VICTA RAILFREIGHT LIMITED

Response to the ORR Consultation Document on The Policy Framework for Investments

1. Introduction

1.1 Victa Railfreight Ltd is an independent provider of rail freight services to customers across the UK. The company's customer base includes manufacturers, importers, retailers, logistics companies, port operators, civil engineering contractors, local authorities, developers and Freight Operating Companies. The services provided include operation of internal rail systems, loading and handling of conventional cargo and intermodal units, logistics planning, train planning, design and management of rail-based facilities such as warehousing complexes, feasibility studies and railfreight consultancy.

2. Background

2.1 Victa Railfreight has considerable experience of the design and development of new railfreight facilities and works closely with Network Rail and train operators to assist clients in realising their aspirations to increase the use of the network for freight. The senior team within Victa Railfreight have extensive experience of operating and marketing railfreight within the UK and overseas at a senior level within the industry, up to and including Managing Director of a Freight Operating Company. The cumulative experience of the senior team amounts to over 200 years.

3. Fundamentals

3.1 Network Rail is a monopoly supplier of access to the UK rail network. The normal market forces of efficiency and competitive pricing that result from a choice of suppliers are therefore lacking. The benefits from the advent of competition between Freight Operating Companies are evident for all to see but are lacking in the provision of rail infrastructure. Too often the response from Network Rail to a proposal which will increase railfreight is disappointingly slow, costly and unsatisfactory.

3.2 It must be stressed that this is not a criticism of the Network Rail freight team who are generally professional, responsive and well attuned to customer requirements. Rather, it is the wider Network Rail organisation which seems unable or unwilling to support the freight team in their endeavours to respond to market needs and aspirations.

3.3 In the face of an unsatisfactory performance from a monopoly supplier, railfreight customers need a structure which requires Network Rail to behave in a more appropriate manner and which can, if necessary, enforce such behaviour. ORR is clearly the body to provide and enforce this structure and the current consultation exercise is welcomed accordingly.

3.4 Freight customers' requirements of Network Rail are very simple: they want a timely response to enquiries, full and accurate information, the most cost-effective solution to meet their requirements and professional delivery of the project. This requires nothing more from Network Rail than should be expected from the professional custodian of the nation's railway infrastructure – which styles itself as 'the heart of the railway' – and an organisation which routinely manages multi million pound investment schemes.

3.5 Freight customers' investment schemes are generally at the small or very small end of the scale – in many cases the simplest possible connection into the network. There are a small number of more elaborate freight schemes but these are the exception rather than the rule and, even then, are small compared to most schemes managed by Network Rail. This ought to mean that the typical freight scheme can be carried out – relatively – quickly and cheaply, with little risk for Network Rail and the customer.

3.6 In almost every case, the freight customer pays the full cost of his scheme, including project development and management costs – there is no sharing of risk/reward by Network Rail. This is in spite of the fact that most freight schemes will result in a significant and clear new revenue stream for Network Rail via access charges paid by the FOC serving the new facility. Furthermore, Network Rail levy on-going charges against the freight customer for the operation and maintenance of the facility through the Connectional Agreement. It is not hard to see why freight customers consider they pay, pay and pay again whilst Network Rail happily receives additional revenue from the movement of their traffic. Not surprisingly, given Network Rail's ownership structure, customers find it hard to reconcile this with the declared Government policy to increase the role of railfreight in the UK.

3.7 It is clear from the above that freight investment schemes are very different from those funded by Government, involving the RAB etc, and different too from passenger schemes funded by a PTE or a TOC.

3.8 Accordingly, we believe that different rules should apply for private party freight investment schemes: that they should be carried out by Network Rail at cost – with auditable records of expenditure – without risk premiums and as quickly and efficiently as reasonably practicable. Further, that there should recourse to ORR for enforcement action if this is not forthcoming. We believe that this is essential if railfreight is to realise its full potential and to ensure that Network Rail behaves in a way which supports this key Government objective.

4. Specific Comments on the ORR Consultation document

4.1 We strongly support the Chairman's foreword in its statements that 'If rail services are to develop to better meet the needs of passenger and **freight** users (our emphasis), and the growth in demand, it is essential that there is an effective framework for delivering infrastructure enhancements' and that '(Network Rail) is a key player in ensuring that improvements are delivered in a efficient and timely manner'.

4.2 We are pleased to see (1.4) that 'ORR's objective is to facilitate appropriate, efficient investment in the rail network' but are, however, concerned that the emphasis in much of the document is on Network Rail's own investment and the funding thereof by Government. Whilst we understand and support the intention to make the overall railway as efficient as possible, at appropriate cost to the tax payer, we need to see specific provision for small private party schemes, which are crucial in delivering the freight growth desired by Government – probably more so than network capacity enhancements, since, without additional terminal capacity, the network enhancement will be for nought.

