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TRACK ACCESS AGREEMENT: RAILTRACK PLC AND ENGLISH WELSH & SCOTTISH RAILWAY LIMITED

1. I enclose, with this letter, directions to enter into a track access agreement.
2. The Regulator has considered the application under section 17 of the Railways Act 1993 ("the Act") made by English Welsh & Scottish Railway Limited (EWS) on 21 December 2000 for directions to be given to Railtrack PLC (Railtrack) to enter into a track access agreement to replace the existing access agreement that will expire on 31 March 2001. References in this letter to the parties are references to EWS and Railtrack, and references to sections or Schedules are, unless otherwise specified, references to sections or Schedules of the Act.
3. In considering the application and in reaching his conclusions as to appropriate directions, the Regulator has taken account of his duties under section 4 and of the criteria set out in the Regulator's December 1994 'Criteria and Procedures For The Approval Of Freight Track Access Agreements'. The Regulator has used the statutory procedures and timescales set out in Schedule 4 to consider the application. This letter sets out the reasons for the Regulator's conclusions.

Section 17 Application

4. The application is for access to Railtrack's network (for which Railtrack is the facility owner). Having considered the provisions of section 17 (1), the Regulator is satisfied that he may consider the application and grant such directions as he considers appropriate. This is because:
 - the railway facility which is the subject of the application is not an exempt facility by virtue of section 20 and therefore the Regulator believes that he is not prevented from giving directions by section 17 (1) (a) which states that no directions shall be given if and to the extent that the facility is an exempt facility;
 - the Regulator does not consider that the performance of an access contract as contemplated by the directions would necessarily involve Railtrack being in breach of an access agreement or an

international railway access contract. (If he considered otherwise the Regulator would be prevented, by section 17 (1) (b), from giving directions to Railtrack.) This is because EWS has already bid for the train paths that it requires to meet the rights described in Schedules 3A and 3B of its application and Railtrack has accepted the bids for the timetable periods within the life of this agreement. In addition, in the course of the consultation carried out by the Regulator no evidence of any breach was identified by the parties or others; and

- on the basis that he has consulted widely and that Railtrack has not advised him otherwise, the Regulator is satisfied that Railtrack does not require the consent of some other person before it can enter into the proposed access agreement and that therefore the provisions of section 17(1)(c) do not apply. In a letter dated 8 March 2001, Railtrack has brought to the Regulator's attention an agreement entered into between the British Railways Board and Railfreight Distribution (Channel Tunnel) Limited (RfD) dated 30 March 1994 (the Back-to-Back Agreement relating to the Channel Tunnel Usage Contract) that guarantees RfD's rights over British Railways' Network and in which Railtrack undertakes not to grant access which may conflict with rights granted to RfD. RfD's rights have been assigned to English Welsh & Scottish Railway International Limited (EWSI). However, neither Railtrack nor EWSI has indicated that any rights in the application conflict with RfD's rights, and indeed EWSI has said that "there are no contractual obligations owed by Railtrack to EWSI which Railtrack may breach if it entered into the proposed agreement". Railtrack also noted, in its 8 March 2001 letter, the arrangements for Thameslink 2000 but none of the relevant consultees have raised any objection in respect of the proposed agreement.

5. The parties have made submissions to the Regulator in connection with his power to give directions pursuant to section 17 in relation to international services. Railtrack has argued that some services constitute international services and EWS has argued to the contrary. The Regulator accepts that he is not entitled to make directions to the extent that the permission to use the railway facility could have been applied for under legislation implementing Council Directive 95/19/EC (section 17 (1) (d)). The Regulator does not believe that his directions would fall within the scope of section 17 (1) (d) because he has identified, from the information provided by the parties, those flows which may constitute international services and excluded them from the scope of his directions. He has indicated to the parties that insufficient explanation has been provided for him to reach any other conclusion on this matter. Accordingly, the parties must give further consideration to the issue and determine whether any particular services may be operated under the agreement or whether the parties need to enter into an access agreement pursuant to the Railways Regulations 1998.

Consultation

6. The Regulator has stressed the importance he attaches to the consultation of those who might be materially affected by the proposed track access agreement. Wide-ranging consultation was therefore undertaken.

7. The Regulator carried out two written, external consultation exercises (the appendix to this letter contains a list of consultees) on the contents of the application from EWS. Following the receipt of various written representations and an oral explanation, on 23 January 2001, from Railtrack of its representations, he provided an opportunity for those who had made material comments to make further comments at a hearing.

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8. The first external consultation was of users, funders and others and included all the passenger and freight operators together with the Passenger Transport Executives, London Underground Limited, the Strategic Rail Authority (SRA), the Department of the Environment, Transport and the Regions, the Health and Safety Executive and the Rail Freight Group.

