

## Annex C – States of the world

1. This annex sets out the work that has been carried out by the Rail Delivery Group (RDG) with ORR’s support to develop a set of alternative states of the world (or scenarios) to consider charging and incentives framework under<sup>1</sup>. RDG defines a state of the world as the environment within which the charges and incentives regime operates. It represents elements of the rail industry that are not part of the regime, e.g. the degree of franchise protection or the extent of regional decision making.
2. Following the implementation of the charging framework for PR18, we expect that the broad structure would continue to apply beyond CP6. If it is to maintain this stability over time it will need to be robust to changes in external factors and the environment in which the new regime would operate. It is important, therefore, that we assess our proposed set of broad options under different states of the world.
3. We think that it would be optimal for our review of charges to be based on the same or similar set of states of the world as the RDG review. We see no reason why they should differ, so long as they are based on what realistically might happen in the future, have an impact of the optimal structure of charges, and are not defined by the set of outcomes that RDG members regard as being desirable. We were, therefore, actively involved in supporting RDG’s work to develop the set of alternative states of the world.

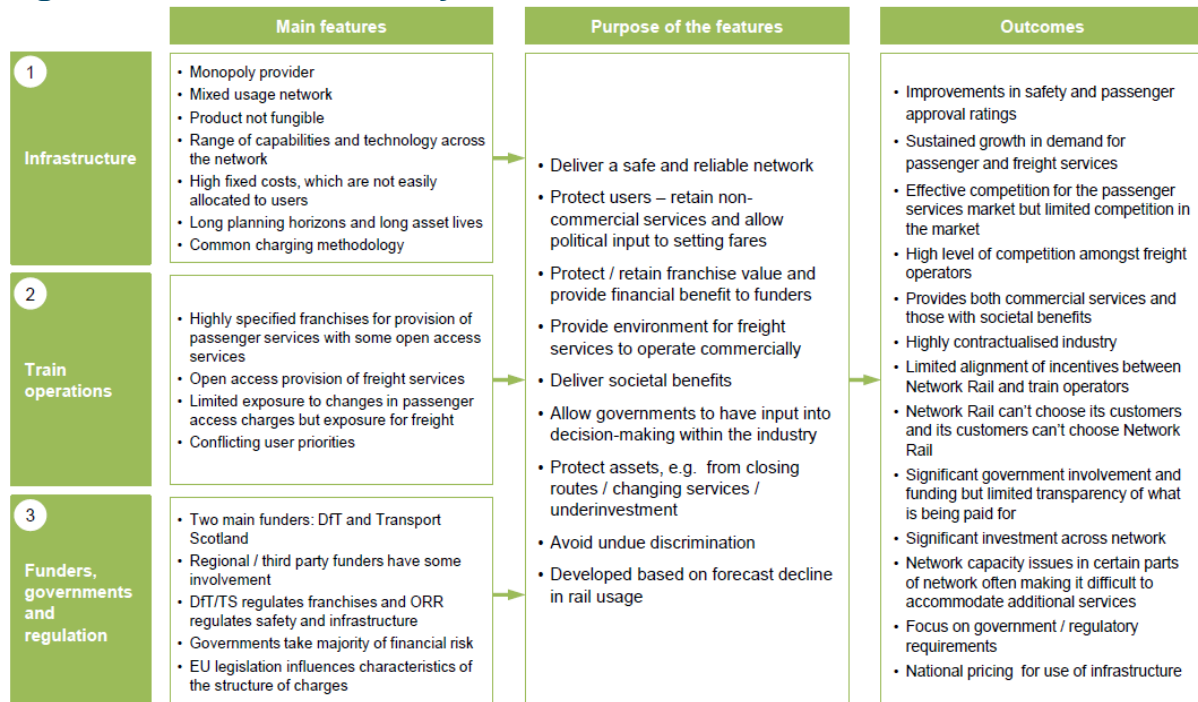
### RDG’s view of the current state of the world

4. The starting point for RDG to develop alternative states of the world was to establish key characteristics of the current state of the world. This was informed by workshops run by RDG to articulate the features, purpose and outcomes of the current state of the world (these are summed up in Figure 1 below).

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<sup>1</sup> States of the World were developed by RDG as part of their own review of charges, available [here](#).

**Figure 1: RDG's summary of the current state of the world**



Source: RDG's Review of Charges

- Elements of Figure 1 above were used to consider the range of factors that could drive changes to the current state of the world over the next 15 years. These were broadly categorised as political, economic, social, technological, legal/regulatory, and environmental. The list of factors was whittled down based on the likelihood and potential impact of each change on the structure of charges, and complementary changes were then grouped to form a set of alternative states of the world.

## Key features of RDG's states of the world

- In selecting alternative states of the world, RDG followed these principles:
  - more than one state of the world can co-exist on the network;
  - avoid 'cluttering' the alternative states of the world so that they are not overly specific; and
  - incorporate changes that are complementary, for example more regional decision making is likely to require a different approach to infrastructure funding.
- Figure 2 below sets out the summary of RDG's alternative states of the world. The first three are focused on different approaches to passenger service delivery, in particular the different degrees of on-rail competition, franchise protection and

franchise specification. The remaining ones focus on specific changes to other parts of the GB rail industry which can be considered separately or in conjunction with other states of the world.

