Rail Freight Operators' Association

Address for correspondence:
Freightliner Group Limited
3rd Floor, The Podium
1 Eversholt Street
London
NW1 2FL

Emily Bulman
Head of Economics
Office of Rail Regulation
One Kemble Street
London
WC2B 4AN

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Dear Emily

Freight Capacity Charge – proposal on methodology

Thank you for meeting us last Wednesday, we appreciate you sparing the time during this busy period during the review. I hope you found it a useful and constructive meeting. We discussed alternative mechanisms for charging the Capacity Charge for freight operators and the purpose of this letter is to lay out our preferred alternative in more detail. I have now discussed this with other members of RFOA, who are also supportive of this approach.

The main objective of the Capacity Charge is to neutralise the increased Schedule 8 risk to Network Rail of accommodating additional freight and passenger traffic on the network. This principle is well understood.

We believe, however, that there is a clear case for levying the freight capacity charge in a different way to the passenger capacity charge. The same method of calculating the cost of the marginal impact can be used as set out and explained in Network Rail's recent capacity charge conclusions document but the actual charge for freight would be levied on an incremental basis based on a comparison between the number of train miles actually operated and an agreed baseline number of freight train miles which was used to calculate the Schedule 8 benchmarks. This comparison would then be used to calculate the actual capacity charge in the form of a 'wash-up' carried out periodically.

Whilst in theory this method could also be applied to franchised passenger operators, the fact that the franchised passenger capacity charge is a direct off-set against the fixed charge would make the proposed methodology meaningless for such operators. For freight operators, however, it is acknowledged that they do not pay a fix charge unless it is a deemed that a particular market can bear a 'mark-up' so there is no such direct 'off-set'.

To summarise the detail of our proposal further, the basic proposition is that a baseline number of freight train miles (excluding Network Rail infrastructure services) is established which would mirror the figure used to calculate the Schedule 8 benchmarks for CP5. Periodically during the Control Period (on a period by period basis or annually), the baseline would be compared to the actual number of freight train miles operated in that period/year by all freight train operators. Assuming this is a positive number the difference is multiplied by the capacity charge rate per train mile and then is charged to each freight train operator in proportion to the total number of freight train miles that they have each operated (ensuring no discrimination between either existing or new entrant operators). If the number of train miles has not increased over the baseline or has reduced the payment would be zero. The mechanism is in practice similar to other “wash-up” mechanisms such as the calculation of the EC4T charge, which is adjusted for actual use at the end of each financial year.

This methodology supports the principle of paying for every new train mile operated on the network. It applies equally to all trains and also retains the principles of transparency, simplicity and symmetry and avoids significant over-recovery by Network Rail. The proposal can also be introduced and operate with low administration costs given that financial transactions are only carried out where the baseline number of train miles is exceeded.

Please see below example of calculation based on actual figures provided by Network Rail for 2012/13.

Capacity Charge Rate £ per mile		0.86		
	Base Train Miles	10% growth	10% decline	20% growth
	25,077,113	27,584,824.30	22,569,402	30,092,536
Actual Capacity Charge Income £		£2,156,632	£0	£4,313,263

We are putting this proposal forward for consideration notwithstanding and without prejudice to the views we have expressed through our consultation responses and representations at industry Working Groups.

We strongly believe that this proposal will have the effect of ensuring that Network Rail remains compensated for the additional Schedule 8 costs it incurs as a result of increased freight activity on the network whilst also limiting the financial impact on freight operators that is inherent in the current method of applying the capacity charge, which it is acknowledged leads to a significant over-recovery by Network Rail.

We have also discussed this proposal with Network Rail and I am therefore copying this letter to Tim Robinson and Peter Swattridge of Network Rail.

We hope that you find this suggestion helpful and a pragmatic way forward. If you would like to discuss this proposal further we would be very happy to do so.

Yours sincerely

L Durham

Lindsay Durham
Chair, RFOA.