9. The second consultation was of 50 'interested persons' who were identified by Railtrack in accordance with the requirements for a section 17 application under Schedule 4. These included the Freight Transport Association, the British Railways Board and European Passenger Services Limited.

10. Replies were received from a total of 20 organisations. They have been placed on the ORR website (www.rail-reg.gov.uk) together with the record of Railtrack's oral representations on 23 January 2001 except in one case where the Regulator has agreed to a request that they should not be published for reasons of confidentiality. Those who made material representations were invited to the hearing held on 7 March 2001. Freightliner Limited (Freightliner), GB Railfreight Limited (GB Railfreight), the SRA, the Rail Freight Group, the Freight Transport Association and Greater Manchester Passenger Transport Executive (GMPTE) accepted the invitation and sent representatives to the hearing. A transcript of the hearing is also available on the ORR website. Following the hearing, EWS and Railtrack both made further written submissions. In addition a meeting of the parties and ORR was held on 20 March 2001 to discuss disputed aspects of the access rights which EWS has requested in its application. An agreed note of that meeting and the further submissions made after the hearing are also available on the ORR website.

11. The issues arising from the external consultation were broadly the same as those raised by Railtrack in its representations on the application. Freight operators were particularly concerned about competition and charging issues. Some operators were concerned about the effects of the application on their own rights. However, there was a broad measure of support for the EWS application from passenger operators and others including the SRA and the Rail Freight Group. All issues raised in the consultation are fully dealt with below.

The specific issues between the parties

Process Failure

12. The Regulator takes very seriously the comments made by Railtrack that EWS did not attempt fully and properly to negotiate a replacement access contract before making its section 17 application; the Regulator notes that EWS denies this.

13. Section 17 is a statutory process available to any person seeking to use a railway facility. An applicant runs the risk that the Regulator will decline to issue directions or will issue directions that he considers appropriate, but which do not match those applied for. However some of this risk is reduced if the parties have already negotiated and agreed particular aspects of an access agreement before any application under section 17 since the Regulator would take into account any such specific agreements in considering the whole application. Furthermore, a negotiated agreement is generally preferable since the parties themselves have ownership and it would therefore be expected to operate effectively in practice. Hence the Regulator generally expects and supports negotiation.

14. Operators may of course continue to negotiate whilst making an application under section 17 in order to ensure that they achieve an approved access agreement before a particular deadline via one or other mechanism. In this particular case, he urged the parties to negotiate in the hope of reaching agreement before he had made his decisions on the application under section 17. If an agreement had

been reached, the section 17 application could have been withdrawn and an application made under sections 18 or 22.

15. EWS has argued that it had difficulty in negotiating a new access agreement with Railtrack given the uncertainties in the rail freight environment, including the Regulator's review of freight charges. However, the Regulator notes that this has been long discussed and that discussions with all freight operators and Railtrack in December 2000 highlighted a range of options which could be used to resolve the issue. Indeed, in its Section 17 application, EWS proposed one of these options (that of retrospective introduction of the Regulator's final conclusions). The Regulator does not consider therefore that this would have been sufficient reason for EWS not to negotiate an access agreement with Railtrack.

16. EWS has also argued that it has limited resources and continuing to negotiate would not be a productive use of those resources given that it also wished to negotiate a new agreement following the Regulator's conclusions on freight charging. The Regulator understands that negotiation may be time consuming but, as discussed above, believes that it is an important element in the commercial relationship between the parties.

17. Notwithstanding this, the Regulator has concluded that in light of his section 4 duties, including in particular his duties to promote the use of the railway network in Great Britain for the carriage of passengers and goods and to enable persons providing railway services to plan the future of their business with a reasonable degree of assurance, he should give directions to Railtrack in this matter.

Conflicts with existing and emerging regulatory principles

18. Railtrack and a number of consultees (including GB Railfreight and Freightliner) have argued that the terms of the application conflict with existing and emerging regulatory policy. GB Railfreight argued in its written representations that the agreement should reflect current or emerging regulatory policy, particularly on usage and capacity charges, and that otherwise EWS would be in a position to 'continue to compete unfairly against other prospective train operators, to the detriment of the industry'. Railtrack drew attention in its representations to the proposals in relation to Quantum Bid Rights and the 'lax use-it-or-lose-it arrangements' that 'restrict the ability of new operators to compete with EWS for existing traffics and might have the effect of frustrating the ability of new operators to gain access to Train Slots on constrained sections of the Network'.

