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Thursday 26 May 2011

Rupika,

**Re: Consultation on the policy on variable usage charges for modified vehicles**

1. We welcome the opportunity to respond to your consultation on the proposed policy on vehicle modification both in CP4 and CP5. We consider it to be very useful to clarify the policy in this area.

2. We are also pleased with the progress that has been made to date, by all parties involved. We fully support operators making track friendly vehicle modifications and we have been proactive in facilitating this. Particular examples are the support we have provided to trials of a novel new “hydro bush” on Siemens Desiros vehicles on the Wessex Route and on mark 4 vehicles on the East Coast Main Line. We have also worked closely with South West Trains and East Coast to determine reduced VTACs for class 444s, 450s and mark 4 vehicles applicable when these modifications are rolled out across their fleets. We are committed to supporting initiatives which reduce ‘whole industry’ costs, and will continue to work collaboratively with the industry in this respect.

*Treatment in CP4*

3. Currently, the variable track access charge (VTAC) is designed to provide signals to operators and their suppliers and funders for the development of vehicles which minimise track wear. We agree that charging a reduced VTAC to operators which make modifications to their vehicles to make them more “track friendly” is a reasonable approach to provide appropriate incentives for efficient use of the network.

4. The VTAC represents the short run incremental cost at an average level across the entire network. For this reason, we consider that there are likely to be



situations where a reduced VTAC may not accurately capture the cost savings to be made as a result of particular vehicle modification on a particular route. Therefore, we strongly support ORR consenting to an alternative approach, subject to the relevant criteria (as set out in paragraph 11 of your letter). The use of the new P12 wheel profile is an example of a beneficial vehicle modification that is unlikely to proceed through the use of VTAC in its current form but which has the potential to reduce system costs when applied on a more specific route or fleet basis.

#### *Treatment in CP5*

5. We consider that VTAC discounts should be 'preserved' in absolute terms for CP5. It is important ORR provides further clarity on this issue in order not to undermine operators' business cases. We note that it is also important for DfT to confirm definitively that the savings to operators would be honoured and not clawed back through the schedule 9 / clause 18.1 provisions in franchise agreements. We have observed through the on-train metering project, how actively train operators engage in situations where cost savings are not clawed back by DfT.

6. Where reduced VTACs are offered, we would be content to include unmodified rates on the price list for CP5 if this is required in order to provide transparency to operators.

7. However, we request further clarity from ORR on how it sees this working where an entire vehicle class has already been modified. In this situation there will not be any unmodified vehicles registered in the Rolling Stock Library, therefore, does ORR propose a "dummy" rate is included on the price list?

#### *Bespoke deals under the track access contract framework*

8. We are pleased that ORR is supportive of bespoke deals that deliver benefits to industry. Such clarification is particularly important in the context of Network Rail's devolution plans, which will facilitate much closer working arrangements with our customers. We believe it is important that the regulatory framework provides flexibility in this respect. We agree that there is a need for transparency in such deals and that they must not unduly discriminate against other rail users. We see no reason why such bespoke deals cannot be as open and as transparent as changes to track access charges.

9. We note that ORR does not expect to consent to bespoke deals which are direct substitutes for track access charges. However, as mentioned in paragraph 4 of this letter we consider that, due to the nature of the current charges model, it may not always be appropriate to use the VTAC as defined by the VTAC model to 'determine' the cost savings made. Therefore we consider that bespoke deals should be encouraged where there are real industry cost savings to be made.





Indeed, as part of the value for money agenda, we consider this to be vital. It is very difficult to predict the types of modifications that can or will be made in the future; therefore we think it is unwise to close out other options of achieving the overall aim of reducing industry costs, as you appear to be suggesting in paragraph 18 of your letter.

#### *Bespoke deals and incentives*

10. We note that your consultation letter does not address the issue that operators may not always be in the position to finance upfront costs of vehicle modifications, despite there being the possibility of substantial long-term savings to the industry from doing so. In these situations it may be appropriate for Network Rail to remunerate the operator for the initial investment, instead of charging a reduced VTAC.

11. Currently, Network Rail is unable to propose changes to vehicles; however we think that the option of allowing Network Rail to propose this should be available. We consider that where Network Rail sees that there are considerable cost savings to be made to whole industry costs by modifying vehicles, but the operator cannot afford to do this, Network Rail should be able to propose such changes and fund the investment instead of charging a reduced VTAC. This kind of approach would make it simpler for Network Rail to look for ways to achieve system optimisation, which would reduce its total costs including costs paid by operators.

12. Were Network Rail able to propose changes to vehicles, it would seek to do so with the support and collaboration of operators although in extremis operators could have a right of appeal to ORR over such changes.

13. This type of bespoke deal may also be effective in mitigating the issues that arise where the VTAC model is unable to model a reduced variable cost despite there being obvious benefits from doing so, for example there may be substantial cost savings to be made on a particular type of track geometry, however the VTAC may not be sophisticated enough, at that level, to recognise the cost savings, and hence a reduced variable cost. In this case, an operator would have little incentive to pursue the investment.

14. We consider that by encouraging the use of bespoke deals including compensation and/or remuneration for investments, it could be much simpler and more effective to reduce whole industry costs.

#### *Single network charging approach*

15. As we highlighted in our response to ORR's Draft Regulatory Statement on the Borders Railway Network, we would stress the benefit of having a single charging




regime across the network, to ensure consistency of approach across the industry. We do believe, however, that a sufficient degree of flexibility within the charging regime is important, such that we can work with our customers to achieve optimal outcomes in the areas in which they operate.

16. We do not consider our response to be confidential, and we are content for it to be made available on your website.

17. If you would like to discuss any of the issues raised in this letter please contact Ben Worley ([Ben.Worley@networkrail.co.uk](mailto:Ben.Worley@networkrail.co.uk)) or myself.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Peter Swatridge". The signature is fluid and cursive, with the first name being more prominent.

**Peter Swatridge**

Head of Regulatory Economics

