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Ekta Sareen
Economist
Office of Rail Regulation
1 Kemble Street
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1 September 2010

Dear Ekta,

HIGH LEVEL REVIEW OF TRACK ACCESS CHARGES

This letter constitutes the response of DB Schenker Rail (UK) Limited ('DB Schenker') to the ORR's consultation entitled 'High Level Review of Track Access Charges' dated 1 July 2010. This response may be placed in its entirety on ORR's website.

General Comments

1.1. The UK rail freight industry has been successful. It has attracted a considerable amount of private sector investment over the last fifteen years allowing it to grow by around 60% despite facing many significant challenges over that time. Only the advent of the current economic downturn that has affected UK, European and World markets has led, not unsurprisingly, to a reduction in overall rail freight movements.

1.2. During the last fifteen years, rail freight has overcome the challenges it has faced by a relentless pursuit of efficiency, striving towards customer satisfaction and a strong control of costs. Rail freight has also benefited greatly from the independence of ORR and its support for rail freight growth. In particular, ORR's policy decisions on rail freight and its conclusions in past Periodic Reviews have been fundamental to the continuing health of the industry.

1.3. However, the current economic downturn and Government budget constraints have now, more than ever focussed the need for stability and certainty for rail freight. These factors are crucial for an industry that depends on the private sector (whether shareholders, customers or debt providers) retaining its confidence that rail freight in the UK will survive the recession and will have a long-term future.

1.4. Rail freight's main competition is from road haulage or road-based logistics services. The major opportunities for rail freight are in these sectors as recognised by the industry forecasts that underpin the vision for the Strategic Freight Network endorsed by Government in September 2009. The key to achieving modal shift will be the ability to match the prices and flexibility/simplicity of road haulage. Maintaining the current structure and level of rail freight access charges would be fundamental in helping to achieving this.

1.5. The Periodic Review for CP5 presents an opportunity to reinforce that stability and certainty but at the same time it also represents a risk. The very act of undertaking a Periodic Review with the associated uncertainties about the funding of the infrastructure provider, the high level output specification and the process for matching the two creates uncertainty. This uncertainty

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is multiplied when there is a possibility that ORR will review the structure of track access charges and, in particular, the charging structure applying to rail freight.

1.6. DB Schenker urges ORR to leave the structure and level of rail freight access charges unchanged so that freight operators can offer existing and potential customers the certainty of rail freight transport costs for many years to come. In these unprecedented times a strong message now from ORR that rail freight access charges will be left more or less unchanged in CP5 will give the industry the certainty and stability it needs, will allow it to begin growing again once the economic climate has improved and to achieve the modal shift necessary to meet the vision of the Strategic Freight Network. It was clear from representations made at ORR's seminar on 20 April 2010 (and indeed subsequently at forums such as Rail Industry Planning Group and Industry Steering Group) that support for such a message would not only come from freight operators, customers and potential customers, but also from the wider rail industry including Network Rail, passenger operators, DfT and Transport Scotland.

1.7. The longer the uncertainty remains over what ORR intends for rail freight access charges in its forthcoming review, the greater risk there will be for existing rail freight customers to become concerned and potential new customers to be deterred from considering rail for all or part of their transportation needs. This is particularly pertinent given the various options presented and discussed in the consultation document, all of which have the potential to increase charges and most to introduce significant complexity both of which the rail freight industry can ill afford.

1.8. DB Schenker proposes that ORR should maintain rail freight charges at their current levels (subject to inflationary increases less any agreed efficiency factors set for Network Rail in CP5). DB Schenker believes that the proportion of Network Rail's income that is represented by freight charges is comparatively small. Therefore, an increase in freight charges will make comparatively little difference to Network Rail's overall income but would have significant detrimental effects on freight operators leading to a potentially significant reduction in the amount of freight currently on rail thereby making growth/modal shift even harder to achieve.

1.9. Given the disproportionate effect of changes in rail freight access charges between freight operators and Network Rail, DB Schenker invites ORR to settle the freight charges element of the Periodic Review for CP5 quickly and in the manner described above.

Specific Comments

2.1. DB Schenker notes that there are six shortlisted options in the CEPA Report for changing the existing structure of track access charges, three of which (regional 'long run incremental cost' approach, track occupancy charge and 'average cost' approach) would require radical changes to the structure of charges currently in place in CP4. DB Schenker also notes that two of the options ('average cost' approach and 'track occupancy' approach) would not provide appreciable benefits or improve the current charging structure.

