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9th August 2012

Dear Mr Quill,

Periodic Review 2013 – Consultation on the variable usage charge and on a freight-specific charge

I am pleased to respond to the Consultation dated May 2012 on behalf of the Scottish Coal Company Limited (SCCL). SCCL is a major component part of the Scottish Resources Group which in turn provides direct employment to almost 900 skilled people, predominantly in rural Scotland where few other employment opportunities exist. SCCL is the largest surface mine coal producer in the United Kingdom providing coal to most of the major electricity supply industry (ESI) operators throughout the UK.

1. Background

Over the past Winter & Spring (Nov 2011 – April 2012) in the UK, electricity from coal fired power stations represented over 50% of total power generated (Source: DECC). Of that figure approximately 6% was from coal mined by SCCL. During this period approximately 1.53 million tonnes was delivered by SCCL to generators in both Scotland and England by rail. Even in July 2012, on some days over 40% of UK electricity was generated from coal which confirms the considerable importance of coal to security of electricity supply for many years to come.

Over 50% of all coal produced in Scotland is transported to England of which 100% is by rail. Transportation of coal within Scotland involves over 60% by rail. There is an understandable desire by local communities and local authorities to see increasing amounts moved by rail and the planning policy and consenting process encourages such rail use. SCCL currently has the potential to provide coal which could generate about a third of Scotland's electricity needs, however owing to the lower environmental emission limits at Scottish power stations, coal is being transported to England where the coal quality is fully compliant for coal fired electricity generation. As a result, rail transport is even more important to the



electricity supply than it would be if Scottish coal was being transported the shorter distances into Scottish power stations.

The SCCL operational coal sites and rail loading facilities are situated in the Central Belt of Scotland, predominantly in Ayrshire and Lanarkshire. Coal is supplied by rail to Longannet & Cockenzie power stations in Scotland, and to other coal fired power stations further afield in Lancashire, Nottinghamshire & Yorkshire. As referred to above approximately 60% of our rail deliveries to ESI operators are to these power plants in England, a distance of up to 300 miles.

2. The Effect of Increasing Track Access Charges.

We strongly believe that the proposed changes to track access charges will have a serious impact on SCCL as a business and, as a result, will have an immediate detrimental effect on both the coal and electricity supply industries. It must be stressed that the proposed increases to track access charges cannot be sustained by SCCL and it will not only affect the need for coal as a secure and stable energy source but will add a financial burden that will close mines and increase unemployment.

This is not a highly profitable business, being at the mercy of international coal pricing, whilst at the same time being highly capital intensive and requiring huge investment in the development of new sites. The operations are in deprived rural areas where the high skill – high pay jobs cannot be replaced if lost. SCCL believes that implementation of these proposals represent a serious threat to the viability of their operations with a genuine threat that they would lead to the complete closure of the business. We believe it is not part of the ORR's undertaking to impose changes which could have such a serious impact on the future of the coal industry in this country and the coal industry in Scotland in particular.

Our principal concerns are set out below with answers to specific consultation questions in a separate section at the end.

3. Basis of Comment

It is understood that an increase in a range between £4.00/tonne to £4.50/tonne is likely. This would apply to all coal being transported by rail from Scotland. We do not believe that there is any objective basis for this. SCCL believe that a view has been formed, in abstract, that the Scottish coal producers could absorb any increase to track access charges. If correct, this must be purely subjective – the report carries no explanation or reasoning behind the conclusion that this cost can be absorbed, readily or otherwise. It is obviously a concern that the conclusion was reached without any consultation with the largest coal producer in Scotland or even its trade organisation.

The following comments attempt to explain why such an arbitrary charge is not well founded, capable of justification, or economically viable.

4. Background on SCCL

SCCL was formed in 1994 when it successfully acquired British Coal's assets in Scotland during the coal industry privatisation process.

SCCL is the largest surface mining company in the UK and currently employs just under 900 direct employees and >1,000 indirect employees. Currently there are 8 mines fully

operational within the Central Belt of Scotland.