19. The Regulator believes that the application has to be considered in the light of his section 4 duties and in accordance with his existing published criteria and procedures for the approval of track access agreements. Although a considerable amount of work has been undertaken by the industry on model clauses, these have not yet been finalised. Other recent agreements have been approved but without requiring re-openers or attempting to anticipate the content of model clauses. Similarly, the Regulator has not yet published the conclusions of his freight charging review. However, in this respect, he has acknowledged the need for providing a retrospective adjustment to charges following conclusions of the review. This is considered in more detail in paragraphs 61 to 67 below.

The extent of change required

20. EWS has stated that its application requires minimal changes to the terms of its current agreement with Railtrack and that it was seeking a "rollover" and thereby accepting the terms of the existing agreement. However the application did include new provisions, for example one which would

have given EWS a priority bidding status for timetable periods beyond the duration of the agreement. These changes were described in the Regulator's letter to consultees dated 5 January 2001 (also available on the ORR website).

21. Railtrack has argued against some of the changes proposed by EWS and suggested instead, in a draft section 22 agreement, terms that are significantly different from the terms of the existing agreement between the parties.

22. The argument for minimal change received broad support during the consultation. Central Trains Limited (Central) considered it the most expedient option in the short term. The SRA, the Freight Transport Association and the Rail Freight Group argued that the directions should minimise change.

23. The Regulator has concluded that he should only issue directions to Railtrack to enter into an agreement whose terms, in so far as is possible having regard to his section 4 duties, mirror those of the existing access agreement. This is because the parties have agreed, and he has approved, following consultation as necessary, the existing agreement. Given other uncertainties and change within the industry, this maintenance of the status quo, in so far as possible, balances the Regulator's section 4 duties. Nonetheless the Regulator believes that some changes are necessary to achieve an appropriate balance of his section 4 duties, given the current state of competition in the industry and the various developments expected (e.g. the publication of the Regulator's final conclusions on freight charging). His directions set out each of the changes which he requires and the reasons for the directions are set out in this letter.

24. The parties have made numerous amendments to the existing access agreement both pursuant to the provisions of section 22 and pursuant to the terms and conditions of the agreement itself. The Regulator has carried out an extensive comparison of the application made by EWS and the existing one (as amended by the section 22 approvals and the further amendments made to the agreement that have been notified to the Regulator by Railtrack).

25. This comparison has revealed that the EWS application differs in certain respects, largely in relation to Schedule 3A Part III and Schedule 3B Parts II and III thereof (the lists of services) from the existing access agreement. Further EWS noted at the hearing of 7 March 2001, that the Schedule 3A Part III it had submitted contained numerous errors and included rights that it had not specifically negotiated with Railtrack. On 9 March 2001, following discussions between the parties, EWS submitted amendments to the Schedule 3A Part III contained within its section 17 application, correcting these errors. Railtrack, in a letter dated 9 March 2001, identified its outstanding concerns, which were then discussed and largely resolved at a meeting between the parties and the ORR on 20 March 2001. Subsequently, on 22 March 2001, EWS submitted further amendments to Schedule 3A Part III and the Regulator has directed that this revised Schedule to the agreement be used on the grounds that it does not add to the rights being sought by EWS in the section 17 application and therefore does not require further consultation – all interested parties have already had a chance to comment on the full contents of the original application. As noted earlier, a record of the meeting is available on the ORR website. The revised Schedule 3A Part III and the Schedule 3B Parts II and III contained in the application form part of the directions.

Duration of the agreement

26. The EWS application is for an agreement commencing on 1 April 2001 and expiring on 31 May 2002, but which may be terminated and replaced by a new agreement in the event that the parties have agreed and the Regulator has approved such a new agreement, before the expiry date. At the hearing the parties made clear that there is no disagreement between them regarding the proposed duration and early termination provisions and the Regulator considers it appropriate that the agreement should have such provisions. In order to ensure that the principle is applied, the Regulator has given directions to Railtrack requiring it to enter into an agreement which will terminate either on 31 May 2002 or an earlier date if a new access agreement is entered into by the parties.

27. Some consultees (including GB Railfreight, Freightliner and Direct Rail Services Limited (DRS)) have argued that the fourteen month period for the agreement is too long. Freightliner argued at the hearing that aspects of the application and the existing access agreement demanded immediate attention and that its “fundamental defects” should not be “perpetuated” for a further 14 months to the disadvantage of other operators. It drew particular attention to the effects of alleged competitive advantages enjoyed by EWS.

28. A number of other consultees (including the SRA, Freight Transport Association and Rail Freight Group) have supported the 14 month term, on the basis that it would reduce disruption and uncertainty for rail freight operators.

