

Response to consultation: Network Charges – A consultation on how charges can improve efficiency

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Instructions for Responding to the Consultation

We would appreciate it if long responses had a summary of the key response points.

Summary of key response points:

- The current charging structure matters and has a direct impact on the viability of rail freight.
- Greater clarity over Network Rails fixed costs is to be welcomed.
- An improved structure of charges could drive positive industry behaviours.
- RDG's 'states of the word' is a useful exercise but needs expanding to cover likely negative impacts.
- The 'gaps' identified cover the principal issues.
- Enhanced focus on the 'wider external impact' of any changes is essential.
- We support the development of the 'infrastructure costs package' in terms of greater clarity of Network Rails fixed costs but are wary about increased costs.
- We do not support the further development of the 'value based capacity' package.
- Any changes to the structure of charges which stabilise and protect freight operators from cost increases is to be welcomed.
- There are improvements to existing freight related variable charges which could be made for wider benefit.
- We would welcome the further development of the 'charge calculator' and 'complexity test'.
- We welcome the focus on freight in the 'next steps' and in particular the development of a mechanism to calculate the benefits of rail freight.

Summary of consultation questions

Chapter 1 Questions	Response
<p>Q1. How much does Network Rail's structure of charges matter today?</p>	<p>Network Rail's current structure of charges has a significant and direct impact on Freight Operators such as Colas Rail particularly through charges such as the 'Variable Usage Charge'. Given the high level of competition within the rail freight industry, both internally and against alternative modes of transport such as road, the current structure of charges plays a significant role in determining how competitive rail freight can be. The variable nature of the charges, in that they can and do change with each Control Period, also exposes rail freight to cost risk which again can render rail uncompetitive compared with rival haulage modes.</p>
<p>Q2. What issues could a new structure address?</p>	<p>The new structure will bring greater clarity over the build-up of Network Rail's costs. This would provide the industry with greater clarity on the costs associated with the various parts of the Network and provide a foundation for allocation of costs as part of a wider charging structure as well as identifying enhancement schemes that deliver the most value.</p> <p>If the new structure is given the appropriate measures to ensure that Rail Freight is fairly treated based on its wider value to society, it could also assist in limiting the exposure to the volatility of charges between control periods as well as allowing fair access to the network for all.</p>
<p>Q3. Can you provide examples of behaviours that would change within your organisation or elsewhere in the rail industry with an improved structure of charges?</p>	<p>A primary example of improved behaviours within the industry that could be brought about by an improved structure of charges can be seen with behaviours resulting from the Variable Access Charge (VAC). This charge directly incentivises operators, particularly in the freight sector to actively utilise, and invest where necessary in improved rolling stock, such as wagons with track friendly bogies, in order to reduce the impact on Network Rail's infrastructure. This reduces the VAC which helps fund the investment that such rolling stock requires.</p> <p>If a new and improved structure of charges were to be implemented which stabilises and protects freight operators from exposure to changes to charges, it could drive improved behaviours on a number of counts. In particular, the previously referenced incentive to invest and/or utilise improved modern rolling stock would likely be strengthened with reduced risk. This not only benefits the impact on the Network, in terms of wear and tear but also has potential benefits to performance too. Given high levels of performance are essential to running an increasingly busy mixed network, the benefit of this</p>