Current coal production ranges 3.0mt to 3.5mt per annum with an additional trading of a further 0.5mt to 1.0mt of coal from coal purchased either within the UK or via imports.

Additional sales are made into industrial market sectors (cement, steel, paper making), domestic heating market and limited exports into the ferro-alloy market.

5. Coal Production in the UK

Coal production in the UK has stabilised at approximately 17.9 million tonnes, with Scotland contributing 5.9 million tonnes (information DECC 2011) which equates to a 33% contribution to the UK coal fired electricity generation requirement.

Additional coal required to generate electricity in the UK is imported from the international coal market.

It should be noted that the carbon footprint on imported coal sources is 25 times greater than that from UK coal sources, primarily as a result of distance travelled e.g.

- US coal requires to be transported for fifteen days by barge before transhipment to sea-faring vessels which then undertake a further fifteen day voyage to the UK.
- Russian coal requires to be transported by rail for fifteen days to a sea port before loading. Once loaded the vessel then undertakes a ten day voyage from West Coast Russian/Baltic Ports to the UK

Coal produced in the UK can be transported from the site in which it is mined to the generators within a matter of hours.

It is well publicised that the coal mining industry in the UK is currently facing some difficulty (see recent UK Coal plc, ATH Resources plc and Hargreaves Services plc announcements), primarily as a result of poor trading conditions which are detailed below. There is no doubt, however, that were it not for these constraints the industry would be in a far better position to further increase opportunities and employment as has been the trend over most of the last decade.

6. UK Coal Fired Generation Market

Demand for coal in the United Kingdom is driven by the need for the fuel as a source of generating electricity.

Currently coal is responsible for a large proportion of the UK electricity generation mix. On a typical summer's day (e.g. 25th June and 10th July 2012) coal fired power generation was responsible for 42% and 41% respectively of all electricity generated in the UK (Source: NETA). This regularly peaks in the winter at over 50%. In spite of this consistent demand for power generation from secure and stable sources, generation of electricity from coal in the UK is forecast to reduce due to conformance with limits set in;

1. Large Plant Combustion Directive (LPCD)
2. Industrial Emissions Directive (IED)
3. Electricity Market Reform (EMR)

Notwithstanding this, the EMR key drivers are security of supply, affordability of electricity and de-carbonisation. Coal has unquestionably proven over many years that it is a secure, stable and economic source of fuel supply for electricity generation. These advantages are recognised by both UK and Scottish Governments. The Scottish Government has stated its position on this point:-

'The Scottish Government's policy on clean fossil fuel technology is clear; alongside the expansion of renewables, Carbon capture and storage and clean coal technologies have the potential to transform the way we generate power and make an important contribution to Scotland's low carbon future. Research indicates that CCS has the potential to reduce CO₂ emissions by up to 90% from conventional fossil fuelled power stations. Without CCS, overall costs to halve emissions by 2050 rise by 70% (IEA CCS Roadmap).

Scotland is well-placed to take a lead in the development and commercialisation of CCS. We have the knowledge and expertise in our universities and industry, the infrastructure in the North Sea, and the strong leadership in government necessary to make this happen and achieve our ambition of a low carbon energy economy.'

7. Market Conditions for Coal in the UK

Coal is a commodity which is traded daily on various platforms throughout the world.

The market value of coal is published daily and in the case of the UK, the value is based on an average price of coal delivered into the North West Europe Market from international sources such as Columbia, South Africa etc. The published coal price is based on coal with a calorific value of 25.12 net GJ and <1.0% sulphur. This benchmark value is quoted in US\$ and is called the Average Price Index 2 (API#2). It is published daily giving a spot price, a 2 month forward price, a 4 calendar quarter forward price and a 4 year forward annual price.

The sterling equivalent price is used as a benchmark when negotiating the sales price for coal in the UK. Coal being sold is then converted to a £/net GJ value. As an example, the current (3rd August 2012) international price gives a spot value of \$94.25/tonne (£2.40/net GJ) which is \$28.0/tonne (£18.0/tonne) lower than this time last year (McCloskey Argus).

