



Railways: privatisation, 1987-1996

Standard Note: SN/BT/1157
Last updated: 18 March 2010
Author: Louise Butcher
Section: Business and Transport

This Note describes the structure of the rail industry following privatisation by the *Railways Act 1993*. It is intended to give a factual account and only briefly touches on the issues involved in reaching decisions about the form of privatisation chosen or its shortcomings. A large number of books are available that deal with these issues from a political perspective.

Further information on rail privatisation can also be found in HC Library Research Papers, in particular: *British Rail and the Railways Bill 1992-93* (RP 93/11); *Rail Privatisation: a Progress Report* (RP 95/96); *The Privatisation of Railtrack* (RP 96/54); and *The Privatised Railway* (RP 97/71). Members and their staff should contact the House of Commons Library for further information on our book and paper holdings. Briefings on other rail-related issues can be found on the [Railways topical page](#) of the Parliament website.

Contents

1	British Rail	2
2	The run up to privatisation	5
3	Privatisation	6
3.1	1992 White Paper and the Railways Bill	6
3.2	Railways Act 1993	8
4	The new structure	9
4.1	Railtrack	9
4.2	Passenger services	10
4.3	Rolling stock companies	11
4.4	Freight companies	12
5	In retrospect	13

This information is provided to Members of Parliament in support of their parliamentary duties and is not intended to address the specific circumstances of any particular individual. It should not be relied upon as being up to date; the law or policies may have changed since it was last updated; and it should not be relied upon as legal or professional advice or as a substitute for it. A suitably qualified professional should be consulted if specific advice or information is required.

This information is provided subject to [our general terms and conditions](#) which are available online or may be provided on request in hard copy. Authors are available to discuss the content of this briefing with Members and their staff, but not with the general public.

1 British Rail

British Rail (BR) was a public corporation established under section 1 of the *Transport Act 1962* as a successor to the rail and shipping activities of the British Transport Commission.¹ The British Rail Board operated passenger and freight services within Great Britain and was almost entirely vertically integrated, that is to say it owned its own trains, infrastructure and carried out almost all track and train maintenance itself.

Under state control, the railways were expected to run economically but also to cater for vaguely defined social needs. For example, section 3 of the 1962 Act said:

...it shall be the duty of the British Railways Board... to provide railway services in Great Britain... and to provide such other services and facilities as appear to the Board to be expedient, and to have due regard... to efficiency, economy and safety of operation.

Section 41 of the *Transport Act 1968* said that BR should perform its functions so as:

...to secure that the combined revenues of the authority and of its subsidiaries taken together are not less than sufficient to meet their combined charges properly chargeable to revenue account, taking one year with another.

In compliance with European rules it also operated passenger services on a non-commercial basis where so directed by the Secretary of State.² The Secretary of State paid BR a grant to cover the cost of providing any loss making services.

The major controls exercised by the Secretary of State over the Board were:

- the appointment of the Chairman and Board members;
- the setting of the external financing limit (EFL) and the public service obligation (PSO) grant;
- determining the Board's investment allocation and approval of major investment projects;
- control over temporary and total borrowing;
- the PSO direction to operate services;
- control over opposed proposals for the closure of stations and services; and
- the setting of financial targets, and agreement on general business plans.

Other statutory powers included the approval of changes in the organisation of the Board; the approval (or otherwise) of extensions of BR's fields of activities; and the disposal of businesses and assets. Many of the powers were procedural, or related to financial propriety.

¹ the BTC was established under the *Transport Act 1947* to provide "an efficient, adequate, economical and properly integrated system of public inland transport and port facilities within Great Britain for passengers and goods", excluding transport by air and came into operation on 1 January 1948 when the various interests in shipping, railways, hotels and road transport that were nationalised

² called 'public service obligations' (PSOs), made under State Aid rules; more information on EU rail policy can be found in HC Library standard note [SN/BT/184](#)

The Secretary of State also had various safety and regulatory powers under railways legislation.³

During the 1980s BR was encouraged to develop greater commercial awareness. This was achieved in a variety of ways:

