House of Commons

Committee of Public Accounts

Increasing Passenger Rail Capacity

Fifth Report of Session 2010–11

Report, together with formal minutes, oral and written evidence

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The Committee of Public Accounts

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Summary

The Department for Transport is eighteen months into a five-year, £9 billion investment programme to improve rail travel, in particular by increasing the number of passenger places on trains by March 2014. This was to be achieved by a combination of longer platforms and other station improvements and more carriages coming into London and other major cities during peak hours. The Department is responsible for securing the extra places on trains from train operators. The Office of Rail Regulation is responsible for ensuring Network Rail delivers infrastructure efficiently.

The Department's latest plans show that all the relevant targets will be missed. There will be 15% fewer extra places delivered in London in the morning peak and 33% fewer into other major cities, compared to the numbers the Department stated would be needed just to hold overcrowding at current levels. Despite the impact of the present economic downturn on journey numbers, we are concerned that the failure to meet the targets set will lead to substantial increases in already unacceptable overcrowding levels by 2014 and beyond. Rising demand for rail travel combined with serious cuts in public expenditure make it imperative that the rail industry becomes more efficient, otherwise the passenger will suffer. The Department told us that levels of crowding, and ticket prices, depend on policy decisions about the level of government subsidy. We are strongly of the opinion that this view is misguided as it ignores the scope for efficiency savings to release resources for front line services. The industry's ability to provide a good quality rail service, including acceptable levels of crowding, depends crucially on the efficiency of all players in the rail industry, and of Network Rail in particular.

Rail infrastructure costs more in Great Britain than in other countries. The Regulator has been in existence for more than a decade yet he still accepts that there is still "a very large potential for Network Rail to improve its efficiency".

The Regulator's ability to drive efficiency in Network Rail is limited by a lack of transparency of Network Rail's costs which, it seems to us, is compounded by the Regulator's lack of urgency and effectiveness in challenging Network Rail's efficiency at a detailed level. Network Rail is a company without shareholders and is the monopoly provider of rail infrastructure. It is vital therefore that its costs are scrutinised and challenged robustly and independently on behalf of Parliament and taxpayers. The National Audit Office is ideally placed to do this.

On the basis of a Report by the Comptroller and Auditor General,[1] we took evidence from the Department for Transport and the Office of Rail Regulation on the measures taken to tackle overcrowding and on obtaining value for money from the rail network.

1 C&AG's Report, Session 2010–11, *Increasing Passenger Rail Capacity*, HC 33

Conclusions and recommendations

1. **All but one of the fifteen English rail franchises have no requirements for the operator to meet demand without excessive overcrowding, and so the taxpayer usually has to provide additional funding for extra carriages.** For future rail franchises the Department should impose clear obligations on operators to avoid overcrowding, and to bear the costs of meeting that obligation themselves.

2. **The current round of planning relied heavily on buying extra carriages and on extending platforms to accommodate longer trains but this approach cannot go on indefinitely. Clearly, alternatives must be found to meet the capacity challenge in the future.** The Department should vigorously pursue and promote smart ticketing and other demand management techniques to reduce the inefficiencies of overcrowding in peak hours and underused rolling stock at other times.

3. **The Department's knowledge of how many people use which parts of the rail network and when is inadequate, sketchy and so gives a poor basis for decision-making.** The Department should require all new train carriages, whether procured by the Department itself or by franchisees, to be fitted with automatic passenger counting equipment to show how many people are travelling on what trains and when. It should require franchisees to provide useful and verifiable data from that counting. It should also report back to the Committee on progress to establish a computer system to capture, analyse and report on this data.

4. **It is not clear to passengers where the money from increased fares has been spent.** For example, passengers in some parts of the Southeastern franchise are paying premium fares to support new services which do not stop at their stations and do little to alleviate overcrowding on the trains they use. The Department should provide transparent information on how many new passenger places it is delivering, on which trains, and at what cost to taxpayers and fare payers.

5. **The Office of Rail Regulation does not have a grip on Network Rail's efficiency and appeared remarkably relaxed about the continuing gap in performance between Network Rail and international comparators.** It is surprising that the Regulator, which has been in operation since 1994, accepts that there is still a "very large potential" for Network Rail to improve its efficiency (for example a potential to reduce costs of platform lengthening by 25% compared to European peers), yet does not have a detailed bottom-up and complete understanding of Network Rail's costs. Particularly given that Network Rail is the monopoly provider of the rail infrastructure, there appears to be marked complacency in the Regulator's approach and he should do much more to challenge the underpinning reasons for existing inefficiencies. The Department should take any steps which are necessary to enable the Regulator to do this.

6. **The unique and complex structure of the rail industry makes it inherently cumbersome and expensive, and provides little external challenge to its vested interest in its own growth.** The Department should conduct a fundamental review of the rail industry's structure, to ensure better accountability and value for money, with the aim of reducing conflicts of interest, aligning efforts on maximising efficiency, and restraining the tendency to seek solutions through growth.

7. **Governance arrangements for the railways do not provide enough independent scrutiny and transparency to drive value for money relative to the sums of taxpayer money involved.** The Department should take the necessary steps so that the Comptroller and Auditor General becomes the auditor of Network Rail, including full access rights so that he can report on value for money to Parliament.

8. **It is unacceptable for Accounting Officers to challenge the findings of a National Audit Office report in evidence to this Committee, having previously agreed the accuracy of the report prior to its publication.** The Permanent Secretary must in future satisfy himself that facts and their presentation within National Audit Office reports are accurate before their publication, and not wait until the committee hearing to reveal new evidence. Such late presentation of evidence also prevents the NAO being in a position to provide us with independent validation of new material. The Treasury should reinforce to Accounting Officers the importance of providing supplementary material in time for the Committee to consider it and for the NAO to validate it.

1 Increasing passenger rail capacity

1. The Department published a 30-year strategy in July 2007 with the stated ambition to double the number of passengers that could travel by rail. In the strategy £9 billion was allowed for the five years to March 2014, with £7.8 billion for infrastructure improvements by Network Rail (for example lengthening platforms to accommodate longer trains) and £1.2 billion for train operating companies to provide extra carriages.[2] The intention was to allow more passengers to travel by rail into London and other major cities without an increase in average levels of crowding.[3] The investment programme to increase rail passenger capacity was put on hold in May 2010 pending the current Spending Review.[4]

2. The Department's plans (before investment was paused) indicated that substantially fewer extra places for passengers would be delivered by March 2014 than it had originally estimated would be needed to prevent increased overcrowding. For example, those plans indicated there would be 15% fewer extra places on trains coming into London (99,000 compared to 117,000), and 33% fewer in other major cities (25,500 compared to 38,000), in the three-hour morning peak, than it had originally envisaged.[5] Nevertheless, the Department expected to avoid increases in crowding because of the forecast effect of the recession in reducing demand.[6]

3. An underlying problem is the lack of incentives for the industry to supply extra capacity without additional taxpayer support. National franchise terms require train operators to use "reasonable endeavours" to deploy their train fleets to give peak passengers a reasonable expectation of a seat within 20 minutes of boarding. However, the national terms do not require train operators to expand their fleets or improve stations to avoid excessive overcrowding. Instead, to get extra places on trains the taxpayer has to bear much of the train operators' costs as well as providing funds to Network Rail for it to build longer platforms.[7]

4. The Chiltern Trains franchise is an exception as it requires the operator to bear the costs of providing enough capacity, in terms of both carriages and platform lengths, to meet demand during peak hours without exceeding maximum loads. The Department is currently consulting on the appropriate terms to be included in franchise agreements in the future, including on whether obligations to avoid overcrowding, similar to that in the Chiltern Trains franchise, should be imposed more widely. The Department will need to take care, however, that the quality of information on which to base demand forecasts is improved and made available to potential bidders so they do not overprice the risk of dealing with overcrowding, due to a lack of information.[8]

2 Q 47; C&AG's Report, paras 1 and 1.6

3 C&AG's Report, para 2

4 C&AG's Report, para 5

5 Q 1; C&AG's Report, para 3.8

6 C&AG's Report, Figure 8 and para 3.8

7 Q 19; C&AG's Report, para 3.11

8 Qq 19–25; C&AG's Report para 3.14

5. Despite the scale of the proposed five-year investment, the Department did not have comprehensive data on the actual numbers of passengers using each service, when it was forecasting demand and planning how best to meet it. Its principal sources of information were annual counts of passengers on a single day at a single point on each route.[9] The situation has improved since, as new carriages are brought into service, with the result that 39 per cent of carriages are now fitted with automatic counting equipment. It is not clear, however, whether such equipment is required for all new trains procured by the Department and train operating companies, or whether it is fitted as standard on new trains in any event. Moreover, the Department does not have the IT capability needed to process information on the scale produced by automatic passenger counting. It has plans to acquire a new IT system to allow it to make full use of the data but the acquisition is on hold pending the Spending Review.[10]

6. The Department's plans relate to blocks of the country and fare increases are also set at the level of franchises. In the area covered by the Southeastern franchise, for example, fares have risen by RPI plus 3% regardless of whether the fares relate to services which have benefited from investment. So, for example, passengers using trains from Orpington pay higher fares although the increased capacity has been provided on services which do not stop there. The ability to align what the passenger pays for a ticket with the investment they see and use on their route does not exist in the British railway system at the moment, though it is a key aspiration which the Department is pursuing with train operators.[11]

9 C&AG's Report, para 1.7

10 Qq 29–30 and 33–37; C&AG's Report, para 1.7; Ev 20

11 Q 32

2 Improving efficiency in the rail industry

7. When the Department was asked about relatively high fares in Britain compared to other countries its answer referred exclusively to the dependency of fares on the level of public subsidy, and not to the relative efficiency of rail systems internationally.[12] Rail infrastructure costs more in Great Britain than elsewhere and the Office of Rail Regulation has concluded that there is "a very large potential for Network Rail to improve its efficiency".[13] The Regulator, on the basis of costs from the Netherlands, has concluded that Network Rail could have made savings of 25 per cent in the costs of platform extensions if it had used modular rather than conventional construction methods. In his evidence to the Committee the Regulator agreed that Network Rail has an "expensive approach".[14]

8. The Regulator is responsible for improving Network Rail's value for money and has been in existence since 1994, yet Network Rail is still less efficient than international comparators. The Regulator's targets for Network Rail require it to increase its efficiency by March 2014 and to close the efficiency gap between it and its European peers by two thirds.[15] The National Audit Office (NAO) found that the Regulator did not have bottom-up evidence of detailed costs of enhancements, their trends over time, or their current levels relative to comparators, when it was assessing the levels of efficiency savings Network Rail could make within its programme of capacity enhancements.[16] In his evidence to the Committee the Regulator was unable to provide broad figures on the financing costs of Network Rail's debt and accepted that the judgements taken on the appropriate allowances for Network Rail's costs are sometimes not fully backed up by all the data.[17]

9. The railway industry is unique and complex; including Network Rail, the train operating companies, the Regulator and the Department. Complexity necessarily brings increased costs and, particularly in the current financial climate, the Committee would have expected to see concerted efforts to drive down costs, for example in headquarters functions.[18] Levels of executive pay at Network Rail are considerably higher than those in the public sector. The outgoing Chief Executive's salary for 2009–10 had been reported as £613,000 with total remuneration of £1.2 million, with the latter figure confirmed as broadly correct by the Regulator. The Regulator was aware of Network Rail's management incentive plan, and had written to the Chairman of its remuneration committee, to inform him of the performance of the company and assist the committee in its considerations.[19]

10. In relation to the costs of extra carriages the Department has already contracted for 650 extra carriages. It has not sought to renegotiate these contracts to increase their value for

12 Qq 31 and 55

13 Q57; C&AG's Report paras 14 and 2.2

14 Qq 61 and 78–80; C&AG's Report, para 2.11

15 Qq 46, 56–59 and 82

16 Qq 60 and 86; C&AG's Report para 2.12

17 Qq 47–55, 60 and 86

18 Qq 52, 71–76 and 98; C&AG's Report, Appendix 2

19 Qq 52 and 91–98

money since it believes the commercial environment has not changed since those contracts were concluded.[20] To meet rising demand, the Department's focus so far has been on increasing the numbers of places on trains by buying carriages and lengthening platforms. It accepts, however, that this cannot go on indefinitely and hopes, in the future, to widen its focus to include managing demand away from the peak by using electronic ticketing.[21]

