Periodic Review 2013

Volume Incentive Consultation

Response from Rail Freight Group

1. RFG is pleased to respond to the ORR's consultation into the volume incentive for control period 5. The volume incentive should be an important part of Network Rail's relationship with the freight operators, incentivising their interest in growing freight volumes.

2. We agree that the volume incentive should continue to have a role to play, as part as a wider range of incentives and output measures for CP5. Incentives such as this are important in driving Network Rail behaviour, although of course they are not the only driver. We note for example that the Network Rail freight team has made some good progress with the industry during this control period, even though there has been no Volume Incentive payment. Nonetheless, we consider that the incentive should remain, at least at present.

Specific Questions

Questions 1 and 2

3. We are slightly surprised, as a matter of process, that the wider context, and the scope for the longer term work programme are included in this consultation. We would expect that such a programme of work would require consideration in its own right, and not as part of another review. We hope that wider exposure to this work package will take place ahead of commencement, and in its own right.

4. There should be greater clarity around what ORR, and other stakeholders, define as 'efficient' use of network capacity. For example, a freight customer may consider 'efficient' as network capacity which improved journey time and hence equipment utilisation and cost.

5. We note, for example, in para 3.6, that one interpretation is offering capacity to 'operators who value it most', but there are clear disconnects between this interpretation and the role of the railway in delivering non cash benefits to the UK (for example, environmental, economic, reducing social deprivation, reducing road congestion etc.).

6. In improving the 'efficient use of network capacity' we would also support moves to consider how a wider range of railway services could be made 'efficient' however defined, rather than being excluded from certain routes/times through charging and incentives . In this context, future replacements for the Volume Incentive might seek to encourage Network Rail to deliver more efficient services as well as simply more services.

7. The outlined possible programme for the longer review of charges appears to be rather insular to the rail sector, and focus in quickly on possible charging

structures. We would expect, in addition, that consideration needed to be given to;

a. The range of outcomes that the UK transport system is expected to deliver, and the desired role for rail within that;

b. The role of charging and incentives in developing the rail sector and improving affordability for key sectors, and the role of competition.

c. The key priorities for the charging and incentive structure for freight , and the need for simplicity;

d. The limit of affordability for different rail sectors – for example, what is the total, capped level of affordable freight access charges, regardless of how that is applied;

e. Development of a stable, long term framework for charges, to encourage investor confidence. This should also include a focus on simplicity.

8. We would also expect that ORR/RDG would require a greater level of analysis and understand from NR of its assets and costs than has been demonstrated in some recent work (e.g. on coal spillage) particularly for any cost assessments other than at a macro level.

Questions 3 and 4

9. We note that the volume incentive has not paid out for CP4 for freight as the trigger levels have not been met. Clearly, the growth, or decline, of rail freight volumes are determined by a range of factors, many or most of which are outside NR's control. Nonetheless, those looking to introduce new services still need to be assured that Network Rail do have an incentive to work with them on their proposals, and the regime remains important.

10. One particular weakness over the last control period appear to be the link between the incentive and freight train miles. Freight train miles have decreased significantly as efficiency has risen, with more goods being conveyed per train. Whilst this trend cannot continue indefinitely, the present incentive is actually working against developing more efficient services at the expense of freight train miles. ORR may wish to consider if this metric therefore remains applicable, or in line with other parts of the incentive structure.

11. Indeed, and with reference to the longer term review, ORR and NR may wish to consider the range of incentives which freight operators are subject to, and prioritise those of the most importance. Presently, the array of incentives is complex, may work against each other, and for the freight operators, the benefits of responding to the incentives are not always clear. A simpler, prioritised system may well be appropriate.

12. We do not support a charge based mechanism, which would in any case need to be considered as a potential mark up and assessed as such.

Questions 5, 6 and 7

13. As we have commented previously, we consider that there are complexities with disaggregating by NR route, as most freight flows do not align well with the route boundaries. Indeed, NR are developing strategic freight corridors to give the necessary focus (e.g. on performance) to key freight flows.

14. We also note that whilst the Route MDs, and their teams, are vital for rail freight, the equally important NR Freight team, including the freight managers and account executives is not devolved. Therefore a disaggregated incentive may in fact weaken the case for action in the centre.

15. We would therefore support the retention of a non disaggregated target for freight. However, if ORR wish to pursue a disaggregated approach then a pro rata by freight tonne-km is most likely to be appropriate.

16. We do not support disaggregation by operating company. In the competitive freight market it would be almost impossible to demonstrate that the respective incentive levels were not anticompetitive. It might also discourage NR from supporting developments for third parties such as ports and terminal operators where the future choice of freight operators was unclear.

Question 8

17. Although we can understand the principle behind considering the downside, we think that in reality it will be very difficult to implement and is likely to be perverse or counter intuitive.

18. Reduction in freight volume could arise from NR's actions, but most typically would arise from economic factors such as the performance of the economy and changes to the customers business. It would seem odd to penalise NR for this, as they have limited or no ability to influence it.

19. Where NR does have influence to reduce freight volumes would be in areas such as (i) persistent bad performance – which is covered by the performance regime (ii) the approach and timing of possessions – which should be covered by the possessions regime (iii) increasing the level of charges.

20. All there may be a short term benefit for operators, it would seem somewhat perverse if NR increases freight charges, revenues rise but volumes reduce, and NR then has to pay back some or all of the increased revenues to the operators under the Volume Incentive. This is wholly illogical.

21. To the extent that a downside is introduced it should therefore be targeted at areas where NR have influence, and which is consistent with the wider incentive

framework. This may just be too complex for the current mechanism.

Questions 9, 10, 11, 12

22. We agree that the Volume Incentive should be applied to all routes. The actions which the incentive needs to encourage are not only about finding paths (although that is important) but also engaging with customers on solutions at terminals, helping to run longer trains etc. These are not necessarily linked to congested routes.

23. For freight, encouraging development of suitable capacity away from congested routes / times is also important and should be encouraged.

24. We agree that ESI Coal and spent nuclear fuel could continue to be excluded. In any event it is unlikely that NR would be incentivising ESI coal given the proposed changes in charging structure.

25. However biomass should not be excluded at present, as it is vital that NR act to support this traffic on rail whilst the market develops.

26. We believe that distinguishing between growth drivers will be too complex and is likely to make the scheme unworkable.

Questions 13, 14, 15

27. We support a continuation of the principles for calculating the incentive rates.

28. We note that the freight rate is higher than the passenger rate, despite the fact that the freight rate does not take into account the value to the final user. As the rates are based upon established DfT values, we do not see any necessity to adjust downwards. We note that no such adjustment is proposed to passenger rates for Schedule 4 and 8 where similar distortionary effects are possible in the other direction.