

Transport Committee

Oral evidence: [Intercity East Coast rail franchise](#),
HC 891

Tuesday 24 July 2018

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Members present: Lilian Greenwood (Chair); Paul Girvan; Huw Merriman; Grahame Morris; Luke Pollard; Iain Stewart; Graham Stringer; Daniel Zeichner.

Questions 321 - 442

Witness

I: Rt Hon Chris Grayling MP, Secretary of State for Transport, Department for Transport.

Written evidence from witnesses:

– [Department for Transport](#)



Examination of witness

Witness: Rt Hon Chris Grayling MP.

Q321 **Chair:** Welcome, Secretary of State. Thank you for coming along on the last day of term. For the record of our proceedings, please introduce yourself.

Chris Grayling: I am Chris Grayling, Secretary of State for Transport.

Q322 **Chair:** Today's session is primarily to wrap up our inquiry on the intercity east coast franchise, but as it is the final opportunity before the summer recess, I hope you will not mind if I ask you a few quick questions on some wider rail issues.

Q323 Yesterday, the Prime Minister announced £780 million for enhancements on the east coast main line. Could you clarify for us where that money is coming from? Is it some of the control period 5 money? Is it part of the £9 billion for enhancements that is being carried forward into control period 6, or is it new money through the rail enhancements pipeline?

Chris Grayling: We have not carried forward money into control period 6. We have a budget for control period 6 of £47 billion for rail infrastructure, divided roughly into £20 billion for renewals; £9 billion for enhancements, which is about £10 billion when you take into account development money; and the rest is operating money for Network Rail. We have not set out in full, although to a degree we have, what the £9 billion is going to be spent on. I have said that £2.9 billion will go on the trans-Pennine upgrade. The £780 million is from that enhancements money.

Q324 **Chair:** It was not the money that was carried forward but the work that was being carried forward because CP5 was reprogrammed. Is it work that was initially planned to take place in CP5 that will now happen in CP6?

Chris Grayling: It is certainly the work that is needed to complete the upgrade of the east coast main line, yes. It is work that was first thought about a number of years ago, as most projects are, but it is now going to happen. We expect the work to start at Christmas.

Q325 **Chair:** Do you think it might have been helpful if your letter, and the Prime Minister's announcement, was a bit clearer about where the £780 million sat? It almost sounded like it was a completely new announcement, but it sounds to me as if it is clarifying something.

Chris Grayling: As you will be aware, there was lots of anticipation last autumn as to how much money there would be for control period 6. The £47 billion was widely welcomed by the rail industry. They were worried that there was going to be much less money available. Actually, it is a big investment programme.



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What we did not do is set out a list of projects that we would automatically do. Through the various analyses that we are doing, we are looking again at what the priorities should be. There is no project that is a certainty for control period 6. We are now looking forward at what the priorities should be. The ones we have clearly announced that we will do are the trans-Pennine upgrade, which is a further project that we will do, and of course, Mr Pollard, we will also be doing the work at Dawlish.

Q326 **Chair:** I am sure that will be very welcome news for the south-west. The second issue is in relation to the Thameslink programme. We have obtained an extract from an unpublished Thameslink programme board governance document. It shows you, as Secretary of State, at the very top of the timetabling decision tree, with all stakeholders, including the programme board and the Industry Readiness Board reporting and making recommendations directly to you, and with you ultimately having the decision-making power. Do you accept, therefore, that ultimately you are accountable for the timetabling fiasco, which is probably a kind way of describing it?

Chris Grayling: Actually, I do not. We have an Industry Readiness Board that, on 2 May, gave a RAG rating for the timetable change of green, green, green and amber, green. It would have been irresponsible, in my view, for a Secretary of State who is not a specialist in rail matters to intervene and say, "This must not go ahead."

It is the job of the Secretary of State to determine when, and how, Government investment is used. I was approached at roughly this time last year when they said, "We want to slow down the introduction of the new Thameslink timetable." I gave my consent to that. That is where the Secretary of State has a role. The Secretary of State is not responsible for rail timetabling, and indeed should not be.

There is a political debate between our two parties. It is the view of the Labour party that the Secretary of State should possibly be responsible for running the railways, but right now it cannot be the case that if we have a private railway the Secretary of State has to be accountable for timetabling. That would be a crazy situation.

Q327 **Chair:** I would accept completely that you are not the industry expert on how to develop rail timetables, and that therefore of course you would want to listen to the views of those with expertise in the rail industry, but it is very clear in this document that the Secretary of State is where all the arrows are directed from the Industry Readiness Board and from the Thameslink programme board. The recommendations come to you. Are you saying that their recommendations were inaccurate but that ultimately you made the decision?

Chris Grayling: No, I did not make a decision on the introduction of the new timetable in May. I received an indication from those who are in place to plan the new timetable introduction. We had an independent assurance panel and we had an Industry Readiness Board, both of which



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recommended that the timetable change should go ahead. I am clearly not going to intervene in that decision making; I do not run the railways. We have rail professionals to do that.

Q328 **Chair:** You made the decision based on their recommendations.

Chris Grayling: I took no decision. I was not asked for any decision to be taken in May, nor did I take any decision in May. I simply listened to the current state of readiness from the readiness board that said all was fine. I was not asked to take a decision, nor did I take a decision.

Q329 **Chair:** So the decision tree diagram that suggests you sit right at the very top of the decision tree, with recommendations from the Industry Readiness Board and the Thameslink programme board, is rather misleading?

Chris Grayling: I am not sitting there at the start of May, and nobody is coming to me saying, "Can we go ahead with the timetable change?" That is certainly not what happened. They simply updated the Department on progress to introduce the new timetable, which to all intents and purposes was positive. What I want to know and understand—it is the reason I commissioned the Glaister review—is how it is possible that a plan that received a RAG rating of green, green, green and amber, green could possibly have gone so badly wrong.

Q330 **Chair:** Do you accept that ultimately you have responsibility for ensuring that the rail system works effectively? You organised the setting up of the Industry Readiness Board, and the Thameslink programme board is a DfT board. Surely you would take responsibility for the overall system. I appreciate that you are not driving the trains.

Chris Grayling: The Department for Transport franchises rail operations. It spends money on behalf of the taxpayer and it seeks conditionality around the spending of that money. In my view, the Department for Transport, and certainly the Secretary of State, do not take responsibility for shaping a train timetable. They do not take responsibility for establishing whether there are the right number of drivers to drive the trains or whether they have been trained appropriately or not. That is why we have an Industry Readiness Board of experts to say, "It's fine to go ahead."

Q331 **Chair:** But surely you should take responsibility for the overall system of delivering the train services that the country needs. That is what the Department for Transport is for, isn't it?

Chris Grayling: The Department for Transport has a strategic responsibility for trying to make sure that we have a smooth-running rail network, but it is not the job of the Department for Transport to micromanage the introduction of a new timetable. It never has been and never should be.

Q332 **Chair:** What about Charles Horton? He resigned as the chief executive of



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GTR, saying that with leadership comes responsibility. He was not personally responsible for setting timetables or organising rosters. Was he right to resign?

Chris Grayling: Of course, he was running the company that has had the problems—

Q333 **Chair:** One of the companies that had the problems.

Chris Grayling: He had line management responsibility for train drivers and their rostering.

Q334 **Chair:** Do you think he was right to resign?

Chris Grayling: He took that decision to go. In the circumstances, it was a decision that was probably to be expected. Of course, it is his decision and a matter for the company, because it is a private company that runs the railway.

Q335 **Chair:** Did you discuss it with him?

Chris Grayling: I did not discuss Charles Horton's future, no—not with him.

Q336 **Chair:** Have you ever considered your own position in relation to the timetabling fiasco?

Chris Grayling: As I said, the Secretary of State does not oversee the introduction of a new train timetable. It is the job of the rail industry to deliver a new train timetable. They have not done it. It is the job of the Secretary of State to ensure that when something goes wrong the reasons are properly investigated and steps are taken to make sure it does not happen again.

Q337 **Chair:** I am not sure that we are going to agree. My view would be that the Secretary of State's job is to ensure that we have a functioning rail system, and that you sit in the Department for Transport to do that.

Chris Grayling: But, with respect, sitting on the Labour side you cannot have it both ways. On the one hand—

Q338 **Chair:** I am not sitting on the Labour side; I am sitting here as Chair of the Select Committee.

Chris Grayling: Okay, but the argument that the Government should run the railways because they are not working well is what I hear all the time from your side of the House. At the same time, you are saying that the Secretary of State should take responsibility when the railways do not run well. Both of those cannot be right.

Q339 **Chair:** As the Chair of the Select Committee, I simply want to understand why the rail industry, which the Department for Transport plays a very important role in overseeing and commissioning, has not delivered the benefits that passengers expected.



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Chris Grayling: I completely agree with you on that. The frustration is that this was designed to bring to fruition a very big investment programme by Government. Of course, I absolutely share your desire to see that work. I am as unhappy about what happened as anybody else, particularly the passengers who suffered as a result. Lessons have to be learned and this cannot be allowed to happen again. When you have the collective expertise of the rail industry on this around a table giving a RAG rating of green, green, green and amber, green, it is absolutely logical that that timetable change should happen. When it goes badly wrong off the back of a recommendation that it is all in good shape, we really need to learn the lessons.

