Department for Transport

Rail Franchising in Great Britain

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LIBERALISATION OF PASSENGER TRANSPORT SERVICES BY RAIL IN BELGIUM

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GB Rail Industry Structure

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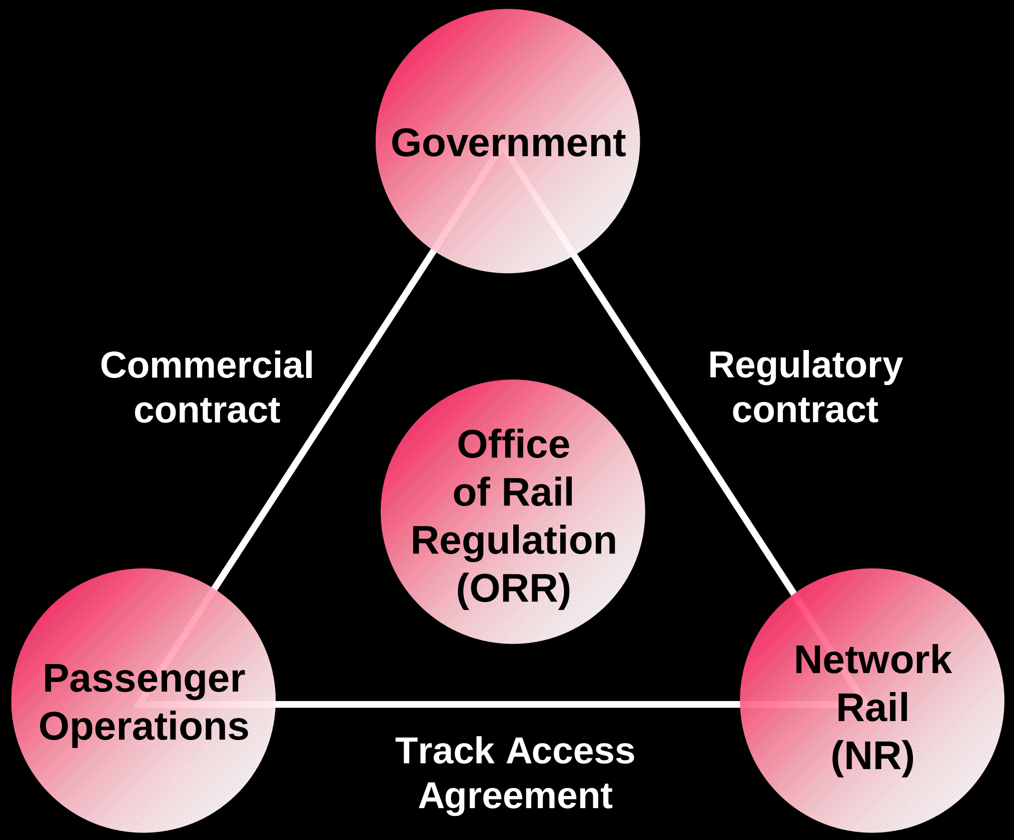

"publicly specified, privately delivered"

Government

- Sets strategy
- Determines budget
- Awards passenger franchises

Network Rail (Infrastructure)

- Delivers Network
- Accountable for reliability
- Leads industry planning

ORR (Regulator)

- Prices rail outputs
- Safety regulation

Train Operating Companies

- Deliver services for customers

How does it work in practice?

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5-YEAR CONTROL PERIODS (currently: CP3=2004-09)

- continuity of planning, delivery, funding

GOVERNMENT SPECIFIES

"What it wants to buy" (High level Output Specification – HLOS)

- Safety: 3% reduction in risk of death or serious injury to rail workers and passengers
- Reliability: punctuality to improve from currently 90% to:
  92% (long distance/regional) / 93% (London and Southeast)
- Capacity: sets out level of passenger demand to be met on each of 23 strategic routes
- Other:
  - 1300 new carriages
  - major improvements at Reading and Birmingham New Street stations

"How much it can afford" (Statement of Funds Available – SoFA)

- commits to £15bn in total Government support for the railway over 2009-2014

ITERATIVE PROCESS

between Government, Regulator, Infrastructure Manager, to agree balance between outputs and funds

