Stobart Group

Michael Scarff
Executive, Stations & Depots Access
Office of Rail and Road
One Kemble Street
London
WC2B 4AN

6 July 2015

Dear Mr Scarff

APPLICATION FOR DIRECTIONS UNDER SECTION 17 OF THE RAILWAYS ACT 1993

Thank you for your letter dated 26 June 2015. We are grateful to you for allowing us the opportunity to provide comments on AGA's letter of 29 May 2015. Our comments are set out below by reference to the relevant paragraph numbering in AGA's letter.

We have avoided as far as is possible repeating explanations of SRL's position set out in our response to AGA's application. For the avoidance of doubt, where specific allegations raised by AGA in its letter may not have been expressly dealt with in this letter, they are not accepted to the extent that they are inconsistent with SRL's full position as set out in this letter and our previous response to AGA's application.

1 Introduction

Paragraph 1.3.1

Since our letter of 1 May 2015, the Station Access Agreement dated 15 July 2011 (the "Original SAA") has been further extended until the earlier of (i) 01:59 hours on 27 September 2015, (ii) where the Station Facility Owner is directed by the ORR under section 17 of the Railways Act 1993 to allow the Beneficiary access to the Station under a replacement Station Access Agreement, any earlier date with effect from which the beneficiary is entitled to access the Station under that replacement Station Access Agreement, and (iii) the discontinuance of services calling at the Station in accordance with section 37 of the Railways Act 2005.

AGA's application relates to its current franchise which is scheduled to end on 16 October 2016 or another date up to seven railway periods thereafter.

For the avoidance of any doubt, SRL's position remains that access should continue to be granted until 18 July 2016 in accordance with the terms of Part F of the Stobart Station Access Conditions 2011 ("SACs") which apply in relation to the Station. These establish the terms of the Access Charge Schedule to be included in access agreements (which is set out in the Schedule to the Access Conditions) and specify what elements are subject to customisation.

SRL remains willing to undertake a review of the arrangements in accordance with the terms of the Stobart Access Conditions 2011 (the "SACs") in the hope that a new agreement can be agreed with AGA to take effect from 18 July 2016 until the end of AGA's franchise, subject to the approval of ORR.

Longer term arrangements beyond the end of AGA's franchise will be a matter for negotiation between SRL and the successful bidder for the next franchise. Such arrangements will require approval by ORR in due course.

2 Summary

We address each issue as set out in detail by AGA.

3 Term and Termination of Original SAA

Paragraph 3.1

AGA comments on and speculates about the intentions of the parties in 2011 although those events took place at a time before they had any involvement.

For the record, in 2011 the DfT insisted that the services would be designated as experimental. They also insisted that they would not approve any operating agreement or associated station access agreement for a period beyond the December 2014 Passenger Change Date because of the franchise programme they anticipated at that time. At no time did the DfT indicate to SRL that the arrangements until December 2014 were intended "to allow a substantial proportion of SRL's investment to be recovered during that period". Indeed, the DfT's notes of a meeting with SRL on 22 October 2013 record that "at the time of the arrangement being agreed there was a degree of scepticism in the DfT that the airport would be a success".

SRL was most unhappy about the requirements upon which the DfT insisted but decided to accept the risks associated with the services being designated as experimental, taking into account that if the airport was successful the ongoing revenue share arrangements would support recovery of its investment and an appropriate return. SRL also accepted that the Original SAA would terminate on the December 2014 Passenger Change Date and that a negotiation would be required with whoever the train operator turned out to be in December 2014, having regard to the established SACs and what might be negotiated in relation to ongoing operating arrangements.

SRL signalled its clear intention in relation to the terms of any future station access agreements in the provisions of the approved SACs. This evidences a very different intent to the arrangements portrayed by AGA. The provisions in the SACs for a five yearly review were finalised after the DfT announced its intention to designate the services as experimental by means of advertisements in the press. The review provisions (which were approved by the ORR and the DfT and are set out in paragraph 5 of the specimen charges schedule in the Schedule to the SACs) are clearly designed to support long term operation of the charging structure by enabling the operation of the charges model to be updated for changes in circumstances (while maintaining the principle of the 0.91 factor) and by enabling interim reviews to take account of other identified developments which might distort the operation of the charging model.

Paragraph 3.2

Although AGA sent a letter dated 19 September 2014 notifying SRL that the agreements would "not continue post December 2014 Passenger Change Date", AGA subsequently withdrew that notification by entering into the extension arrangements referred to above.