Q340 **Chair:** I certainly agree with that. We would rather it had been prevented, but that is the subject of our rail timetable inquiry, which is ongoing.

Chris Grayling: But what would you have us do? Would you have the Secretary of State step in, in the wake of a green, green, green and amber, green rating, and say, "No, this must not happen"?

Q341 **Chair:** I am simply trying to establish where responsibility lies. We will come to the issue around how we undertake our examination. Obviously we want some transparency so that we can understand what went wrong and can conduct that analysis.

The Industry Readiness Board minutes are essential for proper and open scrutiny of what happened in May. Members of Parliament have been asking to see them for months. We asked to see them by writing to you on 12 June. Why are those minutes still a secret?

Chris Grayling: First and foremost, the job of the independent inquiry, the Glaister review, is to go through all the details. This Committee is clearly looking at the issue. Our priority has been to make sure that the Glaister review has had access to all the information it needs. Of course, you can call any member of that board at any time.

Q342 **Chair:** Why are the minutes still secret? Are you saying that you are not going to allow this Committee to see the minutes of the Industry Readiness Board?

Chris Grayling: We will make sure you can see them.

Q343 **Chair:** When can we expect to receive them?

Chris Grayling: I will write to you and get that sorted out.

Q344 **Chair:** It has already been more than a month. It is six weeks since we requested those Industry Readiness Board minutes. Can you understand why people are starting to assume that there is something to hide in those minutes from the fact that six weeks later we do not seem to have sight of them?

Chris Grayling: There is not going to be anything to hide because we have commissioned a full independent investigation of everything



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involved in this process. That will be transparent, so nothing is going to be there to hide.

Q345 **Chair:** Can you use your authority to release the minutes? Will you do so immediately?

Chris Grayling: I will go back and sort out why they have not been released, and I will come back to you very quickly.

Q346 **Chair:** We look forward to hearing that information. Finally, I want to ask something about compensation. Northern, Thameslink and Great Northern have announced their additional compensation packages. What is the Department's analysis of the fairness of the additional compensation schemes they have introduced?

Chris Grayling: The schemes followed pretty much exactly what was done on Southern, with similar problems. It is a useful benchmark when things go wrong in an out-of-the-ordinary way, as has happened.

Q347 **Chair:** Do you think it is fair that passengers, some of whom are experiencing disruption to services more than two months since the timetable change, will be entitled to only one month's additional compensation?

Chris Grayling: If you remember what we did with Southern, we provided, over a much longer period, a compensation package equivalent to a month's free travel. I think that is a fair response to what has happened.

Q348 **Chair:** It is fair compared with the compensation package available to Southern passengers last year?

Chris Grayling: The indication I gave at the start was that we would treat the passengers affected this year in the same way as we treated those last year.

Q349 **Chair:** It applies only to people who travel on season tickets, but we know that working patterns are changing. There are people who work part time and those who work part of the week at home and maybe use carnet tickets or daily tickets. Have you considered their being allowed to have proportionately the same compensation as season ticket holders?

Chris Grayling: The Rail Minister is working on that issue right now.

Q350 **Chair:** Are you taking into account the potential equality impact assessment? Have you done an equality impact assessment?

Chris Grayling: We did an equality impact assessment this time last year over Southern; none the less, we are now looking very actively at the issue.

Q351 **Chair:** When do you expect to be able to tell us what you have decided on the matter?



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Chris Grayling: I hope very shortly. It is a matter of practicalities, but I hope very shortly.

Chair: That is welcome news; thank you. We are now going to move on to look at intercity east coast.

Q352 **Iain Stewart:** It has become clear during our inquiry that in the period between VTEC bidding and being awarded the franchise, and the day they took over, there were serious risks that they were not going to meet the revenue and passenger growth forecasts they had bid for. Given that, was the franchise ever likely to run the full distance?

Chris Grayling: The basic premise that VTEC had when they came to the franchise was that the change in marketing approach—bringing the Virgin approach they had operated on the west coast to the east coast route—would lead to a significant growth in passenger numbers and in revenue very early in the franchise, because actually nothing happened in that period that was infrastructure related. There were clearly going to be problems on the infrastructure side a bit further down the track, but they were expecting a big early boost from Virgin marketing, and it did not happen in the way they expected.

It is very difficult to judge somebody who came in after the franchise began and what the expectations were at that point, but, certainly from talking to the company since, they had the expectation that that fresh marketing approach would drive up numbers very quickly. Their expectations were not met and that, more than anything else, is what caused the difficulties in the franchise.

Q353 **Iain Stewart:** It is clear that revenue and passenger growth happened, just not to the level that was anticipated. Up to what point did you remain confident that they would be able to make up the initial shortfall?

Chris Grayling: By June last year it was quite clear that there was a mounting problem. It was not certain that it was not going to work, but it was looking less and less likely that it was going to work. At that time, I started to put in place a contingency planning process. Shortly afterwards, Stagecoach made an announcement in its annual results statement that it was setting aside money from parent company capital against losses on the franchise. That was the point at which it began to become clear that it was not likely to make it; it was not certain.

By the time we got to my statement in November, it was pretty clear that it was not going to. It was only a question of how long the franchise had. By the time I made the statement in the House in February, it had, effectively, reached the point of default. The franchise had not run out of money, but the parent company capital was fully drawn down and revenue plans showed that it would run out of money. That is the point when I came back to the House.

Q354 **Iain Stewart:** In June, when it was clear that there were serious problems, did you give VTEC a date by which they had to prove to you



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that they could get through the problems?

Chris Grayling: It is not really a question of getting a date because we cannot declare them in default until they actually run out of money, and at no point did they come to me and say, "We are going to want to give up the franchise." They were always determined to try to make it work, so from our point of view it was a question of looking at what was happening in the franchise and reaching our own assessment about what was likely to take place. It was not a question of giving them a deadline date. We were in conversation with them all along, and they were open in saying that it was not meeting expectations, hence their statement to the stock market. There is no process whereby you can effectively give a date and say, "You have to be sorted by then or we will take the contract away." You cannot take the contract away until they reach the formal point of default, and that is an uncertain moment.

Q355 **Iain Stewart:** Effectively, was November 2017 the earliest point that you felt able to make this public?

Chris Grayling: Yes. In the summer it was clear that there was a very real issue. It was not until November that it was pretty clear to me that it was really not going to make it through. At that point, revenues were still way behind expectations. The point when I came to the House in November was really the first moment that I was pretty convinced that it was not going to make it.

Q356 **Iain Stewart:** The focus of your announcement in November was the new partnership.

Chris Grayling: Yes.

Q357 **Iain Stewart:** Had that decision been made independently of the franchise running into difficulty?

Chris Grayling: Last summer, when it became clear that there was a very real risk of the franchise not succeeding, it was palpably clear to me—the franchise having failed twice before—that there was no way we could simply take it back and re-let it again in the conventional way. Also, because I am very strongly of the view that the system is under such pressure that we need greater unification of track and train, I tasked the Department with contingency work on what possible future models could look like.

By the time we came to November and we had to say, "Actually this is not going to make it, and past 2020 we are going to put in place the east coast partnership," we had a pretty clear idea of the potential direction of travel. We did not just pursue the east coast partnership route at that point, with a direct award possibly further down the track; we set up the operator of last resort so that we had all avenues open to us.

Q358 **Iain Stewart:** Let me go back a step and pick you up on the point that there was no way of re-letting the contract or rebasing it in some way.



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We questioned Polly Payne from the Department last week, and in response to my question about whether there was a significant risk that the parent bond would not be enough at the start of the contract or the franchise operating, she said, "We thought that might be the case." Were there any discussions at that point about looking at a different revenue stream or rebasing it in some way to give VTEC a fair chance?

Chris Grayling: Are you talking about the start of the franchise itself?

Iain Stewart: The start of the franchise, yes.

Chris Grayling: Of course, I was not the Secretary of State then, so I am genuinely not aware of what took place at that time. Had I been Secretary of State, I would have been wary of ambitious bids on that route, given what had happened previously. In defence of the officials and the Ministers at the time, not taking an ambitious bid when their own forecasts suggest that bid is able to be delivered is a big step to take.

Q359 **Iain Stewart:** Forgive me, I want to probe a little more. The evidence we have had is clear that they were always going to be playing catch-up, and there was a significant risk that they would never make the targets. From what you have seen, and I appreciate you were not in office, was there any discussion among officials, saying, "Hang on, we can still have a successful franchise here, but just not at the top level"? Was there any discussion of what powers the Department has to rebase a contract in those circumstances?

Chris Grayling: I am not aware that there was discussion of the franchise not going ahead in the form it eventually did. There was a lot of ambition from the company. It was genuinely the case that they believed that bringing the Virgin marketing approach that had been seen on the west coast to the east coast would lead to an immediate surge in revenues. Of course, over the first year or so of the contract that really did not happen. By the time we got to the summer of 2017, it was very clear that they were beginning to eat into parent company capital and were not able to fulfil the premium payments.

It is worth remembering that this railway was still highly profitable at the time. In fact, the money that came in from premium payments over the first couple of years of the franchise was significantly higher than it had been over the previous years. The railway was doing well and it had had an impact, but not as much of an impact as they had expected.