20 Qq 17–18; Ev 20

21 Qq 27–28 and 40–41

3 Governance in the rail industry

11. Network Rail does not pay dividends to shareholders. It is a company which has 100 members at present including the Department and 26 'industry members'. The industry members are drawn from Network Rail's trading partners, principally the train operating companies. The other company members are members of the public.[22] The Government indemnifies Network Rail's debts which reduces the pressure from lenders on it to increase efficiency.[23] Network Rail is also the monopoly provider of railway infrastructure in Great Britain.[24]

12. The Regulator told us that having a single infrastructure provider presents regulatory difficulties, in particular that international benchmarking is needed to challenge Network Rail's costs.[25] The Department and the Regulator are currently co-sponsoring a study to look at the reasons why it is, within the complex arrangements existing in Great Britain, that railways elsewhere in Europe can do a similar job at substantially lower cost.[26] In evidence the Permanent Secretary said that he was not sure whether those parties currently comprising the British railway network are optimally organised or whether their incentives are aligned.[27]

13. Network Rail has a unique structure and position within the rail industry. It provides the plans on which the Regulator bases his determination of what infrastructure works Network Rail should carry out and at what cost.[28] Network Rail receives a subsidy from the Department (£15.3 billion for the five years to March 2014) and the Department indemnifies Network Rail's debts, yet its accounts are not audited by the Comptroller and Auditor General and he does not have authority to conduct value for money examinations of Network Rail.[29]

14. In his evidence to the Committee the Permanent Secretary queried the Comptroller and Auditor General's finding that the Department's expectation that it would spend close to the £1.2 billion originally allowed for support to train operators, while planned capacity increases fell short of those originally envisaged, represented a risk to value for money. The Permanent Secretary told us that the planned capacity figures cited in the report were predicated on expenditure of only £900 million. Spending the remaining £300 million in line with the Department's expectation would have given further extra capacity above the levels cited in the report.[30]

22 Qq 64–70 and 96–97

23 C&AG's Report, paras 2.13–2.14

24 Qq 40–41

25 Q 41

26 Qq 71 and 88

27 Q 104

28 C&AG's Report, para 2.1

29 Qq 31, 70, 81, 87–88, 91–92, 98–103 and 108

30 Qq 2–7 and 15

15. The Accounting Officer was unable to tell us why he had not clarified this matter with the NAO prior to publication on the 2 June 2010 or why the matter had not been raised with the NAO until the week before the Committee hearing. Having failed to scrutinise the draft report adequately at the appropriate time and raised the matter so late, it was not feasible for the NAO to investigate the Department's new assertions prior to the hearing.[31]

31 Qq 8–10

Formal Minutes

Wednesday 27 October 2010

Members present:

Rt Hon Margaret Hodge, in the Chair

Mr Richard Bacon
Jackie Doyle-Price
Matthew Hancock
Chris Heaton-Harris
Rt Hon Mrs Anne McGuire
Mr Austin Mitchell
Ian Swales
James Wharton

Draft Report *(Increasing Passenger Rail Capacity)*, proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 15 read and agreed to.

Conclusions and recommendations 1 to 8 read and agreed to.

Resolved, That the Report be the Fifth Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for printing with the Report.

[Adjourned till Tuesday 2 November at10.00 am

Witnesses

List of written evidence

List of Reports from the Committee during the current Parliament

Session 2010–11

First Report	Support to incapacity benefits claimants though Pathways to Work	HC 404
Second Report	Delivering Multi-Role Tanker Aircraft Capability	HC 425
Third Report	Tackling inequalities in life expectancy in areas with the worst health and deprivation	HC 470
Fourth Report	Progress with VFM savings and lessons for cost reduction programmes	HC 440
Fifth Report	Increasing Passenger Rail Capacity	HC 471

Oral evidence

Taken before the Public Accounts Committee

on Wednesday 15 September 2010

Members present:

Margaret Hodge in the Chair

Richard Bacon	Austin Mitchell
Stephen Barclay	Nick Smith
Jackie Doyle-Price	Ian Swales
Matthew Hancock	James Wharton
Joseph Johnson	

Amyas Morse, Comptroller and Auditor General, **Gabrielle Cohen,** Assistant Auditor General and **Geraldine Barker,** Director, National Audit Office, gave evidence.

Marius Gallaher, Alternate Treasury Officer of Accounts, was in attendance.

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL

Increasing passenger rail capacity (HC 33)

Witnesses: **Robert Devereux,** Permanent Secretary, Department for Transport and **Bill Emery,** Chief Executive, Office of Rail Regulation, gave evidence.

Q1 Chair: Welcome to you. We are looking at rail capacity. We thought we would take it in two separate sections: one looking at the overcrowding and planning issues and then looking at the costs. So, we will try and divide up and get some structure to the questioning that we have of you. I think I'll start the ball rolling, if I may. According to the Report, you set yourselves the task of increasing capacity by about 17%—117,000 more places. You are now saying in the Report that you are spending the same, but getting fewer places—99,000 places. So, can you tell us why that has happened and what on earth that will mean for the commuters who are going to have to continue to travel in cattle truck conditions?

Robert Devereux: Let me just make a brief point about context, if I may, to start. What the Report in front you does is to examine the Department's actions and plans one-year in to a five-year delivery plan. At the stage that we were examined I can tell you that we had contracted one-third of the additional capacity the previous Government had sought and every one of those actions had delivered value for money.

Q2 Chair: As what?

Robert Devereux: And every one of those actions had delivered value for money. Beyond that, we had plans—clear plans—that we could evidence to the National Audit Office to take that third to 80% of the required capacity, by which time, we expected to have acquired around 950 carriages and spent around £900 million. The third thing we were doing then was continuing to work out whether we could identify the interventions that would enable us to get to probably around 1,300 carriages and to develop the full capacity, using the full budget of £1.2 billion. So, the figures you just referred—first of all, the figures you referred to are in respect of London, and so the 117,000—

Chair: Yes—yes.

Robert Devereux: —is what we support for London.

Chair: Sorry, and 37%—yes.

Robert Devereux: And there is another 38,000 that we sought outside of London. And what the charts are showing, effectively, is what had been contracted and what interventions, for which we had very clear plans, the National Audit Office could sign off in terms of what they would deliver. As I say, that amounts to around 950 carriages, but it does not use all of the budget of £1.2 billion that we had available. We were still working through and seeking to spend that money in order to increase the capacity beyond the figures shown in the tables.

Q3 Chair: Well, then why when you signed off—because you sign off these reports before they come to us—did you say that you were going to buy fewer carriages and, therefore, reduce the capacity both in London and outside—33% outside reduction; 15% in-London reduction—but you were going to do that for the same money? In the Report—in the information that we have in front of us, you were still spending £1.2 billion, not £900 million or whatever it is. That was signed off, as I understand it, by the National Audit Office and yourselves.

Robert Devereux: Perhaps if you just look at the critical bullet on the bottom of page 8. What it says is that the Department's latest plans—and by that I mean plans that the National Audit Office would let us score because there was detailed evidence for them—would have delivered, I use the subjunctive tense, significantly less capacity although the taxpayer would have provided as much—

Chair: Yes.

Robert Devereux: They would have provided as much had we bought more carriages than the National Audit Office put in those charts.

Q4 Chair: But the National Audit Office put them in the charts because you told them that was what you were going to do.
Robert Devereux: With the greatest respect, we told the National Audit Office what our plans were as evidenced in terms of quite detailed interventions. It was quite clear, and they were aware that we had some capacity to buy more, but that we did not yet have plans for that. This is the paragraph about risks to value for money, and there was indeed a risk to value for money that we might not be able to spend the rest of the money wisely, but the money we have spent and planned for is going to be spent wisely.
Geraldine Barker: Perhaps I could clarify. What we asked for from the department was evidence of what capacity was going to be delivered by 2014. They provided us with a bulk of data, we looked at that and that's what we have reported. We then asked them how much money they expected to spend to provide that capacity. They told us it was £1.2 billion and they quoted the figure of 1,300 train carriages. At that point, we went back several times and asked them. We felt that there was an inconsistency—you seem to be buying the same number of carriages, but you're not delivering the same capacity. They told us that there was not an inconsistency, but that information was correct, and that is why we have placed those two sentences side by side.

Q5 Chair: So what changed?
Robert Devereux: Well, nothing has changed because I saw it—
Chair: Something must have changed because your officials told the National Audit Office, who then produced a document, which is in the public domain, that the money available to you—the £1.2 billion—was buying you less. That is obviously of huge importance. Suddenly—miraculously—from when this was signed off in end of May to us seeing you here in September, something has changed and you are buying less, but spending less. Something's changed.
Robert Devereux: Well, I can apologise if you think the story is different, but nothing has changed. I can absolutely assure you. We have not changed our plans in any respect. I think, if you listen very carefully to what the NAO said, the fault line looks a bit like this: it was a commitment of the previous Government to deliver 1,300 carriages, for which they had a £1.2 billion budget. So, every time the question was asked, "What do I expect to spend?", the answer came back, "£1.2 billion." It was, as a matter of fact, in figures 9 and 10, when asked, "What plans have you got to deliver it?", the only things we were able to evidence were the first 950. We are still working—we are one year through a five-year plan on exactly what the rest of them are. There are propositions in the Department now—because we are now six months further on—for some more carriages, which we believe will have value for money. We could not evidence that to the National Audit Office when they came. That's the difference.
Geraldine Barker: But nobody told us that there were other plans in the offing. We were given data and told that was what was expected to be delivered by 2014.

Q6 Chair: This is very unusual. We are probably on our seventh or eighth hearing and the basis on which we undertake these hearings is, on the whole, an agreed Report between the Department and the National Audit Office and we can then make sense of the facts that we have in front of us. It is not satisfactory—I have to say that to you—it is not satisfactory to have an interrogation where the facts change as you appear before us now.
Robert Devereux: I perfectly understand that and—
Chair: Clearly, when I read this Report, the thing that hits you—and I am sure all my members would say likewise—what hits you is why suddenly, having planned to spend £1.2 billion to get a certain number of carriages, you are getting fewer carriages but spending less money. Now, you're saying, "No, no, we have miraculously found that we actually can spend less money and get fewer carriages." But you're achieving—that change is not acceptable. I just have to put that on the record.
Robert Devereux: Well, I must accept that. I perfectly understand; I have been here six or seven times before. I know the basis on which this is done and all I can tell you is that this was signed off, and when I went through this with a fine-toothed comb in order to prepare myself for this afternoon, I had to make sure I actually understood on what basis this had been prepared. If your conclusion of that is it should have been more apparent that the tables to do with capacity had to line up with the tables to do with carriages, had to line up with the money, which was not the proposition that was in the draft, then my apologies. We have not sought—I promise you—to try to obfuscate this. We have told you the plans that we had, and we have told you we had expected to spend the money. That is the reality. As far as today is concerned, the position is the position I've just described.

Q7 Mr Bacon: Surely the point is, as Geraldine Barker just told the Committee, you did not tell the National Audit Office that there were other plans in the offing, did you?
Robert Devereux: I'm afraid I was not party to the conversations, so I do not know what was said, but it did—
Mr Bacon: That's not an acceptable reply because you are the Accounting Officer.
Robert Devereux: But it—
Mr Bacon: The Department for Transport did not—Geraldine Barker has told us the Department for Transport did not tell the NAO there were other plans in the offing.
Robert Devereux: If that's the case then I apologise.

Q8 Mr Bacon: Now, unless you are accusing Ms Barker of lying, which I don't suppose you are, we have to take that statement at face value. Why didn't the DfT tell the NAO that there were other plans in the offing?
Robert Devereux: I'm afraid I do not know the answer to that question.
Chair: But you do sign off the report.

Q9 Mr Bacon: When did you first tell the NAO that the facts that you have signed off in this report were not in all respects accurate anymore?
Robert Devereux: Well, in the way I have tried to explain it to you, that when people present things called planned capacity, they mean what I've just said they mean. I am not trying to argue that I am trying to say that somehow we have produced the wrong data. I have tried to understand this on the basis on which actually the National Audit Office has presented it. I did indeed—because you go through this in some detail before you come before your Committee—do quite a lot of work on this in the last few weeks, and in the space of the last week to 10 days it has been quite clear to me that there is a discrepancy in the way that is being understood in the words. For that I apologise and I can only tell you what I believe to be the truth now, and—
Mr Bacon: And what's the answer to my question?
Robert Devereux: I'm sorry?
Mr Bacon: What's the answer to my question?
Robert Devereux: Which was the question?
Mr Bacon: My question was when did you first tell the NAO that the facts were not the facts as you had understood them?
Robert Devereux: I personally spoke to the C&AG I think it was Friday last week?
Amyas Morse: That's right.
Robert Devereux: I had been speaking to my officials who have been speaking to the NAO in the week prior to that. That's the timeframe over which I do the detailed operation.

