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Emailed response via: orr.structureofcharges@orr.gsi.gov.uk

Dear Sir or Madam

Network Charges Consultation

This letter sets out Transport Scotland's response to the ORR's first consultation on the structure of charges for Control Period 6 (CP6) and beyond. It includes some general observations as well as some more detailed comments.

General observations

Transport Scotland recognises that network charges are an important part of the regulatory framework and can have important influences around various outcomes across the industry, whether through recovering costs, strengthening price signals, or improving transparency and decision making.

We also recognise that these influences can be limited by other factors, some of which are out with the control of the ORR and Network Rail. The complexity of decisions around allocating capacity and the protections that can be put in place in franchise contracts to hold operators harmless to changes in the level of charges applied are particularly important. In terms of the latter, protections remain in place for both the ScotRail and Caledonian Sleeper contracts, both of which are due to run beyond CP6. These factors should be borne in mind by the ORR when considering whether any fundamental reform to the charging structure would be worthwhile, particularly when other arrangements currently in play (e.g. the ScotRail Alliance) may offer significantly better incentive properties.

Transport Scotland was involved in the review of charges exercise coordinated by the Rail Delivery Group (RDG) and the analysis and evidence produced as part of this exercise provides a helpful basis for the PR18 process. A key theme that emerged from that work stream was the need to be clear about the purpose of charges before considering the more detailed aspects of the regime and this needs to be firmly embedded in your approach. It should also be underpinned by the principle of simplicity – there is an opportunity through PR18 to challenge the perceptions that rail is too complicated.

We are particularly mindful and sensitive to the potential impact that any changes to charges could have on those parts of the industry that are not protected from variations, particularly the

rail freight sector. Transport Scotland will shortly public a refreshed rail freight strategy which makes clear the need to ensure stability and predictability in charges for freight operators and that they can reflect the economic reality of their business models, which may have a regional dimension to them like we seen with the planned implementation of the freight specific charge as part of the PR13 process.

Infrastructure costs package

We note the range of potential positive impacts that the ORR has identified (transparency and better information potentially helping to reduce costs and better route level cost data) although ultimately the delivery of these would depend on how the package was implemented and some of these benefits may be achievable in Scotland through existing mechanisms.

On the down side, we note that if the ORR were to levy an increased proportion of charges on a variable basis, this would reduce the predictability of charges to operators. We also remain concerned around the potential impact that a more cost-reflective charging structure may have on different parts of the industry, particularly freight operators. We are already seeing the volume of coal being moved by rail reducing significantly due to wider economic and environmental factors and, in a Scottish context, there is no single market or commodity that will help to fill this void in the short term. Accordingly, the rail freight sector in Scotland is facing a significant challenge to its long term sustainability and it is vital that the charging regime is able to provide a firm platform as the industry looks to consolidate and grow its customer base over time. Any charges applied must reflect the reality of the current and expected rail freight market, the needs of freight consumers, particularly around predictability, and ensure that the industry can remain competitive against alternative modes.

At the strategic level, we absolutely agree that the existing Fixed Track Access Charges (FTAC) model lacks cost-reflectivity, a point raised consistently by Transport Scotland as part of the PR13 process in the context of cross-border passenger services. We firmly believe this remains an area requiring particular consideration as part of the PR18 programme of works, not least because of the challenges that remain in terms of incentives for funding critical upgrades to cross-border routes in CP6.

Value-based capacity package

We note some of the theoretical benefits that might be derived through this package although the practical application to the Scottish market would be potentially complex and contrary to Scottish Government objectives for rail.

We are therefore content to note that the ORR is not minded to prioritise this work for further development.

Improvements to short-run variable charges

We note the evidence provided by Network Rail and through the RDG work that suggests there are aspects of the existing regime where the incentive properties work well and should be retained.

At your workshop in Glasgow last month you presented a long list of options that are being considered within this package. In general terms, we would observe that the potential impact of any changes is likely to be limited by the scale of variable costs and indeed face the same challenges as set out above, particularly around levels of exposure.

Supporting packages – competition and complexity options

Transport Scotland would expect any decisions taken by the ORR around competition options to be aligned with the Competition and Market Authority's (CMA) project on competition in rail passenger services.

In terms of complexity, a key pillar of the RDG work is the need for the charges regime to be simple, transparent, and accessible and we therefore welcome the steps being taken by the ORR to review options to simplify the charging system, particularly for freight operators.

Implementation

There are a number of important considerations that we would expect the ORR to make before implementing any changes to the charges regime, many of which are articulated well in the RDG work.

The Scottish Government have made clear their view that the rail industry in Scotland should be fully devolved, including Network Rail in Scotland, to enable greater whole system accountability and for rail services to maximise their full potential through tailored, efficient, localised solutions. These principles also apply to charges.

We are aware of a preference across the industry for the retention of a single approach to setting charging and incentives for the network as a whole, reflecting the cross boundary nature of longer distance passenger and freight services. However, there must be an appreciation within this model that charges and incentives may have different effects in different routes and this is something the ORR should fully consider. As a minimum, it is vital that the ORR fully considers the practical implications for passenger and freight operators across the different parts of the industry, particularly where policy drivers of funders may vary.

I trust this response will be helpful.

Yours sincerely

Steven McMahon
Head of Rail Strategy & Funding