29. The Regulator notes that the proposed duration:

- accords with the timetabling and bidding cycles and procedures. The train paths for which access will be given during the life of this agreement have already been allocated to EWS under the timetabling provisions of Part D of the Railtrack Track Access Conditions;
- avoids some uncertainty for the rail freight industry, in that the necessary paths across the network will be retained; and
- will not have an effect on his own process for concluding the freight charging review (as was suggested by some consultees). Noting the arguments made by some consultees about the potential for different commercial positions after the freight hearing review, the directions provide for retrospective adjustment of charges. This is described in more detail below in paragraphs 61 to 67.

30. He has therefore concluded that it is appropriate for him to give directions for a 14 month access agreement.

Other provisions of the agreement

31. GMPTE, Great Western Trains Company Limited and Merseytravel were concerned for the effects on their own services of the rights being sought by EWS. GMPTE mentioned in particular the Oldham Loop and Merseytravel drew attention to the capacity problems of the Manchester area and the West Coast mainline north of Crewe.

32. The access rights included in the application made by EWS have already been accommodated in the timetable. Railtrack has accepted the bids made by EWS but cannot provide a warranty that if

EWS were to request similar rights in the future, they would not conflict with the unexercised rights of other operators for timetable periods beyond the expiry of this agreement.

33. The Regulator has concluded that in these circumstances, the issue of whether the rights sought by EWS will have an adverse impact on the rights of other operators only arises after 31 May 2002. It is therefore an issue for negotiations between the parties for an agreement for the period after 31 May 2002.

Priority Bidding Rights

34. In its application EWS has sought bidding rights beyond the term of the agreement, and which are greater than those set out in the existing access agreement. EWS wishes Railtrack to accord priority to bids made during the life of the agreement to timetables after the end of the agreement on the basis of its need for 'absolute certainty'. EWS countered the argument that this would give it an unfair advantage by stating that it was happy for this priority to apply to other operators in the same position but that it needed this certainty to fulfil its ongoing contractual obligations.

35. The Regulator would not expect to approve an agreement that conflicts with the Railtrack Track Access Conditions since these are incorporated into all track access agreements. Furthermore, Part D of the Railtrack Track Access Conditions, rather than the terms of a bilateral agreement, should determine bidding priority. The terms of Part D are currently under review by the Class Representative Committee, which has accepted the recommendations of a working party on the way in which bids are given priority. EWS noted these recommendations at the hearing but argued that it would wish to have the priority provisions in its access agreement until any changes to Part D had been implemented, at which point the provisions would "become unnecessary" and EWS would expect to remove them and "rely on the industry process that has been agreed".

36. The Regulator has however concluded that the general principle that the Railtrack Track Access Conditions should prevail over track access agreements remains important in ensuring that all parties face the same processes. In his directions he has not, therefore, provided for this part of the application made by EWS.

Use it or lose it – Schedule 3A paragraph 4

37. EWS has applied to the Regulator for retention of the use it or lose it provisions in paragraph 4 of Schedule 3A of the existing agreement between EWS and Railtrack. The Regulator has considered representations made to him by consultees (in particular those made by Railtrack, GB Railfreight, Virgin Trains (CrossCountry Trains Limited and West Coast Trains Limited), Great Western Trains Company Limited, Central, Rail Freight Group, DRS, Freightliner and the SRA) and the parties themselves. Railtrack has proposed reducing the use it or lose it provision to 8 weeks and other consultees have commented on these issues.

38. EWS has argued that any changes to the use it or lose terms of its agreement with Railtrack should await the outcome of the work on model clauses on this issue. At the hearing it also provided an example of how the terms proposed in its application had, under the same terms in its existing access agreement, led to it relinquishing rights following the loss of a contract to move waste materials.

39. However, a wide range of consultees agreed with Railtrack on the need to strengthen the use it or lose it terms of the proposed agreement. At the hearing Railtrack described its proposal to reduce, from 12 months to 8 weeks, the qualifying period of non-use as a pragmatic way to improve the

management of capacity utilisation. Some consultees supported Railtrack. Others, including the Rail Freight Group, sought changes but were concerned to avoid changes that increased passenger operations and rights of passenger operators at the expense of rail freight.

40. Freightliner argued at the hearing for rights that were treated like a commodity, that were identifiable and exchangeable between operators. Freightliner and GB Railfreight argued for a mechanism for the relinquishment of rights rather than what they perceived as a system that relied on the 'grace and favour' of EWS and Freightliner argued for an active role for the Regulator.