Q10 Mr Bacon: I have to say, Mr Devereux, I don't find this very acceptable. It's not the first time that we have had problems with the Department for Transport and information being given to the DfT that turned out to be inaccurate. You will remember the problem with the evasion of motor vehicle licences and particularly motorcycle vehicle licences. So, I think just we should record the fact in our report that we are not happy about the DfT's co-operation with the NAO.
Robert Devereux: From memory, the evasion figures—what you were told at the time—were correct. It turned out subsequently that further information was available and that's not the same as—
Chair: Well, I mean, it is so obvious—
Mr Bacon: I remember it well and it was radically different from what you had told us previously. But I just think, Chairman, we should probably move on.

Q11 Chair: Yes, okay. Can I now understand, as you are buying fewer new carriages—
Robert Devereux: Correct.
Chair: Are you, therefore, increasing capacity by less?
Robert Devereux: Yes.
Chair: Right.
Robert Devereux: Sorry, let me be very clear: the 950 carriages for which I have firm plans, which the National Audit Office has seen, buys less capacity.
Chair: Right.
Robert Devereux: That is not the same as saying, "Have I given up on providing further capacity with the balance of my budget?" However, there being a spending review on, the—

Q12 Chair: You have offered them up as savings?
Robert Devereux: No—the availability of that is one of the things that the Government are looking at at present.

Q13 Chair: So, if you are buying less capacity, the increase in capacity is now 15% fewer places in London, 33% fewer places outside London. That means overcrowding will become worse.
Robert Devereux: Only if we buy no more with the budget that, going into the spending review, we had spare headroom within.
Chair: Or you will deal with the overcrowding later.
Robert Devereux: Well, these are the considerations that Ministers are having to work through with the spending review. Clearly, in order to reach the 117,000 within London, we will have to do further interventions—that is quite difficult thing to do. First and foremost, it is a problem of affordability. Secondly, it is finding the right transactions.

Q14 Chair: And do you still have your £1.2 billion. Do you still have that budget or have you offered that up as a cut?
Robert Devereux: The £1.2 billion is a budget over five years and it is over that period that Ministers are now trying to make decisions. Lots and lots of things are being looked at upside down and have—

Q15 Chair: So you have so far cut out of it £300 million. You have chosen not to spend £300 million of your £1.2 billion.
Robert Devereux: I have chosen not to spend £300 million—I have no firm plans at the moment to spend the £300 million, but the budget conceptually is the *ex ante* budget that the Government are currently reviewing as part of the spending review, the conclusions of which I don't know.

Q16 Chair: What is rather depressing is that when I looked at the White Paper that you produced in 2007 on which the expenditure of £1.2 billion—not the £900 million—was based, even if you extend capacity to its full—ie don't extend capacity less—you are still running to keep still.
Robert Devereux: Correct.
Chair: The overcrowding is still—
Robert Devereux: About the same.

Chair: —bad. So, were you not to spend your full £1.2 billion, you would then be increasing overcrowding for commuters. You would be making life hell for more commuters on more trains in London and the major cities.
Robert Devereux: There are a great deal of things that, with some available cash, I could make life better with, and the issue, therefore, is simply to do with the position that the Government find themselves in in terms of the overall deficit and the priorities within that that are then set. Your logic is absolutely correct that the previous Government's White Paper accommodated further capacity at pretty much the same levels of crowding as they were before the White Paper. That was a conscious choice because actually, even then, this is costing £9 billion to do, which will be paid for over a long period, and there simply is not a magic well to put even more money in to produce even more capacity and even less overcrowding.
Chair: Matthew.

Q17 Matthew Hancock: There is one way, which is to get better value out of the money that is in the current plan. So, taking the current plan to mean the £900 million, are you looking at that spend in order to try to improve the capacity by more within that part of the budget, given that the extra £300 million is under review in the spending review?
Robert Devereux: At the moment, we actually have contracts that deliver, from memory, around 650 of those carriages, and the balance of the 950 are things for which I have plans that I have not yet contracted and, therefore, exactly, I am in the space saying, "What is the very best price I could get for those?" I am not currently revisiting the contract for the 650 and—

Q18 Matthew Hancock: Have you done any assessment of whether you could successfully revisit those in order to get better value for money given that you are a such large purchaser in this area?
Robert Devereux: Could I get back to you on that because I just don't know whether my colleagues have done that.
Matthew Hancock: Oh, I would hope that they would, but yes.
Chair: Austin.

Q19 Austin Mitchell: Let me present to you a frail old man who has been twice the victim of your incompetence at providing extra accommodation on trains. I travel on the East Coast Line, and twice in the last two years I have been forced to stand all the way to Leeds on a First Class ticket—first by GNER and secondly by East Coast. That is just an absolutely insane procedure because it says in the contracts that operators should make reasonable endeavours to deploy their train fleets to give peak passengers a reasonable expectation of a seat within 20 minutes of boarding. I didn't have one for over two hours. Now, this really is disastrous. Unless you want to say that the companies are going to run cattle transport, why isn't it included in the contract with the companies? You did in the case of Chiltern Trains; why isn't it included in all the other contracts that they have to provide reasonable accommodation—that they must?
Robert Devereux: At the very end of the Report—I am on page 33 now—the National Audit Office goes through the arguments for this and they identify exactly that for Chiltern, which, for a variety of special circumstances that they record as being a single operator, with strong growth potential and a long franchise, that is indeed the nature of the franchise. We have consulted in a consultation document that went out in July on how might we change the franchising arrangement. Some of the options that we have explicitly canvassed include whether we could structure the franchises on the basis that you are buying a franchise within which you will achieve certain levels of, for example, crowding. Now, what the National Audit Office says at the bottom—the very last sentence of 3.14—is that obviously, as the accounting officer, you want to be really confident that the operator knows how to price that risk in such a way that you are not getting anything at a premium just for giving him the—

Q20 Austin Mitchell: But he clearly does not know how to price the risk in terms of giving every customer a seat in peak-time services. Why isn't that a requirement on them when they take the contract? Are you so scared that you won't get bidders that you don't want to enforce—
Robert Devereux: That I won't get what, sorry?
Austin Mitchell: Are you so scared that people won't bid for the contract—GNER gave it up, didn't they?—that you are not prepared to enforce that kind of term on them?
Robert Devereux: No. Let's just look at the capacity of the British rail network. It is an extremely heavily used network. I don't think it is beyond the—it's not going to be—
Austin Mitchell: Yes, but usage has been growing for well over a decade and here we are still cattle transporting. Usage has been growing for over a decade.
Robert Devereux: It has, so we now have probably the most extensively used passenger rail network in Western Europe and it would be delightful to be able to lay on services in which everybody who turns up gets a seat. The cost of doing that is very, very substantial.

Q21 Austin Mitchell: Yes, but it is an expectation that customers will travel in reasonable comfort, isn't it?
Robert Devereux: Yes.
Austin Mitchell: And they are not, particularly in London—and I'm not bothered about London, particularly. If people are daft enough to live down here, they deserve everything that's coming to them, but people on the East Coast Line are much more important and they are not travelling in reasonable comfort.
Robert Devereux: I'd just as soon not agree on who is more important than somebody else. We have tried to establish, as the Chair has just done, that the current level of crowding is already something we are

trying to tackle, but actually there are so many people who want to come into London into the next—

Q22 Austin Mitchell: Yes, but the companies are saying to you that, to quote page 32, paragraph 3.11, they argue that relieving crowding "generates little new fares revenue". Therefore, they will not do it unless they get Government support, which you are providing in this extra subsidy. Now, why are they allowed to get away with that argument?
Robert Devereux: Well, they're not. If it told you that, consistently, the proposals that the train operators provide for us in order to achieve the plans that we have been discussing earlier for these 950 carriages come at a price that my negotiators are significantly reducing, perhaps you'd believe that they are not "getting away with it".

Q23 Chair: Can I just ask you to bring this bit to an end, and then I will move to James. I just want to ask one question if I may. The Chiltern contract does look like a more sensible way forward. Are you attempting—it's almost a yes or no—and I completely understand you will be fiddled on the price you then have to pay, but are you attempting to negotiate that sort of contract within all the other franchises?
Robert Devereux: What we have done is put out a consultation about could that be a sensible way forward.

Q24 Chair: And when are you taking a decision?
Robert Devereux: Consultation closes on 22 October. Ministers will then think about it, but we have two franchises which we need to get on and let, which Ministers want to do on a new basis. Those decisions will therefore be in the autumn.

Q25 Chair: And will you be trying to negotiate that into them—obviously subject to price and everything—but would you able to try—
Robert Devereux: Subject to Ministers making decisions that that package of things is the most effective way forward, because it does actually address the points that the NAO have made—
Chair: Okay.
Robert Devereux: —but, yes, that is what we are trying to do.
Austin Mitchell: There are other passenger questions that I would like to ask.
Chair: May I come back to you, because there is a group of people waiting—

Q26 Austin Mitchell: No, let me ask this part of the question. The allocation was £9 billion for expanded capacity, but £7.3 billion of that was going to infrastructure enhancement such as longer platforms on stations nobody wanted to go to. Only a smaller part of it—much smaller part of it—was going to buy extra rolling stock. Now, are you sure you are not being taken for a ride by Network Rail, which is using this money for its purposes, rather than for relieving overcrowding?
Robert Devereux: Yes, very quickly, half of the number you just quoted is the cost of doing Thameslink. That is an incredibly complicated infrastructure project, involving lengthening platforms that, I can guarantee you, people will use.
Austin Mitchell: Well, it says better stations and longer platforms in this document.
Robert Devereux: Longer platforms are part of that funding.
Chair: Austin, I am going to give other people a chance to have a go. James.

Q27 James Wharton: I am rather fortunate when it comes to rail travel. I represent a constituency in the North East and I have two main operators to choose from—East Coast and Grand Central—and I declare my interest: Grand Central stops at a station in my constituency just up the road from where I live and I find there is very rarely a problem with overcrowding on their trains. So, I come to this from a regional perspective of not seeing a big problem when I set off, but when I get further south I do see that it becomes more and more of a problem, particularly on the trains that stop at further stations as they go south. Then in London, and of course in the South trying to use the trains, overcrowding is certainly a real difficulty. It seems that one of your primary solutions to this is going to be adding carriages on to the end of trains to make them ever longer. At what stage is that no longer going to be possible and you are going to have to look for new solutions to this problem?
Robert Devereux: It is the case that in the current control period—the five years to 2014—one the ways in which we are attacking capacity is by having longer trains. You should not assume that that is the only thing that can be done in perpetuity. So, for example, advances in signalling that would enable us to run trains much closer together and still do it safely would fundamentally improve the capacity of the network. Those are things that we are working on plans for, but they are simply not of a maturity that enables me to solve my 2014 problem now.

Q28 James Wharton: I understand that you have highlighted a couple of other options, and demand management is something that you have actually said is something you do not want to look at because of the disproportionate impact where you find people who can financially afford to overcome demand management through pricing and so on can do so. If you have dismissed that as a policy area that you want to take forward—
Robert Devereux: I don't.
James Wharton: You haven't? So it is something that you will be looking at?
Robert Devereux: It does not say I don't want to do it. What it says is I do not have the technology at the moment in place for that to be a solution for 2014, but I am doing quite a lot of work in changing the franchise terms to ensure that electronic ticketing is a requirement of all new franchises; I am putting electronic gates into the big London termini; I have the Oyster Card working on London suburban services. My expectation is that actually we will

indeed use demand management as another way of actually managing the network in subsequent years and we would have to tackle the question that, as it happens, the evidence suggests that—

Q29 Chair: So can I ask another question arising out of that? Is there a date by which you will know numbers? Because one of the things that strikes you as you read this Report is your lack of information on the future. You do this very odd manual survey, which seems to be very questionable. Your ticket sales are not a very good way of judging it and clearly just counting. When will you be able to do that?
Robert Devereux: Okay. As of today, 39% of all the carriages in the country have automatic counts on them and, since they are on the more busy lines, that probably represents a much larger percentage of the journeys. So, relative to the information that you have here, which is that the manual count itself is probably only picking up 3%, that is a completely transformational position. The thing that unlocks that is the ability to process, really, quite a lot of data—as you would imagine—from every service. The IT project, which the National Audit Office refers to, is currently suspended as part of the reviewing all IT projects by the Government. It is in my view a really critical project to ensure that we have got raw data, which is governing, as you have been though, £9 billion of enhancements. That is, in my view, in the urgent box. I think it is safe to say—

Q30 Chair: If you get the go ahead, it is in by when?
Robert Devereux: 2011 is what the National Audit Office says. That would have been written before the pause that we are currently going through. So, I haven't got exactly in my head which part of 2011 it is or whether it is still 2011 if we give it the go ahead.
Chair: Ian wanted a quick question, then I am going to Jo and then Stephen.