Paragraph 3.4

There is no implication that different terms of access were envisaged to apply after the Passenger Change Date in 2014. However, SRL has never disputed that AGA had a right to request a new agreement on different terms with effect from the December 2014 Passenger Change Date.

Paragraph 3.5

SRL's case for construction of the Station was not "on the basis of higher-than-normal charges only during the period until the Passenger Change Date in December 2014". This is unsubstantiated speculation by AGA about SRL's commercial strategy in 2011. If it had been the case that certain charges would be limited to the period up to the December 2014 Passenger Change Date, then the SACs would not have provided all the provisions they do for a long term approach with a five yearly review.

Paragraph 3.6

SRL wanted to enter into a longer term station access agreement in 2011. It was the DfT who insisted that they would not approve a station access agreement with a termination date after the December 2014 Passenger Change Date. SRL had no commercial choice but to accept the period SRL was able to secure.

4 Charges to be considered at point of application for access

Paragraph 4.1

SRL does not dispute that each application needs to be considered on its merits. The terms of the SACs are also relevant.

Paragraph 4.2

Section 3 of AGA's letter focuses in a forthright manner on what they believe was intended in 2011. The approved SACs contain concrete evidence of SRL's intentions in 2011. These reflected a process undertaken with the ORR and DfT which led to the terms being approved, including by the then operator, by DfT under that operator's franchise agreement and under the Railways Act.

Paragraph 4.4

In deciding whether or not to take a different view of the charges in 2015 than it did in 2011, we submit that the ORR should take into account that:

- it is not the case that "the Revenue Share arrangement was only intended to be for a shorter initial "start up" period";
- the return on investment that SRL will make by the end of AGA's franchise is not extravagantly high – by that date SRL will still be loss-making;

- neither AGA nor the DfT have proposed any "service enhancements to the Station" on the conditional basis postulated by AGA; and
- the terms set out in the SACs and the Original SAA are consistent with the requirements of the 2005 Regulations.

5 Charging principles – the 2005 Regulations

Paragraph 5.1

AGA's selective presentation of the provisions of the 2005 Regulations is not accepted and SRL will refer to the entirety of the 2005 Regulations for their full terms and effect as necessary.

Paragraph 5.2

AGA recognises that SRL "may possibly" be entitled to a reasonable rate of return on its investment in the Station. SRL submits that it is absolutely entitled to make a profit from the investment it made and benefit from the risks it accepted not only in constructing the Station but in creating a market for rail travel and new rail revenue that did not exist before and which, if not for SRL's investment, would not have existed at all.

Paragraph 5.4.1

SRL does not publish a network statement in respect of Southend Airport Station for the same reason that AGA does not publish network statements for any of its operated stations or its passenger services. The relevant network in Great Britain is owned and managed by Network Rail. As the station operator, SRL has provided full details of its access conditions and charges through SACs which are also available via the public register maintained by the ORR. Given that AGA is additionally party to the Station Access Agreement, it can have no complaint as to transparency of charges and this application is not made by reference to network statements but for the purpose of seeking a station access agreement.

Paragraph 5.4.2

AGA's application relates to their current franchise. No other operator has applied or is likely to apply for access to the Station before the end of AGA's franchise, let alone before 18 July 2016. This issue is irrelevant in the context of AGA's application. For the record, there is no reason why multiple users of the Station should not have charges applied in the same way through a revenue share on incremental revenue from calling at the Station. This would be fair and transparent and capable of regular review.

Paragraph 5.4.3

It is not clear to SRL what proposals AGA has in mind or, indeed, what rolling stock AGA has at its disposal to enable it to strengthen services to and from the Station during the unexpired term of its franchise. This is a matter SRL would be willing to consider in the review it proposes to take of the arrangements going forward from 18 July 2016. Needless to say, the extent to which traffic to and from the Station is responsible for any overcrowding generally on the line between London and Southend Victoria will need to be demonstrated. SRL considers that factors other than the Airport are the main contributors to crowding issues.

Paragraph 5.6

It appears that both AGA and SRL consider the circumstances at the Station to be unique.

6 Charging principles – the Draft 2015 Regulations

Paragraph 6.1

AGA has misunderstood the point and is legally incorrect to state that EU charging principles have not been implemented into English law and should not be taken into account by the ORR.