4.3 Para 2.17, correctly in our view, highlights the importance of Network Rail's knowledge of its assets in Planning/project development. In spite of repeated complaints about the lack of such knowledge, stretching back to the days of Railtrack, and repeated statements by Network Rail that the position was improving, there are still massive gaps in the company's knowledge, notably in the precise dimensions of its track and structures which are so crucial in determining what vehicles can use a route and what would be the costs of gauge enhancement. This problem is by no means unique to freight, as evidenced by the problems with passenger rolling stock procurement and introduction.

4.4 We would go further than para 2.18. in that Network Rail should be required, forthwith, to demonstrate that it has full and detailed knowledge of its assets and, to encourage the company in this, that it should not be permitted to charge any associated contingency costs against funders of investment schemes until such time as competent custodianship of a key national asset can be demonstrated. Further, this should be linked to the incentive and reward packages of directors and senior managers of the company, such that bonus payments would be withheld or substantially reduced until the required level of custodianship can be demonstrated. This may seem draconian but safe operation of the network cannot be assured in the absence of comprehensive and accurate knowledge of infrastructure assets, witness Hatfield et al.

4.5 We **disagree strongly** with para 2.19 and believe that it is essential that Network Rail takes full responsibility for the information it provides and bears all liabilities accordingly. If Network Rail cannot provide full and accurate information about its own assets, how can a third party be expected to ascertain the facts and accept risk and liability?

4.6 Also in para 2.19, we accept that there *may* be instances where promoters will require information over and above that required by Network Rail to carry out its activities but, in our experience, this is rare with freight schemes and we would not expect this to feature in more than occasionally.

4.7 We fully support the ORR stance in para 2.21

4.8 In the vast majority of private party freight schemes the customer pays the full cost of the scheme, so that para 2.22 is news to us! We would be delighted to see Network Rail offering to fund such freight schemes but confidently expect a deafening silence on this front!

4.9 Re para 2.25, we support ORR in expecting Network Rail to provide network services in an efficient and facilitative manner and to recover only the incremental direct costs of so doing. Indeed, we believe that this approach to charging should apply to all aspects of private party freight schemes. We do not, however, agree with Network Rail proposals for pooling high impact, low incidence risks and return to this point later in our response.

4.10 We fully support the ORR stance in paras 2.34 – 2.37, with the rider that the range of information listed in the Dependent Persons Code on Network Rail's website is very limited and that it is unreasonable for Network Rail to charge for information other than that listed – which is essentially very general information which has already been published and is of little use to a private party developing a freight scheme.

4.11 Turning to incentives on Network Rail, para 2.48 contains a very big 'if' in the context of offering the customer an efficient fixed price for the delivery of the scheme. The customer *must* be satisfied that the price is efficient, with recourse to ORR if he feels otherwise. We would not wish or expect to see many customers invoking ORR involvement but the provision is necessary to encourage the correct behaviour by Network Rail. Further, we do not consider that Network Rail should retain the surplus from outperformance against contract – we believe that the Company should be required to pass efficiency savings back to the customer, in particular any unused contingency for risk

4.12 Finally in section 2 of the document, we believe the argument that Network Rail has reputational incentives to facilitate and deliver investments to be very weak. We have seen no evidence in favour of this argument and, indeed, have seen several cases of a 'take it or leave it' attitude where the company displayed no concern whatever about its reputation.

4.13 Given that freight customers pay the full costs of their investment schemes, we would expect there to be no provision in the price quoted by Network Rail for return on capital employed (para 3.3)

4.14 Re para 3.4, the basis of price should ultimately be a matter of negotiation between the customer and Network Rail. However, we believe that the default position should be auditable avoidable costs. We consider that there is a risk that Network Rail will 'load' a fixed price to ensure it makes a profit on the scheme. We note with interest that TPWS – which is generally held to be one of the most successful investment schemes undertaken by the rail industry in recent years - was undertaken at emerging cost, subject to a cap and a review of actual costs against estimates at defined stages. We believe that this is a good model to follow and cannot understand ORR's preference for fixed or target price.

4.15 We support ORR's view on risk allocation but would observe that other than Demand and Funding risk, which - as we have seen - is taken by the freight customer, all other risks are no more than Network Rail's discharge of its core tasks and responsibilities i.e they are nothing more than should reasonably be required of a competent operator and custodian of a major asset. Accordingly, ORR must ensure that Network Rail discharges its role in a timely efficient manner, at lowest practicable cost, and does not transfer to or charge the customer for risk associated with its core activities.

4.16 We agree with para 3.16 that small schemes are low risk and that this should be reflected in the price quoted, especially as there is rarely any innovation or new technology associated with freight schemes – simple, robust and tested methods are strongly favoured.