Q31 Ian Swales: Yes, just on Mr Wharton's point about lengthening trains and so on, when one travels abroad, one is struck by two things. One, that the level of fares in our country seems breathtaking. I would not be surprised to be told that we are the most expensive country in the world to travel by train. But the other thing—and the point of my question—is the design of trains. I travelled recently from Antwerp to Brussels on a double-decker train. Are we actually looking creatively at how to solve this problem and why don't we, as the French and others do, have the double-decker trains?
Robert Devereux: On the comparison of fares, I am afraid I have to just point you to choices that different countries make as to the subsidy. The British taxpayer, over the next five years, is putting £15.3 billion into the railway system in order to subsidise people using it. I could make the fares lower still by making that a bigger number. I do not currently have a guarantee of getting more than £15 billion. Chances are I am going to have to work with less than that. So, it is a choice, I'm afraid, about how Governments work. That is the difference. On the double-decker stuff, two things are probably worth saying. One is that double-decker is—what journey were you making? Antwerp to . . .?
Ian Swales: Brussels.
Robert Devereux: Yes. On a long journey you can actually get something useful out of double-decker. What you typically don't get with the double-decker is fast entrance and exits. So, the calculation we have to make is: can I actually make sure that these trains physically go through the various tunnels and over the various bridges of which we have hundreds and hundreds; and, secondly, are they the right sort of train, given that quite often in the British system I need people to be on and off really promptly and, in a sense, I don't want to be having people queuing at the top of stairs.
Chair: Jo.

Q32 Joseph Johnson: Thanks. Well, to use Austin Mitchell's description, I am a daft Londoner and represent a London constituency of Orpington. Just taking the conversation in the round: usage is set to double; capacity is not going to keep up; therefore, overcrowding is going to get worse. But I wondered if you could tell us where in the country overcrowding is going to get particularly bad over coming years. I ask that because the Southeastern franchise, which I use a lot, is virtually—well, it feels like it is reaching intolerable levels of overcrowding at some points. This is particularly unfair in some ways because the Southeastern franchise has been having RPI +3 fare increases and will do until the end of next year. My constituents, for example, have not benefitted one jot from the extra investment that was the justification for that RPI +3 terms of their franchise, in the sense that it was there to pay for fast trains, and these fast trains go from London Bridge and they skip Orpington altogether and they wind up somewhere in Tonbridge or Sevenoaks or wherever, way down the line. So, my poor constituents are getting the worst of all worlds because they are left taking the very slow trains that do all the stops and which end up being incredibly overcrowded because there are tons of people who are not going to these hub towns, so I wondered if you could possibly give an indication of whether it is going to get even worse for people like them?
Robert Devereux: Okay. Well, the plan that we are embarked on, subject to the spending review securing budget that we are working to, is targeting an aggregate average level of crowding about the same it was when the plan started. We have illustrated that in the White Paper that the Chair talked about by reference to individual London destinations but produced a common sense of what level of average crowding we were after. So, I am not currently trying to differentiate and pick winners in where crowding might be. Subject to the spending review, I am trying to make sure that we tackle crowding evenly, as it were. In practice, because the interventions will be different and your particular constituency service is going to be slightly different from something else, there will be changes because at the level at which I am making strategic choices about a £15 billion level of investment, I am

necessarily having to deal with some relatively broad aggregates. But it is the case, as you have said, that we have put very substantial extra capacity into the South East region—not, sadly, fast trains going through Dartford. But, trying somehow or other to make sure that some of that benefit is actually being financed by the users of the service and not by the taxpayer in Manchester and Birmingham seems to me a plausible reason for justifying RPI +3. We are taking blocks of the country; we are not taking individuals. Come the day that I can actually do quite sophisticated things with ticketing and routes—actually, a number of permutations start to open up that I simply cannot do today. Bits of paper as tickets are really quite useless when it comes to dynamic management of the system. I really seriously would want to aspire to a world in which I know what is going on—it comes back to accounts—and I actually have got the technology and the requirements on the companies to think really laterally about how they segment their markets. Right at the moment, you buy a season ticket and it makes very little difference to you whether you go on Friday, take a fast train, take a slow train—you have bought it; it's a year; it's gone. It's an annualised cost and it's just like paying your tax on a car. It makes a really big difference, as you can begin to see in London, when people say, "Okay, so if I make one fewer marginal journeys, I have £1 more than I would otherwise have had." That simply is not in the British railway system at the moment and it is absolutely the next critical thing to achieve.

Q33 Stephen Barclay: Just on that, actually, you just talked about the flaws in data in terms of identifying future capacity. Is it a specification for all the new rolling stock that they will have automatic counting, such as the infra-red sensors?
Robert Devereux: Virtually every new train—newly built train—comes with that because everybody can see that that's the case. Within the—
Stephen Barclay: So it is not a specification?
Robert Devereux: I'm sorry?
Stephen Barclay: It is not a specification from yourselves.
Robert Devereux: I'm not sure whether I specify that if it is a new train, it should have automatic passenger count. Could I let you know?
Stephen Barclay: The Report makes it clear that—
Robert Devereux: The reality is that it has automatic passenger counts because that's how new trains—

Q34 Stephen Barclay: Should it not be a specification? What the Report says is there are problems with relying on ticket prices. It tends to overestimate journeys from cities as opposed to rural stations such as my constituency, and the thing you really want to count is who gets on and off the train. It strikes me that you are in the process of buying a whole lot of new trains. Would you not require as a specification for those new trains they have this facility?
Robert Devereux: I understand. I am going to make a simple point that I am not sure that the market for new trains will ever deliver one without one. I will go back and check—
Chair: And let us know.
Robert Devereux: —whether that's the case.

Q35 Matthew Hancock: Also, did you say virtually every train?
Robert Devereux: Well, that is just because I do not want to say that I absolutely know that every new train is like it, but can I come back to you? I think it is the case that new trains that form part of the 900 that we have plans for will all come with automatic passenger count. That is the only way in which we have got it up to 39%. Be clear—and I don't want to mislead you—within that 950 trains for which we have plans, some of them are reusing stock that is already, as it were, spare, so they are not of themselves new trains.

Q36 Stephen Barclay: And you are not going to retrofit them because of cost?
Robert Devereux: Well, the cost of retrofitting some of that is quite high.

Q37 Chair: High relative to—you are talking about a £9.2 billion programme. It seemed to me reading it, I thought, "For goodness' sake; get the proper data so that you can make proper decisions." What is high?
Robert Devereux: Yes, that is exactly what I thought when I read that sentence too. It is conceivable that actually if—I tried to ask roughly what sort of price are we talking about here, and by the time you multiply that across all the carriages we have not got, I think you could easily be talking about many tens of millions of pounds worth of cost.
Chair: That's still relative to £9.2 billion. It may be an appropriate investment.
Robert Devereux: It may, but if, for example, with 40% of the carriages, which by the way is increasing as I buy new ones, I get a very substantial coverage of passengers, I might not get huge value out of that marginal 60%. I think it is an entirely fair question and actually it is one that we need to think about, but right now, moving from having 3% of the data to somewhere well north of 40% will fundamentally transform my knowledge. The question you should ask me then is, if I were to retrofit all the rest, would I be getting further and better particulars? I might do; I am very happy to take it away and think about it.

Q38 Stephen Barclay: Well, a related issue as well is the Report highlights problems with your modelling and on page 17 says you "do not test the sensitivity of your forecast to variations in the relationship between economic growth and rail demand."
Robert Devereux: Yes.
Stephen Barclay: Why don't you do that?
Robert Devereux: Well, if I'm honest, I thought paragraphs 1.15 and 1.16 were accurate, but I am not sure if you are actually running a model that is trying to get you to some strategic conclusions—they leave

you with the impression that somehow we have not done the right thing. On the question of the relationship between passengers and GDP, as a matter of arithmetic, that is exactly the same as making bigger assumptions about GDP.

Stephen Barclay: It is more than that though, surely, because I remember Iain Coucher saying to me that the average time that a commuter was prepared to spend on the rail element of their commute 10 years ago was around 45 minutes and it is now an hour and a quarter; I don't know if that is correct—that's what he said to me. That is very relevant to my constituency because we are less than 100 miles from London, so it brings us into play. Yet, the new Thameslink trains are stopping at Cambridge, so we have a bizarre situation that those new trains stop there and yet those new trains have the selective door opening that actually allows them to stop at the rural stations that have short platforms, which many of the existing trains cannot. But your modelling is not picking up the increasing demand in the county with the highest growing population, where there is increasing demand in Cambridgeshire to use stations such as Littleport, because your modelling is overestimating the city transport, and at the same time you are saying, "Ah, but we just look at it from a GDP point of view. You are not looking at it in the round."

Robert Devereux: No, sorry. I am making two separate points. If I take a sensitivity analysis that says, "Here's my base case. What happens if GDP is lower or higher?" I am effectively doing something to demand and I can see how that drops through the bottom. Broadly speaking, if I change the relationship between a given GDP that I started with and passenger numbers, I am also dropping it through to demand. So, both of those variables are effectively being tested if I test a wide range of GDP. That is all I am saying. The second thing I just want to say is that if I told you that the model we have, which, as the NAO at least gives me, is based on established building blocks as well as new, innovative work, has to run all through the night to give me one answer because the rail system is so complex and the level of sophistication in it requires that much computation, you might understand why it is that I have to be moderately cautious about how many variants I can test. Even now, the computational requirement to allocate as many people as possible to the right routes and get some answers is quite difficult to do. So, I am absolutely up for being encouraged to do better every year and that is what we are doing, but the sorts of things that are being talked about here are, in my judgment, the sorts of simplifications that go with a model that none the less can actually generate some answers with which you can then affect policy.

Q39 Nick Smith: On demand modelling, I wonder if I could just jump in? In my constituency, Blaenau Gwent in South Wales, we have just got a new train line—absolutely fantastic—from Ebbw Vale down to Cardiff and within six months we were breaking all the records for participation on the railways; it's an absolutely tremendous success. Unfortunately, when the line was built, only one track was laid and now, of course, we have realised we need two tracks because that would make a big difference in terms of being able to get down to Cardiff from the valleys. Unfortunately, it is way too late. If the track had been put in at the same time as the first track it would have been much cheaper. So, now there are greater costs and people are very frustrated because the shine has been taken off a great success because of the very poor modelling of demand. What are you doing about demand at that sort of level?

Robert Devereux: These are comments by the National Audit Office about the planning for quite a big White Paper—how would I spend £15 billion/£9 billion sensibly. That necessarily is not the same as—

Nick Smith: I know it is a different sort of model, but—

Robert Devereux: —should Arriva Trains Wales and the Welsh Assembly think in great detail as to whether it is one track or two tracks in your part of the world. And so, we are talking about two somewhat different things. I would aspire to a world in which my model was so sophisticated it knew whether there should be one track or two tracks in your world. All I can tell you is that these models are already fantastically difficult to manage and get to the right answers. As computing power improves, which is the reality with everything to do with modelling, we will be able to do better and better. This is a snapshot of where I am today.

Q40 Chair: Right, that is very helpful. We are likely to be asked for a vote, but I wanted to move you on to something. If you look at the structure in which you are planning for infrastructure, you have got you, the Department—hopefully we will Mr Emery in as well—you have the regulator, you have Network Rail and you have the operating companies. Two things occur to me out of that structure that perhaps Mr Emery would also like to comment on. One is the position of Network Rail because you use Network Rail to help develop your plans and then they become the sole bidder and provider, and the other is that all of them—except perhaps the Department for Transport, but perhaps you get sucked in—all of you, are into growth. It is in everybody's interest to have growth. So, at a time of public expenditure constraints when growth will be constrained, where is the thinking going on outside the box which will make people's journeys easier, meet perhaps some of the environmental objectives that we and you have as a Department, but not require always an increase in infrastructure? Now, at that point, having asked you that difficult question, we have a Division bell, so I am going to have to go. So, you have a good chance to give us a sensible answer when we come back and I think we want to develop those structural issues a little bit more.

Sitting suspended for a Division in the House.
On resuming.