- **Business organisation and objectives:** for years BR was production-led (i.e. it provided a network of services almost regardless of customer usage). From the early 1980s considerable efforts were made within BR to identify customer demands and to shape the services offered in response to those demands. At the same time moves were made to correlate costs and revenues more closely. Greater commercial acumen had been fostered in response to the Secretary of State's setting of three-year objectives for BR that supplemented the Board's statutory and financial duties.⁴
- **Privatisation of 'non-core' activities:** In 1977 the Chairman of BR suggested the possibility of using joint venture capital to develop opportunities in the subsidiary businesses, generally a drain on BR's revenue, and to free them from the public sector borrowing requirement (PSBR). By 1980 it was agreed with the Department of Transport that it would be to BR's advantage to work towards the disposal of non-rail subsidiaries and the non-operational property such as BR Hovercraft, BT Hotels, Sealink and British Transport Advertising. Section 1 of the *Transport Act 1981* provided the statutory authority for the disposals. It allowed BR to dispose of its subsidiaries and to establish subsidiaries and transfer assets to them. The Secretary of State could direct the Board to dispose of assets.
- **Encouragement of private sector involvement:** BR was encouraging the private ownership of wagons in the freight business as far back as the 1960s.⁵ The three three-year objectives set by the Secretary of State during the 1980s all called on BR to look at ways to bring the private sector into its operations, particularly ancillary services. In October 1991 the Government further encouraged BR to give private operators access to the network by voluntary co-operation (e.g. fair charges and access, privately owned rolling stock and privately-employed crews and drivers).⁶ By 1992 there were a number of examples of private sector involvement in BR (e.g. new rolling stock, signalling projects, track maintenance, joint venture property development, catering and cleaning).⁷

These initiatives contributed to BR's major organisational transformation in the decade preceding its privatisation. The Government's determination to reduce the level of subsidy flowing to the public sector railway stimulated a drive within BR for substantial efficiency improvements. Central to these reforms was the partial replacement of the existing structure based on regions by one formed around distinct rail business sectors, each with managers meeting objectives in terms of marketing, cost allocation and investment decisions. A further reform came in 1991 with the launch of 'Organising for Quality'. Completed by April 1992, this initiative finally abolished the old regions (which had continued to physically run the trains) and defined separate profit centres within each of the business sectors. In some

³ powers derived mainly from the *Transport Act 1962*, *Transport Act 1968*, *Railways Act 1974*, *Transport Act 1980* and *Transport Act 1981*

⁴ set out in the *BR Annual Report and Accounts 1983*, 1986/7 and 1990-91

⁵ proposals from Foster Yeoman to operate its own privately-owned high performance diesel locomotives were eventually implemented in 1986

⁶ DoT press notice, "Rifkind proposes early end to rail monopoly", 9 October 1991 [PN 293/91]

⁷ BR, *Rail Facts and Figures*, March 1992

respects the substantial reorganisation and the accompanying efficiency improvements undertaken by BR in its final decade generated the conditions that made privatisation a more viable policy. The new business sectors formed at least part the basis for the privatised railway and showed the system could be operated as a series of relatively independent components, rather than as a monolithic structure.

The reorganisation also led to a marked reduction in the public sector obligation (PSO) payments paid direct to BR in support of loss-making services: InterCity routes ceased to benefit from PSO grant from 1 April 1988 and from 1988-89, only Network SouthEast and Regional Railways received PSO grant, a proportion of which was intended to cover investment in asset renewal.⁸ The Transport Committee, in a July 1995 report, assessed BR's overall financial position by 1994 as follows:

In attempting to assess the potential value to the Government of this risk transfer, we noted that from 1990-91 to 1993-94 net borrowing by BR ranged from £368m to £894m a year; at the same time, PSO grant also rose substantially, peaking at £1,214m in 1992-93 before dropping back to £949m in the final year of the old regime (all at 1994-95 prices). At first sight, this presents a classic picture of railway finances out of control, as in the 1960s.

However, further examination reveals that in 1988-89 the EFL was only £505m at 1994-95 prices, lower than the grant total at £629m which meant that BR was actually reducing its debt. 16 BR's outstanding loans only amounted to £112m on 1 April 1991, although they had risen to £2,484m by 1 April 1994. In fact, BR did not borrow at all for 10 years up to 1990-91. So BR was living within its means in the 1980s and was not, in fact, being subsidised through loans that might or might not be repaid.⁹

The Board's financing regime was intended to ensure that passenger services would not accumulate substantial ongoing deficits: revenue grants were made to cover forecast deficits and capital grants were made to replace assets used on grant supported services.

As a consequence of all these changes, by the late 1980s BR could be said to be doing well: train miles had increased, costs per passenger had dropped, and subsidy had declined in real terms. The company had become more market-orientated with recognised targets and increased knowledge of its costs. It had become a reasonably well run state industry but one that would always need public subsidy. But after the good times of 1980s, BR's finances collapsed in the early 1990s largely because of increased expenditure on safety following the 1988 Clapham rail crash, the costs of improving lines to the Channel Tunnel and perhaps above all because of the recession, which saw usage fall by ten per cent.¹⁰ Railway economics are highly dependent on the performance of the overall economy.

