

Dear Sir/Madam,

Measuring Consumer Prices: the options for change

This letter forms the Department for Transport's response to the above consultation.

The Department welcomes this consultation and supports the UK Statistics Authority in its consideration on the future development of the UK's range of consumer price statistics.

There are a number of questions raised in Section Three of the consultation, in relation to the Retail Prices Index (RPI), which the Department has an interest in.

We recognise the recent change in status of the RPI, which is no longer designated as a national statistic, and note that the methods used to produce the RPI are not consistent with international best standards. The RPI is deeply enmeshed and widely used within the transport industry and therefore decisions related to the future of the RPI will have an impact on work within the Department. Transition costs and the timeframes involved in moving to a new index would be considerable but would depend on the specific contracts involved. We would welcome working with you on these issues.

We note the Recommendation 7 in *UK Consumer Price Statistics: A Review*, which concludes that the priority should always be to make the main measure of inflation as good as possible. Given the importance of the RPI, the Department believes it would be beneficial for the ONS to continue to ensure that it is as robust a measure as possible whilst it is still being used. From the Department's perspective, however, we would ask you to note that any significant changes to the measure, for example, altering formulas could lead to the termination of contracts.

Uses of RPI and CPI:

The RPI is used throughout the rail industry to index payments. The payments indexed to the RPI include franchise payments between DfT and train operators, the Network Grant paid to Network Rail and the access charges Network Rail charges train operators and it will be used in a range of other contracts within the industry. Network Rail's debt repayments are also indexed to the RPI.

The RPI is used in the regulation of national rail fares, with the maximum annual increase allowed each year for a large number of fares being tied to a formula based on the RPI. The main factors behind the choice of the RPI are historic precedent, the desire for a general measure of price inflation and the availability of independent forecasts. Fares regulation is linked closely to the indexing of premiums and franchise costs. Given the interdependencies, it is important that if there are any changes to using the RPI, all changes occur at the same time across the rail industry. Fare changes are widely reported so it would also be imperative that any measure used could be easily understood by the public and published as part of the ONS's main inflation release.

The RPI is used also in the appraisal of transport projects to forecast fuel costs, as for petrol and diesel forecasts both resource costs and duty are assumed to grow in line with the RPI. It is also used in forecasts of rail industry costs and income, since these are currently tied to the RPI. All other costs used in transport modelling are indexed using the GDP deflator published by the Treasury. This has been recommended since 2012, in place of the RPI which was previously used. The reason for this change was that the wider coverage of the

GDP deflator, reflecting prices of all domestically produced goods and services, makes it more appropriate for deflating public expenditure series.

The Department uses mainly the RPI, the CPI and Average Weekly Earnings indices for forecasting and planning income and expenditure, checking Pension Fund calculations and benchmarking.

DfT is liable also for funding repayments of interest and principal on debt instruments. One of the tranches is index-linked, and specifically linked to the RPI. There are also a number of guarantees linked to the RPI for pensions in previous British Rail schemes.

Local authorities are recommended to use CPI to calculate fare changes related to bus concessions. Therefore, there are a number of local authorities for whom the CPI index influences the bill they are due through the reimbursement model DfT provides.

Uses of sub-indices:

In addition to using the RPI, the Department also uses some of the sub-indices of the RPI and the CPI to understand the cost of transport and how it is changing. In particular this includes the two RPI sub-indices All Motor (CHBK) and Fares and other travel costs (CHBR) as well as the further four sub-indices for motoring costs (purchase of vehicle, maintenance, petrol & oil, and tax & insurance) and the further two sub-indices for fares (rail fares and bus & coach fares). We also use the equivalent Consumer Price Index sub-indices, but there is an issue in that the RPI and CPI transport indices have different coverages and were set up to answer different questions. In particular we would lose some information if we moved from the RPI to the CPI:

- We often have a need for long run data as transport is a long run business, and the RPI runs back much further than the CPI. The current RPI figures go back to 1987, and we have linkages to data running back to the mid-1970s (although the furthest we usually go back is 1980). We are aware of the work taking place on back casting the CPI and this will give us a top level transport series, although currently there are some tax adjustments with an estimate of motor tax removed. However, this doesn't help with sub-indices, for which we would have to have a shorter time series
- The RPI motoring sub-indices include a specific category for "Tax and Insurance" (DOCV) which is not present in the CPI. The CPI handles tax and insurance differently to the RPI:
 - Motor insurance appears in a different category in the CPI. In addition the motor insurance in the CPI only gives the difference between the premiums and the claims (which affects the weighting), whereas the tax and insurance category in the RPI includes the full cost of the insurance. The claims in both are netted off against the repairs and servicing categories
- There are also some specific issues relating to road and rail fares:
 - The CPI "passenger transport by rail" includes Eurostar fares
 - The CPI "passenger transport by road" includes taxi, minicab and charges for home removals – this is an issue in comparing with RPI bus & coach fares

The department looks forward to seeing the results of this consultation and the future development of the consumer price indices.