Reasons for this reduction in the API#2 value include to an increase in availability of coal in the international market mainly due to cheap shale gas in the USA. Whilst the low coal price has increased demand from coal fired generation plants, it is recognised the low price is not sustainable and it should be noted that mine closures are already taking place in the main coal producing countries. Regulatory controls in many of these countries are such that mines can be opened and closed as demand requires with little adverse impact. This is not true in the UK.

8. Effect of Increase to Track Access Charges

A material increase in track access charges will have a multiple effect (details on each follow);

- Non-compliance in the EMR process
- Closure of all Scottish coal mines supplying the power generation market in England
- Increased need for imports to meet demand
- Movement from rail to road within Scotland

- Increased unemployment in rural mining areas where high unemployment already exists
- Increased need for gas which must be imported from a limited number of supplying countries with political instability concerns.
- Government and Local Authority policy conflict (security of supply and reversion to road transport rather than rail)

9. Resultant Non-compliance in the EMR process

The EMR headline drivers are;

Security in Supply: Accepting the proposed increase to track access charges will shrink the indigenous coal market by at least 5% to 10% according to NERA. This will damage security of an indigenously produced fuel source which will consequently reduce a secure base of coal fired electricity generation capacity (40-50% of total generation).

Affordability of Electricity: it has been stated that indigenous coal producers are able to absorb the additional track access cost. This is erroneous, ill-founded and without any objective basis. The publicly listed companies have published their results but as an example, in 2010-11, SRG made a profit of £260,000 on a turnover of £209m. This is a rate of return of <0.1% or 6p per tonne. An increase of £4/tonne is clearly not viable and will be readily confirmed by a brief appraisal of each company's accounts. As a result the increased cost will put the viability of coal mines at risk and force a switch to gas. This will increase price, affect affordability and reduce security of supply.

Decarbonisation: the shrinkage of at least 5% to 10% of indigenous production will have the net effect of increasing imports and increasing the global carbon footprint in transport will lead to a carbon emissions increase.

10. Closure of all coal mines in Scotland supplying the power generation market in England

Coal delivery to Scottish Power at Longannet power station is delivered from mines with the shortest distance to the power plant - predominantly in Fife, Lothian and South Lanarkshire. Coals being transported to England are mined in South Lanarkshire and East Ayrshire. If there is an increase in track access charges as suggested at £4.00/£4.50 tonne, this will completely wipe out any potential to make a profit on coal extracted from South Lanarkshire and/or East Ayrshire.

The estimated transport cost to English power plant would then be circa £12.50/tonne. This is more expensive than the shipping costs from US to the UK or shipping costs from Russia to the UK.

11. Increased need for imports

Cessation or reduced delivery of coal from SCCL will have the direct effect of increasing the need for imports which would not suffer the same additional charge and would make up the shortfall from closed UK mines. As a result it could be argued that the ORR proposed increase is in fact a direct subsidy for foreign producers who are already exempt from UK imposed environmental charges and taxes. This will result in increased tonnage via UK ports and the subsequent potential for rail congestion due to limited capacity from these ports.

12. Movement from rail to road in Scotland

Currently there is a small marginal benefit on delivery to Longannet power plant by rail of approx. £1.00/tonne.

Any additional track access charge will not just put supply at risk but will definitely swing delivery from rail to road. From a producer's viewpoint, this would have a benefit for more local deliveries as it is more effective and would not have a multiple handling cost before delivery at the power plant. However, it would be directly in conflict with political objectives of the Government and local Councils with increased objection from local communities.

13. Increased unemployment in rural areas

Over 75% of SCCL direct employment is in rural areas such as South Lanarkshire and East Ayrshire. Any reduction in the workforce will be sorely felt as there are almost no other alternative employment opportunities. Also, mining is highly skilled and highly paid which makes a substantial contribution to the local economy which definitely cannot be replaced by low paid service sector jobs.

Closure would place a burden on the tax payer and could wipe out the gain on any additional track access charges. There would also be a knock on effect on indirect employment which would also result in an increase in the unemployment figures.