Once again the major problem for the railways (as for any nationalised industry) emerged: the relationship between the state and the industry. BR was always subject to the vagaries of stop-go investment policies of the Government whereas what it needed was a consistent level of investment in order to renew and enhance the network. Governments tended to take a short-term view and not the long-term planning necessary to the railways.

⁸ Transport Committee, *Railway finances* (fourth report of session 1994-95), HC 206, 5 July 1995, para 9

⁹ *ibid.*, paras 13-14

¹⁰ *ibid.*, paras 16-20

2 The run up to privatisation

Although privatisation of British Rail's non-core activities had begun in the early 1980s, privatisation of the core activities only began to be actively and continuously discussed after 1987.

The House of Commons Transport Committee summarised the arguments for and against privatisation in a report in May 1987:

The fundamental objective of advocates of privatisation is to free the nationalised industries from bureaucracy and political intervention and to replace these forces with the disciplines of the market, in the expectation that this will lead to greater efficiency, lower unit costs and a better allocation of resources. The corollary of this, usually welcomed by management, is that the enterprises are freed from constraints on investment and on funding imposed as part of public expenditure controls. It is also argued that the very process of privatisation forces consideration of all the rights, duties and constraints affecting an enterprise, which is the basis for a far better identification of social objectives and their means of achievement than the historic process of control of nationalist industries. Opponents of privatisation argue that it is primarily a convenient way of abandoning the traditional social duties of the public enterprises, and of renegotiating, to the disadvantage of employees, their terms of employment.¹¹

Opponents might also have argued that the goals of reduced bureaucracy, greater efficiency, lower unit costs and better allocation of resources would not necessarily result from privatisation and could be achieved by other means.

At the Conservative Party conference in 1988 the then Secretary of State for Transport, Paul Channon, announced his intention to look at the future of BR to see whether privatisation might be a viable way forward. Subsequently, at an October 1988 Centre for Policy Studies conference he outlined five methods of privatising BR, each with advantages and disadvantages. These options were:

1. **BR plc:** the formation of a single company to run Britain's railway network;
2. **Track authority option:** track would be owned by a track authority or company and independent operating companies would then run the trains (this was put forward by the Adam Smith Institute in 1987);
3. **'Sector' option:** BR would be split into several independent companies based on its business sectors (e.g. InterCity, Southern Region, Freight etc.);
4. **'Regional' option:** BR would be split into a number of independent regional companies (this was put forward by the Centre for Policy Studies in 1988); or
5. **Any combination of options 1-4:** for example, a division into independent companies based partly on regions and partly on sectors or an arrangement where parts of the railway were run by independent vertically integrated companies and other parts had a track authority and operating companies.

¹¹ Transport Committee, *Financing of Rail Services* (third report of session 1986-87), HC 383, 13 May 1987, para 232

Publication of a White Paper, promised for the end of 1991, was delayed until after the 1992 General Election. The first indication of the Government's intentions came therefore in the Conservative Party manifesto for that election. This stated:

We believe that the best way to produce profound and lasting improvements on the railways is to end BR's state monopoly. We want to restore the pride and local commitment that died with nationalisation. We want to give the private sector the opportunity to operate existing rail services and introduce new ones, for both passengers and freight.

A significant number of companies have already said that they want to introduce new railway services as soon as the monopoly is ended. We will give them that chance.

Our plans for the railways are designed to bring better services for all passengers as rapidly as possible. We believe that franchising provides the best way of achieving that. Long term, as performance improves and services become more commercially attractive as a result of bringing in private sector disciplines, it will make sense to consider whether some services can be sold outright.¹²

3 Privatisation

3.1 1992 White Paper and the Railways Bill

The 1992 Queen's Speech promised that "legislation will be introduced to enable the private sector to operate rail services".¹³ On 7 May a 'paving' Bill was introduced to confer on the BR Board "powers to participate in the implementation of proposals for the transfer of their commercial activities to the private sector and proposals for the establishment of new arrangements with respect to their other functions".¹⁴

In July 1992 the Government published its White Paper outlining proposals for privatising British Rail.¹⁵ The core of the Government's proposals was the greater involvement of the private sector in the running of the railways through the sale of some of the BR businesses and the progressive contracting out of the management of passenger services. The principal organisational means of achieving these objectives was the separation of responsibilities for track and operations. The White Paper envisaged the introduction and passage of the necessary legislation during the 1992-93 session of Parliament, with the first franchises to be awarded in 1994.