**Figure 2: RDG’s alternative states of the world**

| Feature                                 | Summary of current state  | How will the current feature change?   | Alternative states of the world |   |                                     |                                 |                                    |  |                                  |
|---|---|--|---------------------------------|---|-------------------------------------|---------------------------------|------------------------------------|--|----------------------------------|
|   |   |  | 1. A more dynamic railway       | 2. On-rail comp. via flexible franchising | 3. More highly specified franchises | 4. Freight protection / subsidy | 5. Beneficiary pays for capability | 6. Change in approach to capacity allocation | 7. More regional decision making |
| On-rail competition                     | Limited competition in the market for passenger rail services   | Increase in on-rail competition  | ✓                               | ✓   |                                     |                                 |                                    |  |                                  |
| Franchise protection                    | Significant protection from changes to access charges   | More / less protection   | ✓<br>(less)                     |   | ✓<br>(more)                         |                                 |                                    |  |                                  |
| Franchise flexibility                   | Limited flexibility due to highly specified franchise requirements  | More / less flexibility  | ✓<br>(more)                     | ✓<br>(more)                               | ✓<br>(less)                         |                                 |                                    |  |                                  |
| Freight protection                      | Limited protection from changes in access charges but indirect subsidies                                  | More protection and / or direct subsidy                                      |                                 |   |                                     | ✓                               |                                    |  |                                  |
| Availability of network capacity        | Some capacity issues across network but surplus capacity elsewhere  | Increase in network capacity (HS2 or technology driven)                      |                                 |   |                                     |                                 |                                    | [✓]  |                                  |
| Approach to infrastructure funding      | Funded by track access charges, 'lump sum' grants from governments and Network Rail's commercial income   | Beneficiary pays for new network capability                                  | ✓                               |   |                                     |                                 | ✓                                  |  | ✓                                |
| Approach to allocating network capacity | Administrative approach, reflecting historic rights, rather than overall benefits of use                  | More analytical approach to allocation, e.g. responsive to changes in demand | ✓                               |   |                                     |                                 |                                    | ✓  |                                  |
| Regional decision-making                | Two main funders / specifiers (DfT and Transport Scotland), one infrastructure and safety regulator (ORR) | Greater regional decision making   |                                 |   |                                     |                                 |                                    |  | ✓                                |

**Please note:** the symbol [✓] reflects that we will consider Alternative State of the World 6 with, and without, increased network capacity

**Source: RDG’s Review of Charges**

8. Below we set out the key features of RDG’s alternative states of the world.
9. State of the world 1 - *A more dynamic railway*:
  - **More on-rail competition** between passenger operators.
  - **Low franchise protection** from changes in access charges.
  - **Increased franchise flexibility** as a result of less highly specified franchise agreements.
  - **‘Beneficiary pays’** approach to fixed costs. For example, governments no longer provide funding of infrastructure via the lump sum Network Grant and instead direct funding to specific projects.
  - Decisions on **allocation of network capacity** are no longer based largely around the rights reflected in the existing capacity and instead reflect other factors, such as the overall benefit of use.
10. State of the world 2 – *On-rail competition via more flexible franchising*:

- **More on-rail competition** between franchised passenger operators or from more open access as a result of fewer services being franchised on certain parts of the network.
  - **Increased franchised flexibility** as a result of less highly specified franchise agreements.
11. State of the world 3 – More highly specified franchises:
- **Greater franchise protection** from changes in charges.
  - **Reduced franchised flexibility** as a result of more highly specified franchise agreements.
12. State of the world 4 – *Freight protection/subsidy*:
- **More financial protection** from changes in charges or a **direct subsidy** for freight operators from governments to reflect the positive externalities/societal benefits of freight.
13. State of the world 5 – *Beneficiary pays for network capability*:
- Governments no longer provide funding of infrastructure via the lump sum Network Grant and instead **direct funding to specific projects** or to Network Rail but for **specific elements of existing capacity**.
14. State of the world 6 – *Change in approach to allocation of network capacity*:
- Decisions on **allocation of network capacity** are no longer based largely around the rights reflected in the existing capacity and instead reflect other factors, such as the overall benefit of use.
  - This state of the world should be considered under **two scenarios** – a) current network capacity/capability remains; and b) a significant increase in capacity resulting from a major enhancements project such as HS2.
15. State of the world 7 – *Regional decision making*:
- More responsibility for **decision making (funding, policy, operational) at a regional level**.
  - **‘Beneficiary pays’** approach to fixed costs. For example, governments no longer provide funding of infrastructure via the lump sum Network Grant and instead direct funding to specific projects.

## Our view on RDG's states of the world

16. We consider the approach RDG has taken in developing the alternative states of the world to be a sensible one. Although RDG does not represent the whole of rail industry, we view RDG's states of the world as a realistic reflection of the types of factors external to the charges framework that might change in the future.<sup>2</sup>
17. We have used these states of the world when carrying out our gap analysis (see [Annex B – Gap analysis](#)) and also referred to them in our assessment criteria used to carry out impact assessment of our proposed charging options. RDG's states of the world do not define the extent that each of their features change, e.g. the extent of franchise protection decrease is not specified. This gives us the flexibility to vary these features as we feel appropriate for our analysis.
18. When using alternative states of the world for our analysis, we adopted a few deviations from RDG's work:
  - *Current state of the world* - we think that the outcomes column of the current state of the world is too subjective and is not necessary in order to assess our options within the current state of the world (see Figure 1 above). We therefore do not intend to use it in our assessment of the options.
  - *Alternative states of the world* - under regional decision making, we also consider greater route level decision making within Network Rail. We also make a distinction between freight protection and freight subsidy because they could both have very different impacts on the appropriate structure of charges.

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<sup>2</sup> We have noted the comments made by the industry stakeholders during our July industry workshop about how the Shaw Review into the structure and funding of Network Rail may require a separate 'state of the world'. At this stage of developing packages, we do not think this requires a separate assessment but we will consider further as we develop and assess specific options.