

Summary of responses to November 2016 consultation on the regulatory settlement for the System Operator

Date of publication: 27 July 2017

Introduction

1. This note is a summary of stakeholder responses to our November 2016 consultation, “*Development of the regulatory settlement for the Network Rail national system operator in CP6*”, which is available [here](#). We sought views regarding the design of the regulatory settlement for the System Operator (SO); the identification of measures of the SO’s operational performance; and the treatment of the SO’s costs and revenues.
2. We received 19 responses from a range of organisations, including train and freight operating companies (and their industry representatives), local and national governments, Transport Focus, and RMT. None of the responses were confidential.
3. In this note, we summarise the main points in response to each of the questions we asked, with a particular focus on Chapter 3 to support our current consultation on possible measures of the SO’s performance.
4. Table 1 below summarises the questions we asked as part of that consultation:

Table 1: Questions on the development of the SO’s regulatory settlement

Q1	What are your views regarding our proposals on: <ol style="list-style-type: none"> i) using, amongst other things, capability-based measures of the SO’s operational performance; and ii) the extent to which SO operational performance measures should be disaggregated (e.g. to each route or operator)?
Q2	What role should the SO’s stakeholders play in informing the development of SO operational performance measures and in holding the SO to account over CP6?
Q3	What are your views on our initial ideas regarding the possible SO measures, as set out in Table 2.1?
Q4	Do we need additional mechanisms regarding the SO’s capital budget, to ensure the SO is properly incentivised to undertake capital expenditure?
Q5	Should the SO be subject to financial incentives so that its revenue varies to reflect the success of its performance?

5. All of the responses to the consultation are available [here](#).

Summary of key messages

6. The overwhelming majority of respondents supported our decision to have a separate settlement for the SO in CP6. Respondents also recognised the need for system operation functions to be undertaken on a network wide basis, although there were some calls to identify opportunities for further devolution, particularly to Scotland.
7. Stakeholders had differing views about the types of metrics to use to measure the SO's performance; the extent to which stakeholders need to be engaged in holding the SO to account; and how financial mechanisms should be designed to ensure that the SO has sufficient incentives to invest. This is discussed in further detail below with regards to each of the questions posed.

Question 1(i): capability-based measures of the SO's operational performance

8. The majority of respondents considered it appropriate to monitor the SO's performance using both capability-based and outcome-based measures. While some stakeholders said outcome-based measures are in theory more preferable, they also recognised the importance of capability measures given the difficulty in measuring some aspects of the SO's performance. Stakeholders also recognised that the SO is not solely responsible for the outcomes of system operation (e.g. use of the network), and that in many cases the SO provides analysis to inform others' decisions, rather than making the final decisions itself.

Question 1(ii): level of disaggregation of SO's operational performance measures

9. The majority of stakeholders envisaged disaggregating metrics to the greatest extent possible, to focus on outputs delivered to routes, operators and other stakeholders. For example, freight parties highlighted the importance of disaggregation by freight customer/sector, suggesting that this could ensure that the move towards route-based regulation does not cause the interests of individual operators to be undermined (for instance, where they are not the lead operator on a route).
10. However, Network Rail and RDG said there is a risk that highly disaggregated measures may create distortions or conflict of priorities given the importance of the "*network aspects of the System Operator's responsibilities*". They said that disaggregation should be dependent on available data.

Question 2: Role of SO's stakeholders

11. There was consensus about the necessity of involving stakeholders (including Network Rail routes) in the process of developing measures of the SO's performance and in stakeholders holding the SO to account over CP6, in line with the approach for the routes.
12. Respondents reported that there are already a number of existing industry fora that oversee some of SO's processes, but that these are not generally perceived as strategic sessions.
13. Some respondents were not convinced that the SO's performance should be managed through purely bilateral arrangements. They said that the SO should be held to account by a cross-industry group that includes operators, passengers' representatives, freight end users, and trade unions. The Department for Transport said that, in its role as a franchising authority, it expects to have direct input to the SO scorecard and a strong bilateral relationship with the SO.

Question 3: Possible SO measures

14. Stakeholders agreed that the SO should be measured and held to account for its performance. We have summarised the responses to this question around some broad topics below:
15. **Satisfaction survey measures –**
 - a. Overall, stakeholders welcomed the emphasis given to the use of stakeholder/customer satisfaction in the assessment of SO activity. However, they also acknowledged that as the SO has to balance competing needs, customers are likely to be dissatisfied with the outcomes of decisions at least some of the time and that survey responses can be influenced by this, implying a 'subjectivity issue'.
 - b. Network Rail considers customer satisfaction a powerful measure of SO delivery that will be most effective if used in a targeted manner i.e. applied to specific activities and processes. Many stakeholders were broadly supportive of inclusion of some stakeholder satisfaction measures, but noted that extensive surveying could be expensive and time consuming.
16. **Optimisation of timetable quality and production –**
 - a. Some stakeholders suggested that the SO should be tasked with (and measured against) continuously developing and deploying approaches that allow timetables/train paths to be systematically optimised. The degree to which the SO delivers improvements through its optimization activity could then be measured, they say.