The White Paper was followed by a series of consultation documents spelling out various aspects of the proposals in more detail:

- *The Franchising of Passenger Rail Services* (October 1992);
- *The Future Status of the British Transport Police* (November 1992);
- *A Voice for the Passenger* (December 1992);

¹² [1992 Conservative Party General Election Manifesto: The Best Future for Britain](#), p35

¹³ [HC Deb 6 May 1992, c51](#)

¹⁴ the *British Coal and British Rail (Transfer Proposals) Act 1993* received Royal Assent on 18 January 1993; the Secretary of State explained the purpose of the Bill at Second Reading, see: [HC Deb 18 May 1992, cc22-35](#)

¹⁵ DoT, *New opportunities for the railways: the privatisation of British Rail*, Cm 2010, July 1992; this was accompanied by a Statement to the House on 14 July, see: [HC Deb 14 July 1992, cc971-72](#); there were further debates on the White Paper in October 1992 ([HC Deb 29 October 1992, cc1160-1222](#)) and on an Opposition motion opposing privatisation in January 1993 ([HC Deb 12 January 1993, cc771-869](#))

- *Railway Pensions after Privatisation* (January 1993); and
- *Railway Privatisation: Passenger Rolling Stock* (January 1993).

In addition, a report by the Health and Safety Commission, *Ensuring Safety on Britain's Railways*, was published on 12 January 1993. The Government accepted in full the HSC's recommendations on measures to secure safety under privatisation proposals. Further documents appeared on charges for access to track and on the restructuring of the freight business.

The *Railways Bill 1992-93* was published on 22 January 1993 and had its Second Reading on 2 February.¹⁶ The Bill was essentially an enabling measure, leaving a large degree of discretion to the Secretary of State, the regulator, and Franchising Director. Further, there was no mention anywhere in the Bill of Railtrack – an indication of the sweeping nature of the powers contained in Part II, which enabled the Secretary of State to restructure BR in any way he thought fit.

The proposals excited a lot of comment. The Transport Committee published a report on the subject in April 1993 which concluded:

It is clear that in terms of previous international railways experience, the form of privatisation adopted by the UK Government is both novel and experimental (in the sense of being untested). It is true that some elements of the Government's proposals have been put into practice or contemplated in various parts of the world. Yet in no country with a rail system of comparable size and density of use is there an example, either in operation or even under consideration, of a complete scheme such as that contained in the Railways Bill. This does not of itself mean that it cannot succeed. To take that argument to its logical conclusion would mean that no innovation ever took place. What it does mean, however, is that because of the lack of previous experience to draw upon, the risk that something could go badly wrong is that much higher. To put it another way, the system of railway operation proposed by the Government probably can work, but, in the words of one witness, it may need to be *made* to work.

The onus lies firmly on the Government to demonstrate that its plans will provide a better service to the travelling public. If all the Government's assumptions are correct about such matter as:

- the prospects for investment;
- the practicality of the relationship between Railtrack and operating companies;
- the response of the private sector to the new opportunities on offer; and
- the feasibility of combining open access with franchising.

then there may be the *potential* for an improved railway system. Whether the Government is right in these assumptions is a matter of political judgement. The final verdict will rest with rail users.¹⁷

Following the Bill's publication the Government's proposals were clarified or developed in various respects. In the debate on Second Reading the Secretary of State unveiled a new package of grants to freight operators which were designed to make such assistance more

¹⁶ [HC Deb 2 February 1993, cc156-255](#)

¹⁷ Transport Committee, *The Future of the Railways in the Light of the Government's White Paper Proposals* (second report of session 1992-93), HC 246, April 1993, paras 523-524

transparent. He also listed the first seven 'shadow' franchise areas. Only one of these, the Isle of Wight, was to be vertically integrated (i.e. to include the track as well as the train service). He announced that Railtrack would not, as originally intended be a subsidiary of BR but would instead become a separate 'Government-owned company'.¹⁸ Other changes made during the passage of the Bill included:

- BR was permitted to become a franchisee (it had originally been excluded under clause 24 of the Bill);¹⁹
- Inter-availability of ticketing and common pricing criteria were to be standard requirements for new train operators, as set out in franchise agreements;²⁰
- Concessionary railcards for the young, elderly and disabled would continue under franchises and travel cards would survive in some form.²¹ and
- The Government was required to provide an absolute solvency guarantee for BR pensions;²²

3.2 Railways Act 1993

The *Railways Act 1993* received Royal Assent on 5 November 1993. Part I set out the respective powers and duties of the Secretary of State, the regulator and the Franchise Director. It also specified line closure procedures, conferred upon the High Court powers to issue Railway Administration Orders in the event of default by independent railway operators, and established machinery for consumer representation. Part II related to the Secretary of State's powers to direct BR to reorganise itself and to form companies for various purposes, including franchising and disposal. Part III of the Act contained miscellaneous provisions relating to safety, railway heritage, the British Transport Police, pensions, freight, financial assistance to BR staff in the preparation of management buy-outs or franchise bids, and other matters.

