



OFFICE OF RAIL REGULATION

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Dear Julie and Mark

Approval of the twenty-second supplemental agreement to the track access agreement between Network Rail Infrastructure Limited and Hull Trains Company Limited

1. The Office of Rail Regulation (ORR) on 15 August 2008 approved the twenty-second supplemental agreement to the track access agreement between Network Rail Infrastructure Limited (Network Rail) and Hull Trains Company Limited (Hull Trains) (jointly the parties) submitted formally to ORR on 15 August 2008 under section 22 of the Railways Act 1993 (the Act). The formal submission followed an earlier informal submission of a proposed supplemental agreement on 17 April 2008, and took account of the comments we made to the parties on that informal submission. The purpose of this letter is to set out the reasons for our decision.

Purpose of this agreement

2. The purpose of the agreement is to grant Hull Trains Contingent Rights to operate one additional service each way, a fifth, between Hull and London King's Cross on Sundays only.¹ In its informal submission, Hull Trains had sought the rights until the expiry of its track access agreement on the Subsidiary Change Date (SCD) 2010 but, for reasons outlined below, we have only approved the rights until SCD 2009.

¹ Note: the service each way first ran on 18 May 2008 with rights for 90 days granted by the twenty-fourth supplemental agreement, approved under the Passenger Access (Short Term Timetable and Miscellaneous Changes) General Approval 2008

Consultation

Grand Union

3. In line with usual practice, Network Rail undertook an industry consultation and only Grand Union Railway Company Limited (Grand Union) commented on the application (also commenting on behalf of Grand Central Railway Company Limited (Grand Central) and Grand Northern Railway Company Limited (Grand Northern)). It referred to ORR's reasons document of 6 April 2006, in respect of the various applications for the rights necessary to run additional services on the East Coast Main Line (ECML), noting that all the services evaluated had been found to offer net economic benefits, with the open access services passing ORR's five-stage "not primarily abstractive" test.

4. In 2005/06, Grand Central had challenged Network Rail's view of the capacity available on the ECML. Subsequently, capacity had been found not only to satisfy the aspirations of Great North Eastern Railway Limited, but also a seventh weekday path for Hull Trains. Of the original applications, only that of Grand Central – dated 24 February 2005 – had not been fully realised, although Network Rail's planners had now (2008) identified additional fourth and fifth return paths between Sunderland and King's Cross, and four to five return paths between Bradford and King's Cross.

5. Grand Union noted that in ORR's decision dated 21 December 2006 on Hull Trains' application for a seventh weekday path, at paragraph 70, ORR had stated:

'We have approved these rights for one year (subject to resolution of the Capacity Charge). However, we are not yet satisfied that this will be the best use of the scarce remaining capacity on the ECML in the longer term. We will therefore consider any request to extend these rights in the context of the ECML RUS [Route Utilisation Strategy] and alongside any requests from operators for additional rights. The fact that Hull Trains will have been operating the seventh path will not be a factor in our consideration and Hull Trains must have no expectation that these rights will necessarily be extended.'

6. Grand Union said that Grand Central had abided by ORR's guidance on applying for further paths pending the outcome of the ECML RUS (which had now been submitted to ORR for acceptance), but in that time had seen the aspirations of others being agreed – albeit with limitations. Had Network Rail undertaken a more comprehensive and detailed capacity study in 2005 the real capacity position would have been clear in 2005/06, and Grand Central would almost certainly not have found itself in a position belatedly to bid for paths that chronologically pre-date every current application, and would have been able to secure for itself the rolling stock needed to operate both service groups to Sunderland and Bradford.

7. In respect of the current application from Hull Trains for an additional return path on Sundays, Network Rail and Hull Trains were seeking to agree this path until the expiry of Hull Trains' current track access agreement. Grand Union claimed that this was contrary to

guidance given by ORR on further applications pending the outcome of the RUS, and Grand Union/Grand Northern objected to the proposed length of the rights as it had from 2005 (initially via Grand Central) an outstanding properly-declared aspiration to Network Rail for the operation of services between Bradford and King's Cross, for which Network Rail had not yet offered (although it had developed) a timetable. Without a fully developed timetable (which pre-dated this application from Hull Trains), it was not possible to be sure that the proposed paths would not prevent Network Rail from finding and offering suitable paths for Grand Northern's Bradford service, which it was planned (subject to ORR approval) would operate from December 2008.

