

John Jellema  
Office of Rail Regulation  
2<sup>nd</sup> Floor  
Tara House  
46 Bath Street  
Glasgow G2 1HJ

**DB Schenker Rail (UK) Ltd**  
2<sup>nd</sup> Floor, McBeath House  
310 Goswell Road  
London EC1V 7LW

**Nigel Oatway**  
**Access Manager**

Telephone: +44 (0)1302 577010  
Fax: +44 (0)20 7833 8449  
Mobile: +44 (0)7801 905240  
[nigel.oatway@dbschenker.com](mailto:nigel.oatway@dbschenker.com)

Dear John,

8 May 2013

## **PR13 CONSULTATION ON ELECTRICITY FOR TRACTION CHARGES FOR CONTROL PERIOD 5 (CP5)**

This letter constitutes the response by DB Schenker Rail (UK) Limited ('DB Schenker') to the ORR's consultation document entitled "*PR13 Consultation on Electricity for Traction Charges for Control Period 5 (CP5)*" published in April 2013.

### *Introduction*

1.1. In principle, DB Schenker supports the movement towards the fitment of meters to electric traction to measure and charge more accurately for the use of electricity as this should help incentivise operators to make their electricity for traction ('EC4T') consumption more efficient. However, for operators such as DB Schenker with relatively small fleets of electric trains that traverse many different routes with both ac and dc supply, the benefits of opting for metered EC4T consumption may be less clear cut when considered against the costs of fitment, the ongoing costs of maintenance and renewal of the equipment and the complexity and cost of managing and transmitting the data generated.

1.2. DB Schenker, therefore, considers that operators who can demonstrate that the costs of moving to metered electricity far outweigh the likely perceived benefits gained through more efficient EC4T consumption should not be penalised for remaining on modelled usage. DB Schenker is pleased, therefore, that ORR has decided not to pursue a policy of applying artificial uplifts to modelled EC4T consumption rates.

1.3. There may also be sound technical reasons why the necessary metering equipment cannot be fitted to certain types of traction without significant redesign and fitment costs (this is an issue that has been challenging DB Schenker with its Class 92 locomotive fleet). Consequently, DB Schenker believes that operators of such traction should also not be penalised for having to remain on modelled electricity usage.

1.4. In the scenarios outlined in paragraphs 1.2 and 1.3 above, mechanisms designed to incentivise operators to move to metered electricity in effect become penalties. Furthermore, in the case of operators who have a choice of traction types, such

'incentives' may have unintended consequences including incentivising increased use of 'less environmentally friendly' diesel traction. DB Schenker strongly believes that if the economic benefits of moving to metered EC4T consumption are overwhelming, then operators would already be sufficiently incentivised to fit electricity meters to their trains. Those that do not would have clear and justifiable reasons why an 'opt-in' to metered electricity is not viable.

1.5. DB Schenker also understands that there are many other significant consumers of Network Rail's traction electricity supply both for traction and non-traction uses that are not currently subject to the same rules that are applied to operators with track access agreements (i.e. freight and passenger operators). These consumers include Network Rail itself, London Underground and operators of Traction Maintenance Depots leased from Network Rail. DB Schenker considers that any rules, incentives and penalties applied to passenger and freight operators should also be applied to these other consumers to avoid possible discrimination and cross-subsidy. DB Schenker, therefore, supports ORR proposals to contractualise such usage through the traction electricity rules.

#### *ORR's Specific Questions*

*Q1. We would like to know your views on all of the issues raised in this section of our letter. In particular, should we amend the traction electricity rules so that we take the decision on the DSLF as part of an access charges review (i.e. a periodic review or interim review), and remove the industry's ability to propose and vote on the same?*

2.1. Although not currently a metered operator, DB Schenker can see the advantages of ORR setting the Distribution System Losses Factor ('DSLF') at each Periodic Review with the intention that it would remain fixed throughout the Control Period so as to reduce uncertainty and promote investment in on-train metering equipment. On the other hand, however, the ability for the DSLF to be amended by the industry through the application of the change processes set out in the EC4T Metering Rules also has its advantages. For example, should the DSLF be proven to have changed materially during a Control Period, such a mechanism would allow it to be modified so that it would remain in line with actual system losses.