Q360 **Iain Stewart:** From what we have heard, this is a network that has a large discretionary element; passengers choose other modes of transport. One of the big macroeconomic changes was the fact that oil prices and motor car costs were significantly lower than anticipated. One of the recommendations in the Brown review was that the contract should be able to be adjusted in light of those big changes. Was that ever factored into this franchise? If not, is it going to be in future franchises?



Chris Grayling: First, in this franchise my view all the way through was that I do not think we can possibly be seen to bail out a company that has made an ambitious bid. My job is to protect the interests of the taxpayer, not of Stagecoach's shareholders. That is the approach I took. If you sign up to a contract, unless there is a change in the practical circumstances that affect you—for example, a major issue around infrastructure—it is your job, if you believe your marketing can deliver something extra, to deliver something extra.

All the franchises that have been issued since I became Secretary of State were set up and tendered before I took the job. We have now put in place risk-sharing mechanisms that make it much less likely that an event like this could recur. Nevertheless, if you sign up to a contract, you have made your own forecasts and decided what you are going to achieve. Of course, things can go up and down in an economy, but you ought to have the courage of your convictions and deliver. It is our job to protect the taxpayer, not the private company.

Daniel Zeichner: The Brown review made a point about not making franchise holders responsible for changes in the economy that are outside their control. It is fundamental, isn't it?

What we saw last week in evidence was your officials saying, basically, that something had happened that could not have been expected, and something different was going on. Doesn't that call into question the way these franchises are set up? You are trying to predict eight or 10 years ahead and you can't do it, can you?

Chris Grayling: But that applies to any business judging what is likely to happen going forward, and reaching its views about how much it can or cannot bid and what sensitivities it has to build in. It is easy to say that the Department got its numbers wrong, but so did Virgin and Stagecoach. They believed they could deliver. This was not over an eight-year period; it was over a two to three-year period when they had anticipated that the marketing they put in at the start, from a high-profile brand, would make a real difference on that railway, and it did not deliver what they expected.

Q361 **Daniel Zeichner:** I accept that, but what I am saying is that a possibly increasingly volatile world—if we look around, there are all kinds of possibilities that may happen over the next three, four or five years—makes this kind of system very hard to create. We seem to be endlessly chasing the next problem. We will quite likely be having the same discussion again in two or three years because something else will have happened.

Chris Grayling: That is why, since becoming Secretary of State, I have put in place, with the team, risk-sharing mechanisms that, hopefully, make this kind of issue less likely to happen. You are absolutely right, but there is a difference between a failure to deliver because you have not marketed well or delivered the right service, and volatility that comes



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from things completely outside your control. We have sought to provide a better balance, but, in this particular case, the collapse of VTEC cannot really be ascribed to a major economic shock or something similar, because there was not one at that period.

Q362 **Daniel Zeichner:** But something else had happened. The point I am making to you, Secretary of State, is that you gave up the cap and collar mechanism, and there were various efforts and different indicators that could be used as proxies for what is going on in the world. In the end, for any independent person looking at the labyrinthine structure that has been set up—600 or 700-page franchise agreements—frankly, central planning in the Soviet Union would look simple by comparison, wouldn't it?

Chris Grayling: It certainly needs some simplification. Given what we have experienced in the last few months, I would judge that the system is too diluted. That is why I have been arguing for the last two years—it started in the current franchise agreements—to bring track and train closer together operationally. We probably need a less fragmented railway to deal with the pressures on us at the moment.

Q363 **Chair:** Secretary of State, it occurs to me that trust in the railway has certainly deteriorated in recent years. I do not know if it is at an all-time low. One of the reasons for that is a lack of transparency and openness.

When you came to the House last November you talked about the east coast partnership. Why did you not tell Members then that the reason for the discussions was that there were significant financial problems with this franchise?

Chris Grayling: It was already known.

Q364 **Chair:** Why did you not come and tell—

Chris Grayling: It was already known.

Q365 **Chair:** By whom? By all Members of the House?

Chris Grayling: Yes.

Q366 **Chair:** But why focus on the east coast partnership rather than telling us what the likely outcomes were on the franchise?

Chris Grayling: Stagecoach themselves had already said so publicly.

Q367 **Chair:** We knew they were experiencing difficulties, but we did not know the state of the financial situation of the franchise. It was not until some time later that you came and talked to the House about that issue.

Chris Grayling: You had known since the previous summer that it was a franchise in difficulties. I came to the House and said that from 2020 we were going to need to do something different. Actually, it proved to be much sooner than that. I cannot announce a breach of contract until it has happened.



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Q368 **Chair:** I think you could have told us about the financial problems that the franchise was experiencing, and that that was the reason you were looking to change the structure.

Chris Grayling: But that was already public information; it was known. I stood in the House. You could have asked me the question. I said in the House that the franchise was not going to be able to continue past 2020.

Q369 **Chair:** I do not think you set out that the reasons for needing to change the structure were driven by the finances. That certainly was not the way your statement was presented.

Chris Grayling: It was in the public arena and had been for ages. It was widely discussed in the rail industry.

Chair: We will probe a little further on that.

Q370 **Graham Stringer:** Who is culpable for the failure of the franchise?

Chris Grayling: In my view, Stagecoach overbid and paid a price for doing so.

Q371 **Graham Stringer:** Where does the responsibility of the Department lie for working out the risk and robustness of the bid?

Chris Grayling: The Department works through a bid and says, "Can this be delivered?" The judgment of the Department at the time was, "Yes, this can be delivered." It was not, but, ultimately, if you and I bid for something and we overbid, we are the ones who pay the price. The shareholders of Stagecoach lost £200 million as a result of this. That is not money taxpayers have lost; it is money the shareholders have lost.

Q372 **Graham Stringer:** I understand that. The bid itself predicted 10% growth year on year. What comparators gave similar growth?

Chris Grayling: As I said, I think the bid projections were based on the belief that bringing the Virgin approach to the east coast main line would drive up ridership. No one would deny that West Coast had been a good, innovative service. I think they thought that they would achieve the same. In some circumstances, that was a perfectly sustainable argument. It just did not prove to be accurate. It did not succeed in driving up passenger numbers in the way they expected.

Q373 **Graham Stringer:** Where are the comparators that give you year-on-year growth of 10%?

Chris Grayling: There are no comparators in similar parts of the rail industry because there was an innovative approach to marketing this railway. It believed in bringing that fresh approach, and indeed it did. This has actually been a railway that stepped up its quality of service. It has brought innovation to what it does. It has just not fulfilled the level of growth that it expected.

Q374 **Graham Stringer:** The Department thought it was a low-risk bid.



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Chris Grayling: I was not around at the time. I certainly would never have assumed that it was a low-risk bid. In fact, I would have been very wary about accepting a high-risk bid on the line. In defence of the officials who took that decision, it is quite hard to walk away from an ambitious bid if you believe there is potential for that bid to be achieved. You have to bear in mind that the Brown review also accepted the fact that sometimes franchises will not succeed.

Q375 **Graham Stringer:** What is the cost to the public sector of the failure of the bid? I am not talking in terms of the lack of the forecast revenue coming in, because we have had that discussion a couple of times.

Chris Grayling: There are two parts to that. The public sector has brought in more in premium money than it would have done otherwise. The cost of making the transition to the LNER is relatively small because a lot of the changes we put in place are long term. I expect the LNER brand now to be the permanent brand. Redoing the trains and repainting the trains is not going to be something that happens in seven years or when somebody comes along and paints something else on the trains. This is intended to be a long-term brand in the same way as GWR is intended to be a long-term brand. We are trying to move away from the situation where every seven years somebody comes along and paints a new corporate logo on the side of the trains, and paints them green rather than red, or whatever.

There is a cost of transition. There is the cost of the OLR team and the cost of changes to the organisation and the back-up, the back offices and so forth. David Horne remains chief executive of the leadership team of LNER, and I have a high regard for him. There is a cost, but it is relatively small, dissecting it from what is needed for the long-term railway. I can write to you and give you more specifics about the exact numbers, but a lot of the cost is permanent cost for a transition that will not disappear.

Q376 **Graham Stringer:** Can you attempt to quantify it now? We could have more specific figures in writing, but what do you think is the ballpark figure?

Chris Grayling: At most, low tens of millions of pounds. That includes some costs.

Q377 **Graham Stringer:** What makes Arup and Ernst & Young more credible operators than Virgin and Stagecoach?

Chris Grayling: The decision I took was not about Ernst & Young. It was about the team who are there. I was very pleased that we persuaded David Horne to stay on as chief executive. Generally, this has been, and continues to be, a well-run railway. It had a sticky few days. It is dealing with some challenges, particularly an elderly fleet that regularly fails, but the staff on the railway have, in my view, been doing a very good job, and David Horne has been doing a good job of leading them. It has grown. It has attracted more passengers, but not nearly enough to meet Stagecoach's projections.



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My view is that the team who are running the railway were doing a decent job, and we tried to make the transition to the LNER as smooth as possible. The fact that the transition happened and nobody noticed, apart from the change of the logo on the side of the train, is a sign that the team have done a really good job of making sure that the migration worked well.

Q378 Graham Stringer: You are saying that as far as you are concerned, in assessing the new operators against the old, there is no material difference?