41. The Regulator has concluded that there are compelling reasons to strengthen the use it or lose it provisions in the agreement, on the basis that the prevailing conditions on the network have changed since the existing access agreement was approved in 1997. The network is more heavily used now than it was then and there are parts of the network where there are very few available paths. Competition issues generally are more to the fore in 2001 than they were in 1997 since new and existing operators are now looking to compete with EWS for business and they expect a level playing field. In these changing conditions the Regulator is especially mindful of his duty to promote competition. The Regulator recognises that Railtrack's proposal, to reduce the period of non-use from 12 months to 8 weeks, does have some merits in increasing flexibility on the network but he notes that it would not help a successful competitor of EWS to move goods immediately on being awarded a new contract.

42. The Regulator does not believe that competition in the provision of railway services can be promoted adequately by the proposals in the EWS application because they limit competitors to applying for rights to paths that are not being used by EWS or which it has not operated for a long period of time. The Regulator believes that users of railways services must be guaranteed continuity of service whilst at the same time being assured of having the benefit of full competition for the provision of railway services.

43. The Regulator has not removed or altered, in his strengthened use it or lose it modifications, the existing mechanism whereby any firm right not used by EWS for more than one year will be removed from the access agreement. The Regulator will be notified of any such change. As stated above, the Regulator sees some merit in the argument for reducing this period but, in accepting that there is a compelling need for change, he is addressing the main issue, which is one of competition.

44. He has instead provided that, on application from another non-passenger operator for rights which are substantially similar to those which EWS holds, Railtrack may, if it is unable to meet the request of the applicant whilst also meeting EWS existing rights, notify EWS and ask whether or not it has a reasonable ongoing commercial need for the rights. The application must contain justification of the need for the specific rights.

45. EWS will then have 10 days in which to respond to the notification – to give information about any such commercial need. If EWS does not respond, Railtrack will be permitted to assume that there is no such commercial need and the rights will be given up automatically. Railtrack will notify the Regulator and may negotiate a new access agreement with the operator who made the application. That access agreement would be subject to regulatory approval. If EWS responds during the 10 days and argues that it has an ongoing commercial need for the rights, but Railtrack may, if it disagrees, then refer the issue to the Regulator for determination.

46. The Regulator has sought to ensure fairness to all parties in these procedures and to that end, has provided for independent determination where the parties are in dispute. He has sought to ensure

that decisions are made in sufficient time (by setting out a specific time frame) and against robust criteria in order to promote effective competition.

47. EWS has noted that it would not necessarily be able to relinquish the right to paths if it lost a contract with an individual freight customer. In some cases, this is because many freight services convey cargo from a range of different customers or different cargos for the same customer. Hence a particular right may still be required even if a single customer's flow has been lost to a competitor. This goes to the heart of what EWS will need to do to prove commercial need. They could for example, be required to demonstrate that the train could not be flexed to provide an additional path or that the remaining cargo could not be attached to other trains, again providing the requisite additional path for the new operator. The Regulator's view is that, in order to promote effective competition and ensure a fair outcome, the standard of proof should be high i.e. that EWS must demonstrate why further flex could not be given or the remaining cargo should not be attached to other trains.

48. The Regulator believes that these provisions will allow new entrants to be reasonably certain of being able to use the network to fulfil a customer contract. In so doing, he has protected paths for the movement of freight by ensuring that the provisions apply only to freight operators. He has also provided EWS with the appropriate opportunity to justify a commercial need to continue to hold the rights.

49. Although there is no evidence that EWS has 'blocked capacity that it has no intention of using', a concern expressed by Freightliner at the hearing, the Regulator considers that he is justified, in the circumstances described above, in making a change that will initially impact more upon EWS than other freight operators. He expects similar use it or lose it provisions to those in the directions he has given on this matter to be included in future track access agreements for all freight operators or to be presented, when he is asked to approve such agreements, with a clear rationale, on public interest grounds, for its exclusion.

Quantum Bid Rights

50. The existing access agreement contains three forms of bidding right for services (other than for Royal Mail services). These are Bidding Cycle Rights (BCRs), Quantum Bid Rights (QBRs) and spot bid rights. BCRs are firm contractual rights to a slot obtained by bidding into a bidding cycle, in accordance with the nominated service characteristics and timing specifications both identified in the agreement at Schedule 3A Part III. QBRs are rights to bid on or after the commencement of the supplemental period in the timetable development period for a specified quantum of train slots with nominated origin and destination, but with no timing specification. Spot bid rights are rights to make spot bids, in accordance with Part D of the Railtrack Track Access Conditions, for services lasting no more than six months and without the need to request the specific prior approval of the Regulator.

51. Under the existing access agreement and the application under section 17, changes to BCRs are subject to agreement by the parties and approval by the Regulator. Other provisions apply to QBRs that allow for self-modification under certain conditions. Concerns were expressed (at the time the existing access agreement was approved) about the cumulative effect on the capacity of the network, of the ability to vary and add to QBRs.

