

Consultation Documents by the Office of Rail Regulation – Periodic Review 2013; First Consultation May 2011; & Establishing Network Rail’s Efficient Expenditure July 2011. Response by the Railway Industry Association, October 2011



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Introduction

1. As previously agreed with Paul McMahon at ORR, this note constitutes the formal response of the Railway Industry Association (RIA) to the above two consultation documents.
2. The Association is the representative body for the railway supply industry in the UK. It has in excess of 160 member companies, ranging from the major Tier 1 suppliers through to SME's and specialist niche suppliers. The membership covers virtually all aspects of infrastructure and rolling stock supply.
3. The comments in this note arise principally from discussion at two meetings of ORR and RIA:-
 - i) The first on 4 July 2011 with RIA staff, RIA member representatives and Michael Beswick (Director Rail Policy ORR) and Paul McMahon (Deputy Director, Competition and Regulatory Economics ORR) to discuss the first document
 - ii) The second on 6 July 2011 with RIA's governing Council, RIA staff and Anna Walker (Chair ORR), Richard Price (Chief Executive ORR) and Michael Beswick (as above).
4. It has been further informed by subsequent input from member companies and the workshop held at ORR on 21 September to discuss the second of the consultation documents.

Substantive Response

5. The points emerging from the inputs mentioned above can be grouped into the following key headings:-

Stability of Workload; Transition Between Control Periods & PR13 Process Timeline

RIA, in response to earlier consultations and in many other fora, has consistently stressed the importance to the supply chain of a stable and predictable future workload. Without this suppliers are unable properly to plan their business, leading to sub-optimal efficiency and increased industry costs.

It is clear that volatility in demand can arise for a number of reasons, even in an industry where asset performance and lifecycle is as potentially predictable as the railway. Some cycles can last over decades, such as that for new electrification work, which owes much to a shift in Government policy - influenced by extensive industry research and analysis. Another cycle is however becoming apparent linked to the Control Period mechanism itself. Both CP3 and CP4 have been marked by relatively low activity at the start of the Control Period followed by substantial back-end loading of work. This is wasteful of resources and so inefficient for all parts of the supply chain involved; it must not be allowed to recur in CP5.

What the supply chain really needs is continuity of procurement planning leading to continuity of workload. Effectively we need to move to a situation where the issue of Control Periods is virtually irrelevant and we have a continuing, living plan driving the effective and efficient delivery of Network Rail's enhancements and renewals programmes. Achieving that outcome will require extensive changes, but three are in our view particularly important:

- (a) ORR and NR should make much greater use of the Early Starts facility to allow preparatory work to begin well before the end of CP4 on projects that will take place in CP5 or beyond. In this industry the needs for renewal work are understood or capable of being understood many years in advance, so it should not be difficult to identify substantial programmes capable of becoming Early Starts without significant risk of spend being incurred unnecessarily;
- (b) We look to ORR and NR to undertake the negotiation of the efficiency improvements to be required in CP5 in a more collaborative manner than has perhaps been evident in the past, so as to allow NR confidence that in undertaking preparatory work it understands the unit cost savings likely to be required. The advance notice of the likely efficiency requirement in CP5 given at the time of the CP4 determination was a helpful step in this direction; but one whose value would be much undermined if either party now aimed for a radically different settlement;
- (c) The early development for PRO13 of the Initial Industry Plan, and the Association's role in it and subsequent workstreams, is already providing helpful planning guidance. However, the PRO13 timeline still leaves the completion of the NR Delivery Plan for CP5 until only a matter of weeks before the Control Period begins, much inhibiting the ability of suppliers effectively to plan their businesses for CP5 until well after it has begun. This is wasteful of scarce resources. It will be offset to the extent that Early Starts are able to drive the

main programmes of work. In addition, however, it appears to us that the timetable should be capable of being brought forward if, as the IIP suggests, the HLOS investment requirements on NR are expressed as a series of funds to achieve agreed overall outputs rather than at individual project level. Any significant bringing forward of the timetable would be valuable for the reasons given above.