Chris Grayling: In relation to the decision I took, I looked at the evaluation. Back in January, I said, "Right, this franchise has reached a point of default and we are going to do final evaluation of whether the OLR model or the VTEC direct award is the best option." What that analysis showed was that there was relatively little difference financially for the taxpayer between the two.

It was then a judgment for me based on two things. The first was that I did not want to be seen to reward corporate failure. This Committee and others would have criticised me for doing that. The other point was that it makes it easier to migrate to the east coast partnership, because it can become a process of evolution, not revolution on a single date in 2020. We can start to mesh the two teams together now. We can create joint ways of working. We can begin to plan the railway together, so we can evolve the LNER into the east coast partnership rather than simply waiting for a handover date in 2020, which would otherwise have been the approach. For those two reasons, I judged that it was the right thing to follow the OLR route.

Q379 Graham Stringer: I do not want to put words into your mouth, but the implications of that are that the franchise failed not because of management systems for day-to-day operations, but from over-ambitious contractual arrangements. Would you accept that?

Chris Grayling: Yes, it failed because it ran out of money—no more and no less than that, literally.

Q380 Graham Stringer: The reason you are giving for the decisions you made is that you did not want to reward failure, even though they were running the railway satisfactorily, but just not against their projections?

Chris Grayling: Yes. I judged two things. One was that it would be seen by this Committee and others to be a retrograde step to say to an organisation that had demonstrably failed very quickly in the early days of a franchise to deliver its expectations, "That's okay; you can have a direct award." This was not in the latter days; it was very early in the franchise. That would have attracted a lot of criticism, probably rightly so. At the same time, though, moving to the east coast partnership structure that I set out last November seemed a better way to reach that point.

Q381 Graham Stringer: To re-ask Iain's question, it would have been cheaper



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to rebase the contract and leave Stagecoach and Virgin in control.

Chris Grayling: That was the whole point. The financial analysis we did showed that there was virtually no difference between the two. If there had been a clear-cut decision that the taxpayer would have been better off if we had left it with Virgin/Stagecoach, I would have done that. I was always very clear that I would follow what was best value for money for the taxpayer. The analysis we did showed that, actually, there was very little difference in value for money terms between the two options for the taxpayer, hence the other factors came into play.

Q382 **Graham Stringer:** The other factor being the integration?

Chris Grayling: The integration, and not being seen to reward corporate failure.

Q383 **Huw Merriman:** Secretary of State, I want to come in off the back of Graham's question. Had it been the case that you allowed renegotiation of that contract, what signal would it have sent to all the other train operators? Would it be that they could renegotiate their own terms as well? Did you have that in mind when you were looking at possibilities?

Chris Grayling: That is the point. It undermines the credibility of the system if you simply let somebody get away with a failure of this kind. There is a difference between a train operator that finds itself in a position where there has been a material change in circumstance—for example, if Network Rail has done something that badly let them down. There, you are in a position where you have to renegotiate. If somebody has bid in the expectation that a piece of infrastructure will be delivered and it is not, that is a material change to the contract. They would certainly win in court if we objected.

In this case, nothing like that had happened. It was simple and straightforward. Their marketing plans had not delivered the extra passengers, and they had run out of money relatively early in the franchise. At that point, I do not think you can say, "That's okay, tick, and we'll let you have another go," unless it is compellingly financially attractive for the taxpayer. We have to be mindful of value for money for the taxpayer.

Graham Stringer is right. If there is a real financial consequence for the taxpayer of a decision, you may think that it is the right thing to do. In this case, that was not the situation.

Q384 **Huw Merriman:** In that situation, if you were before us because taxpayers had lost money, one could understand that there would be quite a lot to discuss. In this instance, where, effectively, the story is almost, "Taxpayer rips off private shareholders," do you find some of the backstory a little baffling?

Chris Grayling: I was a little surprised to discover the Labour party tabling a motion in the Commons calling for my salary to be cut for



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effectively defending the interests of the taxpayer, taking £200 million off a private company and doing what the Labour party called for me to do, which was to bring it back into state control.

Q385 Chair: You just said you did not think it would look right if they were allowed to continue running the franchise, and to bid to do that. Will they be allowed to bid for the east coast partnership when that comes forward for tendering?

Chris Grayling: I am not planning to tender the east coast partnership in the same way. It will not be a franchise agreement in the way franchises were in the past.

Q386 Chair: Will it be a competitive process?

Chris Grayling: That is what we are working through at the moment. Where we are now—the first step on the road—is to drive the next stage of devolution in Network Rail. Andrew Haines starts as the new chief executive in about three weeks. His No. 1 priority is to drive the devolution agenda in Network Rail. It is that that makes the next step towards the east coast partnership operationally workable, because we had to have accountability on the ground and on the line for both the train and the track so that we do not have Network Rail too centralised.

I do not expect simply to advertise for a train operating company in quite the same way. There are a number of different models we could adopt. We are working through different options now, and I will very happily come back to you to talk about that, as we make progress.

One of the things I have talked about is employee participation in the running of the railway, which I believe could be of real benefit. It does not have to be the case that private participation has to come from a train operator, for example. One of the things I am very keen to see on that route is digital rail investment. Bringing in the private sector to help establish a digital signalling system, and operating it as part of the partnership, is a very real alternative.

This is not the conventional paradigm. I do not think we can go back to the conventional paradigm on this railway. It has been tried three times and it has failed three times. I am not going to be the Secretary of State who says, "Well, let's just re-let the franchise again." I am trying to do something different.

Chair: We would like to know more about the future operating arrangements.

Q387 Grahame Morris: I have a few questions and an observation. I am not a spokesperson for the Labour party, but the reason the Labour party adopted the tactic on reducing the salary of the Secretary of State, as they did with the Department for Work and Pensions, is that otherwise the Government do not vote. That is our experience. They do not take the debate as seriously as it should be taken, but it seems to concentrate



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minds when salaries are involved.

How was your trip to Newcastle yesterday, to the Cabinet? Did you go by train?

Chris Grayling: I went by train.

Q388 **Grahame Morris:** What was your experience?

Chris Grayling: The LNER service going up was excellent. It was unfortunate that on the way back a freight train had generated sparks all the way down the line between Doncaster and York, and created about six trackside fires, so the trains were slightly delayed yesterday.

Q389 **Grahame Morris:** I had a similar experience. It took me seven hours to get to London a couple of weeks ago. The brakes had seized up.

Chris Grayling: For all the frustrations we have sometimes with the operation of the rail system, sometimes there are things that nobody can really deal with. Perhaps the freight train company can, but others cannot.

Q390 **Grahame Morris:** This follows from some of your earlier answers about when a judgment was made by you, Secretary of State, and your officials about whether the franchising arrangements were working. I have seen some evidence from a survey conducted by the RMT trade union, which I believe has about 1,600 or 1,700 members on the east coast main line. There was a very high response rate. Many of the staff are long serving and served when it was in public ownership. In fact, that was my first job; I worked for British Rail on that line many years ago and with the privatised franchises.

The results are quite scathing. These are some of the highlights. They asked the workforce if they believed that the VTEC submission was impossible for the company to deliver, and 86% said that they thought it was impossible to deliver from the outset. You highlighted the issue regarding loss of revenue. Someone said, "They are by far the worst of the four companies I have worked for on the East Coast Main Line and did not deserve to be rewarded for failure."

They talk about some of the things they did: "Ticket barriers were not staffed sufficiently and were therefore left open, seeing revenue walk out of the door... Staff morale was at a low ebb... Sickness was higher than it should be... The company was losing money... Surely if the areas were sufficiently staffed and staff were happy, revenue would be higher." The reason I highlight these responses is that we are now looking at future arrangements. Have you given this serious consideration?

I love the LNER branding. I would be interested to know what the costs are, but if the intention is to keep that, could we keep it in public ownership? Is that one of the things you are considering? I want them all to be in public ownership, but is there a huge benefit in keeping at least one, so that it is a yardstick to compare the performance of the private sector?



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Chris Grayling: The first thing is that if you look at the flip side of what you have just presented, in the period when VTEC were running the railway, passenger satisfaction went up. They employed more staff than they had before and they ran more trains than they had before. There are two sides to the story. I do not want to cast aspersions on the RMT members who work on that route and who do a really good job. I travel the route fairly regularly and I think the staff are great. I have no idea how the survey was put together, but it is not in keeping with what passengers were saying, or with the raw numbers of staff and trains.

In terms of the future, there are two elements in the fundamental issue of public versus private ownership. The first is that the pressure on the rail network at the moment comes from the scale of usage of the network. There are more passengers today travelling on the railways than there were in Victorian times when the network was twice as long. All round the network, there are too many trains chasing too little space, or just as many trains as you can squeeze in chasing too little space.

The issue for the railway today is not really about ownership; it is actually about capacity. We are working hard as the Government to try to deliver more capacity. One of the huge frustrations for me of the timetable fiasco in May was that it was part of generating a big chunk of extra capacity in both the north and the south. That will come, but it is coming later and after a lot of pain.