52. EWS would be expected to request Additional or Varied Services to QBRs if it had a reasonable commercial need for these services. Railtrack would then apply its own criteria to determine whether it

could accept such a request. The existing agreement provided for a number of safeguards including caps on movements through particular locations and flex arrangements.

53. Railtrack has argued that the provisions for QBRs being sought by EWS provide EWS with unreasonable flexibility on a constrained network and that this discriminates against other operators. It was supported in these arguments by Freightliner and GB Railfreight. Some passenger operators, including Silverlink and Virgin Trains (CrossCountry Trains Limited and West Coast Trains Limited), agreed that EWS was seeking too much flexibility or that timetable development was being constrained over key corridors. Some consultees, however, including Great North Eastern Railway Limited and the Freight Transport Association, supported the flexibility that these provisions accorded a freight operator.

54. The Regulator believes that the right of EWS to vary QBRs without referral to the Regulator pursuant to section 22 is no longer appropriate. He has concluded that the concerns expressed at the time of the approval of the existing agreement in 1997 about the cumulative effect on other operators and the capacity of the network are relevant in the changed circumstances of 2001. Therefore he has concluded that these particular provisions need to be removed in the interests of promoting more competition for the operation of freight on a congested network. Consequently, whilst not wishing to affect the existing quantum of rights of the parties as set out in the existing access agreement, he has provided that the agreement will require the parties to seek his approval to vary or add to QBRs.

Performance

55. The Regulator notes that the network has become significantly more congested since the original agreement was entered into and also that the total delay identified as being associated with the movement of freight traffic has increased dramatically over the past four years. He recognises that much of the increase in delay has arisen because of an increase in the overall volume of freight train operation. However, he is concerned to ensure that parties are adequately incentivised to improve performance in the interests of all users of the network.

56. The Regulator expects Railtrack to operate the delay attribution system accurately and efficiently at all times because it underpins the performance regimes of all train operators on the network. He notes that this obligation is contained in Track Access Condition B.1.1. EWS has carried out an investigation of the delay attribution system pursuant to Track Access Condition B3. B5 allows for the implementation of alterations. However the Regulator has not been provided with evidence that all of the provisions of Part B have been exercised and that Railtrack has refused to implement any alterations. He notes that if directions are given to enter into the proposed agreement the parties may submit an application under section 22 of the Act to amend Schedule 1 to the agreement. He also notes that EWS, along with all train operators, may dispute the attribution of any delay under normal industry arrangements and the Appendices to Schedule 1 of the proposed agreement.

57. The existing agreement includes a performance regime in Schedule 1. However documentation supplied by EWS and Railtrack in connection with the application has confirmed that for much of the life of the agreement the regime has not been operated as described in that Schedule. The Regulator is aware that EWS has alleged that Railtrack has not operated the delay attribution process in a fair manner. He notes that EWS is proposing that the existing Schedule 1 should be amended to incorporate a in the Minutes Delay to Third Party Trains Attributable to EWS and increase in the Minutes Delay to Services Attributable to Railtrack.

58. The Regulator does not see a general need for the arrangements that have been in place since 1997 to be changed for the period of the agreement and . He has concluded that his directions should include the existing Schedule 1.

Royal Mail Services

59. The Regulator has noted that EWS wishes to obtain firm rights to continue the operation of three Royal Mail services, identified as , which are running currently under spot bid rights. EWS also wishes that these services should operate under the provisions of the performance regime in respect of Royal Mail services. Two of the services operate on the West Coast Main Line and the third service on the East Coast Main Line. The issue between the parties is not one about the operation of these trains. There are paths for them that do not conflict with the rights of other operators for the period of this agreement. The issue is the unwillingness of Railtrack to accept them under the performance regime for Royal Mail services. Railtrack has argued that maintenance and renewal work on the network will increase its performance payment liabilities to EWS and that, due to the West Coast Route Modernisation, it will be unable to deliver the service to the standard that its customer requires.

60. The Regulator has concluded that EWS should indemnify Railtrack for the expected additional costs of the performance regime arising from these rights, through a supplementary access charge. This will therefore ensure that EWS and Railtrack continue to be incentivised to maintain on-time performance. Accordingly the Regulator has directed Railtrack to include a new Part IX in Schedule 1B of the agreement which provides for an access charge supplement for the expected performance regime costs arising from the operation of these trains. Railtrack only provided the Regulator with its estimate of the expected costs of these services on 22 March 2001 and hence neither EWS nor the Regulator have had sufficient time to validate the estimate. Given this, the Regulator has directed that Railtrack must calculate the cost and submit it to the Regulator for his approval. He has also provided that, should EWS conclude that it would prefer not to operate some or all these trains, the access charge supplement is reduced pro-rata to the reduced use of the rights.

