



OFFICE *of the*
RAIL REGULATOR

**NEW SERVICE OPPORTUNITIES
FOR PASSENGERS:**

A POLICY STATEMENT

Contents

Regulator's foreword	1
The Regulator's conclusions on new service opportunities for passengers	3
1. Introduction	3
2. Minimising the risks to existing services and franchise value	4
3. New service evaluation criteria	5
4. Protecting the interests of passengers	5
Timetabling issues.....	6
5. Other Issues	6
Major Investment and Exceptional Protection from Competition.....	6
Passenger Transport Executives.....	6
6. The approval of access rights for new services that take advantage of Stage II	7
7. Implementation of Stage II of Moderation of Competition	7
Next Steps	9
Initiation and the processing of nominations for Stage II.....	9
Further Information	11

Regulator's foreword

The implementation of the first stage of my policy for moderating competition for passenger rail services, which was established before train operators were franchised, has resulted in very limited opportunities for train operators to introduce new services. This is not surprising. It was the natural consequence of the granting of effective exclusivity in order to enable the franchises to be awarded. In October 1997 I published my consultation paper *New Service Opportunities for Passengers*, seeking views on whether it would be in the interests of passengers overall to move to the second stage of the moderation of competition framework first established in 1994.

The responses to the consultation, which I summarised in a further paper published in December, broadly supported the view that the current restrictions on competition were frustrating the development of some new services which could bring benefits to passengers, and that the second stage of moderation of competition should be initiated to allow new services to begin with the introduction of the Winter timetable in September 1999. This approach was, for example, supported by the Franchising Director, by the Central Rail Users' Consultative Committee and by the majority of the Passenger Transport Executives and local authorities who responded to the consultation.

Stage II offers the prospect of new services for passengers which can contribute to the Government's overall objectives for the rail industry, at little or no cost to taxpayers. Potential markets for new services include airport links, services to new developments, such as shopping and leisure centres and park and ride sites, and cross-regional services such as that proposed to link North and South Wales. I am much encouraged by such positive responses from operators and funding authorities, who recognise that efficiency and innovation drive down costs and improve choice. At the same time, there was a clear recognition that approval of new services would need to be based on a proper assessment of the likely impacts, and that there should be continuing controls over anti-competitive behaviour or behaviour which could disadvantage passengers through the loss of network benefits: such as through tickets and inter-available tickets.

Relaxing constraints on competition will, of course, also put additional pressure on franchisees to achieve and maintain greater benefits to passengers, for example through improved services or lower fares, throughout the term of their franchises.

Since December 1997 I have completed further research to assess both the likely scale and nature of new services, and the criteria and procedures which should be established for the

approval of new access rights that might be sought under Stage II. There is more work to be done on some aspects of this, for example on the development of evaluation criteria to assess the benefits to passengers of new services and their impact on the financial position of funding authorities (ie the Franchising Director and the Passenger Transport Executives), and on Railtrack's timetabling criteria to maximise the benefit to passengers of new services. I also want to ensure that the necessary approval and monitoring procedures will be effective, including how best to enable local authorities to express their views on the contribution of proposed new rail travel opportunities to their overall transport objectives. However, I am satisfied that these remaining issues can be resolved, and that robust criteria and procedures can be put in place.

In the light of the consultation responses, and the further work undertaken on the likely impacts of relaxing current restrictions on new services, I have therefore concluded that it would be right to initiate Stage II with effect from the Winter 1999 timetable. I therefore propose to publish the necessary Notices, within the next few weeks. At the same time, I will be developing both the procedures and criteria for the evaluation of new service proposals, and the standards for competitive behaviour to which I will expect the train operators to adhere.

JOHN SWIFT QC

Rail Regulator

March 1998

The Regulator's conclusions on new service opportunities for passengers

1. Introduction

1.1 In his consultation document "New Service Opportunities for Passengers" published October 1997, the Regulator identified four key questions:

- (a) which features of the railway industry need to be taken into account to decide whether relaxation of the constraints on competition will achieve overall benefits to passengers and taxpayers;
- (b) what are the opportunities for new services and passenger benefits;
- (c) to what extent should the train operators take the initiative in identifying opportunities for new services; and
- (d) what are the main potential disbenefits for passengers and franchisees, and what further controls are needed.