There is another point about private involvement. I have no particular weddedness to a particular form of private participation, but it is worth saying that if you have a business that is categorised entirely in the public sector—it has happened with Network Rail—you lose the ability to bring in private investment. Most of the trains operating on the network today are funded privately. If we had a purely public railway, the chances are that they would all have to go on the nation's balance sheet. One of the reasons British Rail struggled over the years to get new rolling stock was that every year it was constantly competing with the demands of health, education and all the rest.

In terms of what the future looks like for east coast, a number of different models are available to us. I have said openly before that I rather like the public-private partnership model that exists around Manchester airport. There are a number of different models involving employee ownership, and participation in the private sector with investment and infrastructure, but I am not planning simply to return the franchise to the private sector in the way that has happened in the past. It will be different.

I suggest we have more of that debate when the time comes, but I genuinely worry about the concept of taking the railways back into the public sector, given the way the ONS has required investment to be put on the public balance sheet, and therefore the railways would have to



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come up all the time with the competition that used to exist for capital each year from the Treasury.

- Q391 **Grahame Morris:** I think there are some holes in your argument, Secretary of State. If you use that service regularly, as I do, you would recognise the old 125 trains. Indeed, the staff survey indicates that there are problems with maintenance and they are not being maintained to a high enough standard. For example, they are not even ordering enough replacement windows when there are breakages; toilets are out of order, and there are leaking ovens and so on. It is not fair to characterise the line as having pristine trains, although you made an announcement about that yesterday.

Chris Grayling: Of course, the pristine trains are arriving shortly, hopefully. There was one on a trial run yesterday; we passed it at Doncaster and it looked very good. It was waiting for the LNER brand to be painted on the side. One thing we definitely agree on is that the LNER brand is meant to be there for the long term. Swapping brands for a railway line every seven years is the wrong thing to do. South Western Railway, Great Western Railway and the LNER are all intended to be long-term brands.

- Q392 **Grahame Morris:** I do not want to prolong this, but in terms of the new operating models, you are going to come back to the Committee with some further advice when you have thought through them, but you are not even prepared to countenance maintaining it as a directly operated public service.

Chris Grayling: My anxiety comes down to two things. First, I think there are benefits from public-private partnership. We are not intending to sell off this railway lock, stock and barrel. Its future will be as a public-private partnership. It will not be a fully private company outside Government with no state involvement at all.

My aim is that it should be public-private partnership but in a different form than has taken place up to now. The example would be bringing in private capital to invest in digital signalling as part of the partnership, and an employee stake in the business. These are the things we are working through now. Because they are now both under the same roof, we can evolve this rather than working to a deadline. We can do some things sooner and take longer over other things. This can be a process of evolution that really gets it right.

- Q393 **Grahame Morris:** I would be very interested to see your plans, and I am sure the Committee would.

Chris Grayling: Absolutely, and I will do that. I will inform the House and this Committee as we make progress. As the essential first step, I am waiting for Andrew. He is really good and I know the Committee will at some point bring him in. He will be a real asset to Network Rail. He is very committed to driving forward the devolution agenda, which is an absolutely essential part of making the east coast partnership work.



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Q394 **Chair:** It sounds like it is still rather at the concept stage. Although there may well be value in bringing together track and train, we heard last week from Network Rail and Stagecoach that none of them really seems to know how this new partnership will work. Given where it is, how can you have evaluated it and worked out that it is the right way to run the line, if you have not quite decided how it is going to operate?

Chris Grayling: There is no question: I have not met a single person in the rail industry who believes that a complete separation of track and train with the two operating together purely on a contractual basis is the right way to run the railway.

Q395 **Chair:** That is how it was written in 1993 when it was privatised.

Chris Grayling: It is. That is correct. We might disagree over the model that has existed up to now, but it has actually seen the railways through a period of unprecedented growth. The challenge the railways have today is of pressure and lack of capacity more than anything else. It is my considered view, and the considered view of all the senior people I have worked with in the rail industry, and has been for many of them for many years, that the need to join up the operation of the railway is absolutely vital. We can see what has been done previously. It has been done in Scotland. It was done not successfully, for reasons of risk sharing, in the south-west. One of the ways performance in Southern has improved was by moving the Network Rail team and the Southern rail team together, with joint management of the railway on a day-to-day basis.

It is common sense that the more we can integrate the teams so that they work together, the more likely the railway is to be able to respond properly to the challenge it faces. What we have to establish with the east coast partnership is exactly what form it should take legally. What I really want on the east coast is somebody in charge able to take decisions about planning maintenance works alongside the interests of passengers and to make sure that the two fit side by side, and dealing with problems when they arise so that services get back to normal as quickly as possible. It is about creating a joint approach to the running of the railway, given the pressures on it.

Q396 **Chair:** We all understand the aspiration. It is just how you do that in the current structure of the railways, particularly on the east coast main line.

Chris Grayling: The first step, which is happening now, is already rolling out in Network Rail, but it is about to get rocket boosters under it with the arrival of Andrew Haines as chief executive. It is the No. 1 thing he is committed to delivering. The devolution of Network Rail from a centralised organisation to an organisation of devolved route-based businesses is the essential next step to paving the way for them to create the kind of partnerships the railway needs for the future.

Chair: We are looking forward to hearing from Andrew Haines early in his new role. He has to deliver £48 billion of investment successfully into the railway.



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Q397 Huw Merriman: One of our experts, Iryna Terlecky, took the view that it would be “completely counter-intuitive” to experiment with a partnership on this particular line due to there being multiple operators and its being complex, as history has shown. On the flip side, you could say that, if there were going to be two years where it is Network Rail and a public operator, it would make more sense. Why do you think she is wrong in her view that it would be completely counter-intuitive to use the east coast for this partnership?

Chris Grayling: The honest truth is that if you were starting off a strategy of joining up track and train on a blank sheet of paper, this is not the place you would start. It is circumstance that has brought us to this point, but the problems are much less clear-cut than people suggest; 45% of the route miles travelled on this route are LNER trains. A substantial proportion of the rest are GTR, and a lot of those are Great Northern.

I have already indicated that as part of the plans for the GTR franchise it is logical to work to integrate the Great Northern services at the bottom end of the line in the LNER. That was recommended to me by people in the rail industry, who said that operationally it would make things work more smoothly south of Peterborough. If you put those two together, you are talking about a substantial proportion of the route miles travelled on the line.

However we shape the railways for the future, this is going to be absolutely essential. Protecting the interests of freight and open access operators by maintaining a proper regulatory structure to ensure there is no unfair competition is absolutely essential. That is true anywhere. If an East Midlands train is travelling to the north-west, or an Arriva Trains Wales, soon to be the new franchise in Wales, is going to Manchester, you have to protect access to train paths for operators that cross operational boundaries.

Q398 Huw Merriman: We understand from the chief executive of Stagecoach that something similar was trialled—I think it was called the Wessex partnership—but that Mark Carne was not a big fan of that approach and therefore it got disbanded. I may be wrong. We talked about conflicts of interest in Network Rail having to serve its other customers, particularly on this line. Was there any evidence that the Department had that this particular line would benefit from the partnership where, in other parts of the network, it had not succeeded or would not be the right place to test it?

Chris Grayling: The south-west is an interesting case in point. In many respects, the alliance worked well. Where it broke down was on finance and on central direction from Network Rail. Network Rail is, and has been, an over-centralised organisation. There is not enough autonomy in the individual routes. There is not enough decision-making power available on a localised basis by the route directors. That is now really going to change. It has changed to a degree, but it has not changed



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enough. It is now really going to change going forward. That makes part of the alliance approach work better.

The other part is where the financial issues sit. The truth is that the train operators we have at the moment do not have balance sheets that are big enough and strong enough to start taking significant infrastructure risks. The state and/or Network Rail have to stand behind them. However we shape things for the future, it is difficult to see any private entity taking on to its own shoulders the risk of failure of a Victorian rail infrastructure. Whatever happens, the state is going to play a role. That is one of the reasons, as I said to Grahame Morris, the future to my mind is public-private partnership. It is not privatising the whole lot. I would not seek to privatise the infrastructure again. The state has a role and will continue to have a role. The state brings strengths and the private sector brings strengths. If you weld them together in a joined-up railway, you probably have the best way of running a railway in today's world and dealing with its very real operational challenges.

Q399 Huw Merriman: I was going to ask what evidence there was within the Department to suggest that east coast was the right precedent. It appears from what you are saying that this will be a very different model, and therefore quite a bit of power will be ceded from Network Rail to the train operator, which is what makes it different.

Chris Grayling: And the local route director. That is the key point. If I understand correctly, where the Wessex alliance ran into difficulties was that the Network Rail people on the ground did not have the autonomy to take joint decisions with the train operators. Everything had to be referred to the centre. This is an organisation that has been too centralised. The strategy follows on from Nicola Shaw's report, which was produced just before I became Secretary of State and which I think is absolutely right: Network Rail should decentralise. Instead of being the classic pyramid organisation, it needs to become an inverted pyramid, where the centre supports the routes, rather than the other way around.

Q400 Huw Merriman: In that situation, where there is perhaps a bit more flexibility from Network Rail, how are you going to ensure that there is no conflict of interest? If you were one of the other operators on that line, the concern would be that that flexibility would mean there was too much of a cosy relationship, and they would suffer. How will the Chinese walls be put in place to ensure that does not happen?

