Report by the
Comptroller and Auditor General

Shadow Strategic Rail Authority

Action to improve passenger rail services

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Executive summary

This report examines the challenges facing the new Strategic Rail Authority.

1 In November 1999, the government introduced legislation which is still going through Parliament to create a Strategic Rail Authority. However, the Authority has been operating in shadow form since July 1999. This report is about the challenges facing the new Authority in its task of improving passenger rail services. In considering these challenges, we have reflected on the experience of the Authority's principal predecessor, the Office of Passenger Rail Franchising (OPRAF).

OPRAF awarded and administered franchises with train operating companies to run passenger rail services.

2 The Railways Act 1993 established a new way of delivering passenger rail services in Great Britain. Under these new arrangements OPRAF, a non-ministerial government department, was given responsibility for awarding and then administering franchises with train operating companies to run passenger rail services. All 25 franchises were awarded by March 1997, with performance standards set at the levels achieved by British Rail before franchising. OPRAF monitored compliance with franchise conditions and paid (in most cases) subsidies to the train operating companies.

Each franchise is a legal contract …

3 Each franchise is a legal contract between the head of OPRAF, the Franchising Director, and the train operating company. The subsidy to the companies, which totalled £1.0 billion[1] in 1999-00, is set at the amounts agreed for providing the required services and is largely unaffected by company performance or compliance with the franchise, except in serious cases of failure. Failures of performance are dealt with through a graduated system of enforcement which is intended to seek restitution and remedy; and repeated or serious failures may lead to termination of the franchise. In addition, some aspects of performance lead to incentive or penalty payments, which amounted to a net £3.3 million in 1999-00 (comprising £25.6 million in penalties and £22.3 million in incentive payments). All train operating companies are also required to have a Passenger's Charter.

… with some years to run, although a replacement process is underway.

4 The existing 25 franchise agreements, with one exception, have another three or more years to run. However, in 1999, the Franchising Director began a process of inviting some train operating companies to voluntarily rebid for their franchise in competition with outside bidders. No franchise has yet been relet under these arrangements but the Authority would like to replace most existing franchises by 2002. It hopes, through this "replacement" process, to remedy shortcomings in the current franchise arrangements.

1 Train operating companies received a further £0.3 billion from Passenger Transport Executives which are not the subject of this report.

We consider what action the Authority needs to take to improve passenger rail services in the light of past experience and current problems.

5 In this report we examine the performance of passenger rail services since franchising; the action taken by OPRAF and the Authority to improve performance; and the obstacles which at present inhibit improvements to performance. We consider what action the Authority needs to take in the light of past experience and current problems. The report focuses on those aspects of passenger rail services with the potential to have made a significant difference to the quality of service received by passengers in the three years since OPRAF assumed responsibility. The regulation of Railtrack's performance in maintaining and renewing the railways is the subject of a parallel report (HC397, 1999-00).

Main findings

Punctuality and reliability

87 per cent of trains arrive within 5 minutes of schedule and 1.2 per cent are cancelled.

OPRAF applied the powers available to it ...

6 Since franchising, the train operating companies have operated more trains than previously and punctuality and reliability have been slightly better than under British Rail. In the two years between April 1998 and March 2000, 87 per cent of trains arrived within five minutes of schedule and 1.2 per cent of trains were cancelled. However, different train operating companies are achieving significantly different levels of punctuality and reliability. The factors affecting performance are numerous and not all within the control of the train operating companies; but franchise arrangements were intended to incentivise train operating companies to make every effort to perform well themselves and to pressure other parties such as Railtrack and maintenance contractors to do so too. We found that OPRAF had applied the powers available within franchise agreements to remedy underperformance where it could. But we also identified some weaknesses.

... but these are subject to limitations.

- The incentive regime for punctuality, which rewards good punctuality and penalises bad, is the only mechanism available within franchise agreements to directly promote improvement beyond the standards set by British Rail. The regime applies to some companies only and is not thought to be very effective.

- The enforcement system has served to remedy very poor reliability, although it cannot bring about performance beyond the levels set in the franchise. Train operating companies with the least demanding performance benchmarks have found these standards relatively easy to meet, compared to those companies with tighter benchmarks.

- There is some evidence that the deterrent effect of enforcement action can influence companies to act in ways which are not in the best interests of passengers. Consultants employed by the Authority found that, for example, reluctance to cancel trains already running very late can cause increased disruption to timetabled services. The Authority has carried out extensive analysis on the effectiveness of its incentive and penalty regimes but has carried out no similar work on its enforcement regime or the Passenger's Charter, including the extent to which these various mechanisms may interact to bring about perverse behaviours.

The Authority has plans to strengthen incentives ...

7 The Authority published its guide to the franchise replacement process in January 2000. The guide announced a number of measures which the Authority will pursue through negotiations with bidders.

- The payment rates in its incentive regimes would be doubled and there would be greater penalties if punctuality falls below a minimum standard.

- Higher and common standards would be set for reliability related to the type of service, although some companies would be allowed a period of time to reach the new standards.

- A common national service guarantee would be required from train operating companies' Passenger's Charters.

The Authority stated that it will expect train operators to "build in sufficient resilience to their plans to deal with problems that are reasonably forseeable, such as staff shortages". It will also seek to build in review points every five to seven years to assess the franchisee's performance.

... but we believe it could go further.

8 We believe that these proposals will go some way towards addressing the current weaknesses in the Authority's influence over train operating company performance. However, **we make the following recommendations**:

- Punctuality should be brought within the terms of the enforcement regime, and common punctuality standards for inter-city and other train operating companies should be set, phased in over time as necessary.