Charges – Schedule 4

Charges – Retrospective Adjustments as a result of the Freight Charging Policies

61. In their submissions on the appropriate charges for the agreement EWS and Railtrack have taken different views on a range of issues often citing as the rationale the context of the Regulator's current review of access charges for freight operators.

62. In its application, EWS proposed an adjustment mechanism to alter the charges retrospectively in line with the outcome of the freight charging review and to incorporate the conclusions of the freight charging review if this was concluded during the 14 months of the agreement. Railtrack argued initially that the agreement should reflect some of the emerging views on costs arising from the freight charging review. However, at the hearing the issue between the parties on the retrospective adjustment narrowed to whether it included the structure as well as the levels of the final conclusions. EWS confirmed at the hearing that it intended the full conclusions of the Regulator's review to be reflected through the adjustment.

63. The Regulator believes that the adjustment needs to be structured so that the full conclusions of the freight charging review can be incorporated into the agreement. This includes the conclusions on the level of charges and also the structure of those charges (including the performance regime). This

latter point implies the need to ensure the final conclusions are incorporated in relation to both the fixed and variable charges and additionally to include any newly defined charges (e.g. capacity charges).

64. Other freight operators made representations in writing and at the hearing for changes to the level and structure of EWS's charges to be made from 1 April 2001. In summary, they argued that any other outcome lacked certainty, gave EWS, with its access to more information, a competitive advantage and enabled EWS to undercut them.

65. DRS proposed that if the new charging system was not finalised, the agreement should include a best estimate subject to review when the final charges were available. The Regulator believes that it would be inappropriate, and fail to achieve the desired outcome, to prejudge the outcome of the review. DRS also argued that Railtrack should in future need to provide quotes to all operators at the same price. The Regulator does not believe this to be the case as EWS will need to take into account the adjustment that will be made to these charges as a result of the review, when bidding for new traffic or re-bidding for existing traffic.

66. Freightliner and GB Railfreight stated at the hearing that the retrospective adjustment places them at a competitive disadvantage with regard to EWS in the period before the retrospective adjustment is made. Freightliner argued that in this period EWS would have a competitive advantage through still being charged its existing charges.

67. The Regulator accepts that, in order to ensure fair competition in the industry, EWS should not benefit from a postponement of the discussion of the way in which freight charging is dealt with in its access agreement until after the publication of the freight charging review. He has therefore given Railtrack directions to include a specific form of words in the agreement. The directions therefore provide that the charges and charging structure shall be reviewed at the time of the publication of the review and the necessary adjustments made to ensure that the conclusions of the review are implemented in full with retrospective effect to 1 April 2001. They also provide that if the parties fail to agree the necessary adjustments, the Regulator may determine them. The Regulator has included this provision in order to ensure that neither party could gain by prolonging the negotiations unnecessarily.

68. Railtrack has noted in its submission its concern that the single till income assumptions made by the Regulator should be consistent with the income it will receive from EWS under the access agreement. As part of the periodic review of Railtrack's track access charges the Regulator has already indicated that, if the current review of freight charging policy results in a change in the expected level of Railtrack's income from freight operators, then this would be reflected in an adjustment to the Regulatory Asset Base (RAB) at the next periodic review.

Enhancement

69. The Regulator agrees with Railtrack that he does not have power to issue directions in respect of enhancement of the existing network in an application under section 17 and has therefore made no directions in relation to such issues.

70. Railtrack has argued that a provision of Schedule 4 to the agreement relates to the incremental costs of modifications "of a capital nature" required to accommodate varied and additional services. Following the hearing Railtrack confirmed, in a letter dated 9 March 2001, that it believes that capital costs contained within the incremental costs of additional traffic would be broadly consistent with the concept of enhancements and their regulatory treatment should therefore be consistent with enhancements. Subject to the materiality threshold in the existing agreement, the Regulator has agreed

with Railtrack that any changes to the network requiring capital expenditure constitute enhancements and should be dealt with consistently with the Regulator's enhancement framework. Consequently the provisions relating to capital costs in Schedule 4 to the existing agreement have been removed.

71. Railtrack has advised the Regulator that it has already spent of the fund created by the provisions of the existing agreement and that the remaining funds are to be committed shortly.

72. On the basis that the Regulator does not have powers under section 17 to direct Railtrack to enter into an agreement regarding enhancement, he has directed that provision is made in the calculation of the network charge to take account of this in advance of the conclusions of the charging review. Henceforth, the Regulator will expect these matters to be dealt with consistently with his enhancement framework and will expect the adjustment to the network charge, which has been made up to the point of the retrospective adjustment, to be taken into account in that calculation.