4.17 Paras 3.21 – 3.23, illustrate our earlier point that the vast majority of freight schemes are in a different league to other Network Rail projects. We believe that there should be a small schemes category – say, under £10m – where the maximum contingency is the 5 –10% range implied in para 3.23. We see no evidence in private party freight schemes of the sort of cost overruns described in para 3.22 and can only assume that these are a feature of large public sector projects with scope drift and lack of the rigorous cost control normal in the private sector.

4.18 We consider para 3.25 largely irrelevant to freight schemes, since the customer pays the full cost and the value of the asset should clearly not be added to Network Rail's RAB. The concept of Network Rail 'buying back' an asset (para 3.34) is unknown in freight and, although we think freight customers would be very interested to explore this approach with Network Rail, do not expect the company to change its stance on the matter. Note, again, that Network Rail levies a charge through the Connectional Agreement for operation and maintenance of a private siding so there can be no argument that the asset should go into the RAB to cover these costs.

4.19 The efficiency of a cost estimate prepared by Network Rail (para 3.36) is of crucial importance to freight customers, since it is an investment full of commercial/demand risk for them in an industry with which they are not well versed. A freight investment is therefore of much greater risk to the sponsor than a similar passenger scheme sponsored by a PTE or similar public body – the freight customer will have to demonstrate internally that the costs of the scheme are robust and reasonable, that it will be strategically sound and beneficial to the bottom line. Many currently struggle to do this.

4.20 As stated earlier, we believe that Network Rail costs should be avoidable direct costs, fully auditable by the customer and, if necessary by ORR. Management and development costs should be clearly identified and justifiable. Insurance costs should be minimal and covered within Network Rail's general policies. We are unclear what schedule 4 or 8 costs are, but if they relate to performance payments to TOC's and FOC's, would consider this to be entirely a matter for Network Rail to manage – these are matters over which the customer has no control or influence and relate to the core competencies and responsibilities of Network Rail. Contingency for risks, quantified, identified or unidentified, should be in the range 5 – 10% for most freight schemes, refundable to the customer if not used.

4.21 We are interested in the concept of 'netting off' mentioned in para 3.37 since, with the customer paying the full costs of the scheme and generating a clear, direct revenue stream for Network Rail via access charges paid by the FOC (plus the Connectional Agreement charges paid by the customer), we consider the idea of 'shared value' may be relevant to many freight schemes.

4.22 Re paras 3.38 –3.42, we consider that ORR should assess the cost of major projects but that, given the small scale of most private party freight schemes, this would happen rarely with such schemes. Nevertheless, it is important that ORR involvement and support can be invoked by freight customers in the event of unsatisfactory performance from Network Rail.

4.23 We agree that provision of design and development services is a core competence of Network Rail and that no charge should be made for such services in the feasibility stage of a project. We note, however, as mentioned earlier, that Network Rail's view of what it is funded to provide, even to dependent persons, is much more limited than we would have expected and implied by para 3.45.

4.24 We agree (para 3.46) that where Network Rail incurs additional costs its remuneration should be transparent – although we would prefer to the term 'auditable'.

4.25 We **disagree fundamentally** with Network Rail's proposed approach outlined in paras 3.50 – 3.64. We believe that, in the vast majority of private party freight schemes, the only body that can manage risk on the network is Network Rail itself. Customers have no influence or control over Network Rail's policies, practices or performance and cannot be expected to cover risks that Network Rail perceives in the discharge of its core competences and responsibilities.

4.26 We see no logic at all in requiring customers to contribute to a Network Rail Fee Fund or an Industry Risk Fund and consider that ORR should dismiss Network Rail's approach forthwith, certainly as far customers are concerned. We consider the same applies to FOC's but it is for them to argue the case for themselves.

4.27 The fundamental point that Network Rail is a monopoly supplier with a poor track record of asset control and investment management should be at the forefront of our minds at all times. We do not believe that the industry and ORR should pander to Network Rail's risk aversion and denial of responsibility for its core activities. Customers accept responsibility for the management of risk in their own activities and expect Network Rail to do likewise – on the grounds of professional management and stewardship, let alone that of monopoly supplier. Contrary to para 3.62, we believe that the proposals provide considerable protection to Network Rail – at the customers' cost – and little or no benefit to customers themselves.

5. Conclusion

5.1 We welcome ORR's consultation on this matter and the opportunity to comment.

5.2 We have serious concerns about certain of the proposals, in particular Network Rail's approach to cost and risk.

5.3 We believe that freight customers already bear considerable demand and cost risk in making railfreight investments, funding full costs themselves and generating new revenue streams for Network Rail in the process.

5.4 We believe, accordingly, that Network Rail should carry out private party freight schemes in a timely and efficient manner at auditable, avoidable direct costs and that customers should have recourse to ORR to ensure this occurs.

5.5 The fact that Network Rail remains a monopoly supplier of access to the national rail network should determine both the overall approach and the detailed provisions for investment by freight customers. We look to ORR to ensure that this occurs