The principal provisions of the Act:

- provided for the franchising of passenger railway services;
- established the system under which train operators can gain access to, and use of, railway assets, particularly the track, which would be owned by a new public sector body, Railtrack;
- established the offices of the Rail Regulator and the Franchising Director;
- allowed rail user consultative committees to comment on all aspects of the rail services provided by BR and private sector franchisees, and set out closure procedures which must be followed before a passenger service could be withdrawn from a line or station;

¹⁸ [HC Deb 2 February 1993, cc156-255](#)

¹⁹ [HL Deb 5 July 1993, cc1068-1104](#)

²⁰ further details are available in HC Library standard note [SN/BT/1904](#)

²¹ [HC Deb 25 May 1993, cc758-774](#)

²² further details are available in HC Library standard note [SN/BT/3109](#)

- guaranteed continuity of services in the event of a closure proposal, or of insolvency on the part of a train operator, or the operator of a network, station or light maintenance depot;
- gave BR and the Secretary of State the powers to restructure BR's businesses and to dispose of them;
- put in place arrangements and procedures to secure the safety of railway operations;
- put in place arrangements and procedures to protect the pension rights of BR pension scheme members; and
- widened and enlarged the scope of the Freight Facilities Grant scheme.

4 The new structure

The 1993 Act provided the legal framework for the privatisation of British Rail and the introduction of a new structure for the rail industry. Many of the principal changes were brought into effect on 1 April 1994.

The legislation radically changed the structure of the railway industry by separating the responsibility for infrastructure and passenger service operations. BR was divided into a body known as Railtrack on the one hand, and a residual BR operating company to run all the other services until they were sold or franchised. The [Office of Rail Regulation \(ORR\)](#) was set up to oversee the charges to be levied by Railtrack for the use of the infrastructure. The core of the Conservative Government's proposals was the greater involvement of the private sector in the running of the railways through the sale of British Rail's freight and parcels businesses and the progressive contracting out of the management of passenger services by a new franchising authority. All passenger services would eventually be provided by private sector operators either acting as franchisees or as independent train operators. Government subsidy would be payable via the Franchising Director to franchisees in respect of socially necessary services. The aim was to enable the huge investment needs of the railway industry to be met, as far as possible, by the private sector and to encourage the transformation of the rail system from an operations-led business to a customer-led one.

The responsibility for a large amount of decision taking in the industry was transferred from the Secretary of State to the two new statutory officers, the Rail Regulator and the Franchising Director. British Rail was split into about 100 companies, almost all of which were sold to the private sector or closed down. The passenger services were divided into 25 separate units and sold to the private sector for periods of between seven and fifteen years. Other parts of the business, including the freight operations and the rolling stock companies, are also now in private hands.

4.1 Railtrack

More information on Railtrack can be found in Library Standard Note [SN/BT/1224](#). Railtrack went into administration in 2001 and in 2002 most of its functions were taken over by Network Rail, more information can be found in [SN/BT/1076](#) and [SN/BT/2129](#).

Railtrack became a separate Government-owned company on 1 April 1994 when the track, signalling and freeholds of stations, other buildings and operational land were transferred to it. It was sold to the private sector in May 1996. It employed about 11,000 people (of whom 6,000 were signalmen and supervisory staff) organised in seven geographical zones. It

owned and managed the vast majority of track, signalling and other infrastructure of Britain's railways. Train operators are granted access rights to the track and are charged for that access. Railtrack was in charge of co-ordinating train movements through central timetabling, train planning and signalling and was also responsible for the safety of the operational network. It operated the rail network, including signalling, and provided electricity for the train operators.

Railtrack was the freeholder of passenger train stations and light maintenance depots, which generally it leased to private sector operators. In most cases, stations and depots were leased to the passenger train operator which ran most of the services through the station or made greatest use of the depot. Railtrack retained responsibility for operating the 14 large mainline stations which had potential for commercial trading or property development and aimed to involve private sector operators in developing these stations. It also had a property portfolio including, as well as the stations, operational railway land, buildings and installations that it took over from British Rail.