Duration of Control Period 5

The consultation requested views on whether a 5-year period was appropriate. RIA has previously argued that, given the nature of the industry planning cycle, a longer period – possibly 10 years – might be more appropriate. In any event, it is fair to say that large parts of the industry work profile are sufficiently predictable to allow planning on the basis of a rolling core programme with a timeline of longer than 5 years and we strongly recommend the adoption of such an approach. The previous adoption of exactly the opposite approach has demonstrably been seriously detrimental to the rolling stock supply chain.

Collaboration / Partnering

RIA has, via its Value Improvement Programme which is discussed further below, been promoting for many years the need for greater industry collaboration in order to reduce costs and improve efficiency. That need now seems to be generally accepted and indeed has been clearly endorsed in the McNulty VfM Study.

With specific reference to Network Rail we believe that that message is clearly shared within the top strategic layers of NR but, critically, has not percolated effectively throughout the rest of the organisation – a view strongly expressed by the last Suppliers Perception Survey. Ensuring that the collaborative approach advocated by NR's own senior management permeates the entire Network Rail structure is paramount but it is accepted that such culture change is difficult and will take some time to implement.

One way to help achieve this is the RIA Value Improvement Programme (VIP), a workshop-based initiative aimed at increasing efficiency and performance by improving culture and behaviours. We are currently in discussion with Network Rail about how we can use VIP to help them achieve accreditation to BSI 11000 (a recently established partnering standard) for four specific projects. We would be happy to brief ORR further on VIP.

We believe there needs to be some way of measuring change in this area. Currently the only output from the annual IPSOS MORI supplier survey measured by ORR is that for Advocacy and we do not believe that this is the most appropriate indicator available. There are a number of other outputs from the survey which might provide a better benchmark in terms of client/supplier relationships, which we intend to discuss further with ORR shortly.

It would also be interesting to know whether the Regulators' Forum could give any examples of how changes in culture or behaviours had been/were being evidenced and measured in other industries.

Whole-Life Costing / Asset Management Information

We believe that pressure on reducing capital costs is driving the industry away from optimized life-cycle solutions towards the lowest initial cost. There is therefore a pressing need to incentivise the industry collectively to move to a life-cycle cost philosophy.

Robust asset information and access to that information are essential for this to happen. We are aware of some of the measures that Network Rail is taking, with ORR amongst others, to understand the assets they control through their new Asset Policies. RIA and NR are now embarking on a major workstream for each asset category to inform further developments in the approach to asset management. It is intended that this should lead to more efficient whole-life solutions being adopted in CP5. In considering the efficiency target for CP5, however, it is important to remember that such an approach can lead to higher initial costs.

Perverse Incentives – Schedule 4

We believe that there is scope to inject much more flexibility in this process through open and early engagement between Network Rail, TOCs and suppliers. There are examples where such dialogue has already led to a more efficient industry outcome. We understand that ORR is in the process of reviewing Schedule 4 and we would suggest that one beneficial outcome of that review would be to encourage much more dialogue of this nature.

Input Price Indexation

This important issue arose during the work carried out as part of the CP4 determination and remains equally important for CP5. In the CP4 discussions we pointed out the very wide range of uncertainty around any estimate of input prices, especially for raw materials, and urged that means be found to ensure that the actual outturn did not disrupt the efficient delivery of the programmes. We noted the very large increases in commodity prices then being experienced and stressed that these major changes in the market were entirely outside the control of either NR or its suppliers. We therefore argued that an adjustment mechanism of some kind was required to allow NR's programmes to be delivered efficiently and effectively without being disrupted by such input price increases, and this principle was accepted. We believe that the adjustment mechanism in CP4 must be retained if the efficient delivery of CP5 is not to be seriously jeopardised.

Conclusion

6. We hope this is helpful and we have noted specific areas where we believe further dialogue with RIA/suppliers would be beneficial. However we do of course stand ready to discuss further with you any aspect of this response.

**Railway Industry Association
October 2011**