

Sheona Mackenzie
Senior Economist
Railway Markets and Economics

1 December 2017

Dear stakeholders,

Consultation on application for consent to obtain recovery of costs incurred in operation of the Heathrow rail infrastructure

Heathrow Airport Limited (HAL) owns and operates the Heathrow Spur¹, a stretch of railway infrastructure linking Heathrow Airport to the Great Western Main Line to Paddington. When Crossrail services begin in 2018, Crossrail trains will access the Heathrow Spur to take passengers to and from Heathrow Airport. HAL will charge the Crossrail train operator along with other operators (namely the Heathrow Express Operating Company) for that access.

HAL's approach to charging for the Heathrow Spur is set out in its network statement. HAL is seeking permission from ORR to levy a mark-up as part of its track access charges for 10 years from 1 January 2019. HAL has published analysis in support of its application on its website².

We are seeking views from stakeholders on the proposed mark-up and the analysis underpinning it by **16.00 Monday 8 January 2018** to help inform our assessment.

The legal framework

Under the Railways (Access, Management and Licensing of Railway Undertakings) Regulations 2016 (the 2016 Regulations), ORR is responsible for establishing the charging framework and the specific charging rules governing the determination of the charges to be set by infrastructure managers (regulation 14(1)).³

¹ The Heathrow Spur encompasses the track, tunnels, running lines and associated equipment (such as signalling and electrification equipment) and the associated stations.

² <http://www.heathrow.com/company/company-news-and-information/rail-regulation>

³ Except HS1 and Eurotunnel, to which separate provisions apply

All infrastructure managers (such as HAL) are responsible for determining the charges for the use of their infrastructure in accordance with the applicable charging framework, the specific charging rules, and the principles and exceptions set out in Schedule 3 to those 2016 Regulations (regulation 14(2)).

The general principle is that charges for the minimum access package and for access to service facilities⁴ must be set at the cost directly-incurred as a result of operating the train service (Schedule 3 paragraph 1(4)). However, by way of exception to that principle, an infrastructure manager may levy an additional mark-up in order to obtain full recovery of its costs incurred (Schedule 3 paragraph 2(1)). It must have the approval of ORR to do this⁵, and such mark-ups must be levied “on the basis of efficient, transparent and non-discriminatory principles, whilst guaranteeing optimum competitiveness, in particular in respect of rail market segments”.

HAL has applied for ORR’s approval of its levying a mark-up to obtain full cost recovery of non-eligible costs incurred in operation of the Heathrow Rail Infrastructure for a 10 year period from 1 January 2019.

We are now considering that application.

The process

We understand that HAL has had discussions with key stakeholders including Transport for London, MTR Crossrail, Heathrow Express and Heathrow Connect before submitting the application to ORR on 11 August 2017.

Our assessment of HAL’s application and its supporting evidence will focus on the question of whether HAL’s proposal meets the requirements set out in the 2016 Regulations to levy a mark-up. This will include considering:

- Whether it has correctly identified the appropriate market segments in accordance with Schedule 3 paragraph 2;
- Whether HAL has properly explained the methodology it has used to allocate its costs incurred as infrastructure manager, given that the effect of any mark-up must not be to enable the infrastructure manager to obtain more than full recovery; and
- Whether the identified market segment(s) can bear the rate of return which HAL proposes should be levied by way of the mark-up.

In approving any mark-up, we will have regard to our statutory section 4 duties under the Railways Act 1993.

⁴ Set out in paragraphs 1 and 2 of Schedule 2 of the 2016 Regulations

⁵ Or in the case of HS1 the Secretary of State

To help inform our assessment we want to hear the opinions of stakeholders (and in particular operators who would be subject to the mark-up if approved) on HAL's application in general, and in particular on the following questions:

1. Do you agree with HAL's proposed approach to satisfying the 2016 Regulations requirements with respect to its levying a mark-up?
2. Do you think HAL has correctly identified and characterised the appropriate market segments in its analysis?
3. If we were to allow HAL to levy a mark-up, do you think it would be reasonable for this permission to cover the period to 2029?

Next steps

If you would like to comment on HALs application to levy a mark-up, please send your response to Sheona.Mackenzie@orr.gov.uk by **16.00 Monday 8 January 2018**.

If you send a written response, please indicate if you wish all or part of your response to remain confidential. Otherwise, we expect to make it available in full on our website. Where your response is made in confidence, please provide a statement summarising it, and which can be treated as a non-confidential response.

We will consider any responses and any evidence submitted before making our decision.

Yours faithfully,

Sheona Mackenzie

Senior Economist