



ASSOCIATION of TRAIN OPERATING COMPANIES

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Dear Hannah

RESPONSE TO CONSULTATION ON “PROPOSALS FOR A REBATE MECHANISM FOR INVESTORS IN LARGE-SCALE NETWORK ENHANCEMENTS: DECEMBER 2005”

ATOC has a great deal of sympathy for a freight operator who wishes to invest in a facility, but who is concerned about the possibility of a competitor using the enhanced facility and paying only marginal costs. This free rider problem clearly dampens the willingness of freight operators to invest.

We must however avoid the proposed cure being worse than the disease. We were therefore concerned by the consultation document and the discussion at the seminar and wish to raise the following points:

- (i) The proposals may significantly add to the risks of franchised train operators and hence the cost of franchises. As you know, franchised train operators are not protected though Clause 18.1 or its equivalent against increases in track charges brought about by the sort of supplement that is being contemplated. Fares regulation and service level commitments meant that TOCs cannot respond to price changes in the normal way i.e. by cutting output or increasing prices. The prospect of a third party investor being able to extract unexpected track charges from a TOC increases risk and increases the cost of franchises.

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- (ii) The proposals will increase disputes between investors and other train operators that are costly to resolve. If an investor can claim a benefit is enjoyed by an operator, some method must be found of resolving the disputes that will arise. Some of the potential benefits that were discussed at the seminar run by ORR are very difficult to quantify (performance benefits for example). Costly disputes will result.
- (iii) The proposals may adversely affect public funding of investment. The suggestion was made in the consultation document that the ability to extract a track supplement is extended to include public bodies (PTEs; TfL; local authorities; Scottish Executive; Central Government). The first point is that public bodies invest today, often without a direct financial return, but rather to benefit local communities and the local economy. The prospect of being able to receive a track supplement from its investments is therefore unnecessary. A second point is that uncertainty over the investment regime could delay current investment while the policy is unresolved. This would be wrong and counterproductive.
- (iv) The proposals may solve one allocative distortion but introduce others. Charging for use at a rate that is higher than the additional costs caused by users can introduce a new allocative distortion. Currently, if a user can pay the marginal costs, they can use the network. This maximises the use of what we have.

Turning to the narrow point of freight investors concerned about the free riders it may be worth considering a regime with the following characteristics:

- (i) Existing users with either franchise commitments or a track access agreement over the route in question will not pay for additional facilities while they hold a franchise or access agreement. Only new franchisees or new open access operators will pay. (But can a charge be discriminatory in this way?)
- (ii) We put on hold the question of public bodies who fund investments while we consider more carefully the full ramifications of this.

I hope that this is helpful. Please get in touch if you want anything clarified or if you want to discuss it further.

Regards

A handwritten signature in black ink, appearing to read 'Alec McTavish', with a stylized flourish at the end.

Alec McTavish
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