14. Increased need for gas

Any coal lost due to an increase in track access charges will be immediately replaced by either imported coal and/or imported gas. We believe that there would be a resultant increase in port congestion from imported coal and biomass, together with an increase in the amount of electricity generated from gas.

15. Conclusions

- It is recognised that the Government's objective is to reduce subsidies and this includes any track access subsidy.
- The proposed increase is without proper foundation; it is based on an erroneous view of the economic circumstances prevailing in the sector; it will have a direct and highly detrimental effect on the viability of the indigenous mining industry; it will merely promote further imports of coal; and, as a result, affect the balance of payments, reduce high skill, high pay employment in deprived rural areas; and increase the carbon footprint resulting from inter-continental transportation of coal.
- It is just not acceptable to state that an arbitrary increase in charges will produce an equally acceptable reduction of 5% to 10% in coal transport.
- It should be recognised that the significant rise in the amount of coal being used for power generation during 2012 is as a direct result of the international price of coal having fallen dramatically, thus placing it ahead of gas in the merit order. This means more affordable electricity for the end-user at the cost of the indigenous coal producer. Margins are being reduced to an extent that in many cases the cost of production exceeds the proceeds for the finished product. Against this background, the indigenous coal industry cannot bear any increase of track access charges.

- The effect of implementation of increases to track access charges would be in complete contradiction of prime Government policy of promoting indigenous industry; indigenous energy production; security of supply; affordable energy supply; maintaining jobs and promoting high skill employment in areas deprived of any form of employment options.
- The UK and Scottish Governments have prioritised the development of decarbonisation technologies (CCS) over the next 5 years in order that the nation may benefit from the huge resources of indigenous coal and the economic and security of supply benefits which are associated with it. It would be totally perverse to introduce measures such as the proposed track access charges which would completely negate the benefits expected of that Government priority.
- The proposed arbitrary level of track access charge MUST be rejected for all the reasons stated above. **As an absolute minimum, the *status quo* must be maintained with no increase in the currently applicable charge.**

Yours faithfully,

William Wishart

Director, Marketing & Distribution

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Responses to Consultation Questions - Periodic Review 2013 – Consultation on the variable usage charge and on a freight-specific charge

(To be read together with comments in main letter.)

Chapter 3 – Variable usage charge

3.60 Network Rail has already consulted on its estimates of variable costs. Do you have any further evidence, subsequent to Network Rail's consultation, that you wish to provide in relation to the process for estimating variable costs and average variable usage charges?

SCCL does not have all the data to offer a fully informed response, but notes that many of the cost elements appear to have been estimated from engineering judgement rather than firm cost evidence. As a consequence we cannot be confident that such estimates are correct or valid. SCCL is also concerned that the cost savings perceived, or targeted in past charging reviews, have been wiped out by the decision to now include costs relating to masonry under bridges.

3.61 Do you agree with our analysis, which leads to a proposed confidence interval of 15% around Network Rail's estimates of variable usage costs?

SCCL does not understand why a 15% confidence interval is required. Surely track maintenance and renewals costs can be more accurately forecast? SCCL notes that ORR has instructed Network Rail to undertake further analysis to determine freight avoidable costs and awaits the outcome of that work. SCCL questions whether such further detailed analysis can be undertaken within the indicated timeframe and presumes this will merely be a top-down analysis rather than a bottom-up approach that would surely be more accurate.

3.62 Do you agree with our approach to estimating an adjustment to variable usage charges for long-run cost efficiency?

If charges are to be more aligned to cost, as proposed, then SCCL believes it is only correct that long run cost efficiencies are included, otherwise there will be an over-recovery of costs.

Chapter 4 – Framework for a freight-specific charge

4.49 Do you agree with our proposed approach to satisfying the Access and Management Regulations with respect to levying a new freight-specific charge?