2.2. As remarked upon earlier in this response, the rail freight industry requires stability and certainty to enable private sector confidence to be maintained and avoid the loss of customers through perceived or real concerns that track access charges will increase or that the system will become too complex. The rail freight industry requires a simple and straightforward charging regime that is easily understood and applied. The current charging structure applied to rail freight with its vast array of usage charges by wagon type, sub-type and commodity carried when combined with other charges such as capacity, EC4T asset usage, coal spillage, coal spillage investment and freight-only line already oversteps the bounds of simplicity. The prospect of further substantial complexity being applied to rail freight charges through, for example, the adoption of one or more of the options described in the CEPA Report would undermine stability and certainty as well as introducing a level of complexity that would discourage growth and reduce confidence.

2.3. This would be particularly the case in respect of the 'regional' based approaches which could exponentially increase the number of variable track usage rates in the tariff. Given that many rail freight services are long-distance covering many geographical areas, this could result in different rates for same train over the same journey that would have to be individually calculated with every boundary/route change. Furthermore, the 'track occupancy' approach would completely change the current structure of rail freight charges and would make it difficult for rail freight operators to quote accurate prices to customers until the service is timetabled. DB Schenker notes that CEPA has expressed its own reservations over this particular option.

2.4. DB Schenker's brief overview of the six options in respect of the impact on rail freight charges is as follows:

- *'Regional Long Run Incremental Costs'*

  This option involves a radical change to the current charging structure and, more importantly, would significantly increase rail freight charges as freight operators would be expected to pay both the long run and short run incremental charges, particularly as freight operators do not currently pay fixed charges. This option would, therefore, undermine stability and certainty as well as discouraging the use of rail over other transport modes for most traffic types thereby having a significant adverse impact on freight operators' businesses.

- *'Average Costs'*

  This option would also involve a radical change to the current charging structure for rail freight charges and could significantly increase costs. This option would also undermine stability and certainty as well as discouraging the use of rail over other transport modes for those traffics for which charges would increase. On a positive note, it appears that this option would reduce complexity when compared to the current charging regime but other than that DB Schenker notes that it would not provide any other appreciable benefits or improve the current charging structure.

- *'Regional Short Run Incremental Costs'*

  It appears that under this option the charges for lesser used routes could increase whilst those of heavily used routes may decrease. Given that rail freight uses many of the lesser used routes, this option has the potential to increase rail freight charges at the same time as taking the complexity of the existing charging structure to a whole new level. The charges for individual rail freight services (particularly those travelling long distance) could change en-route many times as each regional/route boundary is crossed. This would make it increasingly difficult for freight operators to quote prices to customers quickly with any degree of certainty as they would need to wait until Network Rail has provided a Train Slot to discover which route and, therefore, which charging rates will apply. Consideration would also need to be given to charging rules that apply during periods of perturbation (both planned and unplanned) and whether cost effective charging systems could be put in place to calculate and invoice such complex arrangements.

- *'Scarcity Charges'*

  This option would also undermine stability and certainty by introducing an additional charge as well as introducing significant complexity thereby discouraging freight traffic from using rail. DB Schenker considers that existing non financial mechanisms are sufficient to ensure that operators hold appropriate access rights whilst at the same time recognising that freight operators require some flexibility in their use of the network if they are to be competitive with other transport modes. This is particularly the case with road transport that is not required to pay reservation/scarcity charges for use of the UK road network.

- *'Cost benefit sharing'*

  DB Schenker is concerned that this option would have the potential for Network Rail to discriminate between operators on a particular route favouring those with which it had a revenue share agreement. In this regard, DB Schenker recalls the benefit share arrangements Network Rail's predecessor Railtrack put in place with West Coast Trains for the upgrade of the West Coast Main Line during the late 1990s. This arrangement gave rise to untold problems that the rail industry had to suffer for years after. It is crucial, in DB Schenker's view, that Network Rail remains impartial as between the various operators running over its network.

- *Track Occupancy Charges*

  This option also involves a radical change to the current charging structure and, more importantly, may result in many traffic flows becoming unviable. This important aspect is also recognised in the CEPA Report. The CEPA Report also notes that whilst this charging regime is already in place on HS1 it is not applied to HS1's charges for rail freight. Consequently, DB Schenker would expect that, should this option be adopted for Network Rail, similar ring fencing for rail freight would apply. DB Schenker notes, however, that this is one of the two options that CEPA Report considers would not achieve any appreciable benefits over the current charging structure.

Conclusion

3.1. DB Schenker considers that in respect of the charging regime for rail freight, the proposed options in the CEPA Report would be damaging to rail freight as a whole and freight operators' businesses in particular. DB Schenker urges ORR to leave the structure and level of rail freight access charges unchanged (subject only to inflationary increases less any agreed efficiency factors set for Network Rail in CP5) so that operators can offer existing and potential customers the certainty and stability of rail freight transport costs going forward for many years.

Yours sincerely,

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Access Manager