Chair: Now, it was a rather complicated question I put to you both, and just to re-state it, it was about the infrastructure of the four bodies that take the decisions. It seemed to me that one of the issues is can you really get value for money because of the role particularly of Network Rail in providing you costings as well as then bidding. The second issue is that the emphasis will always be on growth and, therefore, is there a proper discussion and deliberation on other options or is growth always seen as the only answer to some of the challenges that you face in getting people around the country as quickly and comfortably as they can. Who wants to start?

Robert Devereux: Can I do the second one first?

Chair: Okay.

Robert Devereux: Let's just first think about what we are trying to achieve here. We have, without a shadow of doubt, long-term trends that show that people want to travel more in the UK and that has been the case for a long, long time. I assume you do not mean that the question is how can I get people off trains and put them back into cars.

Q41 Chair: Not necessarily. They might walk; they might go by bike. That is the thinking outside of the box. That's the old "it's either trains or cars". Are we thinking radically out of the box enough or are we just always thinking: increase train capacity?

Robert Devereux: I am not always thinking about how to increase train capacity because I'm not going to have a budget to do it. So can I take it back to the conversation that we were having earlier about what you would get if you had rather more dynamic pricing on this network; we will have the technology to that. Right at the moment, if an individual has the theoretical choice from their employer to do a day's work from home, there is no cash consequence in terms of their travel costs if they are on an annual season ticket. If you were in a world in which the choice of when you travelled and the choice of whether you travelled fell straight through into the idea of "there is some financial incentive in this", I think that would make a difference. At the moment, the main cost of the train system in London is having so many trains doing one or two journeys in the morning and being parked up for most of the day. So, the more I can do to spread demand, the better it is. The way I will spread demand almost certainly has something to do with thinking about the effect of pricing. That might in itself have a bearing on people's choices about whether to travel in the first place. Whether it would tip them into cycling or walking, I am not sure. That is where the problem is because these people are typically coming in 10, 15 or 20 miles on some of these journeys. Fundamentally, that is the different way of thinking about it because at the moment we have pretty static prices and consequently, what you might say is a very heavily utilised network at one part of the day and not at any other time. It is the same on lots of other networks; it is the same on telecoms networks. In all other networks, people think laterally about how do you match supply and demand, typically through the use of price. I can't help feeling that, as Oyster is beginning to demonstrate in London, you have some possibilities down that track. As for the Network Rail one, maybe that's one Bill would answer.

Bill Emery: Certainly, from a regulatory point of view, having one big infrastructure manager presents a little bit of a problem and one of the ways we tackle that is to say, "Well, we are not going to consider Britain as just so special that you cannot compare it," and just have an argument with consultants against consultants, and we push for use of international benchmarking, and that is, in some respects, a bit of a first for regulation in the effective use of international benchmarking and using that to test whether—

Q42 Chair: I am going to just stop you there because we are going to come to costings later, and we have a load of questions about costings and international benchmarking. At this stage can we just stick to the decision-making structure, because we think it leaves a little bit to be desired?

Bill Emery: I think the 2005 Act that brought in a process by which the Governments both here and in Edinburgh made a decision to inform the five-year settlement as to what it required from the railways and, more particularly, what public funding it was going to make available was a truly significant step forward. The 2008 review required Network Rail, the Department and ourselves to start to try and form the 2007 HLOS and SoFA decisions and try to get the best data that we could. The train operators were a little bit late in coming to the party in that, but they are truly addressing it for the next round of decisions. So there is quite a good process of properly informing the choices that are essentially for Government about what they want from the railway and how much money they are likely to be prepared to put in it. At the end of day, there is a process that says what is the limiting factor—

Chair: You do not really deal with the issue, because all the parties sitting round the table want more. That is what they all want—more.

Robert Devereux: Well, let me just build on what Bill said. Let me outline the difference that the 2005 Act produced, and the way in which the High Level Output Specification is, indeed, just that, because it says "I have got more capacity that I can see coming along; I want this level of crowding; I am not telling you how to do this." So, there is an opportunity in the system to consider the price consequence—in other words, could you think laterally about doing something else, something better. So, I know for a fact—and I cannot remember exactly which one it was—in one of our interventions, we simply managed to achieve more capacity by a rather more sophisticated use of existing assets. In other words, I am sweating the assets more. I have not actually put any more carriages on, but none the less, because I have re-timetabled and done something clever, we have managed to get something out of it. Now, that sort of thing comes out of the conversations between the Department that is paying for this and the bidders who are actually responding to what is specified as output. If I had specified that I wanted 1,300 carriages, I would indeed be locked into the notion of "Well, I have to pay for it." If I specify I need this output, if we can find elegant ways of doing it, which is in a sense what the Department is trying to do in deciding whether to invest, that relieves some pressure. Now, the more that people understand and produce examples that do not require very heavy capital expenditure or—

Q43 Chair: And where does that thinking come from?
Robert Devereux: Well, at the moment, that thinking is coming from a combination of train companies themselves and the Department in challenging them before they sign things off. So, I would not characterise everybody as slavishly thinking the answer to this question is a new carriage, because I do not think that is the nature of the beast. But right now, it is the case that we can, through quite a bit of infrastructure work, get more carriages on the network. The next phase is, as I have described earlier, not going to be like that.
Chair: Stephen and then Nick.

Q44 Stephen Barclay: Yes. It just strikes me that it is very difficult to make an assessment on value for money, given the complexity of the structure in place and the lack of transparency around Network Rail. So, the Report says we have rising cost of new trains, lack of international benchmarks, higher financing cost, complex contract structure and a flawed model and data strategy. So, in terms of the transparency available to you about Network Rail, are you satisfied you have all the information that you need?
Bill Emery: As a regulator, I am never satisfied with having all the information and that is why we are pushing quite hard, and I am taking on board the kind of recommendations—

Q45 Stephen Barclay: Well, what major areas of data do you not have?
Bill Emery: Well, with Network Rail, it relates to ever-improving international benchmarking data to compare and contrast. Only last week we published our most recent report on how Network Rail compared to its European peers.

Q46 Stephen Barclay: But you have been in post for a number of years, have you not?
Bill Emery: We have in been—
Chair: You have been in existence—
Bill Emery: We have been in existence since the beginning, in a sense and—
Chair: And previous to that there was something else.

Q47 Stephen Barclay: Could I go through just a few of the numbers then, because I was having trouble just working them out. On the £9 billion improvement programme, two thirds of that is borrowed money by Network Rail, is it?
Bill Emery: A lot of it is Network Rail's, yes.
Stephen Barclay: £6.1 billion; that's what is borrowed, is it?
Bill Emery: I think that's it.

Q48 Stephen Barclay: The refinancing costs are, is it £800 million?
Bill Emery: Yes, that cost of refinancing—well, the annual cost of financing that level of debt will be be continual—is what it will be, yes. That is how it works on the cost of capital.
Stephen Barclay: Sure. I agree, the £800 million is just for the first five years, so presumably there will be ongoing costs.
Bill Emery: It is ongoing because in fact the capital costs of the enhancements are added to Network Rail's regulatory assets base and that is remunerated at the cost of capital based on all the best information we have, and that follows on throughout, so we are buying those types on enhancements on the basis that these are investments for the long term that will be funded through access charges and network grants on a long term.
Stephen Barclay: Sure, so that will pass to their asset base—yes, we get that.
Bill Emery: Yes, and that is what happens.

Q49 Stephen Barclay: So what are the non-incremental infrastructure improvements? What is the refinancing around those? If we were not doing these improvements on which we are paying £800 million of the financing cost, what would be the financing required just to maintain the *status quo?*
Bill Emery: If it is just a question of the renewal of the existing assets, then that is covered through the normal maintenance charges and revenue through the actual, so it is a kind of pay-as-you-go. If it is an enhancement, then it is in the capital exactly the same way. There are only two ways you can get the money.

Q50 Stephen Barclay: Okay, let's look at it differently. What I am trying to drive at is what is Network Rail's current debt and what is the refinancing cost on that at the moment?
Bill Emery: Its current debt is at the £30 billion level. I have not got the exact number in front of me[1].
Stephen Barclay: What? Give or take a couple of billion or . . .?
***Bill* Emery**: It is running at around about 5% or 6% of return—5% return on the regulatory asset base.

Q51 Stephen Barclay: Right, so what is the refinancing cost? What I am driving at is that, earlier, in the response to Matt Hancock's question, the answer was, "Well, if you give more money to Network Rail, we can bring the ticket price down." What I am just trying to establish is how much of the money we are giving is currently going in financing costs, and then perhaps we can go on to some of the press reports on management costs and consultancy costs and other things. How much of it is going in

[1] *Note by witness:* Network Rail's regulatory net debt in 2009–10 was £22,819 million (nominal prices)
(Figure taken from ORR's September 2010 publication "Annual efficiency and financial assessment of Network Rail 2009–10", page 42).

refinancing costs? You are, with respect, the regulator; I assume you know what the refinancing costs are.
Bill Emery: I have not the precise figures in front of me—I can provide those for you quite happily—as to what the refinancing costs or the return that we incorporated[2].

Q52 Stephen Barclay: Because what just struck me as slightly odd was there is this document, Information Memorandum 2010, which talks about a £35 billion multi-currency note programme, and there is a further £4 billion of other notes on a different programme, and yet at page 26 it says the issuer, Network Rail, is permitted to incur debts outside the programme, included but not limited to bank debt. It talks about the various banks who are involved in this—Merrill Lynch, Deutsche Bank, Morgan Stanley, Barclays Capital, Goldman Sachs, Citi, HSBC, UBS, Royal Bank of Scotland—and none of those come cheap. So, how does this Committee get sight of how much money the taxpayer is giving each year to Network Rail and transparency in terms of how much of that is going on refinancing costs, how much is going to Mr Coucher, who was paid significant sums, to any consultancies, to your costs—your Chairman is on £120,000 a week, I think, for a three-day week—whatever the Chairman of Network Rail gets, a figure of around a quarter of a million for a two-day week has been quoted. And the elephant in the room has to be that the more complex a structure is, on the whole, the more expensive it is likely to be. The Report does cite that this is a unique structure and, at the heart of it, accountability, we are being told, is by individual members of Network Rail; well, we are not sure that is that effective. So, really the accountability is being driven by yourself. And so, as the Committee that is looking at this in terms of value for money, could I come back to the first question? This year, what will Network Rail pay in refinancing costs?
Bill Emery: I do not have a figure in front of me, but Robert might have.
Robert Devereux: The figure that was published in the White Paper showed for each of the five years not only what the taxpayer was putting in, but how much the passenger service would cost to run, what the baseline costs of the actions of Network Rail are in doing maintenance, operations, and so on, and there was a third line that said, "Network Rail financing payments"—so that's the cost annually of the debt, call it £30 billion. Over the space of the five years, the projection was £8.4 billion. So, that £8.4 billion is the cost of carrying the historic debt before you start the control period and then when you borrow a further £6 billion, which is what we were planning, there is an additional financing charge, which is the £800 million that you mentioned earlier on. So, those are the numbers in respect of the financing.

Q53 Stephen Barclay: One can dwell on that, but to move on, that is covering all debt currently owed by Network Rail, is it?
Robert Devereux: I believe so.
Bill Emery: Yes.

Q54 Matthew Hancock: So, do you have the interest rate—the average interest rates?
Bill Emery: No, because I do not have with me the stock at the end of each period to be able to do this sum, so I'm afraid—[3]

Q55 Matthew Hancock: Right. And you do not know how much Network Rail is carrying—how much debt Network Rail is carrying.
Bill Emery: We do know how much Network Rail's carrying—
Matthew Hancock: How much is it?
Bill Emery: We published that in a Report, but I do not have the figures with me at the moment. Our approach to Network Rail is to set an overall revenue requirement and leave the means by which it finances itself primarily in own hands, setting a limit on the expectation of the growth in the RAB, which is a long-term liability that is going to be placed upon the taxpayer, and hold it to deliver on all the obligations that have been set out by both Government and myself as part and parcel of the settlement.
Matthew Hancock: I just want to press on this because something in your earlier evidence surprised me and I wrote it down. You were talking about how there is £15.3 billion subsidy over five years, and you then said—you were talking about rail fares—you said it is a choice about how much subsidy as a country we put in, and that is a political decision; I understand that. But it is not just about how much subsidy goes in, it is also about how much value for money there is in the system. I was astonished that as the person managing all this you did not recognise

2 *Note by witness:* The total financing cost of Network Rail's regulatory debt in 2009–10 was £1,252 million (in 2009–10 prices).
(Figure taken from ORR's September 2010 publication "Annual efficiency and finance assessment of Network Rail 2009–10", page 49.)