Whilst recognising that Government is trying to reduce costs across the board, SCCL is concerned that the proposals contained within this consultation document will have many far reaching effects other than merely reducing Government expenditure on rail freight. A proposal that reverses the previous direction of policy on track access charges, reduces the rail freight market and distorts that market from the status quo, will put at risk past and future investment decisions, create uncertainty about future track access reviews and put jobs at risk (both in the rail industry and in the supply chain). SCCL believes that ORR has

placed a major emphasis on the funds available from Government at the expense of its duty to promote the use of the railway and to enable companies to plan their business with a degree of reasonable assurance.

A material increase in track access charges such as this will increase risk to customers and supply chain players in relation to their future use of rail freight. A consistent and clearly stated interpretation of policy, and of the basis of future track access charges, is required so that industry can plan for the future with a degree of security and confidence.

4.50 Do you agree that the infrastructure costs allocated to freight operators - either for direct funding by freight operators, or explicitly subsidised by government - should be freight avoidable costs, including fixed costs, but not costs common between passengers and freight?

SCCL is not in agreement with this principle.

SCCL draws the attention of ORR to the comparison between road haulage infrastructure charges for freight and those of rail freight, when considering how infrastructure costs should be allocated and/or funded.

Some of the freight avoidable costs are highly subjective and theoretical, based on freight being removed from the network. We do not believe that freight should pay for any costs that are attributable to inefficient historic network infrastructure that already exists. We do not believe it is correct to consider savings that would be achieved by assuming that the network could be remodelled over a 35 year period.

SCCL agrees that the costs of maintaining and renewing freight-only lines and Network Rail's freight staff are real costs that are incurred. Costs that could be demonstrated as being directly saved if there was no freight, we believe are valid.

The existing charges for coal spillage and freight-only lines are directly avoidable costs and should be included in the freight avoidable cost calculation. However, we believe the charging structure should be simplified, and that the different elements of charge should be amalgamated into one overall freight specific charge for each commodity. This would aid the transparency and clarity of the charging regime.

4.51 Do you agree that we should retain our current definitions of particular categories of rail freight commodities as separate market segments?

SCCL has no better suggestion to the ORR's segmentation of the rail freight market. However, SCCL recognises that biomass is intrinsically linked to ESI coal, when used for co-firing for electricity generation. SCCL believes that track access charges should not be discriminatory between market segments.

4.52 Do you believe that we have taken into account the appropriate factors in considering the efficiency of the proposed charges? Do you believe there are other factors we should take into account?

SCCL does not believe proper efficiencies have been considered in calculating the Freight Specific Charge. Historic, inefficient infrastructure on the ground, that permits specific movements to be carried out in a number of ways, will duplicate some charges that feed into the freight avoidable cost figure. It is not right that this duplication is replicated throughout the UK rail system and, given the short time that LEK Consulting has to produce a

credible report, there is a real possibility that the data feeding into it will be incorrect and incomplete, and the output will not be justified.

4.53 Do you agree that our approach (of analysing rail freight traffic) addresses the relevant criteria, when considering to which market segments the charge should apply?

SCCL considers that the analysis undertaken by NERA is primarily focussed on the effect of any increase on the customers of rail freight, something that is interesting but not of primary concern to ORR. The analysis undertaken by MDST is more focussed on the effect on the rail freight market, the subject of the consultation, and totally aligned to the duties of ORR, but is fundamentally flawed in its understanding of the electricity market. The NERA report, conversely, looks at the Electricity Market but is based on “no switching in coal sourcing and transport decisions as a result of changes to charges” (section 6.21) and therefore overlooks the real impact on the freight market and on individual operators. This is a fundamental flaw in the analysis if this is a base assumption of their model and puts a large question mark against the model outputs. This may explain why the modelled £5, £10 & £15 increases result in such small reductions in coal lifted and coal moved. The question of market elasticity is focussed on the electricity market rather than the rail freight market, where elasticity of the market is clearly affected by the length and cost of the haulage.