Railtrack was sold to the private sector on 20 May 1996. In its report on the sell-off of Railtrack the National Audit Office said that the Government could have raised much more money by selling the company in a series of tranches as had been the practice with other nationalised industries. It calculated that sales proceeds might have been increased by at least £600 million if the Government had effected a phased sale and had retained 20 per cent of the shares or £1.5 billion if the Government had retained 40 per cent of the shares.²³

4.2 Passenger services

More information on passenger rail franchising can be found in [SN/BT/1343](#).

The Conservative Government's intention was that all passenger services should eventually be provided by private sector operators either acting as franchisees or as independent train operators. The railway network would be divided into a number of franchises, which would provide the bulk of passenger services. Government subsidy would be payable via the Franchising Director to franchisees in respect of socially necessary services that might not otherwise be provided. Competition in the provision of passenger services would be facilitated by allowing independent train operators (i.e. non-franchisee and not in receipt of subsidy) who could meet the necessary operational and safety standards, to have a right of access to the railway network ('open access' operators).

After April 1994 the passenger railway was restructured so that domestic passenger train services could be offered to the private sector to run on a franchised basis. British Rail reorganised its passenger services into 25 different train operating units. These units were gradually incorporated as subsidiaries of British Rail and run as separate 'shadow' businesses within BR. They paid access charges for the use of track and infrastructure, and rentals for stations and rolling stock, on the same basis as the franchisees have since the introduction of franchising 'proper'. Each operated under its own licence (granted by the Rail Regulator), its railway safety case (approved by the Health and Safety Executive) and a track access agreement with Railtrack (approved by the Regulator). A wide range of station and depot access agreements (also approved by the Regulator), property leases and other contracts were also required by each train operating business.

²³ NAO, [The Flotation of Railtrack](#) (session 1998-99), HC 25, 16 December 1998

Each of the 25 train operating companies (TOCs) was then offered for sale as a separate franchise. Private sector companies, management-employee buy-outs and, if the Franchising Director agreed (in practice he never did), British Rail could bid for the franchises through a bidding process overseen by the Franchising Director. The successful bidder acquired the TOC outright for a fixed number of years. The first franchises, South West Trains and Great Western, were awarded on 19 and 20 December 1995 and the first privatised services started operating on 4 February 1996. The last franchise to be agreed was ScotRail, which started operating in private hands on 1 April 1997.

4.3 Rolling stock companies

More information on the rolling stock can be found in [SN/BT/3146](#).

The Conservative Government's proposals for privatising the provision of passenger rolling stock were set out in January 1993 in *Railway Privatisation: Passenger Rolling Stock*. Most of the privatisation changes were introduced on 1 April 1994, including the establishment of three rolling stock companies – Angel Trains, Eversholt and Porterbrook – to lease rolling stock to the new railway operators. At the time the BR passenger fleet consisted of 11,000 vehicles ranging from brand new locomotives and coaches to those that were nearing the end of their economic life. Each company was given a portfolio of a similar mix of stock with a similar age profile. The new ROSCOs, as they came to be called, would be responsible for acquiring new trains when needed. They were not to have in-house maintenance capabilities but were responsible for specifying all maintenance and for contracting with maintenance suppliers for all heavy maintenance and refurbishment. The idea was that they should offer operating, rather than finance, leases which meant they carried most of the risk of holding and maintaining the rolling stock.

In 1993 the BR passenger fleet was said to have a book value of some £2 billion.²⁴ The proposed sale of the three companies was announced in March 1995²⁵ and bids for the purchase of these companies were invited in May 1995. Details of the contracts for the sales were announced on 9 November 1995²⁶ and were completed in early 1996. Eversholt and Porterbrook were acquired by their managements with development capital backing while Angel was bought by an external management team with the financial backing of Nomura International.

All three purchasers took on the existing train fleet and the Networker fleet on order at the time. They were also reported to be in a position to arrange additional funding for the continuing modernisation of the passenger railways through investment in new trains and refurbishment of existing rolling stock. All the purchasers committed themselves to introduce incentive schemes for employees, whether by way of participation in ownership or otherwise.