1.2 The results of that consultation were published in December 1997. Overall, the responses confirmed that there were expected to be benefits for passengers in relaxing the current constraints on new service development. Some consultees were concerned that the timing of that relaxation needed to be consistent with the ability of the train operators to understand and cope with the implications and opportunities of such a change. However, there was general acknowledgement that if an incremental relaxation of constraints were appropriate, the proposed framework was the right way forward. A number of consultees were concerned as to the impact on network benefits and on the Franchising Director's and Passenger Transport Executive's ability to continue to achieve best value for money when purchasing services. The majority also felt that it was important for the Regulator to be satisfied that the appropriate control mechanisms existed to prevent the erosion of network benefits and the promotion of a balanced timetable, both of which were seen as the worst potential detriments of 'rail wars'.

1.3 The Regulator has since completed further research which has supported the view expressed by consultees that, on balance, there are likely to be benefits from relaxing

the constraints on service development. In addition, it appears that the effect of potential detriments on the Franchising Director's budget can be minimised through the exercise of access and licensing powers to the point where initiation of Stage II of Moderation of Competition can, with some confidence, be expected to bring benefits to passengers with very limited impact on funder's budgets.

1.4 The research has centred on two key areas:

- (a) the quantification of the maximum impact of new service development on existing franchisees and the associated subsidy requirements; and
- (b) the degree to which Stage II might encourage train operators to act in a manner which is not in the best interests of passengers and the effectiveness of control mechanisms in terms of both inhibiting the development of detrimental service proposals and controlling the behaviour of train operators after the introduction of the new service.

2. Minimising the risks to existing services and franchise value

2.1 The Regulator believes that it would not be in the overall best interests of passengers for an un-controlled development of new services to lead to a loss of existing socially desirable services. He agrees that if the relaxation of the current restrictions were to result in a transfer of rolling stock away from services that are at best marginally economic but which have a high social value, then it could lead to passenger detriments. He also agrees that any significant loss to the budgets of either the Franchising Director or the Passenger Transport Executives could equally result in detrimental service reductions.

2.2 The Regulator has considered the issues which might lead to detrimental impacts upon existing services and he is satisfied that neither the redeployment of rolling stock nor the potential impact upon subsidy requirements are necessarily likely to result in significant detriments for either passengers or taxpayers.

2.3 Overall, the Regulator believes that the limited availability of rolling stock until 2002 could itself act as a constraint on the ability of train operators to take advantage of opportunities which will emerge under the Stage II regime, thereby preventing a step change in the number of new services which need to be considered and facilitating a gradual introduction of the type of new services envisaged.

- 2.4 The Regulator is satisfied that, by controlling Stage II in a way that encourages the development of new services that can be incorporated into future franchise specifications, he will enable new service development opportunities to be pursued at minimal or zero cost to the Franchising Director's or the Passenger Transport Executive's budgets. This conclusion requires that a mechanism is in place for evaluating the new service proposals on a case by case basis.

3. New service evaluation criteria

- 3.1 The Regulator welcomed the proposal that individual new service proposals should be evaluated on a case by case basis using criteria similar to OPRAF's own Planning Criteria. He believes that use of such criteria would contribute toward achieving an effective evaluation of the impact of individual new service proposals, particularly when combined with a consultation process which allowed him to take account of the views of other parties such as local authorities whose overall transport objectives may be affected.
- 3.2 In order to take this forward, the Regulator is planning to prepare detailed criteria and procedures for the evaluation of new service proposals for consultation during the late spring of 1998. The formal statement, following consultation, will then be published in the late summer of 1998, at or around the same time as the individual Stage II Notices for train operators are issued.

4. Protecting the interests of passengers

Network benefits and anti-competitive practices

- 4.1 The Regulator believes that train operators already have the option to act in ways which could have a detrimental effect on network benefits or otherwise be considered anti-competitive. Whilst he accepts that the incentives on train operators to indulge in this kind of behaviour may be increased by the initiation of Stage II of moderation of competition, he also believes that the combination of licence conditions, competition legislation and industry wide agreements, membership of which is in many cases a franchise requirement, will largely inhibit the ability of train operators to act in ways that are detrimental to the interests of passengers.
- 4.2 The Regulator accepts that there are concerns as to the effectiveness of the available control mechanisms and he will be taking forward a programme of work to identify those benefits which are most valued by passengers and those practices which could

reduce their availability. That work will also include the development of a mechanism for ensuring that train operators have a clear understanding of what kind of action would be considered to be predatory, exclusionary or anti-competitive behaviour.