4.54 Do you agree that certain market segments should be exempt from the new charge?

SCCL believes that track access charges should not be discriminatory between market sectors. Any increase that leads to a reduction in the rail freight market is clearly more than the market can bear. Therefore any increase must be capable of being absorbed by that market, without reducing the size of that market. Any increase should also be justifiable and demonstrably apportionable to the costs of serving that rail freight market, and be compliant with UK and EU legislation.

In view of the economic position of indigenous coal at the present time, coal should ideally be exempt or that no additional charge should apply. The *status quo* position is the minimum acceptable arrangement for the reasons set out in the accompanying letter.

4.55 What do you think is the most appropriate methodology for allocating costs, and what is your reasoning?

SCCL does not support an increase that leads to a reduction in the size of the rail freight market. It believes that this places ORR in breach of its statutory duties. SCCL equally does not support an increase or change in charging mechanism that creates a distortion in the rail freight market.

4.56 Do you consider it is appropriate to cap the new charge for particular market segments according to its impact on the associated freight traffic (in addition to a constraint relating to relevant avoidable costs)? Do you wish to propose an alternative?

Any assessment of what the market can bear is extremely subjective. Whilst an overall percentage-based approach may appear to show modest impacts, however the costs were to be recovered would create market distortions and winners/losers. In some circumstances this could lead to significant closures, job losses and stranded assets. Industry margins are already tight and the notion that these costs can be absorbed is not credible.

Also, the proposed 10% test of price elasticity and market impact is exercised at the national i.e. UK level but that is also arbitrary and masks the potentially devastating impact at the regional e.g. Scottish or Welsh level. If, for example, the Scottish market, which accounts for some 30% of GB coal production, were considered a sub-sector within its own right, then clearly the implications could be much more serious, as illustrated in the MDST Stage 2 analysis.

We note that the MDST Stage 2 Report concludes that an increase of £10 will result in a national decrease in railfreight of 23%, and that there will be dramatic regional fluctuations. For example, Ayrshire mines will lose 24% of their market, even if they reduce their gate price of the coal by £2.50/tonne, and Hunterston would see a drop in business of 41% even after reducing its port charges by 50p/tonne. Should these supply points be unable to absorb any of the proposed increase in charges, then obviously such geographic market impacts would be even greater. All the MDST Stage 2 analysis demonstrates that the market cannot bear the modelled increases of £5, £10 or £15 per thousand net tonne km.

As referred to above and in the accompanying letter, maintenance of the *status quo* is the only viable option for coal transport.

4.57 What should be the unit of the new charge? Please explain your reasoning.

Whilst SCCL does not propose a specific mechanism for future track access charges, it wishes to comment on the proposed options that ORR appears to be considering, as follows :-

- If track access charges were levied on the basis of tonnes lifted, then it would lead to an increased probability of a modal shift from rail to road. For example, if track access charges increase as proposed, there would be a significant volume of short distance haulage that would switch from rail to road. This methodology could have a more dramatic effect on opencast coals that often have a road leg to move the coal from mine to railhead, before onward transport by rail. For mid-distance rail journeys there is an increased risk that the increased track access charge will tip the balance and make it economical to leave the whole journey on road, especially within Scotland where all the indigenous coal is opencast.
- If the proposed track access charge increases were levied on the basis of tonne/kilometres, then it would significantly alter the competitive position of different players in the rail freight market for ESI coal. This would put at risk jobs and investments associated with longer distance movements, which have been established on the basis of current arrangements, whether at power stations, mines, ports or on the railways. Investment decisions already sunk could not have reasonably anticipated these costs.

Maintenance of the *status quo* is the only viable option for coal transport.

Chapter 5 – Freight avoidable costs

Do you agree with our framework for estimating freight avoidable costs? Please explain any suggested changes to the framework, including your calculations (noting that there will be further opportunities to contribute to this work as the cost estimates are refined during the periodic review, for example in relation to Network Rail’s strategic business plan).

For the reasons already stated in response to 4.52, SCCL does not agree with the framework

for estimating freight avoidable costs. At several levels it appears to be too broad in its accuracy with a real likelihood of taking too much cost into the equation.