The actual sale price payable by the purchasers was approximately £1.8 billion but some £800 million was also paid to the Government in cash as dividends from the ROSCOs before the sale. The Government therefore maintained that total proceeds from the sale exceeded £2.5 billion, while opposition parties accused the Government of selling the companies "on the cheap".²⁷ However, some commentators – such as Roger Ford, then editor of *Rail Privatisation News* and not known as a fan of privatisation – was quoted as saying "This has

²⁴ DoT press notice, "New companies to manage passenger rolling stock after railways privatisation", 29 April 1993

²⁵ DoT press notice, "Mawhinney announces details of rolling stock sale", 20 March 1995

²⁶ DoT press notice, "Britain creates new train leasing market with £1.8 billion sale", 9 November 1995

²⁷ "BR rolling stock sold "on cheap" for £2.5bn", *The Guardian*, 10 November 1995

to be a good deal for the taxpayer. We have got rid of a fleet of trains, two thirds of which are geriatric, to the private sector for not a bad price".²⁸

In March 1998 the NAO published a report into the privatisation of the ROSCOs. Sir John Bourn, then head of the NAO, stated his belief that "the then Government saw major advantages in an early sale ... Their over-riding objective was to secure the sale of the companies as soon as practicable in 1995". Sir John further reported that the "chosen timing of the sale probably had an adverse impact on proceeds".²⁹ The NAO reported that it would have been possible to undertake a comprehensive valuation of the rolling stock companies on the basis of an analysis of cash flows, despite the absence of external comparators. They calculated that at the time of privatisation the value of the companies' future cash flows, under continuing public ownership, would have been £2.9 billion. The value obtained by the Government (sale proceeds, risks transferred and possible tax receipts) was considered to be only 'up to £2.2 billion'.³⁰

The Public Accounts Committee also published a report on the privatisation of the ROSCOs. The report concluded:

We note that the timing of the sale of the ROSCOs and its sequence in the overall rail privatisation programme was a key factor in the loss of value to the taxpayer as demonstrated by the much greater price achieved for them by the new owners shortly after privatisation.

We are concerned that the Department did not update their preliminary analyses of the cost of selling the ROSCOs ahead of the Train Operating Companies. More than a year ahead of the sale, they calculated the likely cost as being between £100 million and £300 million. The actual cost may have been much greater. We find their argument that there were too many uncertainties to arrive at a meaningful figure unconvincing. We are also surprised that the Department did not attempt an analysis of the wider benefits of early sale of the ROSCOs which they told us should be offset against the financial loss. We consider that the Department should have given more detailed consideration to the implications for value of the terms achieved.³¹

The ROSCOs are not subject to regulation under the *Railways Act 1993*, although they are subject to general competition law.

4.4 Freight companies

More information on rail freight can be found in [SN/BT/151](#).

The 1993 Act abolished BR's statutory monopoly of rail freight services. For example, two companies, National Power and DRS, started their own rail freight operations with their own locomotives and drivers. Freight operators obtained the use of the track through track access agreements with Railtrack. The Government's proposals for the privatisation of rail freight were outlined in *Rail Freight Privatisation*. The key proposals were:

- to split BR's existing trainload businesses into three geographical companies for transfer to private ownership;

²⁸ "BR's train fleet sold for £1.8bn", *The Times*, 10 November 1995

²⁹ NAO, *Privatisation of the rolling stock leasing companies* (session 1997-98), HC 576, 5 March 1998, p2

³⁰ *ibid.*, p4

³¹ PAC, *Privatisation of the rolling stock leasing companies* (sixty-fifth report of session 1997-98), HC 783, 10 August 1998, paras 26 and 35

- to establish the Channel Tunnel freight business on a sound commercial footing with the aim of privatisation as soon as possible;
- to invite proposals from the private sector on the future of the Freightliner domestic and deep-sea container business; and
- to privatise Rail Express Systems which carried Royal Mail letter traffic as soon as was practicable.³²

British Rail's freight business had been split into two operating units since 1988, Trainload Freight (TLF)³³ and Railfreight Distribution (RfD).³⁴ The trainload operations were restructured into three companies of comparable size based on geographical regions, but when it came to sell the companies, bidders preferred to buy all three as an entity. It was announced in February 1996 that the three companies were to be sold to North and South Railways, a consortium led by Wisconsin Central Transportation Corporation. The company had already purchased Rail Express Systems in December 1995.³⁵

Railfreight Distribution was the smaller of British Rail's two freight operating units, and had a more complex structure than the trainload businesses. The domestic trainload services offered by the contract services division of RfD (approximately one quarter of RfD's total turnover) was merged with the trainload freight companies prior to privatisation. The remainder of RfD was considered in two parts: Freightliner and Channel Tunnel. Freightliner offered a network of train services carrying containers between major ports and inland terminals, located in or near major centres of industry and population. This form of operation is known as 'intermodal' as it relies on road transport to convey the containers between the rail terminal and a customer's facilities. Freightliner was sold to a group of former managers. The remainder of Railfreight Distribution operated around 160 international freight trains a week through the Channel Tunnel, carrying containers, swap body traffic, cars and conventional freight. It was announced in March 1997 that it had been sold to English Welsh and Scottish Railway, or EWS (the former North and South Railways), although it took some time for clearance by the EC.³⁶

5 In retrospect

By the end of the 1980s the railways were operating more successfully than previously, but performance still left much to be desired. Privatisation was seen as an attractive option by the Conservatives for both political and economic reasons.