Overall aim of franchising

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- to reduce the net cost and increase the value for money for both the passenger and taxpayer

- supporting objectives:
  - a continuing improvement in operational performance
  - enough capacity to accommodate forecast passenger demand – (generally within existing infrastructure constraints)

Franchising; a brief history

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- Introduced in 1993 Railways Act as the means by which government would procure rail passenger services
- All passenger train services transferred to franchisees 1996-97
- Since then, all franchises have been replaced, in some case with significant changes

Possible Models

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Who decides what services are provided?	Who provides the services?	Model	Pros & cons
Public sector	Public sector	Nationalisation	A proven model. Gives government a high degree of control. Would public sector operators be efficient?
Public sector	Private sector	Franchise	See next slide
Private sector	Private sector	Full liberalisation	Cuts subsidy bill? Maximises competition and enterprise. But only works for profitable services. Market will disengage from unprofitable ones.

The franchise model; options

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Franchise
A time-limited, regulated "monopoly"
Has to be competed for

	Gross margin	Net margin
How does it work?	Government sets the fares and service pattern. Franchisees collect revenue, and surrender it to government.	Government sets service pattern. Franchisees set fares, and take revenue-risk.
Franchisee has incentive to	Reduce cost.	Increase revenue, and reduce cost.
Optional extras	Bonuses and penalties for service quality.	

The British rail franchise model

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- Based on Net Margin approach
- Main competitive element is in bidding to win franchise
- Some competition between franchisees where they operate on the same route
- Also competition from “open access” operators

The franchising process

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- Plan – Specification
- Buy – Procurement
- Do – Franchise management

Specification

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- In setting a base specification for each franchise, the Government is seeking to:
  - ensure the provision of a minimum level of service and capacity it wants to buy;
  - protect passengers from monopolistic actions in specific markets (e.g. through fares regulation);
  - protect the benefits of a national rail network;
  - provide a fair and common basis for franchise competitions; and
  - allow flexibility so that, over time, private sector innovation and commercial judgment will enable it to evolve.

Main considerations in developing the franchise specification

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- Assess growth in demand using Government forecasts and industry models
- Assess potential to increase revenue
- Develop timetable options which are operationally practicable
- Service levels specified will reflect current and predicted market needs; they will not always be a copy of existing service structures
- The specification will reflect a total product offer - not just a train service level - including fares and ticketing, station access, passenger safety and security
- Assess likely costs
- Calculate with Network Rail a realistic level of overall operational performance and actions necessary to deliver this

The final specification ...

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- is affordable within financial budget
- offers value for money
- gives bidders as much flexibility as possible
- is possible within infrastructure constraints
- is possible within known rolling stock constraints

Procurement

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The process is designed to:

- shortlist bidders with a proven record
- ensure we get the most competitive price
- contract a bid which will work operationally and financially

Franchise management

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Process is designed to:

- ensure that contracted benefits are realised
- give a light-touch approach (i.e. avoidance of "micro-management")
- focus on most important outputs (i.e. operational and financial performance)

Rolling stock

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- All rolling stock is privately owned
- Choice of rolling stock is at the franchisee’s discretion
- Normally, rolling stock is owned by a third party (“ROSCO” = Rolling Stock Company), and leased to the franchisee
- Sometimes, ROSCO maintains trains (‘wet lease’); otherwise franchisee maintains (‘dry lease’)