Secondly, the inclusion of twenty one new people into Network Rail's freight planning team should not occur, as these people have been employed to improve current network performance, and not for CP5 planning purposes.

Chapter 6 – Market Analysis

6.83 Do you have comments on our write-up, interpretation and application of the studies carried out by MDST and NERA? Is there any further evidence that you believe should be considered?

Base assumptions – We have serious concerns about the base assumptions upon which the model is based. Section 3.1 shows the base case forecasts before any impact of changes in track access charges. These base case statistics appear implausible to SCCL members who are closely involved in the market.

- Firstly, 2012 & 2013 show a step change up in coal demand compared to recent years. This has indeed occurred in the first half of 2012, but for next year a number of coal stations have already announced early closure as a result of hours being 'used up'. The UK coal industry, which produces approx 17.9 mt, is capable of placing that tonnage into a UK generation market which will still be burning a considerably larger tonnage post LCPD closures i.e. it wishes to maintain tonnage but increase market share from the current 33%.
- Secondly, the step change back down, onwards from 2014, presumably reflects the impact of LCPD opt-out plant closures, the start of carbon price support and then the effect of IED legislation, but an increase in demand in years 2015, 2017 & 2019 again appears implausible (compared to previous years and compared to 2014), and does not seem to reflect the ramping up of the carbon price floor and expected increase in gas generation.
- The reference to the IED appears grossly over-simplified. The Transitional National Plan (TNP) option is not mentioned, whereas we would expect this to be the most likely route for the majority of generators.
- A coal demand of circa 40mt in 2020 simply does not look credible (and contrasts to DECC's central case projection of less than 70 TWh including coal with CCS).
- This modelled base case (before any effect of changes in track access charges) appears inconsistent with all other projections, including those of DECC. If the base case is flawed this leads us to have serious concerns about the overall accuracy of the modelling and the robustness of any ORR decisions around it.

Methodology – The "fundamentals" model used to estimate the effects on generation is accepted as probably amongst the best currently available, assuming that the base case inputs are correct (see above). However the subsequent inputs need careful consideration.

- There appears to be no appreciation or recognition of port or shipping costs that affect the delivered price of coal to the power stations. For example, the cost of delivering a cape-sized vessel of coal into Hunterston or Redcar will be significantly different to the cost of a panamax vessel into Immingham or Liverpool, or a handy-

sized vessel into Hull. The cost of sea-freight and the cost of port handling (discharge, stocking & re-loading) appears to have been omitted from the analysis.

- There also appears to be no analysis of rail freight capacity (paths) on the key routes. E.g. how much additional traffic is it possible to accommodate on the route out of Immingham? How will this be further impacted by increased biomass traffic with its much lower heat content and bulk density?

Supply Patterns - Any increase in access charges will distort the supply pattern if the increase is linked to distance. So the modelling premise that *“we have assumed that the proportions of coal that each power station sources from and transports via different routes remain unchanged”* is a seriously flawed assumption. This fact is then recognised in later parts with comments about shorter routes being favoured over longer distance routes. It is not clear how these conflicts are dealt with in the model.

Scottish Coal Producers – There is a suggestion that some of the potential track access charges can be absorbed by coal producers, specifically in Scotland. There does not appear to have been any analysis of the profitability of the various Scottish mining companies (or English coal producers). We believe this is essential before any conclusions can be reached. The *“expectation that the greater part of Scottish opencast production will continue to be sold in Scotland”* appears implausible given the closure of Cocksfield and the uncertainty around the future of Longannet with respect to the IED.

Impact of FOC’s – There is interesting comment about the potential impact on FOC’s. Section 4.4.2 speculates about the possibility of some of the increases being absorbed by FOC’s, but (as per the UK mining company comment in point 4) analysis of the profitability of FOC’s would deem this highly unlikely. The report then comments that *“An indirect but more far-reaching impact on rail industry investment might occur if increases in track access charges lead to changes in the nature of competition between FOC’s.”* This appears to infer the real prospect of a FOC(s) withdrawing from the market. This would clearly raise a question as to whether the market can stand such an increase if the result of that increase would cause such a ‘far-reaching impact’. The analysis undertaken is purely subjective and, given the conclusions stated, it is clear that further work is needed to fully understand the possible impacts.