8. Grand Union said that it was content for Hull Trains to operate the proposed additional Sunday paths until December 2008, but not beyond at this stage. By that time, ORR would also have properly considered representations and applications for ECML services in line with the letter sent by ORR to all parties on 29 February 2008².

9. Grand Union concluded that this section 22 application contrasted sharply with Network Rail's position on Grand Central's fourth Sunderland path, where it would not agree to sell the rights, citing ORR's letter of 29 February 2008, but ignoring the fact that Grand Central's fully ORR-evaluated application was originally from February 2005, pre-dating this application from Hull Trains by many months.

Network Rail

10. In responding to Grand Union, Network Rail said that it distinguished this application from that of Hull Trains for its seventh weekday path, and Grand Central's application for a fourth Sunderland path, in that this application was for Contingent Rights only to operate on Sundays. It argued that the considerations in relation to weekday paths were very different to those at weekends, reflecting the lower demand for capacity at weekends. Network Rail said that it was satisfied, taking into account that the ECML RUS had been published, with the availability of capacity for the paths which were the subject of this application, and that these did not conflict with other aspirations notified to Network Rail. The fact that these were only Contingent Rights provided additional assurance of the priority which would be given to any Firm Rights during the process of the initial construction of timetables throughout the balance of Hull Trains' track access agreement.

11. Network Rail claimed that we had acknowledged the distinction between weekday and weekend rights by quoting from paragraph 15 of our decision letter of 16 November 2007 extending Hull Trains' rights for a further year³:

² http://www.rail-reg.gov.uk/upload/pdf/s18-ECML_acc-rgts_290208.pdf

³ <http://www.rail-reg.gov.uk/server/show/ConWebDoc.8442>

'Whilst we have approved these rights for one year, we are not satisfied that granting Hull Trains rights to a seventh weekday service each way will be the best use of the scarce remaining capacity on the ECML in the longer term'.

Grand Union

12. Grand Union in turn responded to Network Rail, commenting that the specific reference quoted by Network Rail in the preceding paragraph was not valid in this context, and that as Network Rail had not yet fully developed the Bradford – King's Cross timetable, it was not possible for Network Rail to be confident that the proposed paths did not impact on paths being developed for Grand Northern on Sundays. It continued that Grand Central's application for a fourth Sunderland path had been rejected by Network Rail on the basis of other submissions made by the Priority Date, which was exactly the same position faced by Grand Union on this application from Hull Trains, irrespective of the day of the week.

ORR's position

13. We believe there is a clear distinction between the Contingent Rights sought by Hull Trains for services on Sundays, and the Firm Rights sought by Grand Northern with specific Departure time ranges for services on Sundays. Hull Trains is not seeking rights to specific paths. There is substantially less demand for capacity on the ECML on Sundays than on weekdays, and we are not aware of aspirations for track access sufficient to consume that capacity by 2010. Even though Hull Trains is not seeking rights to specific paths, we note the comment of Network Rail that the paths for which Hull Trains had bid did not conflict with other aspirations notified to Network Rail (including those of Grand Northern for its proposed Bradford services). We believe that, given the greater availability of slots on a Sunday, it is unlikely that one additional return journey between King's Cross and Hull would materially prejudice Network Rail's ability to path the services for which Grand Union made representations.

14. However, as indicated in our letter of 8 August 2008 to the industry, explaining how we proposed to deal with applications for the renewal of rights for services already running on the ECML⁴, whilst we are content to approve the rights sought until SCD 2009, we do not feel it is appropriate at this stage to approve them beyond that date. This duration will give sufficient certainty to Hull Trains to sell tickets for these services, and to passengers wishing to use the services, and we will consider any application to extend the duration of these rights on its merits and in line with our published criteria and procedures.

Operational issues

15. When we were previously considering applications for additional rights on the ECML, the offer of paths from Network Rail was subject to two safety caveats – one in

⁴ http://www.rail-reg.gov.uk/upload/pdf/s18-ecml_stkhldrs_080808.pdf

respect of certain level crossings, and the other in respect of signals where there was a higher than average SPAD⁵ risk - both of which were subsequently satisfactorily resolved. We therefore asked Network Rail to confirm that it was content that the additional services proposed by Hull Trains did not raise any such concerns.

16. Network Rail advised that for services outside the core hours of 07:00 to 19:00 Monday to Friday there was not a requirement for it to undertake a review of level crossings or signals.