2.2. DB Schenker believes that a compromise between the two options may prove to be the best way forward. ORR could set the DSLF at each Periodic Review with the intention that it would remain fixed throughout the Control Period. However, the mechanism in the EC4T Metering Rules would be modified so that the DSLF could be proposed for modification without the need for a vote should it be proven to have changed above or below an appropriate materiality threshold. This is because if ORR's proposal to exclude metered operators from the volume wash-up in all cases is adopted, it is hardly likely that metered operators would vote for any increase in the DSLF. In any event, given that ORR has the final approval of any changes to the DSLF, this would ensure only material changes that can be fully justified could be implemented.

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*Q2. We would like to know your views on all of the issues raised in this section of our letter, in particular the questions below:*

*(a) we are minded to set a DSLF by ESTA and establish new ESTAs for new electrified infrastructure, at least for CP5. Do you agree with this policy? Please give reasons for your view. It would be useful if you could cite specific examples why you think this would or would not be appropriate;*

*(b) we propose to change the basis on which transmission losses for metered consumption are charged so that the DSLF is applied to the gross metered consumption, rather than metered consumption net of metered regenerative braking, as it is currently. Do you agree that this will deliver a more cost-reflective basis of charging for transmission losses? Please give reasons for your view; and*

*(c) we propose to accept Network Rail's median estimate of the DSLF, subject to it being levied on gross consumption, but we do not accept Network Rail's assertion that losses would necessarily increase over CP5. Do you agree with our assessment? Please give reasons for your view.*

2.3. DB Schenker agrees with ORR's proposal that a DSLF should be set for each ESTA as this would increase cost reflectivity. DB Schenker also agrees that additional ESTAs should be created for any new electrified infrastructure. However, DB Schenker would only expect an additional ESTA to be created where the new infrastructure is material and not, for example, the addition of a small number of newly electrified sidings within an existing ESTA.

2.4. DB Schenker agrees with ORR's proposal that transmission losses for metered consumption are charged so that the DSLF is applied to the gross metered consumption, rather than metered consumption net of metered regenerative braking, as it is currently.

2.5. DB Schenker agrees with ORR's assessment that concentrating solely on traffic growth as a proxy for losses would potentially exclude other factors, such as targeted investment to reduce losses that would act in the opposite direction. However, if DB Schenker's alternative suggestion outlined in paragraph 2.2 above was adopted, this would provide an opportunity for the DSLF to be adjusted in cases where material changes in the level of losses (either up or down) are proven to have occurred.

*Q3. We would like to know your views on all of the issues raised in this section of our letter, in particular we propose that metered services be exempt from the volume wash-up, even in cases where more than 90% of consumption is metered, this reform would be coupled with Network Rail being exposed to the volume wash-up. We seek your views on this proposal.*

2.6. DB Schenker would support ORR's proposal of excluding metered operators from the volume 'wash-up' in all cases, provided that DB Schenker's alternative suggestion outlined in paragraph 2.2 above was adopted (i.e. the DSLF can be modified if losses

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are proven to exceed a certain materiality threshold either up or down). This would ensure that Network Rail and non-metered operators are not unduly subsidising metered operators (or vice versa) in cases where losses are known to be materially above or below the level of the DSLF set by ORR at the start of the Control Period.

*Q4. We would like to know your views on the issues raised in this section of our letter, in particular our proposed formulation for Network Rail to share the volume wash-up. We welcome your suggestions for specific alternative formulations.*

2.7. DB Schenker supports ORR's proposal that Network Rail should take a share of the volume 'wash-up'. The formulation suggested by ORR in the consultation document seems as good an option as any.

