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The Scottish Ministers' Guidance to the Office of Rail and Road

June 2018

Statutory Guidance from the Scottish Ministers to the Office of Rail and Road – issued under the Railways Act 1993

A strong, effective, independent regulator supporting Scotland's railways and communities

1. Scotland's railways are vital to vibrant, connected communities across Scotland. They support inclusive, sustainable economic growth through support for business, education and skills development. They support a growing tourism market, enabling Scotland's visitors to visit all it has to offer. Critically, they offer a real alternative to road and air travel, improving Scotland's environmental impact.
2. Our ambition is for Scotland's railways to be a source of pride, with an international reputation for efficiency and service, supporting sustainable economic growth to make Scotland a better place to live and more competitive place to do business. The realisation of that ambition will be achieved by delivering the following outcomes for rail services:
 - Improving journey times and connections
 - Reducing emissions
 - Improving quality, accessibility and affordability
3. Our ambitions and priorities for Scotland's railways have been reflected in the required outputs laid out in [High Level Output Specification \(HLOS\) for Control Period 6](#) which was published on 20 July 2017. We would expect that these outputs will be addressed in full and may not be in a position to accept a Determination from the ORR which falls short of this.
4. Scotland's railway needs a strong, independent and most of all assured regulator to help it to reach its full potential. Key to this, is the ability of the ORR to adapt its approach in order to meet the needs of rail users in Scotland and the policy requirements of the Scottish Government as primary specifier and funder, particularly where these may differ from other parts of the GB network. Therefore, in discharging its duties, the ORR should have full regard to the exact requirements outlined in the HLOS, in addition to any other strategy, policy or objective either published or otherwise notified by the Scottish Ministers. This should include strategies and policies which are wider than specifically rail, such as the Scottish Government's economic and environmental strategies. The ORR should note that revised versions of the Scottish National Transport Strategy and Strategic Transport Projects Review are likely to come into effect through the lifecycle of Control Period 6.

The Legislative Context

5. Section 4(5)(aa) of the Railways Act 1993 (“the 1993 Act”) requires the ORR, in exercising its functions (other than safety), to have regard to any general guidance given to it by the Scottish Ministers about railway services wholly or partly in Scotland or about other matters in regard to Scotland that relate to railways.
6. This document revokes and replaces the guidance issued by the Scottish Ministers on 21 June 2012.

The Scotland route at the leading edge of route devolution and empowerment

7. Primarily as a consequence of Executive Devolution under the Railways Act 2005, the Scotland route is at a more advanced stage of devolution than the other routes on the GB Network. This has meant closer working and greater integration on the Scotland route, including through the ScotRail Alliance. This has been a key factor in the better financial and operational performance on the Scotland route in Control Period 5. We expect that progress towards a fully empowered Scotland route will continue, with support from the ORR, and that progress towards this will not be hindered by the regulatory frameworks.
8. We are of the view that railway operations are most effective and most efficient where the interface between the providers of services (and their control of costs) and the user of services is closest. We therefore expect the ORR to continue to support the further devolution on the Scottish route by:
 - ensuring that where ORR’s decision making processes and policy development has the potential to impact Scotland, it acts in the best interests of the Scottish route and its users, the ability to adapt should not be overridden by a preference for GB-wide uniformity
 - recognising in full that the Scottish route has constitutional as well as operational devolution, and therefore the priorities which drive Network Rail Scotland’s policies, actions and behaviours on the route may be legitimately different to other parts of the GB network
 - supporting greater decentralisation of the key decision-making processes, delivery functions and resources of Network Rail in Scotland in the best interests of users, funders and the Scottish economy
 - ensuring that the regulatory frameworks and incentives put in place are suited to alignment and integration between rail delivery partners and the Scottish Government, and do not place unnecessary complexity over the relationship between Network Rail in Scotland and franchise and freight operators, which at its base level should be a simple one

Improving the competitiveness of rail through improved journey times and better performance

9. To maintain and improve its competitiveness against other modes of transport, it is essential that passengers and freight users can be assured of consistently high performing and resilient services. The performance requirements within the HLOS - 92.5% for passenger services, 93-94.5% for freight – are clear. We have a very clear expectation that the ORR will bring all regulatory levers to bear to ensure that Network Rail continues to remain focussed on the delivery of the outputs in full. As a minimum, that the negative experience in Control Period 4 and Control Period 5 is not repeated in Control Period 6.
10. Equally clear is the requirement outlined in the HLOS for improvements in journey times in Control Period 6 in order to attract more passengers and freight users and improve resource efficiency. We expect the ORR to use all regulatory levers to ensure that Network Rail continues to remain focussed on delivering the outputs in full, working effectively with the industry to achieve the journey time requirement.
11. We will not accept a position where performance requirements are met at the expense of journey time improvements, or vice versa.