3 *Note by witness:* Summary of average interest rates on Network Rail's debt:

	Actual 2009–10 (A)	*PR08 determination (B)*	*2009–10 budget (C)*
Average interest rate on nominal debt—FIM covered	5.4%	5.0%	5.0%
Average interest rate on nominal debt—unsupported	n/a	%	n/a
Average interest rate on index linked debt—FIM covered	1.4%	1.5%	1.4%
Accretion on index linked debt—FIM covered[3]	4.4%	2.3%	−1.5%
Total average interest rate on index linked debt—FIM covered[3]	5.8%	3.8%	−0.1%
FIM Fee rate[3]	0.8%	0.8%	0.8%

(Figures taken from ORR's September 2010 publication "Annual efficiency and finance assessment of Network Rail 2009–10", page 50.)

that improving the service is not only achieved by putting the subsidy in, but by getting better value for money. And now, Mr Barclay asked a basic financial question about Network Rail and the regulator, who is the only person to whom Network Rail is accountable, as far as we can work out from the structure of that very obscure—well, it is not a company; I don't even know what to call it—does not even know the financing numbers.
Bill Emery: We do know the financing and we get comprehensive information.
Matthew Hancock: Well, what is it?
Bill Emery: I can quite happily provide you with the details behind all that as to where we are, and our Report on the financial performance of Network Rail in the last year is available, and it was published last week. It sets out exactly what those particular numbers are and our focus is on testing whether they are consistent with our projections, which were set out in the public domain. It is all covered in our determination.

Q56 Matthew Hancock: You said your approach is to set out the obligations you want for Network Rail, and then let it get on with financing it. Well, who is delivering value for money and driving value for money through Network Rail?
Bill Emery: We drive value for money through Network Rail when looking at what it needs to do to operate, maintain, renew and enhance the network. We look at its current performance and the costs, establish what we think an efficient company could do and then set it a trajectory based on that, and hold it to deliver on all its obligations. So, it has to deliver on punctuality, it has to deliver on the programmes, it has to maintain the network, it has to operate in the normal way. We hold the company to deliver on all the outputs that we set out in our determination, and Network Rail then further refines that in its delivery plan. We hold to that. We have large amounts of information on the financial flows from Network Rail to test whether or not it is improving its efficiency.

Q57 Chair: I want to interrupt this because you have been around, or your predecessor body has been around since 1994; you have been around since 2006. Your job has been to secure greater value for money, yet you say in the Report, on page 20, paragraph 2.2, there is still "a very large potential for Network Rail to improve its efficiency". So, what we are left wondering is what on earth have you, and your predecessor organisation, been up to since 1994. When you come to particular efficiencies that are mentioned in the report, they all seem based on finger-in-the-air data.
Bill Emery: Clearly, progress was made in the early years in Railtrack before the actual costs exploded—when it went into administration—and there had been a progressive drive from the Office of Rail Regulation to set challenging targets on Network Rail.

Q58 Chair: If this is a progressive drive, how can you say there is a very large potential for Network Rail?
Bill Emery: Because there is.
Chair: So where has the drive been successful?
Bill Emery: Well, Network Rail was set a target to improve its efficiency by 30% in the last control period. We have set them a target to improve its efficiency by 21%. That represents two-thirds of the gap towards the European peers. Given all the other challenges facing Network Rail, we felt that was a balanced judgment as to pace of change required by Network Rail to address that target. We have identified here—

Q59 Chair: But, hang on, what have you achieved—or your predecessor—from 1994. What have you achieved from 2006? You have been around—
Stephen Barclay: You started in September 2005, I thought.
Bill Emery: I started in September 2005.
Mr Bacon: This is what puzzles me. You have been there for five years and the report says not only did you not—and you talked about benchmarking as if you were doing it; I know it has probably started now—but the Report says, "The regulator did not specifically seek international benchmarks for new infrastructure schemes to enhance capacity. It reduced costings by removing schemes." And there is a chart—
Bill Emery: There is a chart, yes.

Q60 Mr Bacon: —on page 20, I think, summarising the schemes that you removed. And, again, the Report says further down, paragraph 16, that the NAO was concerned about your ability to assess whether Network Rail is providing value for money because of the limits imposed by the level of detail available on Network Rail rail's costings. You have had five years—since September 2005 to the month—five years in which to get a grip on Network Rail's costings, and five years after you took up this office, as Chief Executive of the Office of Rail Regulation, the NAO is saying you do not have a grip on Network Rail's costs isn't it? Why not?
Bill Emery: The level of costs—Network Rail's costs and its relative efficiency is something that we have been teasing out over the whole of this five-year period. We started to commission detailed international benchmarking to support the decisions for our 2008 Periodic Review. Network Rail were being driven by the previous regulator's settlement to improve its efficiency by 31%. It actually achieved 27% in this period. We have set it some targets. We actually did substantial amounts of benchmarking support—the 2008 determination. The point in the NAO Report, which we accept, is that for the purposes of the enhancement programme there was a limited scope for us to do that because of the nature of the information and the projects. There was international benchmarking available on things like platform lengthening, which we did utilise. We follow an approach that is consistent across many regulatory sectors. We look at the comparative benchmarking on operation, maintenance and renewals, which identified the gap of between 30%

and 40% or a little bit more between Network Rail and the leading companies in Europe, and ask why that is different in terms of enhancements.

Q61 Chair: There is an example—I can't find it—in terms of enhancements where the Report cites that Network Rail did not think about modular platforms. As I read that, I thought, "What on earth was everybody up to? Why was it that Network Rail hadn't a clue about this, after all these years of driving efficiency." I can't remember, and I am probably misquoting, but I believe it saved 25%. Huge savings. Massive.
Stephen Barclay: It's on page 25, paragraph 2.11, the reference to "the actual costs from the Netherlands, the regulator concluded that savings of 25% could be achieved on platform extension by using modular rather than conventional construction methods."
Chair: Now, something is systemically wrong where we have an organisation, Network Rail, which has dubious accountability, but yet absorbs a heck of a lot of public money, where the drive for efficiency had been a priority since 1994—you have been in post for five years—when the previous regulator was in post. Yet, here we are coming along with a £9.2 billion investment programme—a heck of a lot—and bang: a 25% saving was missed because they had not thought about modular platforms. It just seems nutty to us. That is what you have to try and understand.
Bill Emery: There is clear scope within Network Rail to learn from what is going on elsewhere.

Q62 Chair: But why has that not been driven before? I think that is what we are asking you—where is the accountability for all this? It just does not feel right to us.
Bill Emery: Certainly, Network Rail is accountable to us to deliver on the package that we have set it and comply with its licence obligations.
Chair: But when you talked about accountability—I am sorry to keep interrupting but otherwise we get off the point—it was quite interesting that you talked about them delivering the service, not delivering value for money. You did not talk about economic efficiency; you talked about effectiveness. You talked about service effectiveness.
Bill Emery: Well, there is a whole series of judgments that are taken as part and parcel of the review on looking at what are the outputs required and what is a reasonable cost to pay for that. That is part and parcel of the decision in the High Level Output Specification and SoFA. That decision, essentially taken by the primary funders, governs what would represent value for money in terms of improved performance, improved capacity. Our drive is to push Network Rail to test out whether or not the costs of the infrastructure interventions necessary to support that represent a reasonable level of cost. That is what we do and that is what we have done pretty effectively to drive and force them to find better solutions and not just jump to the old way of doing things.

Q63 Chair: I think our question is that a) the structures of accountability for Network Rail are insufficient; and b) you are the organisation that has the job of ensuring efficiency, and it just seems to us that it has been a task; we do not really have evidence of its impact and effectiveness.
Bill Emery: Well, we would say that we are driving Network Rail, and have driven it, and, given where it was, we have set it a really challenging settlement to deliver all the expectations and outputs driven by the Government and to improve its efficiency, and do that at a pace that will be a continual challenge throughout this period. One year on, as we reported last week, Network Rail has improved its efficiency by 3.6%. There is still 18% to go to stay within our settlement over the remaining four years. We are pushing them and we will incentivise them to try and actually beat that as part and parcel of the way that we have set up the framework for Network Rail for this control period.

Q64 Mr Bacon: Would it help you in your relations with Network Rail and in your ability to scrutinise and regulate them if the National Audit Office were their auditor?
Bill Emery: I am not certain that would be necessary at all because in fact we are picking over a large amount of information. Network Rail and I do employ reporters to scrutinise the data and, in a sense, the start is to say that this is still a private company. What the Government is buying is a whole set of improved services—increased capacity, the likes of Thameslink—and we are holding it to deliver on that.

Q65 Mr Bacon: Sorry to interrupt, but you just said it is a private company. I know it is a company and it is a not-for-dividend company.
Bill Emery: Yes.
Mr Bacon: Can you just remind us who owns Network Rail?
Bill Emery: Who owns Network Rail are its members.
Mr Bacon: And its members are?
Bill Emery: Its members are 120 people, or 100 people.
Mr Bacon: 100 people own Network Rail?
Bill Emery: Formally, because it is a not-for-profit company.
Mr Bacon: It is a not-for-dividend company, isn't it?
Bill Emery: Not for dividend.
Mr Bacon: It's not a not-for-profit company; it's a not-for-dividend company. I just want to be clear about this because you have just described it as a private company—who are these members, these 100 or 120 people?
Bill Emery: Some are private individuals. Some are representatives of the company's partners and train operators. So they are drawn from that. Some are from the industry—
Mr Bacon: Who they are negotiating with.
Chair: Who they then coin. That's outrageous.

Q66 Joseph Johnson: Do they have any equity, risk capital, that stake in Network Rail?
Bill Emery: No.

Q67 Joseph Johnson: Can they trade their interest in Network Rail?
Bill Emery: No.

Q68 Mr Bacon: So it is not a normal private company in any sense, is it?
Bill Emery: It is not. It is an unusual company.

Q69 Mr Bacon: Did you say an illusory company?
Bill Emery: No, an unusual company and it's—

Q70 Mr Bacon: It's a legal fiction, isn't it, Mr Emery?
Bill Emery: This is the company that the Government sold Railtrack in administration to, and the one that we regulate.
Chair: Yes, but we are on from that and I think our concerns here are both accountability and efficiency. I am going to bring in Nick, then I am going back to Stephen.
Nick Smith: Chair, I am not sure we should move on from this issue.
Chair: No, let's keep this issue going for a—
Nick Smith: It is certainly my view that the National Audit Office should take responsibility and crawl all over the accounts and that should be part of our recommendations from our discussions today. I don't want to get in the way of further discussions.
Chair: Okay, Stephen.

Q71 Stephen Barclay: I am just a little surprised, in that I can understand that you have to operate within the structure as it is set up, which is why I am saying, "Are there areas of information that you are not receiving", and we can look at why it was set up in that way, but, as the Chair said, I would rather look forward. As part of that, firstly, what appetite is there to revise the structure? Because to me the complexity of the structure and the complexity of the contract negotiation goes to the heart of the issue. As you have just alluded there, you have people from the train operating companies as members of Network Rail, Network Rail is providing the infrastructure improvements that this Report focuses on, and yet any improvements before it can start work, it has to go and negotiate with 15 or so rail companies on the rolling stock. So, there's clearly conflicts of interest in the structure as it is and what I am trying to understand is the impression you are giving the Committee that no, actually, you have, broadly speaking, the data you need.
Bill Emery: I think certainly from the regulatory point of view, and our focus on the infrastructure manager, there is a high degree of knowledge and exposure of what the data is, and we get lots of information. And we are reporting regularly, quarter by quarter, on Network Rail's performance against the settlement, and annually against its financial performance as well. I think you are right that this whole industry is quite complex, and there are issues around value for money, which is why we were very happy to be joint sponsors with the DfT of the Rail Value For Money Study that is currently being undertaken, and that is actually going to look at all the areas on this, and I think that one of the things that we have told it, and that the colleagues in DfT were very happy with, is that there should be no no-go areas in this, and that includes Network Rail structure—if there is a better structure for Network Rail. But mainly, I think it is getting Network Rail to work closely with its partners to find better solutions to what the travelling public want.

Q72 Stephen Barclay: It is perhaps more for the Department to consider what appetite there is to look at the structure, but can you just tell us how many consultations your body has commissioned in the last three years?
Bill Emery: I can't give you—[4]

Q73 Stephen Barclay: Can you give us a ballpark?
Bill Emery: It must be in the 20s, 30s, 40s, but I can't give you a precise number.