	<p>cannot be overstated.</p> <p>A government subsidy as an alternative means of protection would likely also drive improved behaviours such as those outlined above. It is important to note however that a guarantee over the longevity and validity of such a subsidy would be essential to driving confidence to invest amongst freight operators. Credible subsidies could also be introduced to drive CO2 reduction from modal shift from road to rail.</p> <p>Other areas of charging that could drive behaviour would be to offer credible discounts for running longer routes, that freed up benefits to the wider railway. Also discounts could be offered for less busy time slots to try and regulate capacity throughout the day.</p>
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Chapter 2 Questions	Response
<p>Q4. To what extent does the use of scenarios, in the form of the RDG 'states of the world', help to understand the likely effectiveness of future charging structures?</p>	<p>Overall, the RDG's 'states of the world' provides a useful exercise in articulating potential outcomes resulting from improved future charging structures.</p> <p>Whilst highlighting a number of potential outcomes and highlighting the benefits of why that approach has been selected, it does however over simplify or fail to mention likely negative impacts resulting from proposed changes to the charges structure.</p> <p>As an example, 'states of the world no.6' discusses potential changes to how capacity is allocated. The impacts of this could be considerably negative for freight and open access operators whereby under this scenario franchised passenger operations are potentially given preferential treatment regarding capacity allocation as they are deemed to be the most beneficial.</p> <p>Likewise, 'states of the world no.1' discusses the proposal that operators effectively pay for enhanced Network capability and capacity as the primary beneficiaries. Whilst this proposal certainly has some merits, it fails to take into account the wider market forces that would likely render it unviable from a freight operator perspective. As an example, a franchised passenger operator may be incentivised to directly fund or significantly contribute to a particular enhancement scheme that benefits them on the basis that the franchise is for a suitable duration of time. In the rail freight market, commercial contracts are typically in place between 1-5 years with little protection if the wider</p>

	<p>industry/commodity being served suffers decline such as that recently seen in the coal and steel markets. As such, it is unlikely that a freight operator would be able to justify investment in a specific scheme regardless of short term benefit to them as there is no guarantee of a long term return in investment unlike a long term franchised passenger operator.</p> <p>It is our view that the RDG's 'states of the world' exercise should be enhanced to consider the wider implications of each of the scenarios, both positive and negative so that a more holistic, informed and complete discussion can be held.</p>
<p>Q5. Are the high-level gaps (in Figure 4) a good starting point for developing solutions? Would you have expected to see any other high-level gaps and, if so, what are they?</p>	<p>We believe that the gaps identified broadly act as a useful starting point for developing potential solutions.</p> <p>The reference to the uncertainty caused by the changes to the structures of charges is a particularly sensitive issue to freight operators, not least as often commercial contracts span Control Periods exposing operators to significant levels of risk.</p>
<p>Q6. Do the assessment criteria accurately reflect the main factors we should consider for assessing the impact of options?</p>	<p>We believe that the assessment criteria does accurately reflect the main factors that should be considered when assessing the impact of options.</p> <p>In particular we would stress the importance of focussing on the 'wider external impact' criteria as we believe this has the potential to highlight risks to freight operators which otherwise may not be apparent. Examples of wider external impacts are highlighted in the response to Q4.</p>

Chapter 3 Questions	Response
<p>Q7: To what extent do the packages of options represent the key strategic choices available to improve the existing charging structure?</p>	<p>The packages highlighted attempt to tackle a number of the fundamental issues surrounding the current industry structure of charges.</p>
<p>Q8. Would you expect the infrastructure costs package to deliver more benefits than the value-based capacity package at this stage and, if so, why?</p>	<p>We believe that the infrastructure costs package would deliver more benefits at this stage than the value based capacity package as the Value based capacity (to user and society) would need very careful calibration across all users in order to provide a fair and incentivised solution. However for the infrastructure cost package great care will be needed to taken for freight users to ensure that the allocation of cost and/or applied subsidy allows fair access to network capacity at a cost that is sustainable</p>

