivering for your customers. Please also feel free to highlight any areas where you think system operation could help you in the future.*

As HS1 is not an operator we have no particular comment in relation to this question.

However, HS1 Ltd has examples where improved coordination across IMs has improved services for our customers and the ultimate railway users:

- HS1 Ltd organised a workshop between Eurostar, and the IMs in France and Belgium to discuss how we could better align our timetabling offer to meet Eurostar's needs and how this fits within the constraints that each IM has in its domestic operation; and
- we have had discussions with NRIL around the coordination of possessions and system running at the interface between HS1 Ltd and NRIL at Ashford where LSER high-speed services transition between the two networks.

There are further opportunities to do this through the Kent Long Term Planning Process (LTPP) work that is just starting, and for specific projects such as the Hastings extension.

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## 6. Consultation question 4

*To regulate and incentivise Network Rail, we use a range of tools, such as regulating and monitoring Network Rail against certain outcomes and providing for a charging regime that should encourage economic and efficient behaviour by all users.*

*Do you have any views on what the desired outcomes and functions associated with system operation might mean for the regulation and incentivisation of network system operation?*

*Please highlight any particular areas where you think a different approach to regulation or incentivisation of system operation could help you better run your business in the future, and why.*

We agree that the incentives for current system operation are weak in the way that ORR has identified – for example that operators do not face the full incentives of the access charges, and NRIL has weak incentives to increase the number of train services (particularly given other targets such as PPM). The HS1 Ltd experience with Eurostar is a good example of how commercial incentives work and sharpens up focus on both sides. This is similar to the case study learnings from the Credo consultancy report.

It is clearly not a trivial matter to amend the incentive framework. The Network Rail model is very different to HS1 with a significant amount of public funding involved and hence a large degree of centralised planning. For example, instead of auction / market systems for capacity, the system uses indirect valuation methods of wider policy benefits. The difficulties and time taken in deciding on open-access operator requests shows the inherent complexity of such an approach. Changes to incentives would imply a radical change to the charging framework – which has been considered in detail by ORR in the past and there has been difficulty making any possible framework work with the franchising approach.

As well as the incentives framework, the debate ideally also needs to also look at the structure of how these functions are performed. The railway industry outcomes are driven by a combination of these two things and neither can be considered in isolation. We set out in our general remarks above a suggested way forward in terms of considering the structure of system operator functions.

Again there appears to be no consideration of how regulation and incentivisation is applied in other similar sectors which may be appropriate. For example in the electricity sector:

- price controls are done over 8 years with a 4 year output alignment on the basis that 5 years is not a long enough period of time to make proper decision on system operator investments etc; and
- strategic enhancements such as major transmission upgrades are starting to be regulated separately outside of the normal regulatory cycle. Although it is useful to have the holistic view of enhancements within NR's overall asset plans it seems wrong to set allowances etc on these at this arbitrary 5 yearly period when some of the enhancements could be at very early GRIP stages and therefore likely subject to significant cost / scope variation.

Finally, consideration needs to be given to establishing a mechanism for third parties to access the services provided by the system operator with a fixed tariff system and a standard template contract. There would also need to be a mechanism to amend. This is much like the approach to the regulated set of contracts governing train operator access to the network, or indeed a connection agreement in the energy sector. This is of specific relevance to HS1 Ltd given we currently have access to systems like TRUST and ITPS by virtue of our contract with Network Rail High Speed (a wholly-owned but distinct subsidiary of Network Rail) who in turn contracts with NRIL. But in a future world where there may be increased devolution then we are unlikely to be the only party requiring fair access to such systems.

## **7. Next steps**

It is understood that ORR will not publish any formal conclusions or recommendations, but will use responses to the consultation in preparing for PR18. A consultation covering this wider work is expected in early 2016.

Should you wish to discuss any aspect of our response in more detail please contact by phone:                    or email:

**Head of Regulation, HS1 Ltd**