Annex B - Glossary

December 2016

This document has been published alongside 'Improving incentives on Network Rail and train operators: A consultation on changes to charges and contractual incentives'.

We have tried to keep the language in this consultation simple but it is necessary to use some technical terms in places. This glossary provides more detail regarding the terms used in the consultation document.

Access Charge Supplement (ACS)

Schedule 4 payments to franchised passenger operators are part-funded through the ACS which is paid to Network Rail by franchised passenger train operators in return for receipt of full Schedule 4 compensation.

The total ACS is intended to reflect the amount Network Rail is expected to pay out to franchised operators in Schedule 4 compensation as a consequence of maintenance and renewals activities over the control period.

Alliances

Alliances describe a wide range of different relationships from project-based partnerships through to potentially long-term and comprehensive commercial arrangements covering a wide range of activities carried out by Network Rail routes and train operators. The common factor is that Network Rail and a train operator reach agreement to work together more closely and share the benefits of doing so, within the framework of their existing individual accountabilities and responsibilities.

Avoidable costs

Avoidable costs are costs that would no longer be incurred by Network Rail if a particular type of traffic, or increment of traffic, no longer ran on the network. For example, freight avoidable costs refer to the costs that would be avoided if freight trains no longer used the network. The time dimension over which costs would be avoided can vary – e.g. short, medium or long-term.

Charter operators

Charter operators are train operators that generally run excursion trains or privately hired trips which do not appear in the National Rail timetable, do not carry passengers at ordinary fares and which operate on a bespoke basis.

Common costs

Common costs, as used in our document and in Network Rail's cost allocation pilot study report (available here), refer to those costs which are not linked to or directly attributable (cost attribution and cost drivers are defined in this glossary) to specific services on the network. These costs would still be incurred even at minimal traffic levels (of say one train per day), as long as existing network connectivity is preserved.

Control period

The control period is the period over which the ORR sets Network Rail's funding, charges and outputs. Control period 5 runs from 1 April 2014 to 31 March 2019. We expect CP6 to run from 1 April 2019 to 31 March 2024.

Cost allocation

While cost attribution (defined in this glossary) refers to identifying the factors that drive costs, cost allocation is how we decide to allocate these costs to different users, principally for the purpose of charging. The appropriate way to allocate different cost categories will depend on the results of a cost attribution exercise plus some other factors. For example, if attribution exercises are unable to link a cost with a specific driver of these costs, we may have to use another method to allocate these costs to users. Even if costs can be directly attributed to a train service/operator, we may want to consider which metric to use for example to allocate the charge (e.g. a lump sum charge for each year of the control period regardless of operator behaviour or a charge based on a metric the operator can control to some extent such as per train km). As part of our December 2015 consultation[1] we published a draft impact assessment on the 'infrastructure costs package'. This document provides more information on what we mean by cost allocation.

Cost attribution and cost drivers

The attribution of costs is the process of identifying the factors that are causing the costs to be incurred (i.e. the cost-drivers). Costs are attributable to a use if changes in that activity lead (immediately or over time) to changes in the overall level of cost. For example, the cost of electricity infrastructure on a line could be attributed to any electric rolling stock, but not to those that are diesel powered. And signalling infrastructure provides use for particular geographic areas, and so could be attributed to those areas. As part of our

[1] Network Charges - a consultation on how charges can improve efficiency

December 2015 consultation[2] we published a draft impact assessment on the 'infrastructure costs package'. This document provides more information on what we mean by cost attribution.

Cost directly incurred

By costs directly incurred we mean costs incurred by the infrastructure manager as a result of allowing a particular train service to operate on its network. EU Directive 2012/34/EU, as transposed into UK legislation by The Railways (Access, Management and Licensing of Railway Undertakings) Regulations 2016, requires certain access charges to be set at the cost directly incurred as a result of operating the train service.

Cost-reflectivity

In this consultation, cost-reflectivity describes a situation where the charging structure allows costs to be attributed / allocated to those who cause the cost to be incurred. Cost-reflectivity has desirable qualities. For example, if users face the costs they impose, this will provide them with the appropriate incentives to reduce those costs, as this would subsequently feed into reduced charges.

The cost-reflectivity gap analysis published as part of our December 2015 consultation assessed where the existing charging structure has limited ability to drive down costs, encourage efficient decision making and to achieve value for money.

Counterfactual

The counterfactual is the scenario which we are comparing the options against. For the purposes of this assessment, we define the counterfactual as a 'do nothing' scenario. This means no substantial changes to the structure of charges for access to Network Rail's network, as well as no substantial changes to contractual, funding and regulatory arrangements in the wider rail industry. More information relating to our assessment framework can be found in Annex C.