An efficient, value for money railway

12. Under Section 4(5)(ab) of the 1993 Act the ORR is “to give what appears to it to be appropriate weight to the extent (if any) to which the guidance relates to matters in respect of which expenditure is to be or has been incurred by the Scottish Ministers”. Under section 4(5C) of the 1993 Act, in performing its duties the ORR must also have particular regard to the interests of those using or who may use railway services, the interests of those providing railway services, the interests of those funding railway services and the general public.
13. We expect the ORR to have full regard to the [funds available to the Scottish Ministers](#) to support the rail industry and the requirement of the Scottish Government to provide that support within its allocated resource and capital budgets, while securing best value for money from that public expenditure. In making its Determination for Control Period 6, the ORR must clearly demonstrate its commitment to ensuring value for the use of Scottish public funding through the financial framework for Network Rail in Control Period 6. Areas where we would expect to see a particular focus would be:
 - the setting of challenging, but achievable efficiency requirements for Scotland across all Network Rail disciplines which are rigorously monitored, clearly reported and, where required, enforced

- a fair approach to cost allocation to the Scottish route and operators using the Scottish route, including allocation of central costs and fixed costs
 - that the ORR takes full cognisance of the need for cost allocations to be aligned with the funding arrangements between the Scottish and UK Governments
 - providing reassurance that the principle of contestability is truly and demonstrably embedded within Network Rail Scotland's internal processes, in particular the choice about whether to procure services from central functions, and in its approach to procuring services from the external supply chain
 - a clear understanding that even small variations in Network Rail costs, including renewal works, can have significant consequences for the Scottish Government's capital budget, hence that we will require much greater assurance on efficient costs
14. If the ORR considers that it is necessary to exercise or intends to exercise its duties or undertake an activity in a way that is likely to have a negative or positive, material, financial consequence for Scottish public funding of railways, then we expect the ORR to notify us as soon as is reasonably practicable so that we may make representation to the ORR. In such circumstances, we may seek to conduct a review to ensure consistency of the approach taken or to be taken by the ORR against the HLOS or any policy, strategy or objective in respect of the rail network in Scotland.
15. Providing that there is no adverse impact on the financial position of Network Rail and/or passenger or freight operators, we expect the ORR to apply the flexibility that exists within the framework of government accounting rules, including adjusting the balance between payment of grant and access charges in future years where this represents the best use of Scottish public resources.
16. The ability to secure greater certainty over track access rights and a fair pricing regime for track access is key to supporting our decisions on investments in rail capacity and services and attracting third party funding. We are therefore of the view that protecting the investment made by us and others in rail should be regarded as a key consideration and priority in the development and application of policies on track access rights and charging, and on rail competition. Specifically, we expect the ORR to discharge its functions in such a way as to permit the Scottish Ministers and others to invest with assurance that the timetable outputs underpinning the investment case for planned infrastructure enhancements will be deliverable through track access rights without risk of compromise.

New arrangements – stronger governance

17. The UK Government's decision to remove Network Rail's debt facility, and as a consequence the move to capital grant funding, means that Scottish Government governance arrangements and financial oversight have to be strengthened in order to comply with the Scottish Public Finance Manual. This is also an opportunity to ensure that lessons are learned to mitigate the risks presented by the operational, project delivery and financial performance of Network Rail in Control Period 5.
18. At the time of the writing of this Guidance, the final governance and financial oversight arrangements have still to be finalised. We would expect the ORR to fully support those arrangements, once they are in place. The ORR's regulatory frameworks and its approach to licence conditions should align with wider governance arrangements for rail in Scotland. As a minimum, those frameworks and conditions should not undermine the statutory requirement of the Scottish Ministers to ensure best value for the use of public funds.