	<p>against other modal providers.</p> <p>Fundamentally understanding the drivers behind Network Rail's costs is essential and should drive improved decision making around investment and drive cost to benefit optimisation without a detrimental impact on quality. Whilst we would welcome improved understanding of area specific costs we would be wary of them being passed onto operators in the form of a new charges structure. Higher charges to operators using particular parts of Network Rails infrastructure could result in freight and open access operators being effectively priced off some parts of the Network unless a mechanism existed within the charges structure to protect or subsidise against any increase in cost.</p> <p>For value based costing to work across the industry, it would need to be calibrated to take into account the wider value to users and society. This is a significant task and if not done correctly, the higher charges associated with parts of the Network deemed to have most value to end users could effectively force freight, open access and lower usage passenger operators from using them. Whilst this may generate some intended benefit, such as reducing capacity constraints on key corridors, it could have a significantly detrimental impact to the wider value of the railway to society as a whole.</p> <p>Increasingly the end customers who utilise and rely on rail freight demand reduced transit times. If freight operators are forced to use less congested, longer routes then there is a real risk that traffic could be lost unless subsidies/discounts are given for this.</p> <p>In summary there is a risk around how the value and benefits of the Network and wider Society are calculated under the value based capacity package. Given the inherent differing nature between passenger and freight operators and their traffic, coupled with the differing nature of commodities, there is a risk that a sound and agreeable calculation method may be very difficult to identify.</p>
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Chapter 4 Questions	Response
<p>Q9. We welcome your views on our proposal to prioritise further development of the infrastructure costs package.</p>	<p>As referenced previously, we welcome greater understanding and transparency regarding Network Rail's fixed costs.</p> <p>Given the potential benefits of the infrastructure costs package, we support its further development but would urge particular focus around the benefits, practicality and impacts on freight operators. The infrastructure costs package represents a potential significant increase in freight operator's costs which would need to be</p>

	factored in to any development particularly around how this greater exposure could be mitigated.
Q10. What costs and benefits do you see with the infrastructure costs package? Do you think our draft impact assessment is missing any significant impacts or has misrepresented any impacts?	<p>Benefits; Greater transparency over Network Rail's fixed costs is to be welcomed and we agree with the benefits outlined in this section particularly around the enhanced ability to challenge and make decisions based on quality accurate data.</p> <p>Costs; The impact on freight operators resulting from the implementation of such a package could be significant and far ranging. The impact on freight operator's costs could impact the ability for rail freight to compete with rival modes of transport and could force freight operators to use alternative less congested routes which, whilst creating some benefit, could again put rail freight at a disadvantage compared to rival modes of transport in terms of journey times, cost and Network capability (e.g. gauge).</p>
Q11. To what extent do you think the benefits of this package can be realised through more information, rather than through the use of charges?	<p>Undoubtedly greater understanding, transparency and knowledge of Network Rail's fixed costs would drive improved decision making regardless of whether an associated charging regime were put in place.</p> <p>Due to the complex nature of reflecting any changes to the structure of charges specifically to freight operators, it may be the case that improved information is the first stage of a longer consultation process.</p>

Chapter 5 Questions	Response
Q12. We welcome your views on our proposal not to prioritise further development of options based on the value of capacity.	<p>We agree with your position not to prioritise development of the value of capacity at this time.</p> <p>The value of capacity if combined with the wider benefits to society including quantified reduction in both CO2 and heavy haulage on the roads could be a viable mechanism for the future. However it seems unlikely that an accurate methodology could be developed in the short term which successfully reflects the value and wider societal benefits that rail freight realises.</p> <p>If not correctly developed and calibrated, this could create a situation where deemed higher value passenger services are always given priority over freight services. This would be to the detriment of the rail freight industry, the economy and to society as a whole.</p>

<p>Q13. What costs and benefits do you see with the value-based capacity package? Do you think our draft impact assessment is missing any significant impacts, or has misrepresented any impacts?</p>	<p>Benefits; There has been much work undertaken by the freight operators and Network Rail to rationalise the number of freight paths in the WTT in order to make better use of capacity. We feel initiatives such as these ultimately serve a similar purpose to the stated aim but without the consequences.</p> <p>Costs; As referenced in Q12, we foresee a number of issues associated with the value based capacity approach. Principally such an approach could result in rail freight being at a disadvantage to passenger operators (and potentially to other freight operators) which could limit rail freights viability and attractiveness to customers from a cost and feasibility point of view.</p> <p>Impact Assessment; We believe that the impact assessment could do more to highlight the specific risks and impact associated with this approach when considering freight operators. This in turn would aid the overall discussion and highlight the real risk associated with such an approach.</p>
<p>Q14. Would you expect a better understanding of costs to be an essential precursor to value-based charges?</p>	<p>We would expect a better understanding of costs to be an essential precursor to value based charges as to be done correctly the cost of capacity (and any potential increase) for each area of the network needs to be know a part of the calibration of charging based on value to users and society.</p>
<p>Q15. To what extent do you think the benefits of this package can be realised through more information alone, without passing that into charges?</p>	<p>We strongly believe that the development of more information on the cost of the infrastructure and the relative/actual value to users and society of running differing types of trains at different times would be of huge benefit to developing optimised solutions for the railway as a whole. For example there may be a business case for longer less frequent trains and associated infrastructure that would not self-fund in the passenger operator environment alone, but when the wider value of the paths that could potentially be released through this initiative are fully quantified and included, the proposition may then be viable to proceed with. Without the information readily available then these possible improvement scenarios remain subjective at best.</p>