The consequent problems of the railway industry were probably less to do with privatisation itself than the way that it was done. Problems included:

- BR was loss making and the railways were going to continue to need public subsidy, unlike other privatisations;

³² DfT, *Rail Freight Privatisation: The Government's proposals*, 1993

³³ the vast majority of rail freight business - over 80% of total revenue - was concentrated in the "trainload" markets; trainload services are dedicated to individual customers and typically operate under contract; customers send full trainloads of commodities, principally coal, metals, petroleum and aggregates, from private siding to private siding in a single train movement

³⁴ Railfreight Distribution specialised in container traffic and distribution of finished products

³⁵ BRB press notice, "BR freight companies sold to North and South Railways", 24 February 1996 [5/96]

³⁶ DoT press notice, "Sir George Young announces go-ahead for sale of Railfreight Distribution", 13 March 1997 [PN 80]

- There was insufficient discussion about the structure of the privatisation, for example, Railtrack was not mentioned in the 1993 Act as Ministers had not decided exactly what form the company would take; also the requirement for competition was essentially a non-starter and open access was quietly dropped by the Regulator in 1993;
- There was no focus within the privatised industry for long term strategic planning; after 1994 there was no planning body in the industry with a similar duty to BR to monitor passenger and freight demand and develop a strategy to provide the capacity to cater for it;
- Railtrack lacked knowledge of the asset base, contributing to later problems (e.g. dealing with the aftermath of the Hatfield crash);
- The desire to complete the privatisation prior to the 1997 General Election meant that in some cases wrong values or methods of sale were used (e.g. in respect of the rolling stock companies);³⁷
- BR was broken up into around 100 component companies, including: Railtrack; 25 train operating companies; three rolling stock leasing companies; five freight operators; and 19 maintenance suppliers. Splitting the track and the operating part of the company was not in itself unworkable but the resulting contractual base of the relationships between companies meant that often the wrong message was conveyed (e.g. that punctuality was more important than safety). Furthermore the sanctions available to the regulatory authorities were unwieldy (e.g. a train operator could not be fined for a breach of the franchise agreement, however serious, if it was unlikely to recur). Finally, the legalistic structure fostered a confrontational and antagonistic atmosphere amongst the individual operating companies and between the operating companies and Railtrack, whereas co-ordination and co-operation was perhaps needed;
- A lack of clarity about role of the regulators led to confusion between role of the Franchising Director and the Rail Regulator;
- There were frequent and well-publicised shortcomings in a range of network benefits, such as impartial retailing of tickets, the national rail enquiry service, and passenger compensation (these network benefits were supposed to be protected under privatisation, so passengers could make seamless journeys and receive consistent information to help them plan those journeys); and
- Railtrack in particular suffered from poor management. It appeared to be inept at estimating the costs of large projects and it managed its subcontractors badly. It also failed to reconcile its public interest objectives with the interest of its shareholders to maximise profits.

But the history of the railways in the immediate period after privatisation was not all bad. As the centre-left think tank the IPPR said in a 2002 report:

In spite of the short-term difficulties, railway reform should recognise the strengths of the current structure as well as addressing its weaknesses. The record of the railways

³⁷ though part of the problem by this point was uncertainty caused by Labour being well ahead in the polls and committed to renationalisation if it won the 1997 election

since privatisation has been mixed. Until the Hatfield crash in October 2000, there was strong growth in both passengers and freight. Railways were carrying more passengers than at any time since World War Two. Punctuality and reliability, on passenger's charter standards, were overall slightly better than in the final years of state ownership. Standards of safety were gradually improving, notwithstanding the major fatal accidents at Southall, Ladbroke Grove and Hatfield. Privatisation arguably introduced some useful innovations, notably competition in the delivery of passenger and freight services, performance incentives linked to the passenger's charter, transparent regulation, security of funding and access to private finance for investment.³⁸

³⁸ IPPR, *Getting back on track*, June 2002, executive summary