Q74 Stephen Barclay: I was trying to work it out—it looked like you had 21 last year and 35 in 2008, but I do not know if that is them all. It just struck me, looking at your website, there is this whole long list of consultations, policy frameworks, investment frameworks.
Bill Emery: Yes.

Q75 Stephen Barclay: The whole thing is just so complex and there must be loads of people producing these reports, appraising these reports and having meetings on these reports, which is money that could be going to build longer platforms and other things. So, how much do you spend on consultants a year?
Bill Emery: Not a great deal. I haven't got any—
Stephen Barclay: Well, you must know—you are running the thing.
Bill Emery: We do know how much—we do know. Out of our budget of around £30 million, it is around £4 million to £5 million on consultants[5].

Q76 Stephen Barclay: Right. It is just, as Matt Hancock was referring to, a supermarket—one of the first things it will be doing is looking at the cost of its suppliers, trying to drag down its cost, cutting out fat at Head Office—and none of that seems to be happening here.
Bill Emery: We have, as a regulator, in the last five years, progressively reduced our revenues, and we have, as part and parcel, at the end of last year, reduced the size of the ORR quite substantially. We are cutting back, but we have—

Q77 Stephen Barclay: How many people work for the regulator?
Bill Emery: 309. It depends a little bit on full-time equivalents.

[4] ORR has issued 18 consultations this financial year. Of these, nine consultations were required as part of ORR's statutory functions. In 2009–10, 52 consultations were issued. Of these, 33 were statutory requirements. Statutory consultations include for example those on licence applications or licence exemptions to operate on the railways, in accordance with the functions given to ORR by Parliament.

[5] In the past three years, ORR's expenditure on consultants is as follows:
2009–10: £1,917,000
2008–09: £2,145,000
2007–08: £2,613,000

Q78 Chair: Looking at Network Rail, our infrastructure costs are among the highest in the world.
Bill Emery: They are.
Chair: Why?
Bill Emery: Because the whole—and that is precisely why—
Mr Bacon: Finish the answer before you go onto the next bit. Why are they so high?
Bill Emery: Why they are is part and parcel of Network Rail's approach to doing work, which has been driven through—

Q79 Mr Bacon: They have an expensive approach?
Bill Emery: They have expensive approaches to work.

Q80 Chair: What does that mean?
Matthew Hancock: Why haven't we changed them?
Bill Emery: It means that the way that they do possessions, the way they contract out—there are lessons they can learn—

Q81 Mr Bacon: The amount they spend on paying people off with confidentiality agreements in sexual harassment cases—that is another cost, isn't it? When you look at the management side of Network Rail there are enormous costs there in all directions and you, as the regulator, are the supervisor and the scrutineer of them. What have you done to draw the attention of the public and Parliament and taxpayers to these concerns that have been widely reported?
Bill Emery: We have—we are aware of what Rick Haythornthwaite and his non-executive director colleagues on the Board are doing on these particular things and how they, with their auditors, are looking at that. That is as far as we have gone on these matters. I go back to the point that, as a regulator, we are holding Network Rail to deliver on all its licence obligations—
Matthew Hancock: But, hold on, could I just, before—
Bill Emery: —and all the outputs.

Q82 Matthew Hancock: You have been down that route before. You just listed a series of reasons why Network Rail has high infrastructure costs and whilst you have been in place for five years, you are still saying that these have not been addressed and I would like you to comment on that.
Bill Emery: Although Network Rail has been making progress since its inception in 2002, along the efficiency trajectory that set for it in the last control, when we looked at this and compared it against its peers across the world, it was clear that there was still a substantial gap to do.

Q83 Matthew Hancock: So, do you regret not putting more pressure on earlier in your period in office as its regulator and only value-for-money driver?
Bill Emery: No, the settlement that was made for the last control period was a combination of outputs and revenue.

Q84 Matthew Hancock: In which year?
Bill Emery: In which it required Network Rail to improve its efficiency by 30%.
Matthew Hancock: In which year was that?
Bill Emery: That was in 2004.

Q85 Matthew Hancock: In 2004. And so we are now six years after 2004 and still you have listed a series of very broad reasons why Network Rail has very high infrastructure costs and is not a value-for-money organisation.
Bill Emery: We are saying that we have pushed Network Rail further and faster to address the issues on its costs and drawing attention to where the practices elsewhere—

Q86 Matthew Hancock: So, do you accept the NAO Report where it says that these levels of efficiency savings were not supported by bottom-up evidence of actual costs, their trends over time or their current levels relative to comparators.
Bill Emery: We accept that there are elements of the—
Matthew Hancock: Do you accept that statement in the Report?
Bill Emery: We accept that there are elements of the work that was done on the enhancement programme that were not—that the judgments that we took—the expert judgments we took, supported by consultants on what was an appropriate level of cost to incorporate within the settlement, sometimes are not fully backed up by all the data, and we are addressing that and going forward in any event.

Q87 Matthew Hancock: I would put it to you that having the NAO being able to scrutinise Network Rail might help you support evidence of savings with bottom-up evidence of actual costs and trends over time, etc. If you are so keen to improve value for money in Network Rail as you said that you are—although given the track record over the last five years, there is not much evidence of that so far—I am surprised that you are not supportive of the idea of more scrutiny of value for money within Network Rail. After all, you are the regulator and you are virtually the only person at the moment in the current structure who can scrutinise Network Rail for value for money. Its members can't.
Bill Emery: And that is what we are doing.

Q88 Matthew Hancock: Why don't you want any help with doing it? I don't understand why there has not been a—
Chair: I think we are going circular here. Let me bring Nick into the discussion.
Nick Smith: Thank you, Chair. Mr Emery, you and the Department are co-sponsoring a study of the cost structure of the railway sector—page 30 of our Report. How have you been able to challenge Network Rail up to now, when you have not had this information?
Bill Emery: We have, for Network Rail, spent a lot of time looking at other infrastructure managers. The Rail Value For Money Study is building on our look at Network Rail and, in fact, the McNulty

Study is saying that the work that we have done should be extended to all other aspects of the railway, be it the train operators and all the supply chain, to look holistically across the whole of the railway sector and look at the contractual side arrangements and all that. So, the Rail Value For Money Study starts off with looking at what we have done; it will scrutinise what we have done and, in fact, it is extending the levels of international benchmarking into the whole industry costs rather than just the infrastructure manager side. So, we have been doing it on the infrastructure manager side; the Rail Value For Money Study is going to look across it all and look at all the reasons why, within this complex arrangement we have, we are not delivering value for money, and why it is that railways elsewhere in Europe can offer and do a job substantially lower, and what are the steps necessary. That is why we are really keen that this study comes up with answers and a programme to go forward.

Q89 Nick Smith: Why did you not do this study five years ago?
Bill Emery: There was certainly work going in to look at the structure of the industry for the 2005 Act and some of the problems there. There was a settlement made for improving on Network Rail. Our role was on Network Rail, and that is what we did, and I think it is possible that could have been done five years ago, but that is hindsight. We are at this position now. Part of that has been informed by a really close look at international benchmarking to demonstrate the gap. That has exposed this kind of thing much more clearly than it ever has been before.

Q90 Joseph Johnson: I have some concerns about governance at Network Rail. In your answer to Matt Hancock's question as to why the NAO should not audit Network Rail, you said, "Well, we have reporters who do that sort of thing for us." I was not quite sure what you meant by that—do you mean journalists?
Bill Emery: Reporters are essentially engineering consultants and other people who look at the detail and give us a view on the robustness of the regulatory terms that Network Rail provides for us. So, it is a technical and a cost audit of Network Rail, to test whether or not it is actually—what it says to us in its returns to us are a proper reflection of these matters, and it can pursue those things and other aspects. We have a number of people looking at enhancement programmes, looking at the overall information flows and looking at the approach to asset management as well.

Q91 Joseph Johnson: Great. Turning to the governance questions, reporters who have been looking at Network Rail, including a June/July issue of *Private Eye* do point up to some rather unusual goings on there. Reading a column called "End of the Line", it reports that someone called Iain Michael Coucher, the former Chief Executive, was paid £1.2 million a year, which made him the highest paid public sector manager in the land. What did he do to deserve that much money? Was his performance so exceptional?
Bill Emery: The remuneration of Network Rail executives is a matter for Network Rail's remuneration committee.

Q92 Chair: But that is why the thing is not accountable. I know it might seem to you a small point, but I think what we are trying to get you to is you are the only body that holds this hugely important, odd organisation to account, which spends a lot of money and certainly is of massive importance to all our constituents in the service it provides.
Bill Emery: Absolutely.
Chair: And it is not your business and the advantage of having the NAO examine it is it would put all its expenditure and its efficiency, and its value for money in the public domain—right well and truly bang in the public domain, through us.
Bill Emery: I think there is a substantial amount of information on Network Rail's performance available on all the regulatory returns.
Chair: And it's rubbish. It is the worst.

Q93 Stephen Barclay: The basic salary reported in the director's remuneration for Iain Coucher is £613,000, which is obviously very different to the £1.2 million quoted in the *Eye*. Now, I would assume part of the gap is around the management improvement programme and what was paid for that. Is that £1.2 million figure correct and, if so, do you know how that breaks down—how much of it was incentive based, how much of it was core pay?
Bill Emery: I think if you look at Network Rail's annual report, it describes its whole approach to executive remuneration. It describes how it has benchmarked total remuneration packages of its executives against a whole series of companies.
Stephen Barclay: I have it here, and it is very opaque. We are asking for your help, as the regulator. Do you have clarity as has just been asked as to whether it was £1.2 million?
Bill Emery: I think the actual number is around that number. We would not normally pick that up. It would come out of the accounts. We are aware of Network Rail's management incentive plan, and we provided information to Network Rail.
Stephen Barclay: So it is for the individual members—these same members that are being negotiated with by Network Rail from the companies, or members of the public?

Q94 Ian Swales: Who is on the remuneration committee? That is the key point of what Mr Barclay is saying.
Bill Emery: The remuneration committee is led by a non-executive Director called Steve Russell, and it is made up of all the non-executive Directors of Network Rail.

Q95 Chair: Are they from the operating companies?
Bill Emery: No, no, no. These are non-executive Directors of the Board of Network Rail. The members are separate from that and it is the Board reports to—

Q96 Matthew Hancock: In a dividend paying private company, the shareholders have the opportunity to look at and scrutinise, and veto, both a wider plan in terms of driving value for money and specifically on director and management remuneration. And you have just said—and you are effectively the only people who can scrutinise this—that it is not to do with you how much people are paid at the top. Your first response to Mr Johnson was, "It's up to the remuneration committee", who are accountable to nobody.
Bill Emery: The company's AGM with its members—

Q97 Matthew Hancock: The company's AGM with its members? Those 100 people? These 100 people—but they have no interest in scrutinising.
Bill Emery: They have certainly got an interest, and I think the reports of their AGM show that it was a reasonably close thing as to whether they would approve the remuneration package and bonus decisions on that, because we had identified a whole series of questions when I wrote to the Chairman of the remuneration committee at the back-end of April on the reforms. I identified a whole series of things that had gone well and a whole series of things that had not gone well, and drew attention to all these issues, to inform the remuneration committee of Network Rail on the performance of the company, to assist it in its task. Now, that seems to us to be an appropriate position for the regulator to be in. We were recommending that the remuneration committee look quite carefully at what the company's executives were saying about the progress on efficiency because we did not think the evidence at that stage pointed out that they were achieving that—and further analysis we published last week reinforces that there is scope for improvement. And we also were drawing attention to issues around the problems on the integrated train planning system and all the other bits, which were the flip side of what was quite a strong performance from the company in terms of taking the functions of railway and punctuality and passenger satisfaction to very high levels.
Chair: Right—we will have Austin, then Stephen and Richard. And then I want to draw it into another area.