Chapter 6 Questions	Response
<p>We welcome your views on our proposal to develop the package of improvements to current short-run charges further.</p>	<p>We would support any proposal which stabilises the variable costs freight operators are exposed to such as the ‘Variable Usage Charge’ as the risks associated with it can create uncertainty.</p>

	<p>We would point out however that whilst charges such as the ‘VUC’ can and have encouraged positive behaviours such as investment in improved track friendly rolling stock, the level of such investment is often significant. As previously stated, commercial freight contracts often only exist between 1-5 years in duration meaning such investment in improved rolling stock is not guaranteed to provide a return on investment. As such, whilst charges such as the ‘VUC’, and any subsequent changes to variable charges which stabilise/protect freight operators may encourage proactive positive behaviours there are other factors which may mitigate this.</p> <p>Finally, whilst we note that under the proposals a situation may arise where, for example in the case of greater use of geographic disaggregation, decisions about where track friendly or track un-friendly rolling stock can and can’t be used we would highlight the impact this could have on freight operators in restricting the number of routes available for use where modern rolling stock isn’t present.</p>
<p>Q16. What options would you expect to see in a long list of improvements to Network Rail’s short-run variable charges?</p>	<p>We would expect to see greater protection for freight operators being exposed to changes to variable charges such as the ‘VUC’. Commercial contracts often span Control Periods which brings about a significant risk that charges could significantly increase with a change in Control Period which impact the viability of a commercial contract for the remainder of its duration.</p> <p>We also believe that variable charges such as the ‘coal spillage charge’ could be improved. Although Colas Rail do not currently haul coal as a commodity and as such do not pay the ‘coal spillage charge’ (although we have in the past), we believe that there is a lack of clarity over how funds raised from the charge are used by Network Rail. In our view if such a charge is to continue then the funds it generates could be better utilised and decided by the wider industry in collaboration with Network Rail. It is also worth noting that given the decline of the ESI coal market that the effectiveness and purpose of such a charge should also be reviewed as the amount generated from it will continue to decline.</p> <p>On a similar note we would welcome greater clarity/transparency on the volume incentive and its mechanism. Again, whilst Network Rail does currently engage with freight operators on how to grow traffic to meet the volume incentive, more work could be done to improve how the volume is baselined/forecasted and how decisions could be made. The volume incentive is also unable to respond to significant/abrupt shifts in the rail freight market (such as the decline of ESI coal) resulting in a negative impact to the wider industry.</p>

Q17. What options do you see as a priority for this package?	We believe the options highlighted in Q16 are a priority for this package.
Q18. What costs and benefits do you see with this package?	<p>Benefits; Improved stability to variable charges is essential to removing uncertainty from the rail freight market. Improving the mechanisms of charges such as the coal spillage charge and volume incentive, as outlined in Q16 could also be of significant benefit to the industry.</p> <p>Costs; If improved stability can't be gained then the risks to freight operators and the associated uncertainty such instability creates could be significant.</p> <p>As highlighted at the start of this section, would be wary around any outcome which reduced the geographical/route availability to freight operators operating older stock that does not benefit from track friendly bogies.</p>