Directive 2012/34/EU is in the process of being transposed into law for GB but it is itself a recast of the First Railway Package which included Directive 2001/14/ EC on the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure. The original formulation of the "EU charging principles" was contained in Directive 2001/14/EC (noting in particular Article 8(2) for specific investment projects) and has been retained in all relevant respects going forward in the recast Directive 2012/34/EU. In particular Article 8(2) of 2001/14 and Article 32(3) of 2012/34 are effectively in the same terms, confirming the charging principle relating to the encouragement of investment and recovery in relation to it (as confirmed by Recital 34 of Directive 2001/14/EC).

The 2005 Regulations do not merely set out an equivalent set of principles as suggested by AGA. As the Regulations and accompanying Explanatory Memorandum themselves make clear, the 2005 Regulations were the specific implementing regulations of the First Railway Package including Directive 2001/14/EC (as amended) and the EU charging principles contained within them. The EU charging principles embedded in the 2005 Regulations are therefore directly relevant to this application and must be taken into account by the ORR.

For the avoidance of doubt, SRL considers that the charging arrangements for the station are in accordance with applicable EU charging principles.

7 Investment Recovery Charge

Paragraph 7.3

AGA is in no position to speculate about what SRL's commercial strategy in respect of public transport to and from the airport would have been had it not been given the assurances in the DfT's letter of 6 October 2009 which led to the subsequent negotiations that resulted in the suite of agreements entered into in 2011.

SRL regards having a train service to the airport as highly desirable. However, had the experimental train service failed to meet the DfT's criteria for being made permanent and the train service ceased, the airport would not have closed. In those circumstances SRL would have been incentivised to encourage passengers to access the airport by car and to use the airport's car parking facilities.

Paragraph 7.4

SRL was minded from the outset when it first developed proposals for the Station that a revenue sharing basis would be desirable in order for it to be incentivised to encourage passengers to travel by rail. The income it has received since the Station opened is not a "windfall". The income has been made as a direct result of SRL's actions in accepting all the risks and growing the number of passengers from the small number that used the Station when it opened in July 2011.

Paragraph 7.5

See our comments on paragraph 7.4 above and sections 8 and 9 below.

Paragraph 7.6

This is a key issue. SRL submits that the ORR should not prohibit the use of revenue sharing as a basis for charging by requiring one of its standard templates to be used in perpetuity. This would be a failure to take account of the particular circumstances applicable to Southend Airport Station as a privately funded, new station, agreed from the outset to be constructed, operated and maintained on a different, revenue sharing basis. The standard templates do not address the situation where a new station is to be funded, but are designed to apply for the far more usual situation of access to established stations where there is no present requirement to fund their construction.

8 ORR Duties under the Act

Paragraphs 8.2.1 and 8.2.3

SRL is surprised by AGA's threat to consider reducing the number of services calling at the Station during its current franchise. There is no mention of such a threat in sections 4.3 and 4.6 of their application. This appears to SRL to be an unreasonable attempt to place pressure on the ORR to determine the application in their favour.

Paragraph 8.2.2

It is not clear what additional capacity AGA considers it is necessary for it to provide for the unexpired term of its franchise in order for it to provide "adequate capacity" for the users of the service from the Station. See also our comments on paragraph 5.4.3 above.

Paragraph 8.2.4

Speculation about a 30 year period is outside the scope of this application as the application relates to the current AGA franchise. Such speculation takes no account of the provision for reviews in the SACs or what may be agreed in the future in relation to operators committing to call or provide additional services or additional capacity.

Paragraph 8.2.5

AGA has been able to plan its business with a precise degree of assurance in respect of the arrangements at the Station. It has always known that the services would be designated experimental until 7 July 2016. It became clear to SRL from AGA's letter of 3 October 2012 that AGA had become disenchanted with the arrangements at the Station. Since October 2012 SRL has made it clear on repeated occasions that the terms it was willing to offer in any new agreement from the December 2014 Passenger Change Date until 17 July 2016 would be based on the approved SACs.

Given the clear and consistent position explained by SRL, AGA was in a position in October 2012 or at any time thereafter to submit an Application for Directions under Section 17 of the Railways Act 1993 (see also our comments on section 11 below).

Paragraph 8.2.6

The charges are not exceptionally high by any estimate. AGA's comment takes no account for the provisions for review in the SACs or what may be agreed in the future in relation to operators committing to call or provide services.

