



Rolling stock requirements: a national strategy?

**TAMMY SAMUEL and
DOUGLAS JOHNSTON**
*examine some of the
recent publications
and pronouncements
concerning UK
rail rolling stock
and consider the
implications*

The rolling stock market in the UK could be facing change on a scale not seen since railway privatisation. Three papers produced over the last fifteen months identify and build upon solutions to perceived issues in rolling stock procurement, taking a high level, industry-wide approach, with a goal of achieving a step change in cost savings by 2018/19. These papers are complemented by a new paper from the Association of Train Operating Companies (ATOC), which addresses at a more granular level the needs of the industry over Control Period 5 (CP5 – April 2014-2019). And the Department for Transport's (DfT) recent HLOS announcement, trumpeting new electrification schemes and other capacity enhancements, only serves to further emphasize the need for a co-ordinated approach to rolling stock procurement. Do these proposed changes signify a step towards

a much-vaunted national rolling stock strategy and what does it mean for participants in the industry?

First up was the McNulty Report. McNulty was charged with examining barriers to efficiency and scope for cost reductions in the British railway industry and identified a number of such barriers in the rolling stock supply chain. The report considered that there is scope for efficiency improvements in the procurement, leasing, operation and maintenance of rolling stock, laying the blame in relation to inefficiency at the perceived ills of existing railway industry structures, such as fragmentation, perverse priorities and short-termism.

Then ATOC produced the operating community's response to the McNulty recommendations on rolling stock: *'Rolling stock and value for money'*. This paper agreed

that savings and efficiencies were possible, but not to the extent envisaged by McNulty. Amongst the approaches proposed, the development of a high-level rolling stock strategy is highlighted. This ATOC paper envisages the establishment of an industry-wide group on rolling stock, with input from TOCs, Network Rail, ROSCOs and DfT.

Moving on to March 2012 and the DfT issued its Command Paper, *'Reforming Our Railways: Putting the Customer First'*. This paper recognises that better value for money can be achieved in the rolling stock supply chain and expresses strong support for an industry-wide rolling stock strategy, as proposed by ATOC. It encourages TOCs and ROSCOs to work together to achieve value for money, but offers little help as to how these two stakeholders can be encouraged to do just that. Identifying commonality in rolling stock is recognised as a potential area for cost reduction, as well as a need for greater market transparency. There is also a commitment to improve relations between government and suppliers, with a topical (if potentially controversial) requirement for rolling stock bidders to establish a local presence.

Against this background, ATOC then produced a paper setting out its overview of the likely requirements for rolling stock in CP5. This paper does not pretend to be the proposed national rolling stock strategy, but describes itself instead as an early input into that strategy. That paper sees rolling stock procurement as being potentially driven by a combination of two key factors: franchise bidding and aging stock. With potentially half the UK franchises and concessions up for grabs before the end of 2014, franchise bidders will be looking hard at whether to offer new rolling stock as part of their bid or instead refurbish existing stock. Meanwhile a significant number of ex-BR fleets are due to reach life expiry by April 2019, with as many as 3222 vehicles theoretically reaching the end of nominal term of use by the end of CP5. This, coupled with the requirement for compliance with the passengers with reduced mobility TSI by 1st January 2020, may tempt franchisees towards investment in new-build stock where that might provide value-for-money.

Under an envisaged 'medium case' scenario, the paper predicts a need for a further 2500 vehicles (in addition to the 2100 to 2900 being procured for Crossrail,

Thameslink and IEP), to be provided through new build or refurbishment of existing stock. The paper considers the "most likely requirements" for new-build rolling stock to be between 400-1200 vehicles for this medium case scenario, with as few as 200 on the low case scenario or potentially as many as 2500 on the higher case scenario.

While this ATOC paper recognises its own limitations and that rolling stock procurement will ultimately be driven by the commercial decisions of franchise bidders, it serves a useful purpose in taking a top-down look at rolling stock needs across the sector, a firm step towards the sort of high-level view that Government and industry recognise is needed in the future. It certainly provides some food for thought for the rolling stock manufacturing and ROSCO industry, with a large potential for new units to be required.

Since the ATOC paper, the Government released on 16th July an announcement of the High Level Output Specification (HLOS) for CP5. That announcement went further than had been expected by the industry, with several new electrification projects being unveiled in addition to those projects already committed to. While the likely timing of these schemes is yet to be finalised, substantial investment in rolling stock will of course be required to reap the myriad benefits of electrification – perhaps taking estimates of new units to be procured to the higher end of the ATOC estimate. This is starting to look and feel like a national strategy – tying together both rolling stock and infrastructure requirements.

Throughout all of the published papers and commentary, it is clear that the refranchising process will play a key part in what new and refurbished stock will be procured. It seems almost inevitable that DfT will need to play some role – by both specifying franchises in a way that encourages new rolling stock and also in ensuring that its commitments to infrastructure spending are matched by investment in rolling stock. How this will manifest itself remains to be seen given the much reported issues with the IEP and Thameslink procurements and substantial delays, it might be considered unlikely that DfT will want to take the lead on a large-scale procurement any time soon and perhaps this leaves space for operators to manage the process. Also, traditionally 'section 54' undertakings had guaranteed the ROSCOs a return on their investment and a residual value

for a specified period, but in these uncertain times will a cash-strapped Government with a stated desire of weaning the rail sector off public money be willing to make this sort of long-term commitment?

This leaves open opportunities for operators and ROSCOs to consider how they might be able to fund rolling stock procurement without DfT support. Under European law, public service contracts (i.e. transport franchises or concessions) in the rail and tram sector are limited to 15 years' duration. However the duration of the contract may be extended by up to 50 per cent if the operator provides significant assets for use in carrying out the services. And the spectre of franchises of even longer duration is raised in the regulations which states that: *"If justified by the amortisation of capital in relation to exceptional infrastructure, rolling stock or vehicular investment and if the public service contract is awarded in a fair competitive tendering procedure, a public service contract may have a longer duration."* Meaning that the DfT has the legal ability to award considerably longer franchises (25-30 years perhaps) where a franchisee is promising exceptional investment in new rolling stock. A prize that we would imagine both ROSCOs and operators would be very interested in pursuing.

So a great deal of change for the rolling stock market. Lots of new opportunities on the horizon as part of a seemingly joined-up national strategy between franchising, rolling stock and infrastructure developments. A strategy that should help the industry to identify future needs of rolling stock with some certainty and hopefully provide some of the efficiencies and savings that both the industry and the Government need. ■■



Tammy Samuel is a partner and Doug Johnston is an associate in the rail team at SNR Denton UK LLP. They are experts on railways law and regulation and regularly advise on franchising, rolling stock and railway infrastructure transactions.