Chapter 7 Questions	Response
We would welcome comments on how charges might apply to open access in future. In particular, we would welcome comments on:	N/A as section primarily focusses on open access passenger operations as set out in paragraph .150.
Q19. whether open access operators should face charges implemented under the infrastructure costs package;	N/A as section primarily focusses on open access passenger operations as set out in paragraph .150.
Q20. what forms of adjustments to charges might be appropriate for open access operators, relative to franchised operators;	N/A as section primarily focusses on open access passenger operations as set out in paragraph .150.
Q21. how current incumbent open access operators should be treated; and	N/A as section primarily focusses on open access passenger operations as set out in paragraph .150.
Q23. Would you like to see either of the complexity options developed further?	<p>We would support the development of both complexity options further. In particular we believe that the creation of a 'charges calculator' would be a useful mechanism for operators (both freight and passenger) to work out likely charges and subsequent costs which would improve visibility and drive improve costing.</p> <p>We would also support the 'complexity test' as any greater clarification on how charges are levied is to be</p>

	<p>welcomed. We would also welcome retrospectively applying the test to any remaining charges to ascertain whether greater clarity could be realised which we feel would be of benefit to the wider industry. Rail freight's wider customers, and potential new ones, often comment on the perceived complexity of the industry and as such any greater clarity is to be welcomed.</p>
<p>Q24. Are there other options you would like assessed to reduce complexity?</p>	<p>We're satisfied that the two options highlighted in Q23 are sufficient if developed in tandem to reduce complexity.</p>
<p>Q25. What costs and benefits would you expect with these complexity options?</p>	<p>Benefits; The ability to accurately calculate charges, and as such cost, would be a significant benefit to operators when establishing budgets, targets and driving positive behaviours. Likewise any reduction in the complexity of charges can only be a positive outcome.</p> <p>Costs; The creation of a charges calculator would likely be complex owing to the complex nature of the charges structure. It would also need to be accurate in order to be of greater use.</p>

Chapter 8 Questions	Response
<p>Q26. In chapter 8, we started to highlight issues associated with implementation of a new charging structure and potential actions to alleviate negative impacts. Do you have any views on options for implementing a new structure and what would be the impacts of these options?</p>	<p>We welcome the focus on freight operators and in particular the consideration relating to groups, such as freight operators, who are highly sensitive to rail charges. We also welcome the focus on developing mechanisms to establish and proportionally recognise the wider benefits of rail freight. We believe establishing such mechanisms could be achieved through existing forums such as the RDG or via a separate work stream involving freight operators, end customers and trade bodies such as the Rail Freight Group.</p> <p>We believe that 'shadow charging' could be a useful means of establishing the likely impact of changes to the structure of charges. Ultimately, the simulation of any proposed changes prior to implementation is essential in order to garner an accurate view as to the short, medium and long term impacts on the users of Network Rails infrastructure.</p>
<p>Q27. We understand the structure of charges has the potential to impact different groups in different ways. In developing the options in this consultation (particularly in the draft impact assessments),</p>	<p>As discussed in previous responses, we feel that whilst the impact assessments have recognised the potential impact on freight operators of any proposed changes to charges, the implications highlighted are somewhat vague and need to recognise the wider impact on the rail freight market. The impact assessments also need to consider how the rail freight market is structured and operates as it is directly relevant to the impact of charges.</p>

have we drawn out the implications for different groups? Please explain your response.

As previously referenced, the comparative duration of commercial contracts needs to be considered when discussing the impact of changes and the aspirational behaviours it intends to drive such as investment in track friendly rolling stock. Likewise, the impact of potentially restricting freight operators to certain parts of Network Rail's infrastructure needs to be fully considered in terms of the impact this would have on freight customers and the overall viability of moving rail freight.

If there is anything else regarding the current structure of charges that you would like to feedback to the Office of Rail and Road, please include this in your response.

How to respond

We would like your views so please get in touch by responding to this consultation by **4 March 2016**. You might find it useful to use this pro forma to record your responses. Please send responses to: Orr.Structureofcharges@orr.gsi.gov.uk.