Electric current for traction charge (EC4T)

The electric current for traction charge (EC4T) allows Network Rail to recover the vast majority of its traction electricity costs from train operators who require electricity to run their electrified train services.

Fixed costs/charges

In this consultation, we refer to fixed costs as all those costs which are not short-run variable costs (defined in this glossary). These costs vary over longer periods of time or over larger increments rather than with every train service. Where these costs are

[2] Network Charges - a consultation on how charges can improve efficiency

reflected in charges, we refer to these charges as fixed charges for the purpose of this consultation. Annex A includes the current charges that fit into this category.

Fixed track access charge (FTAC)

The fixed track access charge (FTAC) recovers Network Rail's net revenue requirement. The net revenue requirement is the revenue that we determined in a periodic review is required by Network Rail to run its business, after accounting for the income received from short-run variable track access charges, regulated station charges, other single till income and the network grant. The FTAC is only paid by franchised passenger train operators.

Franchised (passenger) operators

Franchised operators are train operators providing passenger rail services who hold a franchise contract with a national or local franchising authority, with associated franchise payments that constitute subsidy or premia.

Franchised stations

Franchised stations are the stations at which a franchised train operator is the Station Facility Owner (SFO). The majority of stations on the network are franchised stations.

Freight only line charges

The freight only line (FOL) charge was introduced as part of PR08. It is intended to recover the fixed costs of freight only lines (i.e. those lines used only by freight trains) for the commodities on which it is levied. In legal terms, it represents a mark-up on charges for costs directly incurred on those market segments which we determine to be subject to the charge. Coal for the electricity supply industry (ESI), iron ore and spent nuclear fuel are the commodities that have paid a FOL charge in CP5.

Freight specific charge

The freight specific charge (FSC) recovers freight avoidable costs, i.e. costs that Network Rail could avoid if freight services did not use its infrastructure (net of the costs recovered by other charges that freight services pay). In legal terms, it represents a mark-up (defined in this glossary) on charges for costs directly incurred on those market segments which we determine to be subject to the charge. ESI coal, iron ore and spent nuclear fuel are the commodities that have paid a FSC in CP5.

Liquidated damages regime

Schedules 4 and 8 are largely 'liquidated damages' regimes in which payments made between parties are determined by a formula set in advance. This significantly reduces transaction costs and removes the requirement for parties to negotiate the financial impact

of disruption after each event. It should be noted there are elements of compensation in these regimes that are not determined formulaically.

Managed stations

Managed stations are the stations at which Network Rail is the SFO. There are currently 18 managed stations, these are all large stations. A list of the managed stations is available on the Network Rail website here.

Mark-ups

In the context of access charges, mark-ups refer to charges, in accordance with the provisions of EU Directive 2012/34/EU, as transposed into UK legislation by The Railways (Access, Management and Licensing of Railway Undertakings) Regulations 2016. The legislation requires that certain access charges for use of rail infrastructure shall be set at the cost directly incurred as a result of operating the train service, but that mark-ups may be levied to recover additional costs subject to the market can bear test (defined in this glossary).

Market can bear test

The market can bear test is an assessment, applied at the level of market segments, required in order to levy mark-ups above cost directly incurred. The legislation does not set-out a detailed definition of how the market can bear test should be conducted but it does require us to consider at a minimum the following market segments when assessing ability to pay: services within the framework of a public service contract, other passenger services and freight services.

Network grant

A proportion of Network Rail's income in the past has been paid directly by DfT and Transport Scotland in the form of network grants. Over CP5, more than 60% of Network Rail's income is forecast to come from network grants.

Network Rail loss incentive mechanism

This is a term that Network Rail has used to describe the mechanism that we introduced in CP5 to provide a financial incentive for Network Rail to better manage transmission losses and to ensure the risk associated with errors in the estimation of transmission losses is shared between modelled operators and Network Rail. It consists of allocating a proportion of the volume reconciliation to Network Rail in each ESTA, with the proportion being higher in ESTAS with a high proportion of metering, and all the volume reconciliation being allocated to Network Rail in the case of fully metered consumption.

Notification discount factors (NDFs)

Network Rail receives a discount on the amount of Schedule 4 compensation it pays to franchised passenger operators for early notification of restrictions of use; this is known as the notification factor. The discount reflects the reduced impact on operators' revenues where customers/passengers receive early notice of service disruption. These factors have three levels of notice known as notification discount thresholds.

Open access operators (OAOs)

Open access operators are train operators of scheduled passenger services that are not franchised operators.

On-rail competition

We use this term to mean competition in provision of rail passenger services between different operators (i.e. when different operators provide similar services to passengers in direct competition). Currently, competition in passenger rail services in Great Britain mostly happens through the competitive award of franchises (in essence, competition 'for' the market). There is, in addition, a degree of competition within the market as some franchisees compete against each other on routes where franchises overlap, and also where a franchisee faces competition from services provided by an open access operators which has been granted access rights by the ORR.

