

Unredacted minutes released following an application under FOIA and therefore published in full on the ORR website, January 2015

Office of Rail Regulation

Minutes of the a telephone meeting by the ORR Board on 11 December 2013

(16:30 – 18:00), ORR offices, One Kemble Street, London

Present:

Non-executive directors: Anna Walker (Chair), Tracey Barlow, Peter Bucks (both on the phone)

Executive directors: Richard Price (Chief Executive), Ian Prosser (Director, Railway Safety)

In attendance, all items: John Larkinson (acting Director of Railway Markets and Economics), Richard Emmott (Director of Communications), Tess Sanford (Board Secretary), Brian Kogan, Rob Plaskitt, Ian Williams, Paul Hadley.

On the phone: Dan Brown (Director of Strategy), Juliet Lazarus (Director, Legal Services)

Apologies: Mark Fairbairn, Stephen Nelson, Ray O'Toole, Steve Walker, Alan Price.

Item 1: Welcome and apologies for absence

1. The Chair welcomed everyone to the meeting and noted the apologies.

Item 2: Declarations of interest

2. None.

Item 3: Alliance application for access to the west coast main line (WCML)

3. Rob Plaskitt explained that the paper had been updated and clarified following the discussion at the board on 26 November. Responding to a request from the Board to have more detail on the hurdles that would need to be overcome to reach a positive decision on this application, the team had updated their paper accordingly. This discussion would only be about the application before the Board – it was important that nothing in the consideration of this application should inadvertently limit our ability to consider any other application on its own merits.

4. We agreed that the updated paper did set out more clearly than the earlier paper the various criteria and the process that the team had applied; and the areas of uncertainty were acknowledged alongside reasons for their recommendation.

5. Juliet Lazarus drew the Board's attention to the section of the paper which set out those statutory duties that had been identified as most relevant in consideration of this case. She thought the paper captured and reflected the proper application of our process. Ultimately, the board would have to balance their various duties and reach a judgment whether to reject the application at this stage or continue to wait for better information. She felt that they could be assured that the process had been robustly applied.

6. The Board reflected on the four key criteria that are considered in weighing an access application.

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~~*Redaction of paras 7-20 on the basis that they contain information relating to the discussion and application of a regulatory function.*~~

7. On capacity, Rob Plaskitt reminded the Board about the lack of current capacity for the peak services sought: there were three theoretical off peak paths each hour. There were some issues about consistency with the Northern Hub requirements under the franchising and HLOS process. Finally (and quite late in the process) uncertainties had appeared about HS2's impact which suggested there could be serious additional constraints on capacity at the southern end of WCML from 2016 onwards.
8. We discussed how any rights granted for this application would inter-relate with existing franchise operators and passenger services into Euston. Rights granted now to Alliance for 2016 and beyond would take priority over existing franchise operators (whose rights did not run so far). The risk was that, should capacity become more constrained, heavily used commuter services would be displaced by the proposed Alliance priority rights. This would clearly risk disbenefit to large numbers of passengers and the most likely outcome seemed to be that the Alliance rights would have to be bought out. We noted that the commuter services were almost full whereas services on the longer routes run by Virgin still had some on-train capacity – particularly in the off-peak.
9. Brian Kogan reminded us about the issue around charging design. Franchisees are required to provide core services and are charged accordingly. Open Access charges were set to reflect the expectation that they would be supplementary services meeting marginal costs and operating on the margins of capacity. Our policy had not previously been tested by an application which might displace significant existing services.
10. We agreed that we would need to revisit our open access policy in future to ensure that we considered these issues. In the meantime we should continue with the application before us. We agreed that there was no obvious capacity to accommodate this size of application.
11. The second criterion considered in our application process is the likely impact on performance. We have previously accepted that, given the congestion on the network, additional services are always likely to risk negatively impacting on performance. NR had concerns about selling the three theoretical paths because of the potential serious impact on performance. Recasting the timetable in a way that might allow additional paths would require significant work across the industry and might cause knock-on issues such as insufficient rolling stock or an unbalanced timetable. Again, these issues had arisen before the uncertainty around the impact of HS2 emerged. NR was prepared to offer one path an hour, but this was clearly below what Alliance was seeking. We agreed with NR that there was a real risk of serious negative impact on performance if all the available off peak paths were sold.
12. The third criterion was impact on the Secretary of State's funds. Again, we reminded ourselves that most open access operations abstracted some revenue from franchise operations and therefore risked an adverse impact. The issue in this case was the possible scale of any impact. The previous paper had speculated on the DfT's