- New franchises should include provision for all performance benchmarks to be raised through the life of the franchise to take account of infrastructure improvements, technological enhancements and other efficiency gains.

- The Authority should commission further work on the effectiveness of enforcement, including the extent to which it promotes perverse behaviour by train operating companies.

Passenger numbers, capacity and overcrowding

Growth in passenger numbers combined with limited capacity have caused increased levels of overcrowding.

9 Passenger numbers are growing fast in all areas of Great Britain. This growth has exceeded that predicted by the industry's existing forecasting models. Since franchising, almost all train operating companies have increased the services they offer but overcrowding, where it is measured, has also increased. The information currently available to the Authority on overcrowding lacks accuracy, frequency and completeness and there is limited scope within franchise agreements to address overcrowding. OPRAF applied its powers where it could to encourage train operating companies to provide agreed seat capacity, to ensure that companies placed their rolling stock where it was most needed and that they had plans to address overcrowding. However, the Short Formation Incentive Payment regime, which penalises train operating companies which fail to provide the required number of carriages on peak hour trains, appears to be more effective with some companies than others, probably because the penalty rates are not high enough.

Network capacity is the main factor limiting capacity.

10 The main cause of increasing overcrowding is the growth in the number of people travelling by train. Cancellations and failure to provide agreed seat capacity exacerbate the problem. But the main limiting factor is the physical capacity of the network, in terms of track and platforms. New rolling stock is therefore unlikely to do much to alleviate the overcrowding in London and the South East, and in any case most of the planned investment is to replace existing rolling stock.

The Authority needs better information on passenger growth and overcrowding, which it is trying to obtain.

11 The Authority is seeking to improve the information available to it on passenger growth and overcrowding. It has begun to analyse where passenger growth is occurring and why, and is developing more accurate ways of measuring passenger numbers. There are inherent difficulties in counting passengers disembarking from trains manually and the Authority is seeking to encourage train operating companies to adopt more accurate and flexible electronic systems.

It also has plans to increase capacity.

12 The Authority is trying to address the challenge of unanticipated passenger growth combined with the physical constraints of the network. In its guide to the franchise replacement process, it announced that it intends to introduce the following changes to new franchise agreements.

- The penalty rates for running trains with fewer than the agreed number of carriages would be doubled.
- More frequent and accurate recording of the number of passengers travelling on all services would be required.
- The Authority would consider adjustments to fares to encourage passengers to avoid the high peak.
- Companies would be allowed to raise fares, in some circumstances, to pay for capacity improvements after these have been delivered.

The cost and quality of passenger rail travel

OPRAF successfully contained fare rises ...

13 OPRAF was successful in containing average fares increases through its strategy of regulating key fares, although there are significant price differentials between regions for reasons which are largely historical, and some unregulated fares have risen by more than inflation. In particular, passengers in London and the South East pay more for key fares. In 1999, train operating companies agreed to keep average fares increases, both regulated and unregulated, below inflation.

... but the Authority intends to retain a fare adjustment mechanism which results in some passengers paying more.

We question the effectiveness and fairness of this mechanism.

14 In its guide to the franchise replacement process, the Authority has said that it proposes to continue to regulate key fares within an overall cap of RPI-1%, but changes to the cap will be considered where fares increases could be used to increase capacity or pay for "significant quality improvements". The Authority proposes to retain the fares adjustment mechanism for London commuter train operating companies. This mechanism allows fares to be raised for companies which improve punctuality and reliability compared to the previous year and requires lower fares increases for companies which perform worse. The fares adjustment mechanism is unpopular with train operating companies, whilst passenger groups consider that it rewards companies for performance which is still mediocre. There is a lack of evidence of its impact on performance. The Authority proposes to increase the effectiveness of the mechanism by removing the corresponding subsidy adjustment which compensates train operating companies for income lost because of performance-related fares adjustments. But this still leaves passengers in London and the South East paying more for improved punctuality and reliability, which they may not be inclined to do, particularly in the light of current levels of overcrowding.

OPRAF had little direct knowledge of the quality of service experienced by passengers …

… and its attempts to raise passenger satisfaction had little impact.

15 OPRAF used surveys of passenger satisfaction to measure the quality of service experienced by passengers. It undertook very little direct verification of the services delivered, even for those aspects of service such as station standards which are spelled out in the franchise agreements, preferring to rely on self-certification by the train operating companies. Where OPRAF attempted to raise passenger satisfaction through action plans agreed with train operating companies, these have not had the desired effect of increasing satisfaction levels. The Authority has recognised that other factors may influence passenger satisfaction but has not discovered a way to allow for these other factors so that it and train operating companies can target their attention where it is most needed. The Authority is piloting 'mystery shopping', where customers are paid to record and report on the service they receive, on two companies. This may offer a viable, and relatively cheap, alternative approach, provided that train operating companies take action to address any shortcomings found.

In future, the Authority may introduce financial incentives and penalties linked to passenger satisfaction levels.

16 The Authority has told bidders for replacement franchises that it is intending to link the results from its national surveys of passenger satisfaction to an incentive regime. It has also set out a range of quality of service issues it wants bidders to consider in formulating their proposals, designed to improve passenger services and reduce the barriers to switching from car to public transport.

17 In addition to its current efforts to raise passenger satisfaction, **we recommend** that the Authority institute a programme of station inspections to determine whether standards laid down in the franchise agreements are being met. In doing so, the Authority should re-examine whether the currently defined station standards are sufficient to encourage meaningful improvements and, if necessary, revise the standards when negotiating new franchises. It should also consider whether the 'mystery shopping' approach could usefully be brought within franchise agreements so that train operating companies would have to take action in response to shortcomings it reveals.