*Q5. We also seek your comments on our assessment of risks and the incentive properties of the different options.*

2.8. In addition to Network Rail taking its share of the volume 'wash-up' other modelled users of EC4T should also bear appropriate risk under that mechanism if they do not do so already (e.g. London Underground and owners of Traction Maintenance Depots leased from Network Rail). If such third parties were not included in the volume 'wash-up' this could result in Network Rail and modelled operators subsidising such third parties which would be unacceptable.

*Q6. We would like to know your views on the issues raised in this section of our letter, in particular:*

*(a) do you agree with our views on PFM and the basis on which it should be charged?*

*(b) what is your view of our suggested method for allocating the volume wash-up?*

*(c) do you have an alternative formulation that you wish to propose?*

*In all cases, please give reasons for your views and/or proposals.*

2.9. DB Schenker is pleased that ORR has decided not to implement proposals which would have resulted in the imposition of financial penalties as a means of incentivising or, as some might say, forcing operators to move to metered electricity. As mentioned earlier in this response, DB Schenker believes that if the benefits of metered electricity are as overwhelming as is suggested by the number of operators who have already 'opted in' to metered EC4T consumption, then the only reasons for not 'opting in' would surely have to be valid and justifiable ones. These may include situations where: (1) the benefits of metered EC4T consumption are outweighed by the ongoing management and operational costs (for example, where operators have small or diverse fleets); or (2) that it is extremely difficult to retrofit metering equipment to existing vehicles for technical reasons unless substantial sums are expended in redesign, modification and fitment works (for example, in the case of DB Schenker's Class 92 locomotives).

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2.10. In such cases the financial incentives to move to metered EC4T consumption instead become penalties for not adopting metered electricity or, in other terms, constitute 'mark ups' which are of course not permitted for freight operators unless it is deemed that the particular market sectors can afford to pay them. The introduction of such penalties could also result in perverse outcomes, such as incentivising operators who have a choice of traction types to increase their use of 'less environmentally friendly' diesel traction.

2.11. DB Schenker agrees that it would be appropriate for the industry to devise the rules for PFM, subject to ORR's approval. It also considers it essential that if PFM is proceeded with it must be able to deliver accurate estimates of EC4T consumption for the services that are not metered. Initial concerns that DB Schenker would have with PFM include that (1) the partially fitted trains should operate over the same routes as the non-metered trains (i.e. if the metered trains operate over routes with less challenging topography, for example, this may significantly underestimate EC4T usage for the non-metered trains that may operate over different routes which have a significant gradient profile), (2) the metered and non-metered trains are used on an equivalent basis in terms of availability to ensure that sufficient readings can be taken and used to extrapolate across the fleet.

2.12. Given that a pre-requisite for PFM is that the metered and non-metered trains are treated on an equivalent basis, DB Schenker wishes to understand how PFM would be applied to freight services which, by their very nature, are individually varied both in terms of routing, timing and trailing load.

*Q7. We would like to know your views on the issues raised in this section of our letter, in particular whether you agree that Network Rail's metered consumption should be treated on an equivalent basis to other metered consumption? What conditions do you think should apply to this? Please give reasons for your views.*

2.13. DB Schenker supports ORR's proposal that Network Rail's EC4T consumption and the consumption of EC4T by third parties should remain in the volume 'wash-up' and be contractualised in the traction electricity rules. This will ensure that all modelled and non-metered users of EC4T are dealt with an equivalent and transparent basis avoiding any cross-subsidisation.

2.14. Notwithstanding the comments in paragraph 2.13 above, provided that the standard of Network Rail's metered electricity consumption data is at least as high as that required to be provided for OTM, then DB Schenker considers that it would be difficult to argue that such consumption should not be excluded from the volume 'wash-up' (following an appropriate 'mark-up' for transmission losses).

Yours sincerely,

***Nigel Oatway***  
***Access Manager***