SRL further notes that the combination of the operating agreement offered by SRL and the SACs has been designed to ensure that the operator's marginal costs of calling at the station are covered, it is protected from calls at the station abstracting revenue from neighbouring stations, SRL funds and bears the costs of the station and the incremental revenue generated by the presence of the station is shared between the parties on the basis set out in the SACs. SRL considers it has shared fairly in the incremental revenue generated by the risks, costs and investment it has undertaken, while the railway is also benefitting significantly from the incremental revenue generated by the airport which would not be present but for the station.

The effect of Southend airport on the markets for airport services and air travel more generally and any relative effects in relation to Stansted Airport are properly exogenous factors, outside the scope of the possible abstractive effects which ought properly to be (and are) taken into account in the charging arrangements under the SACs.

Paragraph 8.2.7

SRL has submitted a response to the representations from the DfT.

9 Fair, transparent and non-discriminatory charging

Paragraph 9.1

No other operators have applied or are likely to apply for access to the Station during the unexpired term of AGA's franchise so the issue about other users is irrelevant to their application. A qualifying expenditure and long term charge arrangement is not the only way of charging in a fair, transparent and non-discriminatory fashion. SRL is concerned that the template charges arrangement would not be a fair way of charging for a privately funded, newly built station, where costs and risks in relation to its build have to be addressed. The SACs provide for fair, transparent and non-discriminatory charges and in no way act to deter other users.

Paragraph 9.3

AGA refers to the "long term". This is outside the scope of their application.

Paragraph 9.4

It is not the case that 73% of all ticket revenue is paid to SRL. This is an over-simplification of the formula that applies. From LENNON reports provided by AGA, the average yield to SRL per standardised passenger, wherever they are travelling, appears to be in the order of £6.30.

Paragraph 9.5

See our comments on paragraphs 8.2.1 and 8.2.3 above in respect of AGA's threat to reduce services.

Paragraph 9.6

SRL has submitted a response to the representations from the DfT.

10 Airport charging and the role of the CAA

Paragraph 10.4

The statement "Airports should be funded by the airline industry rather than by the rail industry" is nonsense. Any airport that invests in and/or owns transport facilities such as railway stations, car parks and facilities for coaches, buses and taxis is entitled to charge for and make an appropriate return from those facilities.

Paragraph 10.5

If the ORR believes that the CAA has a statutory role in determining the extent to which an airport should benefit from an investment it has made in enabling passengers to travel to an airport by train, then SRL will welcome the involvement of the CAA in this matter.

11 Retrospective access charging – December 2014

In all discussions with AGA subsequent to receiving their letter of 3 October 2012, SRL made it clear on repeated occasions that the terms it was willing to offer in any new agreement from the December 2014 Passenger Change Date until 17 July 2016 would be based on the approved SACs. AGA had adequate opportunity to submit an Application for Directions under Section 17 of the Railways Act 1993 in a timely fashion for the matter to be resolved in advance of the December 2014 Passenger Change Date.

In the event, AGA chose not to make an application until 31 March 2015 thereby rendering it impossible for the matter to be resolved even by the May 2015 Passenger Change Date. The issue of retrospective access charging would not have arisen at all if AGA had submitted their application in a timely fashion.

Clause 11.5

Given that AGA "appreciates that private companies may possibly be entitled to recover and make a reasonable return on their investment in accordance with the 2005 Regulations", SRL will limit its further comments on this general matter to such comments the ORR might invite it to make in the light of SRL's experience as a pioneer of this type of station investment.

12 Other comments on SRL Response

Paragraph 12.1.1

See our comments about service enhancements above.

Paragraph 12.1.2

The reference to a 30 year period is not relevant to AGA's application which relates to the unexpired term of their franchise.

Paragraph 12.1.6

From LENNON reports provided by AGA, the average yield to SRL per standardised passenger, wherever they are travelling, appears to be in the order of £6.30. These services have now transferred to the Crossrail operator thereby putting SRL in a position to monitor the effect, if any, on its yield. This is one of the factors that will inform SRL's review of the

arrangements scheduled to take effect on 18 July 2016 and its negotiations with the successful bidder for the next franchise.

Paragraph 12.1.7

This is an unsubstantiated assertion as AGA do not know what SRL charges would have been had they been made on the "standard" industry basis.

Paragraph 12.1.8

SRL would welcome any data AGA might provide that would help SRL refine its estimate of the percentage of airport passengers who travel to and from the airport by rail.

Paragraph 12.1.9

SRL has indeed been unwilling to agree terms different to those in the SACs, Original SAA and Operating Agreement but only insofar as such new terms as might be agreed to take effect and apply before 18 July 2016.

Yours sincerely

Andrew Tinkler
Chief Executive