Connection Charges

73. The Regulator believes that connection agreements and the provisions thereof are permissions to use a railway facility and therefore appropriate for directions pursuant to section 17.

74. The EWS application included a waiver for the charges for other commercial agreements to replicate the separate arrangement it currently has with Railtrack. Railtrack argued that this should not be included. Instead, it argued that the waiver should be terminated and the network charge correspondingly reduced.

75. The Regulator has concluded that it is not appropriate for the waiver to be rolled over and that instead matters dealt with in separate agreements should remain separate. Prior to the application of the retrospective adjustment, the Regulator will expect any payments due under connection agreements existing between Railtrack and EWS on 1 April 1997 to be subtracted from the Network Charge. Following the application of the retrospective adjustment, the Regulator will not expect the track access agreement to be linked to the connection agreements financially. These agreements deal with separate issues and the costs which Railtrack recovers in each case have different drivers.

Other matters raised

76. Great North Eastern Railway Limited proposed in its representations that "freight operators should bear the full track costs that their services cause including the opportunity costs when trains are operated by night thereby preventing routine maintenance". This issue is a matter for the Regulator's review of freight charging.

77. GB Railfreight proposed that the SRA should subsidise rail freight. This issue is outside the scope of the consideration of this application.

78. Railtrack, with support from Great Western Trains Company Limited, objected to EWS seeking to restrict flexing rights for BCRs more than currently provided for in the existing access agreement. Great Western Trains Company Limited in its response to the consultation argued that the proposed flexing requirements were a minimum requirement. In July 1997, the then Regulator published his conclusions on the existing access agreement and acknowledged the concerns expressed by consultees about the adequacy of the Railtrack flexing right at commencement of the contract. Because of the changing nature of network capacity and the difficulty in identifying particular areas of

constraint, he modified the proposed agreement to strengthen Railtrack's flexing rights. These considerations are still relevant and the Regulator has decided that the terms of the existing access agreement in respect of flex should continue for its term.

79. Both Railtrack and EWS raised issues regarding private wagons. EWS has argued that the issues did not have a "direct bearing on" the track access agreement. Railtrack did not accept that "the terms of the existing access agreement relating to" the private wagon registration agreements had been fully addressed. However, it did not propose changes to the existing agreement. The Regulator has therefore concluded that this issue does not require changes to the existing arrangements.

80. The Regulator wishes to make clear that nothing in the directions or in this letter, save where expressly stated, should be taken as creating a precedent for future approvals or regulatory policy in relation to access agreements.

81. I am copying this letter to all consultees. Copies will also be placed in the ORR library and on the ORR website.

NICOLA SHAW

APPENDIX: CONSULTEES

- Anglia Railways Train Services Limited
- British Railways Board
- c2c Rail Limited
- Cardiff Railway Company Limited
- Central Railway PLC
- Central Trains Limited
- Chiltern Railway Company Limited
- Connex Rail Limited
- Department of the Environment, Transport and the Regions
- Direct Rail Services Limited
- English Welsh & Scottish Railway Limited
- English Welsh & Scottish Railway International Limited
- European Passenger Services Limited
- Eurostar (UK) Limited
- Strategic Rail Authority
- Freightliner Limited
- Freight Transport Association
- Gatwick Express Limited
- GB Railfreight Limited
- Great Eastern Railway Limited
- Greater Manchester Passenger Transport Executive
- Great North Eastern Railway Limited
- Great Western Trains Company Limited

- Health and Safety Executive
- Heathrow Express Operating Company Limited
- Hull Trains Company Limited
- London Underground Limited
- Mendip Rail Limited
- Merseyrail Electrics Limited
- Merseyside Passenger Transport Executive
- Midland Main Line Limited
- Northern Spirit Limited
- North Western Trains Company Limited
- Prorail Limited
- Rail Freight Group
- Railtrack PLC
- RfD (Channel Tunnel) Limited
- Scotrail Railways Limited
- Serco Railtest Limited
- Silverlink Train Services Limited
- Societe Nationale des Chemins de fer Francais
- South West Trains Limited
- South Yorkshire Passenger Transport Executive
- Strathclyde Passenger Transport Executive
- Thameslink Rail Limited
- Thames Trains Limited
- Tyne and Wear Passenger Transport Executive

- Virgin Trains (CrossCountry Trains Limited and West Coast Trains Limited)
- Wales & West Passenger Trains Limited
- West Anglia Great Northern Railway Limited
- West Midlands Passenger Transport Executive
- West Yorkshire Passenger Transport Executive