- b. A number of respondents raised accuracy of the timetable planning rules (TPRs) as an issue, and stakeholders were supportive of measures in this area (both of outcomes and the capability of staff/processes in managing them). Some operators suggested the adoption of 'big data' approaches to timetable planning, making use of increasingly accurate real-time train location data to review the accuracy of TPRs (such as sectional running times).
- c. The production of working timetables on time was a recurrent issue reported by stakeholders, with operators saying it is a key requirement for them, a view echoed by passenger groups. Respondents also said that being able to re-plan the timetable in emergencies and eradicating inevitable delay from the timetable caused by planning errors were priorities.
- d. A common view was that these problems arise due to a relative lack of data and an absence of technology that drives an over-reliance on individual knowledge/experience and the need for considerable manual work. Some respondents suggested that measures of the capability of the SO's human resources could be a useful proxy, and recommended the strengthening of a defined and attractive career path for skilled timetable planning staff.

17. Measurement of outcomes of enhancement schemes –

- a. Some stakeholders reported that at times Network Rail has declared enhancement schemes as successfully delivered, without demonstrating the delivery of the actual business case benefits. They welcomed a greater focus on measuring the degree to which the expected train service outcomes of enhancements are actually realised, as well as the timeliness of realising these benefits after the work was complete.
- b. Operators also encouraged the SO to champion the delivery of more flexible signalling and safety rules where these are directly limiting the capability of the network, such as the systematic removal of permissive working arrangements at many stations.

18. Distinction between output-based and quality measures –

- a. Overall, stakeholders preferred trying to measure the quality of outcomes rather than the production of outputs or utilisation of inputs. However, many acknowledged that outcomes could not be measured in all areas and that measuring outputs or process could be an acceptable alternative (e.g. milestones of development projects).
- b. Some also noted that even where outcomes could be identified, it would be important not to insist on measures that could drive incentives that might not meet the needs of all parties, for instance encouraging the creation of paths in order to hit targets but sacrificing performance or regular service patterns in order to do so. Some expressed the wish not to see cost-driven metrics (e.g. number of trains per member of staff), which might lead to a prioritisation of cost cutting over improved quality.

19. Importance of a freight perspective –

- a. Overall, freight groups and FOCs broadly agreed with the measures proposed. However, they highlighted that when defining metrics, it is important to consider the intrinsic characteristics of freight operators, specifically which freight operators run services across Network Rail routes. While route-based output enhancements and benchmarking are welcome, for freight a ‘corridor-based’ approach around end-to-end freight flows is crucial.
- b. Freight stakeholders consistently noted a perceived imbalance within Network Rail to protect performance at the expense of capacity, but also noted that the quality of freight paths (e.g. average speed) was as important as increasing the availability of paths to the industry. Responsiveness to short-term requests for access was also noted as a priority and a possible area for measurement.

Question 4: Financial mechanisms – ‘protections’ for the SO’s capital budget

20. Amongst stakeholders, there was strong consensus around ORR’s conclusion that direct charges on operators to fund the SO would not be appropriate.
21. There was also general agreement among stakeholders that the SO must have adequate funding, including through its capital budget. Stakeholders commented that investment in optimising the timetable to get more out of the existing infrastructure would be substantially cheaper than investments in new infrastructure, and that a historic lack of adequate supporting technology had led to some investment decisions on network enhancements that could have been avoided through improved timetables (e.g. ECML Joint Line upgrade).
22. Some stakeholders said that a ring-fenced budget would be appropriate, and funders acknowledged the advantages of a separate revenue allowance for the SO as a means of providing some protection for the SO budget. However, some respondents questioned whether a regulatory asset base (RAB) mechanism would encourage efficient investments, or be too onerous.

Question 5: Financial mechanisms – exposing the SO to financial incentives

23. The large majority of stakeholders considered financial incentives as not being positive and possibly not linked to the desired effects for the following main reasons:
 - a. A high proportion of the SO cost base will be fixed (at least in the short term) and will not easily vary with volume;

- b. There may be potential detrimental impacts and perverse effects of a 'penalty clause' approach to under-performance, i.e. paying a penalty for failure might result in cuts that could worsen performance even more;
 - c. There is a risk that financial incentives trigger a focus on managing the SO to its efficient cost requirements, and not necessarily on the quality of its outcomes. Financial incentives linked to revenue would need to tie in to the wider set of measures to protect quality (e.g. financial measures not centred solely around the number of paths created but also the quality of those paths and the downstream effect on operational performance);
 - d. It may be difficult to identify the SO's direct contribution to outcomes compared with other parts of Network Rail/industry, making it difficult to attribute any financial payments in an accurate manner; and
 - e. PR18 already involves considerable change over the next few years.
24. Some stakeholders said they could see merit in exploring options for an upside-only scheme that incentivises better outcomes. For example, this could be a share of the volume incentive in its current or future guise, or an incentive linked to recognising improvements in the allocation and identification of capacity or the quality of train paths in the timetable.
25. There was a recommendation that the SO could be held accountable for its element of Schedule 8 delays (i.e. those delays caused by timetable errors, known as 502a delays).



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