Public service obligation (PSO) levy

We use this term to mean a mechanism that could be designed (in accordance with European and domestic legislation) to mitigate the impact on government funds of more competition between franchised passenger operators and open access operators. This would be achieved by enabling open access operators to contribute towards the cost of unprofitable but socially valuable services. This in turn would make provision of services by franchises or open access operators broadly financially neutral to government.

Rail Delivery Group (RDG)

The Rail Delivery Group (RDG) is an association, established in June 2011, of Great Britain's major passenger and freight train operator groups and Network Rail to lead and enable improvements in the railway.

RDG set up its own review of charges and has been considering possible future reforms to Network Rail's current charging structure. This work has now concluded and is published here.

Regulated outputs

These are outputs that we determine as part of our periodic review that Network Rail is required to deliver over the relevant control period.

Route-Level Efficiency benefit sharing (REBS) mechanism

A mechanism intended to strengthen the incentive to reduce infrastructure costs. It works by increasing passenger and freight train operators' interest in these costs by exposing them to these costs in each year of the control period.

Schedule 4

Schedule 4 (the possessions regime) is the part of passenger and freight operators' track access contract with Network Rail that sets out arrangements for compensation to the operator in the event of planned disruption to their services.

Schedule 8

Schedule 8 (the performance regime) is the part of passenger, freight and charter operators' track access contract with Network Rail that sets out arrangements for compensation in the event of unplanned disruption to services.

In this context (and throughout this glossary), by performance we mean operational performance, e.g. delays / punctuality.

Schedule 8 benchmarks

The Schedule 8 benchmarks for Network Rail set the level of performance, in the form of unplanned delays and cancellations, that operators get for the charges they pay. Network Rail compensates the operator for performance worse than the level of the benchmark, and the operator pays Network Rail a bonus for better than benchmark performance. The payments are determined formulaically, based on evidence on the financial impact of delay on operators. Similar benchmarks are used with respect to operator-caused delays, because of the delays they may cause other operators.

Station Facility Owner (SFO)

The SFO at a station is responsible for the operation and management of that station. At the majority of stations on the network a franchised train operator is the SFO, for a small number of the larger stations Network Rail is the SFO. It should be noted that there are also stations on the network where the SFO is not a franchised train operator or Network Rail, such as Southend Airport Station.

Strategic business plan (SBP)

Network Rail submits its strategic business plans as part of the periodic review. They set out what the company proposes to deliver and the costs associated with doing so for the next control period.

Sustained planned disruption (SPD)

The SPD mechanism is designed to protect passenger train operators from instances where there is severe disruption caused by possessions over a sustained period. Additional compensation for SPD is triggered when the impact of severe disruption crosses a pre-defined level (in terms of revenue lost and increased costs) at which point train operators may claim additional revenue/ cost compensation above that covered by the liquidated sums payable under Schedule 4.

Sustained poor performance (SPP)

The SPP regime provides additional compensation to a passenger train operating company when lateness and cancellations attributable to Network Rail reach a specified threshold, beyond which it is considered the liquidated sums nature of Schedule 8 could start to significantly undercompensate the operator. That additional compensation is measured in relation to the benchmark level of Network Rail's performance.

Short-run variable costs/charges

Every train service causes some costs to be directly incurred on the network. For example, every train service causes some wear and tear to the track, accelerating the need for renewals. Any cost that is directly incurred as a result of operating the train can be considered a short-run variable cost for the purpose of this consultation. Passing these costs in to charges gives us short-run variable charges. Annex A includes the current charges that fit into this category.

TOC-on-TOC delay

The consultation document refers to the delay that the passenger operators cause to other operators (including passenger, freight and charter operators) as 'TOC-on-TOC' delay.

Variable usage charge (VUC)

The VUC is set to equal the operating, maintenance and renewal costs that vary with traffic. The VUC is differentiated by vehicle class. This differentiation reflects the significant variation in infrastructure wear and tear costs associated with different vehicle characteristics, for example vehicle operating speed and axle weight. In the case of freight, the charge is further disaggregated by commodity type, reflecting the different axle loads associated with different commodities. The rates are averaged across the network as a

whole, resulting in a single Great Britain-wide price for each permutation of vehicle type and commodity.

The volume reconciliation (also called volume wash-up)

This is the year-end process whereby modelled and actual electricity consumptions (in kWh) in each electricity supply tariff area (ESTA) are reconciled. The process results in an increase/decrease in the allocation of kWh consumption to train operators resulting in a payment to or from the operator to Network Rail.

Only modelled operators and Network Rail participate in the volume reconciliation. Metered operators do not participate in the volume reconciliation because there is much less uncertainty in the volume of their consumption.

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