Length of franchise

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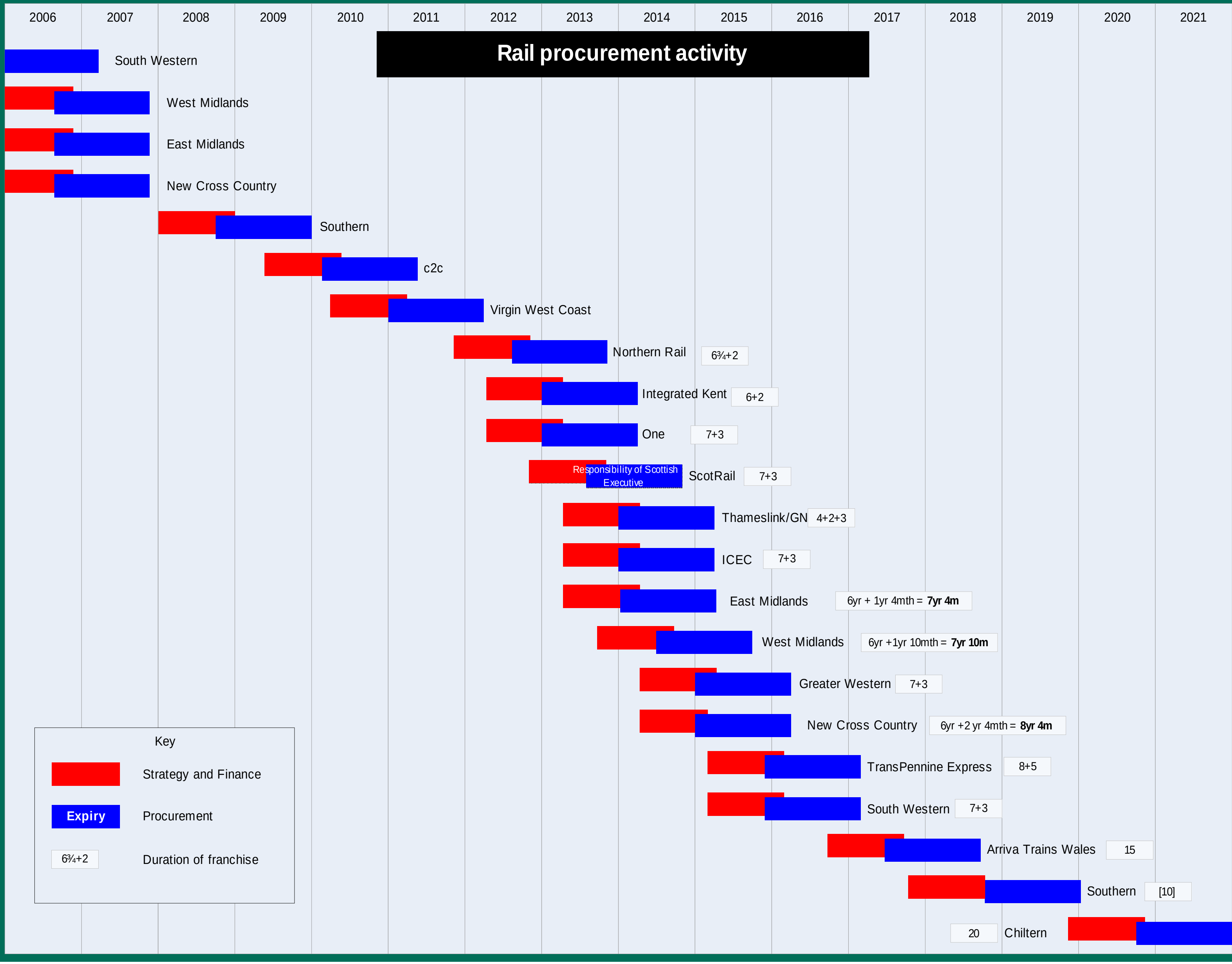
- Generally 7-10 years **Why?**
- Franchisees generally don't have strength of balance sheet to bring investment to justify very long franchises
- Long-term prediction of revenue by bidders is extremely hard
- 7-10 years is a balance, allows some return on investment, eg train refurbishment, but also allows government to return regularly to the market and get benefits of competition

Franchise replacement cycle



Sequential franchise renewal

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- Bidders have adequate resource to bid, and to mobilise and operate the franchise if they win
- Bidders can predict how many franchises they might be running
- Government uses staff resource sensibly
- Continuity means lessons can be learnt by Government and implemented in subsequent competitions

UK rail franchising – success or failure ?

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Franchise system

- working well
- some changes in approach (franchise duration, specification detail), but fundamentally unchanged
- lively competition
- most original franchises heavily subsidised, recently substantial premia
- but: Government leadership often needed for major innovations

Usage

- considerable growth, forecast to continue
- rail share of travel up from 5% to 7%
- passenger journeys up from 800m to 1.1bn

Passenger satisfaction

- steady upward trend
- > 80% of passengers now satisfied with journey overall
- intangibles of travel experience greatly improved (station facilities, personal security, ticket availability, availability/helpfulness of staff)
- satisfaction with value for money only around 40%