17. We also asked Network Rail to confirm that it had considered the possible effect on engineering access prior to agreeing to support the application, and that it was content that it would not be compromised by the rights sought by Hull Trains.

18. Network Rail confirmed that it had considered the impact of the rights sought on engineering access and concluded that as the paths sought by Hull Trains were in the main part of the day, when a number of other services were already operating, it did not believe that the additional rights would impact on engineering access.

Framework and process for considering revenue generation and abstraction⁶

19. We have a long-standing policy of not approving rights to new competing services that are primarily abstractive of incumbents' revenue without compensating economic benefits. ORR's policy on competing services was set out in our final conclusions on moderation of competition, which were published on 18 May 2004⁷. In considering the Hull Trains twenty-second supplemental agreement, we have applied a methodology consistent with our final conclusions on moderation of competition.

The "not primarily abstractive" test

20. Our final conclusions on moderation of competition explained that the expression "primarily abstractive" is not intended to imply a rigid benchmark. Such a test would be unrealistic given the uncertainty about forecasting future revenue effects, and this test alone would not allow all relevant factors to be taken into account. Instead, we have considered whether the overall effect of approving the rights proposed by Hull Trains is

⁵ Signal passed at danger

⁶ The informal submission of 17 April 2008 was not accompanied by any data to suggest that the proposed additional services would be likely to pass our "not primarily abstractive" test. We asked Hull Trains to provide suitable data on 23 April 2008, and it did so on 9 May 2008. We were unable to review the data in time to reach a decision prior to 18 May 2008, when Hull Trains wished to commence running the services, so the parties entered into the twenty-fourth supplemental, approved under the General Approval, thus enabling the services to operate for 90 days pending the completion of our review.

⁷ <http://www.rail-reg.gov.uk/upload/pdf/195.pdf>

likely to attract sufficient new patronage/revenue to rail such that abstraction from other operators could not be considered the primary impact of its proposal. The test is described in paragraph 3.18 of Moderation of Competition: Final Conclusions⁸.

21. In earlier applications by open access operators to increase their number of services, we have considered the previous step up in the number of services as a proxy for the proposed increase in services. The previous increase in Sunday services from three to four return services is complicated, as it was shortly after Hull Trains' move from 100 to 125 mph rolling stock and was impacted by the July 2005 bombings. We have, therefore, placed more weight on other parts of our analysis.

MOIRA analysis and initial estimate of revenue abstraction

22. The first part of our assessment involved the use of MOIRA software to estimate the level of generation and abstraction. Hull Trains and we have independently carried out MOIRA assessments based on the timetabled paths supplied to us for the fifth Sunday return service.

MOIRA analysis	Ratio of generation to abstraction
ORR	[]
Hull Trains	[]

23. Our policy states that MOIRA is likely to under-predict the proportion of revenue generation from new services such as those of Hull Trains. As the number of Hull Trains' services increases, we might expect MOIRA to become a better indicator of the impact of additional services (as the incremental impact of additional services is smaller and so the elasticities underpinning MOIRA become more applicable). Evidence from previous increases in services suggests that MOIRA is still under-predicting the generative effect of additional Hull Trains' services. The generation-abstraction ratios quoted above are therefore likely to under-predict the generative effect of the fifth Hull Trains' Sunday service and we would expect ratios to be somewhat higher.

Hull Trains' submission

24. Hull Trains provided us with expectations of the revenue impact of the fifth Sunday path. These projections suggest that Hull Trains would not only generate revenue on its services but for the railways as a whole. Given the impact of previous additional Hull Trains' services, we regard an entirely generative impact of the fifth Sunday path as unlikely.

⁸ <http://www.rail-reg.gov.uk/upload/pdf/195.pdf>

25. Hull Trains also provided two other pieces of analysis:

- data showing the growth of key flows over a six year period; and
- estimated passenger loadings for Sunday services derived from LENNON.

26. The key flows data shows the revenue growth on key flows between 2001-02 and 2007-08. Over this period, Hull Trains increased frequencies from three to seven return weekday services per day and introduced new 125 mph rolling stock. The data shows that revenue growth at stations with a direct Hull Trains service has far outstripped national average growth rates.