Chris Grayling: There are two things. In a rare moment of being sympathetic to European law, I think European law has got it right on this. It is what we will inherit in our law as a result of inheriting the *acquis* after Brexit.

There are two things we have to keep separate. One is the pricing of access and the other is the allocation of access. There has to be a mechanism that precludes an organisation operating the track and the trains from excluding someone else. There has to be clear independence.



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That is where the real regulatory role comes into play: to make sure there is fair competition across the network and that space is made available. I was very clear about the east coast main line. We absolutely have to have protection for open access operators and freight operators. Historically, of course, when the railway was in different companies, that was always the case. Indeed, there were train companies that did not have tracks, but just operated across everybody else's networks.

Q401 Huw Merriman: I am going slightly off piste. We know that the rail regulator does not currently have much of a role in regulating the train operator, although it does of course with Network Rail. By inference, does this mean that the new model could see the rail regulator given more powers towards the train operator, because Network Rail may have a more joined-up approach?

Chris Grayling: The role of the regulator in future should be much more customer focused, to make sure that customers' interests are looked after, and that in doing that we have diversity of service. There is a competition element and there is a customer element. Up to now, the role of the regulator has been very much about analysing cost. I think the role of the regulator in the future could be much more consumer focused than competition focused.

Q402 Huw Merriman: I will get back on the slope now. As you pointed out, passenger satisfaction is very high on East Coast at 92%. Given that one of the drivers of the partnership has been stated to be an increase in passenger satisfaction—of course everyone always aims for 100%—doesn't that suggest that it would be better started in an area of the country where perhaps passenger satisfaction is not quite as great? Southern comes to local mind.

Chris Grayling: The future of the GTR franchise is an interesting question. Indeed, on Southern, we have worked towards creating a much greater alliance between Network Rail and the Southern team. One of the things Chris Gibb did when he went in to do his work on Southern was to bring together the two operating teams in a joint control room at Three Bridges, so they now work together in a much more proactive way.

Interestingly, perhaps slightly ironically, through the turbulent times for GTR, the Southern franchise has been generally performing pretty well, particularly given the disruption on parts of its network. Operationally, Southern is now working much better than it was. That is partly because there is real joint teamwork between Network Rail and the Southern train operating team. It makes a difference when that happens.

Interestingly, South Western has performed less well in recent times. Sir Michael Holden is doing work for me on that and he will report shortly. One of the things he highlighted was a decision by Network Rail to move its control operations from Waterloo to Basingstoke. In doing that, it disrupted the quite good joint working between the two teams that was



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taking place at Waterloo. Where I see joint working, it seems to improve performance.

- Q403 **Huw Merriman:** Given that East Coast already has 92% satisfaction, is this really going to make a difference? Some have said that because of what has occurred, and the need to give more confidence on this particular route, the partnership could be seen as a bit of a smokescreen and a gloss on what has occurred. Is it more than that? Is it really going to change things?

Chris Grayling: If you were sitting with a blank sheet of paper trying to create a regionally integrated railway, you would not necessarily have started here. It was circumstance that brought us to this point. However, the potential benefits of doing this are quite substantial. The £780 million that we announced the start-of-works time for yesterday is going to lead to significant disruption on that railway over the next few years. Having a joint team planning passenger services around that and working out how to deliver the best possible service to passengers, and at the same time getting the work done, is an example of where a more joined-up railway can make a difference.

We have problems elsewhere when things are not joined up enough. We have seen ongoing difficulties on the Great Western electrification, notwithstanding the fact that there is quite good working between Great Western and Network Rail some of the time, but not always. Planning together, understanding revenue impacts together and trying to mitigate revenue impacts together, as well as customising customer satisfaction together, is a really important part of delivering infrastructure works. It does not happen as well as it should at the moment. Joint teams doing that are bound to make things smoother, better and less disruptive.

- Q404 **Chair:** Secretary of State, it seems quite extraordinary that you seem to be suggesting that the model brought in through the 1993 Railways Act—the privatisation—which is specifically based on splitting responsibility for infrastructure from responsibility for train operations and responsibility for the rolling stock, is broken.

Chris Grayling: I have said for the last two years that I think the railways now need to move to a point where track and train are more integrated. The reason is that this is a very different railway from the one that existed 20 or 25 years ago. At that point, it was a declining railway. British Rail had been closing lines. One of the frustrations I have at the moment is that bits of capacity that are desperately needed were taken out by British Rail because they were not needed at the time. They are desperately needed now. Since then, the number of passengers travelling on the railways has rocketed.

Back in the 1990s, there were 110,000 passengers a day using Waterloo station; it is now nearly 250,000. That is an absolute quantum leap. By definition, it means that ways of working on and running the railways are going to have to evolve to meet that challenge. It is just a very different



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challenge from the one that was there before. I have been saying for two years that, in order to meet that challenge, the track and the trains need to operate more closely again. I am not in favour of going back to a big monolithic monopolistic British Rail, but we need more joined-up working.

Q405 Chair: There is no question but that we need a change. Do you accept that the franchising model as currently conceived, or conceived back in 1993, is broken?

Chris Grayling: I absolutely accept that it is going to need to evolve, but the whole system is going to need to evolve.

Q406 Daniel Zeichner: This is a very interesting discussion. Under normal circumstances, one would look at this and say that you are trying to rebrand the system, which normally takes about two years, and trying to do something quite different. What gives you the confidence to think that you can come up with this new model in less time than it has taken in the past to do something that was fairly well tried and tested?

Chris Grayling: This is one of the reasons that, with a fine dividing line, I took the decision I did. It means that evolution to the east coast partnership can now happen a step at a time. It does not have to happen on one set date in 2020.

Andrew is going to move ahead with driving route devolution. We can start to really drive joint working between the two teams on the east coast route. We can look at the right approach for staff participation and what investment we need to bring in. Not everything now has to be done on one date in 2020. That was one of the attractions for me of going for the OLR alternative. Given the fact that there was no clear case that it was best to give VTEC a direct award, because it is clearly financially much more attractive for the taxpayer, it seemed logical to evolve the two elements towards the partnership together, and in a much more evolutionary way than saying that there is one date on which it all starts in 2020.

Q407 Daniel Zeichner: That is what you are doing in this situation. Would you envisage a similar approach to other parts of the railway when they come up for rebranding?

Chris Grayling: We are already building an alliance structure into the south-eastern and midland main line franchises. It is depth; there are different degrees of integration. There is an alliance structure, where the two parties are basically integrated together under an operational leadership, moving through to the point where somebody has oversight over the budgets for the infrastructure and the trains. With the east coast partnership, the LNER, I expect a chief executive who has responsibility ultimately for making sure that both budgets operate, rather than just one and then the other. I do not envisage a train boss and an infrastructure boss. I expect an integrated leadership structure.

Q408 Daniel Zeichner: Essentially, you are saying that in the east coast



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partnership you do not expect to run a traditional franchising process?

Chris Grayling: No.

Q409 **Daniel Zeichner:** You are expecting to see a similar model elsewhere?

Chris Grayling: That is possible. I am not going to dive in and make a massive change everywhere. We have already set a path towards greater alliancing in other parts of the network. Here we have an opportunity to go one step further and create a genuinely integrated operation. We can all then, as we see those take shape, say, "What is the best way to take this forward?"

Q410 **Daniel Zeichner:** It sounds to me, Secretary of State, as if you have slipped out on the last day quite a potentially dramatic change: the slow death of rail privatisation.

Chris Grayling: I do not think I have said anything today that I have not said many times before. I have always said to this Committee that we need to integrate track and train. The strategy document last year very much predicated greater integration. Its themes were greater integration between track and train and more capacity, fundamentally. Indeed, it also talked about employee participation in the railways. I do not think you will find anything I have said today that could not be found in that document published last November.

Daniel Zeichner: Interesting. Thank you.

Q411 **Chair:** It does feel, though, that you are suggesting that there might not be a competitive process to be part of this new partnership. Is that right?

Chris Grayling: There are different ways of shaping the partnership. We have not decided how we would run the competitive process. There are a number of ways. You can have a tender or you could do a share sale; you can do a variety of different things.

As far as I am concerned at the moment, the challenge is to get on with the devolution of Network Rail, work over the coming months to integrate those two more closely and look at the issue of employee participation. I am very much of the view that I would like greater employee participation in the success of the railways in the future. We can build a model together and then take a decision in a few months' time about what we want the private sector to bring to the table.

It could be very different from what was there in the past. It could be attracting investment to a specific part of the east coast project. It might be bringing in passenger train expertise. It is not decided definitively yet. I will come back and talk to you as we evolve it. Now that we are not working towards a set date in 2020, we can do it a step at a time.

Q412 **Graham Stringer:** Will any of these proposed changes require primary legislation?



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Chris Grayling: No, not as far as I am aware. At the moment, we are subject to European legislation. We will incorporate that into the acquis. As far as I am aware today, we can move down this path without primary legislation. It is permitted under European legislation as long as you keep separate, which we should anyway because it is the right thing to do, the questions of pricing and protecting access for open access operators.

Q413 **Graham Stringer:** I may be wrong, but I understood that the European legislation required separation of track and operators, once you had separated them. If you still have an integrated system, it is different, but once you separated them, you had to do that. I am not as familiar as perhaps I should be with the original Act that privatised the railways and the Acts that changed Railtrack into Network Rail, but I would have thought there was quite a lot in there that you are talking about changing.