Continuing to improve our railway through investment

19. Cost uncertainty and overruns and the late delivery of projects significantly weakens the case for investment in rail, particularly when taken against investment in other public services. In that context, the experience of Control Period 5 cannot be repeated. We would expect the ORR to fully support our approach in the use of appropriate procurement strategies, such as fixed costs, and be open to the use of new and innovative approaches to contracting. We would also expect that an effective ORR will be able to provide authoritative advice about benchmark unit costs for standard railway tasks in order to build confidence within the Scottish Government and other investors in Scotland about what efficient railway costs should be.
20. A strong and assured regulator can play a vital role in ensuring we can achieve value for money from investment. As part of a Transport Scotland project assurance toolkit, we may call upon the ORR to provide independent advice on the efficient costs of railway improvement works for presentation to the Scottish Ministers Investment Decision Making Boards, in support of any specialist advice that we may seek. We may also call upon the ORR to utilise its regulatory levers to support Transport Scotland's work to ensure that projects are delivered on time and within budget so that rail users receive the full benefit of investment at the earliest point.

Our railways helping to create a greener Scotland

21. We see a clear role for the rail industry in contributing towards a greener Scotland. In support of this, we expect the ORR to:

- ensure that Network Rail in Scotland can accurately measure and present its carbon emissions so that the Scottish Government can assess the contribution being made by Network Rail to the wider Scottish carbon emission reduction targets contained within the Climate Change (Scotland) Act 2009
- in line with the HLOS, that Network Rail in Scotland is effectively measuring and monitoring the impact of climate change in making its network and operations resilient to predicted future changes and making efficient use of resources and energy in support of a sustainable development strategy
- provide oversight and challenge to the effective stewardship of the natural environment for which Network Rail is responsible

Creating an environment for rail freight to thrive

22. Rail freight is vital to Scotland's economy and a key contributor to environmental targets. This is a challenging time for this part of the rail industry, and the [Scottish Government's rail freight strategy](#) lays out a framework for communities, business, the rail industry, logistics and the Scottish Government to work together deliver a sustainable future for rail freight.

23. In supporting this, the ORR should:

- ensure the delivery of the requirements for rail freight outlined in the HLOS, including work on the Scottish Gauge Requirement, score-cards and, as far as the ORR is able, the Network Rail management incentive mechanisms; and
- in developing the track access charges arrangements for freight operators, we expect the ORR to use a mechanism which supports the industry in Scotland and which maintains the attractiveness of rail to business

Managing Scotland's railway assets

24. A substantial proportion of the rail industry subsidy requirement is in relation to the maintenance and renewal of the network assets. Therefore we have a very clear expectation that the ORR will ensure that Transport Scotland is fully involved in the development of Network Rail's policies and strategies for the Scottish route. This includes a requirement, in defined circumstances, for Transport Scotland investment approval of strategic renewal spend.

25. We also expect the ORR to ensure that the development and delivery of asset management strategies are underpinned by accurate information on the rail assets and their condition and capability and that this information should be promptly available without further expense to, and may be dependably relied upon by, rail industry parties who may reasonably require it in pursuit of railway business. This specifically includes the Scotland Gauge Requirement, as outlined in the HLOS, in order to avoid any further unnecessary expense and delay to business development as incurred by operators, rolling stock owners and investors in CP5.

Information is key

26. Section 51(2) of the Railways Act 2005 imposes a duty on the ORR to provide information, advice or assistance to us in connection with our functions or activities in relation to railways or railway services. We therefore require that the ORR share information and, critically, provide analysis, as soon as is reasonably practicable about anything that is likely to be material to operational delivery, policy development or to forward financial planning. In particular, we expect the ORR to ensure that we receive regular, timely, transparent and reliable reports on Network Rail performance, operational and financial, disaggregated to Scotland route level, to ensure that an accurate understanding of the network is maintained at all times.

Engagement

27. We wish to maintain close working relations with the ORR. We require that the ORR provide advice and information freely and consult with us as early as possible on matters which have a direct or indirect impact on Scotland's railways.
28. To build upon the current, positive working relationships, Transport Scotland's Director of Rail will issue a separate letter to the ORR on future engagement. That letter will then form part of this Guidance.

Resourcing

29. We welcome the good base that the ORR has established in Scotland, and the strong working relationship established with Transport Scotland. We request that the ORR continue to monitor its resourcing, ensuring that it can continue to provide the required capacity and capability to discharge its functions in Scotland in line with this Guidance.



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