

Response to ORR's December 2016 Charges and Incentives Consultation

This pro-forma is available to those that wish to use it to respond to our consultation. Other forms of response (e.g. letter format) are equally welcome.

Please send your response to pr18@orr.gsi.gov.uk by **9 March 2017**.

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Please make any comments regarding the questions in the accompanying text box. We welcome comments in relation to the information outlined in both the consultation document and supporting documents, or regarding the policy areas more generally.

Chapter 2: Infrastructure Costs

Fixed cost charges:

1. Do you support our proposal to levy fixed cost charges on all operators, including open access operators, to the extent that they can bear them (option 2)?

Yes.

Fixed cost freight charges:

2. Do you support our proposal to simplify the current charging regime by having a single freight mark-up charge?

Yes.

Fixed cost freight charges:

3. Do you support the recommendation to apply Network Rail's cost allocation methodology (discussed in this chapter) to freight mark-up charges?

Yes.

Station charges:

4. **Long term charge (LTC):** Do you support our recommendation that the methodology for the LTC at managed stations be recalibrated?

Yes.

Station charges:

5. **Qualifying expenditure (QX):** Do you agree with our recommendation that we support the work to make total QX charges more transparent at both managed and franchised stations?

Yes.

The current system of unregulated QX charges seems difficult to justify. It gives Station Facility Operators (SFOs) and Network Rail (in the case of managed stations) a clear monopoly with respect to other franchised train operators (who are effectively required to make a certain number of calls at each station and whose demand elasticity to QX charges is therefore probably very low). It also adds an extra layer of uncertainty to the franchising process (SFOs will be unsure how much exactly they will be able to extract in QX charges and non-SFOs will be unsure how the level of charges they may be liable to pay).

We support the ORR in its proposal to require the publication of QX charges, and we would encourage it to go further and request the publication, on a consistent and disaggregate basis, of information relating to station management costs and outputs (e.g.: quality of services provided). This additional information would be essential in order for the ORR and other interested parties to carry out a meaningful benchmarking exercise to determine the efficient level of station maintenance and operation costs.

Chapter 3: Short-run variable charges package

Variable usage charge (VUC):

6. Do you support our recommendation not to make fundamental changes to the VUC for PR18?

Yes.

Variable usage charge:

7. Do you have any suggestions for 'recalibration' style changes to the VUC you would like

to see considered for PR18 implementation?

No.

Capacity charge (CC):

8. Do you support our recommendation not to replace the CC with adjustments to Schedule 8 benchmarks?

Yes

Capacity charge:

9. Do you think we should: (a) retain the existing CC (but remove the caps on open access, freight and charter operators); (b) remove the existing CC and recover lost revenue through fixed cost charges; or (c) do you have any alternative proposals?

We are minded to support option (a). Following the changes made in PR13, the capacity charge does play an incentive role, albeit imperfect, and this would be strengthened if the caps were removed on open access, freight and charter operators.

However, we would like to remind the ORR of the position we have held throughout PR13 and into PR18, which is that the very limited variation in the capacity charge levied between time periods and between days of the week (in particular, Sunday v other days) significantly undermines the objectives of the charge. We would point to the example of subsidised off-peak services (e.g.: late evening or Sunday services), which impose little or no capacity costs on the network, but are typically levied the same capacity charge as peak services operating on the same route. The consequence of this anomaly is that certain off-peak services, which would operate under a more differentiated charging structure, may not do so, with a resulting loss of efficiency.

We would therefore encourage the ORR to consider introducing greater differentiation by time period and day of the week into the capacity charge.

Traction electricity charge:

10. Do you support our recommendation to keep the loss incentive mechanism?

Yes.

Electricity asset usage charge (EAUC):

11. Do you support our recommendation that the EAUC not be altered, beyond recalibration, in PR18?

Yes.

Coal spillage charge (CSC):

12. Do you support our recommendation to abolish the CSC?

Yes.

Chapter 4: Contractual Incentives Regime

Schedule 8:

13. **Passenger compensation:** What are your views on the options of passenger compensation recovery and improving the transparency of compensation relating to Network Rail's actions?

The consultation document provides a comprehensive and robust assessment of the advantages and disadvantages of different options. We agree with the ORR's assessment that neither of the options being considered is clearly superior to the alternatives.

As a matter of principle, passenger compensation recovery by train operating companies directly from Network Rail should only be considered if incentive effects, and resulting benefits, are expected to offset the additional administrative cost, complexity and uncertainty. Our current view is that this is unlikely to be the case though we would support further work in this area.

Schedule 8:

14. **Approach to setting benchmarks:** Do you support our recommendation to only make changes to delink passenger operator benchmarks and Network Rail benchmarks for freight operators from past performance (but to leave the approach to the other benchmarks unchanged)?

Yes.

Schedule 8:

15. **Measure of passenger operator performance:** Do you support our recommendation to change the measure of passenger operator performance to one based on the delay caused to other operators?

Yes.

Schedule 8:

16. **Sustained poor performance (SPP) provisions:** Do you support our recommendation

to limit SPP to costs compensation only?

Yes, conditional on revenue losses continuing to be recovered through Schedule 8 claims.

Schedule 4:

17. Do you support our recommended prioritisation of schedule 4 issues? If you think we should reconsider any of the areas we have de-prioritised please submit supporting evidence.

Yes.

Schedule 4:

18. Do you wish to submit relevant evidence regarding: (a) processes associated with planning possessions; and/or (b) planning alternative arrangements to deal with planned disruption (e.g. the notification that is needed to arrange bus replacement services)?

No.

Aligning operator and network rail incentives:

19. Do you have any views on how financial incentives could be improved to encourage collaboration between Network Rail and operators to reduce industry costs?

As we have argued in our relevant response to PR13 we don't think the REBS mechanism is likely to be effective. This is largely because (a) there are significant asymmetries of information between Network Rail and TOCs, (b) the impact of specific interventions by any one agency are difficult to isolate from background trends and from the actions of other stakeholders and (c) because the effect of actions by one stakeholders on others are small in scale.

We believe that any measures that increase transparency and our collective understanding of cost information and cost drivers would have a positive effect on the ability of any one stakeholder to influence the behaviour of others, and on their willingness to work collaboratively with other agencies.

More generally, we believe there are fundamental challenges in the way Network Rail is regulated, which render it virtually un-accountable to its direct customers and to stakeholders other than the DfT and the ORR. We have previously argued that the devolution of franchising powers and infrastructure funding to local stakeholders such as transport authorities and sub-national transport bodies would enable these organisations to challenge and incentivise the behaviour of both TOCs and Network Rail more effectively than DfT or the ORR are able to, by virtue of their greater knowledge of the local context in which the rail network operates.

Aligning operator and network rail incentives:

20. Do you have any views on the cost categories you think could be controlled by operators and whether these costs would be suitable as the basis of a potential future mechanism?

No views.

Any other points that you would like to make

Thank you for taking the time to respond.