Chris Grayling: The key point, first of all, is that I do not envisage us seeking to sell off the infrastructure. I do not see Network Rail ceasing to be the owner of the infrastructure and the state being the owner of the infrastructure. What European law does permit is greater integration. After 2023 it will change. The fourth rail package requires you, after 2023, to competitively tender any new service that you introduce, although of course we will have left by then.

Vertical integration is still possible under EU law, as long as you have protections against anti-competitive behaviour. Of course, it is a question of degree. This is why we are moving in most areas towards alliancing. My approach has been that we should create operational integration so that the two teams can work together. That was one of the centrepieces of the strategy document last year. We are looking to go one stage beyond that.

This is not plucked from the air by me. The McNulty report recommended three different elements to vertical integration. It said that vertical integration could be a better way of running the railway. It recommended alliancing. It recommended joint ventures and it said you could do full vertical integration in places. We are looking at the first two of those.

Q414 **Chair:** It certainly feels like a more radical departure than we had previously anticipated, and still feels rather nebulous and uncertain, although I do not disagree with some of the concepts behind what you have said, Secretary of State. Do you think 2020 is realistic?

Chris Grayling: The strategy is very much shaped from the McNulty report and the Shaw report. The McNulty report said more joined-up railways; the Shaw report said devolution of Network Rail. You need the Shaw report to achieve the McNulty report. If you do not devolve Network Rail, you cannot do it.

The point about 2020 is that it is now no longer set in stone in the way it was. There is stuff we can do sooner that we would not have been able to



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do. There is stuff we can take a bit more time over if necessary. We are not now working towards a set date in the summer or autumn of 2020 to do everything. There is stuff we will do sooner, and stuff we can do later if we need to. That was one of the reasons for a fine decision; let us not reward corporate failure and let us make it easier to shape the east coast partnership.

Q415 Chair: It feels like we are going to have to look quite carefully at what is going on. I do not feel as if I have a clear view of what the end product is going to be like.

Chris Grayling: Forget the ownership structure for a moment. The end product is somebody in charge with a team that oversees both; a team that plans possessions where there is infrastructure to be done, in a way that works in the best possible way for passenger services, and that operates the railway jointly on a day-by-day basis. If there is a trackside fire in Doncaster, they work together to get trains back to normal as quickly as possible and to divert trains where necessary. That happens to a degree at the moment, but very often people default to contractual relationships and requirements. Getting beyond that and having one team of people who run the railway, plan the railway and shape the right investments in the railway has to be the best way of doing it.

Chair: I am sure we all recognise the need to do all those things. It is about how you do that and deliver a good service at an affordable cost to passengers and taxpayers, which we have all been focused on for a long period.

Q416 Huw Merriman: Does this mean that the chief executive of the train operator would have the most senior person from Network Rail report to them in east coast?

Chris Grayling: I expect it to be a single team—either a contractual or corporate joint venture. We will probably talk more about a contractual joint venture. The entity that is created will have one boss responsible for the train and the tracks, and will have a team of track engineering types and a team of train people working for him or her, but a joint team will be running it.

Q417 Huw Merriman: Do you have a view on whether the boss, the ultimate chief responsible, will be from the train operator or from Network Rail?

Chris Grayling: I do not have a strong view. The truth is that we have two really good people running that railway now. Rob McIntosh is at Network Rail and David Horne is at LNER. Either of them could do the job. They are both very good and very experienced rail people.

Q418 Chair: I am not sure I entirely understand how it fits with the other train operators also operating on the east coast main line. As we know, it is a line that has a multitude of operators, including open access and other franchise holders. I know there are rules about access to the tracks, but surely it is just as important that TPE, Hull Trains and Grand Central have



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a close working relationship with Network Rail in the way that engineering works affect their services, just as the main intercity operator does.

Chris Grayling: That is one of the reasons one of the first people I had a conversation with about this was the rail regulator. They are on board working with us as we shape this, because we have to protect the rights of other operators.

Q419 **Chair:** It is not just about rights though; it is about wanting the benefit of joint working to apply just as much to the other operators as it does to the operator of the intercity franchise.

Chris Grayling: In terms of miles travelled, the intercity operator, particularly if we add elements of Great Northern, is by far the biggest.

Chair: We look forward to more information. We now want to look at the wider franchising system.

Q420 **Luke Pollard:** In your Department's submission to our inquiry, Secretary of State, you said that franchise failure does not necessarily matter provided it is managed in the right way. Doesn't that attitude get to the heart of what has been going wrong with the East Coast franchise? You are accepting and predicting, and you have created a system that allows for and predicts a certain amount of franchise failure.

Chris Grayling: This was predicated in the Brown review four or five years ago in the wake of problems on Virgin West Coast when the franchising process went wrong, as you will remember. I do not think that the public sector should be afraid to push the envelope of getting money for the taxpayer. It should not do so in a way that confidently forecasts failure; that would not be the right thing to do. But if you do not push the operators to a degree, and if you give them too comfortable a life financially, you do not maximise value for the taxpayer. That is what I think was meant by that remark.

Q421 **Luke Pollard:** Do you think you have the right balance between protecting the public sector, protecting taxpayers and protecting the current franchise system?

Chris Grayling: I think we have a better balance now. Since I became Secretary of State, we have advertised three franchises: the west coast partnership, south-eastern and midland main line. All those have new mechanisms in place for risk sharing. I would not personally go back to the exact system that was there before. I want to push the envelope and get the best possible value for the taxpayer, but I do not want franchises collapsing regularly.

Q422 **Luke Pollard:** Have you thought about value for the taxpayer as to just how much DfT resource is sucked into rail franchising? It is my understanding that you have quite large teams in the DfT responsible for creating, managing and assessing bids. As we have heard from previous evidence, that is a very expensive process for the taxpayer. Could it be



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reformed so that it is more efficient and cost-effective?

Chris Grayling: It is very likely that we will want to make changes to simplify things. Potentially longer franchises is one of the things I predicated in the strategy document last year; possibly moving to longer franchises. Yes, I think the situation is too complicated. I also think that, although Ministers do not do some of the things people think we do, the Department has too much of a role now in running the railways when it comes to, for example, areas where we participate in investment such as the specification of trains.

Q423 **Luke Pollard:** We heard previously that East Coast was not the only train operating franchise experiencing financial difficulties. We also heard from your officials that you are prevented from telling Parliament about any TOCs having financial difficulties, due to the Railways Act. Are you anticipating that there will be similar financial collapses or requirements for you to step in on any of the TOCs that we have around the country?

Chris Grayling: The reason we are circumspect in what we say about these things is that a lot of the companies are listed. You cannot just make market-sensitive statements on the hoof. As I said to Mr Stewart earlier, I first put the east coast main line on to the Department's action list last summer when we started doing contingency thinking about what would happen if the franchise did not succeed. As of today there is no other franchise at that point.

Q424 **Luke Pollard:** But there are franchises earlier in that process?

Chris Grayling: It is a matter of record that revenues have not lived up to expectation. FirstGroup, with TransPennine Express, has just made a £106 million provision against that. They are adamant that they will be able to see out their franchise. As I say, there is no other franchise that has reached the point on my desk that East Coast did last summer.

Q425 **Luke Pollard:** Are there franchises that are eating into the parent guarantee at the moment?

Chris Grayling: The TransPennine one certainly has, yes.

Q426 **Luke Pollard:** Do you think your Department could have an element of greater transparency in publishing when TOCs are getting into trouble in future franchise deals? I appreciate that it might be difficult in your current agreements, but what about in the future? There is an awful lot of public interest in the health of train companies, especially when their falling over can potentially have such profound effects.

Chris Grayling: It is a balance. A company can have a bad six months and be way behind its forecasts, but can then have a good six months and start to catch up. For us to give a running commentary on the performance of a company that is nowhere near being in breach of contract would not be the right thing to do. There is an expectation that, when a company is approaching a breach of contract, the Government should say something, and I did that with East Coast. It is about being



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careful. Every business has its ups and downs, and if Government started giving a running commentary on those it would undermine confidence.

Q427 Luke Pollard: In the evidence given by some of your officials to our inquiry, we heard about the size of the operator of last resort team in the DfT. Considering that this is an area you have gone to in relation to East Coast, are you confident that that team has sufficient resources to manage not only East Coast but any other train franchise where they may be called on to take action and intervene?

Chris Grayling: I think so. In the wake of the issues around GTR, I stepped up the capabilities of the OLR team in case we had to take back control of that franchise. That would not be for financial reasons; it would be for operational reasons. It is my hope that we do not have to do that right now. I do not think it would be helpful to passengers, but I am very willing to do so if we need to. As I have said, we are clearly not going to operate that franchise in the same way in the future. We will break it up.

Q428 Luke Pollard: You said to me just now that no other franchise is in the same state of financial collapse as East Coast was, and GTR fits not into financial collapse, but into management failure or service provision. Are there other franchises, apart from GTR, that fit into the service provision set-up that might lead to the operator of last resort?

