



HOUSE OF COMMONS

LONDON SW1A 0AA

Rt. Hon Philip Hammond
Secretary of State
Department for Transport
Great Minster House
76 Marsham Street
London SW1P 4DR

20 October 2010

Dear Philip

Southeastern Fare Formula

I am writing further to the Spending Review announcement that Train Operating Companies are now permitted to raise their fares in accordance with the formula RPI +3%.

You will be aware that Southeastern's franchise agreement, agreed by the previous Government in 2006, is subject to a fare formula of RPI +3% as opposed to the more favourable formula expressed in most other franchise agreements of RPI +1%. This difference in fare formula relates to the recent investment in rail services in the South East, which has ultimately controversially saddled commuters with fare increases above inflation since Southeastern was awarded the franchise agreement. I welcome the announcement today which brings some parity to rail fares across the country.

Of course RPI is not the sole measurement of inflation used by the Government and as you know the Consumer Price Index is thought to be a more accurate measurement of inflation, it is the preferred measurement of the Bank of England and it is the measure adopted by the Government for its UK inflation target. There is currently a 1.5% differential between the value of RPI and CPI and if rail fare increases were to be subject to the latter, the increase would be more sustainable for Southeastern commuters.

Given the harsh economic climate and although my constituents will understand the need for cuts to public spending, I believe that we should consider every option available in relieving the financial burden they face in simply travelling to and from work whilst continuing to invest in our rail infrastructure. In light of this, I would urge you to consider the use CPI as the measurement of inflation, when reviewing the formula in the future.

Yours ever

Tracey

TRACEY CROUCH MP



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20 DEC 2010

Dear Tracey

Thank you for your letter of 20 October to Philip Hammond about the use of the Retail Price Index ('RPI') as the basis for rail fares regulation. I am replying as Minister responsible for Rail.

May I start by emphasising that the Government is well aware of the concern felt about rail fare levels? It might be helpful if I set out a summary of the regulation that is applied to rail fares.

The Government regulates the existence and price of a number of key rail fares. We protect commuters by placing a cap on average increases in regulated fares. The majority of long distance, off-peak fares (specifically those that were previously referred to as Saver Return tickets) are also regulated. For most operators, the cap is currently set at RPI+1%.

Other fares are unregulated, and train operators are permitted to set these fares on a commercial basis. This does not necessarily mean that operators will increase fares, since they compete with other modes such as cars, coaches and airlines. A number of operators have demonstrated this by introducing low cost advance purchase fares, similar to those charged by budget airlines. This has helped to make some leisure travel services significantly cheaper and filled emptier trains.

In the Comprehensive Spending Review, the Chancellor announced a significant programme of investment in rail. Despite the huge pressure on budgets caused by the deficit we have inherited, the Government has taken the decision to prioritise rail because of the economic benefits it generates and because of passenger concerns about overcrowding.

However, if we are to deliver this major upgrade programme, we need to ask fare payers to contribute as well as taxpayers. The pressing need to tackle the deficit has forced us to take difficult some decisions on fares, much as we would like to have avoided this. Our plan is that for most operators, regulated fares will be capped at RPI+1% from January 2011, rising to RPI+3% for the following three years.

However, the Coalition has formally committed itself to delivering fairness in rail fares. That is one of the reasons why the Government believes it is so important for costs in the rail industry to come down. Sir Roy McNulty is currently carrying out a value for money study on the UK's railways. We hope this will help explain why the railways cost more to run in Britain than in the rest of Europe and provide ideas for addressing this problem.

We believe that reform to deliver lower costs and to put railway finances on a more sustainable footing is essential if we are to be fair to passengers in the years to come and deliver the improvements they want to see on the rail network.

As you have noted, the RPI+3 fares formula for the Southeastern franchise was set by the previous Government. The reason was set out by Alistair Darling MP, then Secretary of State for Transport, when he announced the award of the Integrated Kent Franchise to Govia on 30 November 2005.

He noted that the taxpayer had invested "more than £600 million in new rolling stock in Kent (i.e. 57 four-car Class 375 Electrostars and 36 five-car Class 376 Electrostars) in the last three years" and that Kent had seen "£93 million of investment in power supply, stations, depots and related infrastructure". He went on to announce that the total subsidy for the franchise would be £585 million over 8 years (in addition to the grant to Network Rail which also benefits rail passengers).

The fares regulation regime in use before 2003 for Southeastern's predecessors, which linked fare increases with rail performance, had driven fares down. Since performance had substantively recovered by 2005, it was proposed that Southeastern fares would be raised over five years to reflect investment made and to address this low base.

Next year will be the final one in which Southeastern has a different fares regime from other parts of the network. From 2012, RPI+3 will become the standard formula across most of the country, including Southeastern.

With regard to your suggestion that we should base fares regulation on the Consumer Price Index rather than RPI, I should first say that there is no clear-cut argument in favour of one index over the other in terms of relevance to rail passengers' expenditure. However, the use of RPI is consistent with the general indexing approach adopted across the rail industry. For example, franchise payments/premia, network grants and franchise financial models are all indexed against RPI.

The Office of Rail Regulation uses RPI as the index for Network Rail's revenues, such as access charges. Therefore, with other rail costs linked to RPI, the Department's budget forecasts can be more accurate if rail fares are also linked to the same index.

For these reasons, we do not consider it appropriate to change the basis for fares regulation away from RPI.

Thank you for taking the time to contact me to set out your views on this matter.

*Regards
Theresa*

THE RT. HON. THERESA VILLIERS