27. The train loadings data shows that estimated loadings for Sundays are slightly higher than predicted by MOIRA, with MOIRA under-prediction greatest where Hull Trains provides the main direct train service (i.e. Hull, Brough, Howden, and Selby). Where National Express provides the majority of services there appears to be a tendency for over-prediction. This is similar to our findings when we reviewed the impact of the fourth and sixth weekday paths (eighth and fifteenth supplemental agreements respectively).

28. The fifth Hull Trains Sunday service is currently timetabled to depart Hull at 12:12 and London at 16:04. The loading data indicates that services either side of these departures (the 10:12 and 14:10 from Hull and 14:44 and 17:44 from London) are the most heavily loaded of Hull Trains' Sunday services.

Consultation responses

29. The only consultation response received, from Grand Union, did not dispute whether the additional Hull Trains service would pass the "not primarily abstractive" test.

Impact of the move from three to four Hull Trains Sunday services per day

30. In earlier applications, we have considered the impact of the previous step up in services as a proxy for the impact of the proposed increase in services. For the move from three to four Sunday services, which took place in December 2005, this analysis is complicated by a number of factors:

- the market for long distance Sunday rail travel is to some extent linked to demand and services on Fridays and Saturdays. Many long distance passengers make outbound trips on Fridays and Saturdays, returning on Sundays as passengers make weekend trips away. The demand for Sunday services will therefore be affected by the service levels on Friday and Saturday as well as Sunday. The move to four Sunday services shortly followed the move to seven weekday services and five Saturday services (June 2005), making the identification of separate impacts difficult;

- weekend trips mean that the return trip is on a different day to the outbound trip, making the allocation of revenues more difficult, and reducing the reliability of revenues forecasts based on LENNON;
- the move to four Sunday services shortly followed the move from 100 to 125 mph rolling stock. This reduced journey times, increasing both revenue generation and abstraction; and
- the period immediately preceding the move to four Sunday services was affected by the impact of the July 2005 bombings, making reliable comparisons more difficult.

31. Based on the above, we do not consider that generation-abstraction ratios derived from the move from three to four Sunday services will be a reliable indicator of the move from four to five Sunday services.

32. The fifth Sunday return path has been operating under General Approval since May 2008. This could provide information on the impact of the fifth path. However, as the operation of the service had been severely affected by engineering possessions, at the time we undertook our analysis the service had operated only four times. While analysis of LENNON revenue data shows an increase in total revenues on the days that the fifth service operated, the sample size is too small to enable us to draw firm conclusions.

33. Previous increases in Hull Trains' services have shown generation abstraction ratios ranging from between [] to between []. Based on this evidence we would expect the extra Sunday service to continue to generate and abstract revenues in a similar ratio to those found in the past.

Conclusions on generation and abstraction

34. Overall, our analysis suggests that the generation-abstraction ratio for the additional Sunday service is likely to be in a range that passes our test. We indicated in our decision letter on Hull Trains' eighth supplemental agreement that we would be prepared to approve additional rights where the expected ratio was marginally lower than the range 0.3 to 0.5. The MOIRA analysis suggests that the ratio will be towards the bottom end of this range. However, as MOIRA has under-predicted revenue generation for previous Hull Trains' service increases, we believe that the ratio will at least be within this range, and probably above it. We therefore conclude that the fifth Sunday path passes our "not primarily abstractive" test.

35. We have also considered the potential level of abstraction in absolute terms. The estimate for abstracted revenue based on MOIRA suggests that this will be around £[] million per year (although there is a degree of uncertainty over the ramp-up profile to this level). The overall impact on other operators and the Department for Transport's financial position is therefore considered to be relatively small.

Conclusion

36. In considering the application and in reaching our decision, we have had to weigh and strike the appropriate balance in discharging our statutory duties under section 4 of the Act. We have concluded that approval of this supplemental agreement is consistent with our section 4 duties, in particular those relating to:

- protecting the interests of users of railway services (section 4(1)(a));
- promoting the use of the railway network in Great Britain for the carriage of passengers...(section 4(1)(b)); and
- enabling Hull Trains to plan the future of its business with a reasonable degree of assurance (section 4(1)(g)).

Administration

37. Please find enclosed a copy of the approval notice together with a copy of the supplemental agreement. Copies of the approval notice and the supplemental agreement will be placed on ORR's public register and copies of this letter and the supplemental agreement will be placed on the ORR website. I am copying this letter to Steven Saunders at Network Rail and Ian Yeowart at Grand Union.

Yours sincerely

Brian Hopkinson