Q98 Austin Mitchell: Well, I think that is a fascinating can of worms that Stephen has opened for us. I think he is in danger of becoming the new Richard Bacon, but, as the Chair pointed out, this is a complex, messy structure, and of their nature, complex, messy structures are both more expensive and more cumbersome than simple, straightforward structures. That brings in the question of regulation. The Americans seem to me to regulate almost on the assumption that the people you regulate are bastards. In this country, we always seem to regulate on the assumption that the people who are being regulated are chaps—honest chaps who do their best. The regulation of chaps by chaps is the basis of our system. Here we have a structure which, on the evidence that you've dragged out of the witnesses, isn't producing efficiencies, isn't producing low costs, is producing excessive remuneration and other problems. So, let me turn the heat on Mr Devereux now and ask him: are you happy, Mr Devereux with the cost, the efficiency, the executive rewards and the value for money of Network Rail and wouldn't it benefit from having the National Audit Office turned loose on it.
Robert Devereux: If I might observe, when you talk about it being a complex structure—
Austin Mitchell: Well, you pump a lot of money into it. You must have answers.
Robert Devereux: Well, I am going to answer you. Let me just observe though that we have now been through a period when the entire thing was nationalised. We went through an entire period when it was a private company that went into administration; and it is now in Network Rail. We are working with what we have at the moment, but the straight answer to the question, why have we asked Roy McNulty to have a go at the entire industry, over and above simply looking at Network Rail, is because it is a really interesting question right now, when we are really pressed for cash, whether we have got, as it were, almost by architecture, problems in the system that we need to address. So, that work which he is doing, I am really expecting to produce some useful material on which we can make an analysis of whether there is indeed a much better way of doing this.

Q99 Chair: You are putting us off. Where are you thinking?
Austin Mitchell: Yes. Are you happy?
Robert Devereux: Well, I am not putting you off, but I am simply observing that we asked him to report by the end of March next year. We asked him to give us a progress report by the spending review. I am hoping to see that very shortly. As things currently stand, two things might be true. One is actually, it being complicated, you are probably right to assume that there are some frictional costs in there that we might do something else with. We might just be a little bit humble, but three times we tried to design the way the railway works and each time we have reached: do we do it again?

Q100 Austin Mitchell: Yes, but we are where we are. You are putting a lot of money in, so are you happy with the way it is being used by Network Rail, and wouldn't it benefit from an analysis by the National Audit Office?
Robert Devereux: I can't be comfortable with a situation in which the regulator tells me that they are off the pace of European comparisons. What the regulator has told you has been that in successive periods they have improved Network Rail's efficiency; I am pleased with that. He has also told you that there is still a gap. So, you have been

pursuing the question: could they have done better? Could they have got them down there faster? That is ultimately, in the current structure, a judgement for the regulator between how big the target is and what is the art of the possible from where they are. Now I can see, and I share your sense, that insofar as there is any gap at all, the answer must be—not enough work so far, but the regulator has been making those judgments.

Q101 Chair: What is your view?
Mr Bacon: What is the answer about the NAO?
Robert Devereux: Well, my view—
Chair: On the NAO? There are two things.
Mr Bacon: The Financial Services Authority was not scrutinised by the NAO, and if it had been it is quite possible that many of the inadequacies that contributed to the 2007 banking crisis would have been spotted earlier and dealt with—like not having enough legislation of the right kind on the book to take over a bank quickly. Now, we are asking you, as an accounting officer, do you think there would be value—in the way, personally, I think, there would have been with the FSA earlier—in having the National Audit Office having the right to audit Network Rail?
Robert Devereux: I would pause on assuming the answer to that question is yes because I am not sure what the technical competence of the National Audit Office is in that regard.

Q102 Mr Bacon: The National Audit Office employs 850 people and also, may I point out, their staff is not a static entity. It changes according to needs. They have economists, statisticians and, for all I know, social philosophers, but they employ a range of people according to need, and when their needs change they ask Parliament for the extra resources to employ more people. If they had a new audit client, Network Rail, I imagine—and I do not want to speak for the C&AG—they would structure themselves accordingly. And if that meant hiring a few rail specialists, I think it is probably not beyond their wit to do that. So, can we get back to the question, which is: do you think there would be value in the main watchdog of taxpayers' money—and after all, you are putting a lot of taxpayers' money into this body—having the ability to audit Network Rail?
Robert Devereux: It would be very easy for me to say yes. Why wouldn't I? But let me just observe that most of the questions you have asked have not actually been as to information—they are actually to do with governance and who is making decisions, and who is accountable. What the regulator is saying to you is that they put an awful lot of information into the public domain. It is not in this Report because that is not what this Report was about. So, I am not sure that the problem of Network Rail is a lack of publicly available data. I think probably you are teasing away—

Q103 Mr Bacon: The NAO Report says it is.
Robert Devereux: I'm sorry?
Mr Bacon: The NAO Report says that one of the problems is a lack of publicly available data. Paragraph 16, page 7: "We are concerned that the regulator's ability to assess whether Network Rail is providing value for money is limited by the level of detail available on Network Rail's costings." They say that in terms.
Robert Devereux: Okay, then in that case, the National Audit Office would add value if the powers that you gave it to do this exceeded the powers of the regulator that has been set up by the previous Government, I am guessing that the NAO is implying that the regulator does not have power to do this. So, if you gave either the regulator more power or the National Audit Office, it would be much the same.

Q104 Chair: Can I just tell you the relevance of this and then I'll bring in Stephen? The relevance is that there is an issue around efficiency of Network Rail.
Robert Devereux: There is.
Chair: We think that is linked to governance because there does not appear to be proper accountability and we then think—and the impact of that, going back to passenger capacity—is that, when you come to cuts, which you are doing, you cut services. So, our constituents are all affected by this. Whether it's Barking or whether it's Orpington, whether it's Norfolk or whether it's Grimsby, we are all affected by this. Our constituents are suffering from overcrowding, lack of capacity, because we do not have an efficient Network Rail—the least efficient in Europe. So, that is why we are asking questions around governance. It is not just that we are interested in it for its own sake.
Robert Devereux: No, please—that is exactly why I would be interested in it too. So, the reason we are doing the McNulty Study right now across the entire industry, because there is more to life even than the regulator, is to get to the bottom of what could you do differently that would address these systemic issues to do with whether those cost comparisons are right. The story as it is now is these things are not well-compared. In respect of OMR, there is actually some quite decent benchmarking data out there and we know that that—and the regulators are pressing down on it—it has not got to zero, an interesting question. When it comes to big capital works, actually that is the stuff which the work on the HS2 that was published back in January began to dig into why is it that these things cost so much in the UK. That is, in a sense, the jumping off point for the work we have commissioned. So, I am entirely with you that we cannot assume that the three or four parties who are currently comprising the current British rail network are optimally organised if actually, in one part of the forest, you get this evidence and in another part of the forest, you are not sure whether our people have actually got aligned incentives. I am not wholly sure they do. McNulty is saying, "Okay, let me just think about where this might be". And the only thing I say about making changes is it is always easier to vote for "Let's all change it round again" and by and large, when you change things round radically you lose several years in the process. Which

is essentially what happened when Network Rail was created post-Railtrack. It is essentially what happened when you had the privatisation. We need to be careful that we choose the right solution, but we are actively looking at the evidence about what that solution should be.

Q105 Mr Bacon: Two very quick questions for Mr Emery. First of all, you mentioned these reporters or consultants who you send in to check that the costings of Network Rail are reasonable. In your terms and conditions for employing these reporters or consultants, do you prohibit them from working for Network Rail separately?
Bill Emery: They are not allowed to work for them on similar items of work. If we prohibited them from doing any work on the railways then we would have a very small number of reporters, so there is a balance here to be struck.

Q106 Mr Bacon: But you actively try to make sure that these reporters do not have conflicts of interest?
Bill Emery: We certainly actively try to make sure that they do not have a conflict of interest and we look to make sure that if they are engaged in one part of our reporting role they are not engaged doing that type of thing with Network Rail. That is the way we have finessed it. Otherwise we would end up having to employ consultants who did not have a detailed railway knowledge. So, we struck a balance there, which says that if they are dealing with, say, our monitoring side, that they are not going to be working for Network Rail on those sides. If they are dealing with the enhancement side then they are not going to be working on that, and that is the way it works.

Q107 Mr Bacon: One more question. Are you satisfied that, as regulator, you have adequate powers?
Bill Emery: Yes.
Chair: Okay, Stephen.

Q108 Stephen Barclay: Just on that and on the last point, I am trying to look forward, and to me one option is to look at the structure, and I understand the difficulties of that—it is another change and there are difficulties around the debt and how that figures into red brick, and the attractions of the existing structure, which is where I think the question were coming from the Committee on "Where's the transparency?" What I find amazing is that there seems a reluctance to have the NAO or greater transparency on this as well. As the accounting officer, it is clear that there are problems on the international benchmark, on customer finance and on a number of things in the Report. Given that problem, how realistic is it to expect dramatic improvements in three or four years' time?
Robert Devereux: I don't know why I'm bothering to argue this really, but the regulator has just told you that he thinks he has enough powers to get the data he needs. I perceive that behind your questions the suggestion that somehow or other Network Rail is pulling the wool over somebody's eyes. That comes down to a question of power. Can you actually get what you want out of the organisation? The regulator is telling you he has got that power and so one question might be, is he using it enough? It is not self-evident to me why I give another body essentially the same powers, which I deem to be enough. You may say that therein lies the difference—that if I gave them both the same powers, the NAO would do better. I guess I am just not sure. The really important question is: do we think somebody has actually got the fundamental right to ask all the hard questions and get the truthful answers. That is the thing that, as a matter of the way it has been set up, is what the regulator was supposed to be capable of doing and what the regulator is saying he can do.

Q109 Stephen Barclay: But the Report itself is saying, for example, on the affordability test, there is a degree of circularity. So, the Report is talking of structural issues.
Robert Devereux: No, no—I'm sorry, what that says is there is a circularity if the person who is trying to think what something might cost is the person being regulated. That is a different point from: does anybody have the right powers to see the information. It just is. There is no point in asking me and the regulator to sit down and work out what things might cost *ab initio*.

Q110 Chair: I suppose the other question is: are you happy with the regulator's performance to date?
Robert Devereux: Sorry?
Chair: Are you happy with the regulator's performance to date?
Robert Devereux: Since we are still in the position where there is a manifest shortfall against the best practice, I would prefer that wasn't there. But the regulator's judgement in reaching these determinations, which of course would obviously be challengeable, is: is it a reasonable degree of progress given the circumstances that prevail. Now, I'm afraid I am not in a position to second guess that judgment; all I can observe, exactly the same way as you, is there is still daylight that I am trying to close. So, the reason for doing the McNulty thing is to make sure there is nothing still going wrong in this system, which I am perfectly happy to change, if that turns out to be the right thing to do, notwithstanding the cost of change. I want to know what those choices are, because the thing I cannot abide is ending up with costs that are higher than they should be. That is what I am paid for.
Chair: Okay. Well, thank you. I think we have taken it as far as we can today. Apologies for keeping you waiting whilst we voted, but I think that was quite a lively session and thank you for answering our questions in the best way you can. We will report as soon as we are able to. Thank you very much.

Supplementary memorandum from the Department for Transport

ADDITIONAL INFORMATION TO THE COMMITTEE

Question 18 (Matthew Hancock): *Have you done any assessment of whether you could successfully revisit those (the 650 carriages already contracted) in order to get better value for money given that you are such a large purchaser in this area?*

Franchise Agreements do not contain clauses that would allow the Department unilaterally to revisit the basis upon which these transactions were concluded. Any re-opening of these deals would therefore require the agreement of the train operators, who are likely, in turn, to seek to re-open other aspects of the Franchise Agreement which they perceive to be to their disadvantage. Since the business and commercial environment that existed at the time these deals were struck in 2009 and 2010 have not substantively changed, the Department judges that there is little to be gained by Government in attempting to re-open these Deeds of Amendment, a position which has been agreed with the Cabinet Office (through the Efficiency and Reform Group).

Questions 33–34 (Stephen Barclay): *Is it a specification for all the new rolling stock that they will have Automatic Passenger Count systems?*

When directly procuring new trains the Department includes in the output specification a requirement that a system is fitted which will allow the automatic calculation of the number of passengers in each carriage,

Question 36 (Stephen Barclay): *Are you not going to retrofit [older carriages] because of the cost?*

A number of older carriages have already been retrofitted with Automatic Passenger Count equipment and the Department seeks further retrofitting of carriages when letting a new franchise; for example, Northern Trains have met a franchise commitment set in summer 2007 to provide a representative passenger count sample by fitting Automatic Passenger Count equipment to 25% of its train fleet.

The two main types of Automatic Passenger Count systems work either off the air-bag suspension system or through infra-red beams across the doorways. Trains that have spring suspension systems and that were built before digital technology became commonplace can be expensive to modify. In such cases, the Department and industry parties review the expected train life, the passenger services the train will be used on and whether extensive detail of passenger counts will be important to understanding the usage of these passenger services. If the trains are not used on busy routes there may not be much value in having detailed passenger counts and simpler routine manual counts may be sufficient.

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