Timetabling issues

- 4.3 New services on routes wholly or partially served by other operators will generally bring greater benefits for passengers if the timetable is balanced. In the deregulated bus industry, for example, one aspect of behaviour which was not in the interest of passengers was the tendency of operators to time services to run just in front of a competitor.
- 4.4 The Regulator is satisfied that appropriate controls can be developed which will require both the train operators and Railtrack to develop new timetables in a manner that promotes an even-interval timetable wherever possible. The Regulator will be developing this matter further as part of his policy statement on Timetabling which is due to be published in the near future. In addition, the approval of individual access rights will be subject to criteria that examines the manner in which the new services will be timetabled in relation to existing services.

5. Other Issues

Major Investment and Exceptional Protection from Competition

- 5.1 A number of responses to the consultation suggested that train operators should be restricted from developing new service proposals which take advantage of the Stage II arrangements if they themselves are protected from any relaxation of the current restrictions. The Regulator acknowledges that there may be some injustice in allowing train operators to develop new services while at the same time enjoying protection from competing new services themselves; but he believes that to restrict such operators from developing new services would not be in the interest of passengers. Indeed, the Regulator would not wish to deny passengers the benefits of new services where they are not expecting to otherwise benefit from significant investment by both the train operators and Railtrack.

Passenger Transport Executives

- 5.2 A number of PTEs made representations in response to the consultation which identified concerns regarding the inability of the Stage II mechanism to protect their

interests, particularly in markets where the PTE was accepting the revenue risk. Indeed the mechanism could have been considered to generate incentives for train operators which positively encourage them to expose PTE revenues to more rather than less competition.

- 5.3 Having held discussions with the PTEs, the Regulator has identified a process by means of which the relevant PTE will be able to sponsor nominations via the appropriate train operator in order to protect its budget. The details of this process are included in a separate document. In addition, PTE's can expect to be consulted about individual new service proposals as part of the access agreement approval process. The Regulator is therefore satisfied that there are unlikely to be detriments for PTEs that would argue against the initiation of Stage II.

6. The approval of access rights for new services that take advantage of Stage II

- 6.1 The Regulator's timetable for the implementation of Stage II is specifically designed to enable train operators to develop new service proposals that take advantage of Stage II such that they might be included in the Winter 1999 timetable. At this time the Regulator does not expect to approve access rights that take advantage of the Stage II regime where those access rights would allow the introduction of new services prior to the introduction of the Winter 1999 timetable.
- 6.2 The Regulator is also concerned that he may be asked to consider proposals for new services without having sufficient time to complete the required procedures and evaluation. He therefore expects that any proposals for access rights for the Winter 1999 timetable that require to be considered in the light of the 'New Service Evaluation Criteria' will be submitted before the end of 1998 in order that approval can be given well in advance of the last bid date for the Winter 1999 timetable. In the event that late submission of an agreement leads to the Regulator being unable to complete the necessary evaluation, he would expect that the introduction of the new service would be delayed until such time as a fully informed decision could be made.

7. Implementation of Stage II of Moderation of Competition

- 7.1 The implementation of Stage II requires that each train operator will nominate flows for protection. The procedures by which this is to be done, and the procedures and criteria that will be followed by the Regulator in processing those nominations are identified in a separate document "New Service Opportunities for Passengers: Criteria

and Procedures for the Approval of Train Operator's Proposals for Stage II of Moderation of Competition" which is being published as a technical appendix to this policy statement. That document also identified a number of technical changes and clarifications to the mechanics of Stage II, including issues relating to common control of more than one train operator, the use of lower materiality thresholds, protecting the interests of Passenger Transport Executives where they accept revenue risk, and restrictions on the use of alternative stations/termini.

Next Steps

Initiation and the processing of nominations for Stage II

The implementation of Stage II requires a number of activities to be completed before 30 September 1998. The full programme is as follows:

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|-----------------------|---|
| by 31 March 1998: | notices will be issued adjusting the Stage II initiation date; |
| by Mid April 1998: | the Stage II initiation notices will be issued; |
| by 30 June 1998: | all nominations must be made by train operators; |
| by 30 September 1998: | all notices identifying approved and rejected nominations must be issued; and |
| by December 1998: | receive all proposals for new services possible under Stage II to be introduced in Winter 1999. |

In addition the Regulator expects to have consulted upon and issued the criteria and procedures for the evaluation of new service proposals by 30 September 1998.

Further Information

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