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likely reaction to a positive determination in this case: the executive had now included its actual responses. The DfT argued that the application, if successful, was sufficiently large that it could be expected to result in a reduced premium for the WCML franchise. In addition there was the risk of displaced franchise services, and the inconsistency implied by undermining the Northern Hub and risking delivery of the extra peak capacity commuter services specified in the HLOS for Euston. While Alliance might deliver some of the HLOS requirements, government would have no certainty over what would be delivered or whether it would continue to be delivered. DfT had also raised the issue of the risk of compensation payments, which were likely to be significant, to sort out any future access constraints.

13. We discussed the scale of the application and the team were very clear that they believed the possible financial impact on the SoS funds was significant – much more material than under previous open access applications. A specific range was impossible to set, but we had already heard there would be significant abstracted value from the franchise operator and the additional risk of compensation payments if those arose. There was also an increased risk that the HLOS would not be delivered so the potential cost to the Secretary of State was likely to be on a scale that would give real concerns in relation to our duty to have regard to the Secretary of State's funds.

14. We noted that on the three criteria we had considered so far there was an absolute lack of current capacity at peak times, an acknowledged disbenefit on performance and a sizeable negative impact which would likely be more than usually adverse on the SoS funds.

15. The fourth criterion was the NPA [*not primarily abstractive*] test which we would normally use to assess the impact of new services on an existing timetable to ensure that they generate a level of additional revenue. The test was designed to deal with marginal propositions against existing services – which open access applications we have previously considered had been. Applicants must pass the test, but passing the test did not automatically mean that an application should be permitted.

16. We had already understood that this proposal could displace existing services, and it could not be accommodated without a major recast of the timetable. Staff explained that very rough early calculations had indicated that the application might not generate sufficient additional income to meet the NPA test (less than half the required 0.3 margin) - but the main problem was that there was no proper data on which to run the full test. The test could not be run on the existing timetable – because the new services could not be accommodated within it. A re-cast timetable to include the new services would require significant work across the industry but there was no guarantee that the services would actually be accommodated within a recast timetable. Finally, there would inevitably be an extended period before the medium term impact of HS2 could be understood well enough to gauge the effect on this application. That meant that we could not run an effective NPA test at this time or at any foreseeable future date.

17. We noted that the scale of the application had been relevant to our consideration of the four criteria.

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18. We reflected on our relevant statutory duties, particularly those relating to protecting the interests of users of railway services, to promote competition for the benefit of rail users, to have regard to the funds available to the Secretary of State and his guidance, and to enable operators to plan their businesses with reasonable assurance. We noted that we begin the process with an assumption that open access operations will offer benefits to users but that at this time we could not say that about this application. We agreed that the arguments were well rehearsed in the paper and had been supported by our discussion.

19. We asked about the quality of the underlying information provided by NR. Brian Kogan said that NR's original capacity assessment had been rejected by the team as insufficient but the second one had been competent. In the same way, the team's analysis suggested that the impact on the Secretary of State's finances would be less bad than DfT's initial claim – but it was still a significant impact.

20. We also considered our duty to promote competition for the benefit of rail users. We recognised that this statutory duty had to be weighed against our other statutory duties. We also recognised that the Alliance application would offer more competition in the market. However, given its size, it would have an impact on what franchisees might bid and so potentially diminish competition for the market. We also recognised the need to factor into our decision making our duty to have regard to the Secretary of State's funds and the interests of the other users of the network.

Redaction ends

21. On the basis of the arguments set out in the paper and rehearsed in our discussion we agreed that we should reject the Alliance application now.

22. Given the detailed consideration that the Board had given this application, we asked that the final decision letter should be approved by the Chair and the Chief Executive before it was issued.

23. We noted that the usual practice is to give applicants an opportunity to comment on decision letters before they are published and that this practice would be followed in this case.

Action: Draft of the decision letter to be approved by the Chief Executive and Chair before being issued.

Action: Alliance to be given the opportunity to comment before the final letter is sent.