Biomass – The almost casual references to biomass (especially about subsidies) and the future investment decisions of generators (and others) appear to be highly subjective, with little demonstrative evidence to support the statements. The implication that DECC may pay more subsidies to cover increased TACs seems naïve, especially when considering that the recent DECC announcement on ROC’s has resulted in a reduced level of subsidy to those indicated during the consultation process. The use of 2011 biomass burn capabilities to justify a statement that *‘biomass usually makes up only a small proportion of fuel burned’* is extraordinary, when the study relates to the post April 2014 Track Access regime. The impact of the ROC banding review and the potential major increase in co-firing or full conversion has major implications for port and rail capacities and future investment decisions.

Maintenance of the *status quo* is the only viable option for coal transport.

6.84 Do you agree with our proposal, on the basis of MDST’s analysis, to not levy a mark-up on certain rail freight commodities, including intermodal, construction materials and metals?

It is not for SCCL to support increased charges for other commodities, whatever the outcome for coal. However, SCCL is concerned that any variation in the charging of different market segments of rail freight could be deemed discriminatory and potentially in breach of EU legislation.

Maintenance of the *status quo* is the only viable option for coal transport.

6.85 Do you agree with our proposal to levy the proposed charge on ESI coal traffic?

Please see full details of our comments and reasoning in the accompanying letter. SCCL is fundamentally opposed to ORR's proposed change in policy to a market segment approach, based on an assertion that ESI coal 'can bear the increase'. This unprecedented change will have a negative impact on jobs and investment in coal production, generation and freight as well as a potential negative impact on power security and energy prices at a time when these are already subject to major impacts from energy and environmental policy developments. We are also fundamentally challenging the assertion that a wholly arbitrary and subjective 10% reduction in business activity, in any given market sector, is somehow "acceptable". We would argue that no reduction in business activity is justifiable if its full ramifications are not understood and where it is based on policy decisions which could not have been reasonably anticipated and planned for.

The proposal is also discriminatory in its application to freight only. For it to be non-discriminatory, the ORR would need to consult that it should also be applied to the passenger rail business i.e. whether a 10% reduction in passenger numbers or revenue would be acceptable as a result of an ORR pricing decision which significantly reduced the burden of providing the passenger railway upon the taxpayer.

Maintenance of the *status quo* is the only viable option for coal transport.

6.86 Do you agree with our proposal to levy the proposed charge on spent nuclear fuel traffic?

It is not for SCCL to support increased charges for other commodities, and SCCL is concerned about the potential discriminatory effect of such charges.

6.87 What views do you have on our analysis of the iron ore market segment? Do you consider that there is also a case for levying the proposed charge on iron ore?

It is not for SCCL to support increased charges for other commodities, and SCCL is concerned about the potential discriminatory effect of such charges.

6.88 Do you agree that we should revisit our policy on levying a charge for the biomass market segment to coincide with the recalculation of its credit (subsidy) regime (from 2017 for England and Wales)?

Biomass Investment decisions associated with biomass co-firing will be taken in conjunction with decisions on the future of the coal infrastructure and capacity on which it depends.

Simply deferring the decision on biomass charging adds further uncertainty to the investment case at ports and on the railways as well as at power stations. The reduced co-firing ROC level makes biomass investment decisions even more marginal, and uncertainty over track access charges for biomass could be the final straw. This investment is required to deliver the Government's strategy of supporting co-firing of biomass, as part of the decarbonisation of the electricity market. Regulatory uncertainty on track access charges for



biomass will undermine Government energy and climate change objectives.

6.89 Do you consider that the proposed charge should be levied on other (non ESI) coal flows?

SCCL's opposition to the proposed charge applies equally to other (non ESI) coal flows. Any analysis of these other sectors would doubtless demonstrate that they would be at even greater risk from increased charges than ESI coal.