Chris Grayling: No. People have asked the question about Northern. The point to make about Northern is that I place the blame for the troubles in Northern firmly at the door of Network Rail, and the failure of the infrastructure projects between Manchester and Blackpool to deliver in time. There are two investigations taking place. One is by the rail regulator into the specific licence issues around Network Rail and Northern Rail, and the other is the Glaister report more broadly into what has happened. Northern have not necessarily covered themselves in glory, but the main culpability lies in the failure of that infrastructure project to deliver on time.

Q429 Luke Pollard: Although I appreciate you cannot tell us which of the franchises is having problems, could you set out briefly what additional steps your Department is taking to support those franchises and to help them get back on track, or to manage impacts for travellers in particular?

Chris Grayling: There are no impacts for travellers. What you have is an industry that is, at the moment, going through a period when growth was forecast to go like this, but it is going like that. Passenger numbers are still rising, but where a business is continuing, whether it is having an up or a down is not a matter for the Department. It is a matter for the business. I am not passing comment one way or the other about other franchises. TransPennine has clearly made a provision, but there is no other franchise at the point that East Coast was last year.

Q430 Luke Pollard: You have managed to pull together an awful lot of the commentary on franchising at the moment and, effectively, you are telling us, without using the phrase, that the current rail franchising



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system is broken and you want to change it fundamentally. Is this a programme that has full Government buy-in, or is your Department going out on a limb?

Chris Grayling: No. The Government fully supported the strategy published last year, the decisions we have taken over East Coast and the direction of travel bringing back together track and train, across Government.

Although we probably differ over ultimate ownership, I do not get the sense that there is any great division of opinion, either politically or in the rail industry, about the need to have greater integration of track and train.

Q431 **Chair:** In the eight years that I have been in Parliament, there have been quite a lot of changes in the rail system, usually in response to shocks or problems. The collapse of the West Coast franchise was a big one, and it feels like we are going through a similar process now. There is concern that trust in the railways may lead to a drop in passenger growth, which would have wider implications.

Do you think it is a problem, Secretary of State, that Secretaries of State for Transport do not tend to last as long as some of the structures on the railways? It is a problem for a complex network that works to long timelines that there is not a clear and coherent long-term strategy provided by having the same person for a long period.

Chris Grayling: I hope to deal with that for you. I am not planning to go anywhere any time soon. I have been doing this for more than two years. If anything, my initial views have been hardened by what I have seen, and they are the things I have said to you this afternoon about the need to move forward with greater working together of the two parts of the industry. Of course, since 2012 you have had only two Transport Secretaries, which was not always the case previously. I think we are doing a slightly better job and I hope to be around to give evidence to you for a little while longer, and to come back and talk about progress on these matters.

Chair: We certainly want to make sure that you are held accountable for delivery, albeit you take the view that you do not appear to be running the railways.

Q432 **Paul Girvan:** I want to go back to a point that was raised in relation to partnership between Network Rail and franchisees and how that can work. In an evidence session we had last week, there was a clear indication that those involved in delivery of the franchise at the VTEC end of things had a claim against Network Rail for failure on many occasions. It did not amount just to millions; it was tens of millions. On that occasion, somewhere in the region of £78 million was mentioned. I just want clarification. How do you see this partnership, and why did they not see it as a necessity to be working as a partnership already?



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Chris Grayling: Part of the challenge is that today's industry is too contractualised. If you need possession for a piece of infrastructure work, Network Rail pays a compensation payment to the train operator under a certain formula. Interestingly, when stories appear in the media about £X hundred million paid in compensation and only a small proportion to the passengers, it is because we have this financial merry-go-round in the industry to compensate for possessions. I would much rather have a team saying, "Right, let's do this because it will mitigate the impact on the passengers, keep the service flowing as well as possible and keep revenues up," than people worrying about who is going to pay what compensation to whom.

Q433 **Paul Girvan:** I appreciate that is Network Rail's ruling, but where does the compensation ultimately come from?

Chris Grayling: It comes from the project costs. If we, as Government, pay a sum of money towards a project, part of that flows to the train companies as compensation for lost revenues because possession was taken at the time.

Q434 **Chair:** Can I clarify that? Under the new partnership arrangements, will schedule 4 and schedule 8 payments continue as they do now?

Chris Grayling: Ultimately, I would like to get to a position where a joint decision is taken without worrying about contractual mechanisms. Exactly how we do that is to be worked through. If you clearly have somebody who is in charge of both the track and the train operations, it becomes easier to plan in a way that works best for passengers and minimises the financial impacts. There is always going to be a cost in lost revenue of an infrastructure project. At the moment, the industry is too contractualised.

Q435 **Chair:** But they would still be arguing about schedule 4 and schedule 8 payments?

Chris Grayling: If it is the same organisation, they are taking a decision about what works best for the engineering project and for the passengers.

Q436 **Chair:** But even if they decided how things work, there would still be compensation payable for the time when the network was not available?

Chris Grayling: Yes, of course. There is a loss of revenue that comes from an investment project, which inevitably has to be costed into the business case for that investment project. That will always be the case, but it could probably be done in a slightly less contractualised way in a more joined-up railway.

Q437 **Graham Stringer:** In your original answers, you talked about the hopes for the East Coast franchise being based on Virgin's ability to market the east coast and sell tickets. You also said that the failure of the franchise was Virgin and Stagecoach's responsibility. Do you therefore agree with me that Branson's statement blaming Network Rail for the loss of their



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franchise was a piece of fake news that Donald Trump would have been proud of?

Chris Grayling: I do not think I would put words into your mouth or anybody else's. There are Network Rail issues on that line, as there are elsewhere, but real Network Rail issues would have arisen. There is a delay of about 12 months. We are getting under way now with the upgrade. I announced the start-up works yesterday and confirmed that they are going ahead. It was originally the intention that some capacity works would take place on the east coast main line earlier. That would have affected the franchise in the next year, because the work has to be finished, but it did not affect the performance of the early years of the franchise.

Q438 **Graham Stringer:** In more moderate language, it would have been inaccurate to blame Network Rail for the failure of the franchise?

Chris Grayling: I would not blame Network Rail for the failure of the franchise.

Q439 **Luke Pollard:** You know that I am going to take the opportunity to talk about the south-west at some point. I have not said the word "Plymouth" yet, and now it is time. In particular, I want to ask about your plans to re-let the CrossCountry franchise. You will be familiar with the public consultation document that suggested cutting the number of trains in Devon and Cornwall, including west of Plymouth and to Torbay, as well as in Scotland, as part of a revised CrossCountry franchise; it was in a section of the document called "The Extremities of the Network". Are you aware of just how insulting it was for people in the south-west to be called an extremity at the same time as having a proposal to see their trains cut?

Chris Grayling: I went down there recently, and it is now the start of the network, given the investment in the new depot at Penzance. The document also offers the option of more trains rather than fewer, so it is consulting on a variety of options.

I have absolutely no intention of reducing trains to the south-west. Indeed, under this Government we are going to see far more services running from Plymouth to the west, down to Penzance. I went on one of the refurbished trains recently; the intercity express trains are now arriving down there and will be going in and out of Penzance station. There is big investment for the new depot, and the new signalling system is making more capacity possible. I am very glad that we are expanding services down there.

Q440 **Luke Pollard:** I am very glad that we are getting more GWR services that go from Penzance through to London, but the CrossCountry service goes from the south-west to the midlands, the north and to Scotland. The proposal from your Department is to cut the number of CrossCountry trains on that route, which means you would have to swap trains instead of having more direct routes. That is what the document says.



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Chris Grayling: But it also offers the option of more trains.

Q441 **Luke Pollard:** Are you quite comfortable with the general view of the west country that cutting those CrossCountry trains would be a bad idea? For me, the only solution to having more trains for what the document said was the core service - Bristol, the midlands and the north - is to buy more trains. Colleagues may agree that is the core, but not when you are an extremity, as the seat I represent would be described.

The only solution is to buy more trains. We will have more trains. We will have more seats, which means there can be a greater range of fares. Importantly, trains will be able to go through Dawlish when the weather is bad, because the current fleet of CrossCountry Voyagers cannot do that. It is not in your consultation document, but is buying more trains an option you are looking at in relation to CrossCountry?

Chris Grayling: First, I have absolutely no intention of reducing services to the south-west. Even without the Dawlish question, which is a very real one, the level of overcrowding on parts of CrossCountry means that the new franchise has to have more or longer trains.

Q442 **Luke Pollard:** I agree. Finally, if I can be really cheeky, in one of your earlier answers you talked about not repainting corporate logos on the sides of trains—effectively, keeping a brand for a route network—which seems like a very good idea and will save money as well. Does this mean that your proposal on the GWR franchise is not looking at splitting the GWR franchise from the west country and Welsh routes, as is currently being consulted on?

Chris Grayling: I cannot remember which date we are publishing the outcome, but I will give the Committee a sneak preview. Having consulted, the general view is that we should not, and therefore we will not.

Luke Pollard: Brilliant.

Chris Grayling: It was a genuine open question. Some people suggested that it might be a good idea to give the south-west its own franchise. The general consensus is not, so we are not going to.

Luke Pollard: It is unusual that I thank you for a decision, but that is a good decision that your Department has taken. Thank you for that.

Chair: Thank you for giving evidence today, Secretary of State. That concludes our public session.