OFFICE OF RAIL AND ROAD
TRANSCRIPT OF ECML INDUSTRY HEARING
HELD ON
4TH MARCH 2016

PERSONS PRESENT:

Office of Rail and Road
JOHN LARKINSON
JULIET LAZARUS
CHRIS HEMSLEY
EMILY BULMAN
ROB PLASKITT
DAVID REED
MICK DONOVAN
ELIZABETH THORNHILL
JOE QUILL

CH2M Hill
CHRIS JUDGE
OLIVER HAYCOCK
JON CLYNE

GHD
CARA MURPHY

Systra
JOHN SEGAL
JENNY CROSS
CHRIS POWNALL

DfT
SIMON SMITH
DAN MOORE
ENRICO RUSSO
EVI BELL
ANDREW MURRAY

SDG
LUCY KAVANAGH

Network Rail
FIONA DOLMAN
ELAINE FOLWELL
GRAHAM BOTHAM

FirstGroup
RUSSELL EVANS
JOHN FAGAN
CHRIS JACKSON
STUART JONES
ANDREW WALLS

VTEC
DAVID HORNE
ANDY SPARKES
PHIL DAWSON
MARTIN PRIOR
THE CHAIR: Good morning. Thank you for coming. Welcome to the Office of Rail and Road. My name is John Larkinson and I’m the Director of Railway Markets and Economics, and I’ll be chairing today’s meeting.

With me on the panel are Juliet Lazarus, our Director of Legal Services; Chris Hemsley, our Deputy Director of Markets and Competition; Emily Bulman, our Head of Transport Economics; and Rob Plaskitt, Head of Access and Licensing.

We’re joined by Mick Donovan, who is our Operations Advisor; Chris Judge and Jon Clyne from our consultants, CH2M Hill, and John Segal from Systra, the auditors. Other members of the case team - David Reed, Joe Quill and Liz Thornhill - are also in the room.

Around the table we have representatives of the applicants, who are Alliance, Virgin Trains East Coast and FirstGroup. And we also have representatives from Network Rail and the DfT.

Representatives of other stakeholders, including passenger and freight operators on the route are also present.

A transcript is going to be taken of what’s said today. Can I ask you when you speak to please give your name and your organisation to help the stenographer.

The transcript will be prepared as quickly as possible and a draft will be sent to those who speak. You will be able to propose amendments but without changing the substance of what you have said, and the final transcript will be published on our website.

The acoustics in this room are not very good, so we have got a sound system. In addition to the table microphones we’ve got a couple of roving microphones, so if you’re not in front of a table microphone please wait for one of the roving microphones to be passed to you before you speak.

The purpose of today is to help ensure that we have the information we need to make decisions about the proposed services, in line with our duties. But we’re not going to be taking any decisions today. This is one part of the overall process which will assist us in making a recommendation to our board, who will take the final decision on these applications.

It’s important that our decision is properly informed by your views. This meeting is a practical opportunity for the parties to participate in discussion of the key points. With this in mind, given the number of participants there’s a necessary degree of formality needed to ensure that everyone is able to make a fair contribution, and we’ll try to keep this to a minimum.

This hearing is part of the decision-making process, and my legal colleague, Juliet, is here to ensure that due legal process is followed.

In the interests of time, given the number of people here, please could you try to keep your contributions focused on the most significant issues? We will not have time today for you to repeat all the detailed points you already made to us, but they will be picked up as
part of the consideration process.

In terms of structure, this morning we’re going to start by discussing capacity, and then we’re going to turn the economic analysis of the applications. We’ll discuss demand modelling in our session before lunch, and following lunch we’ll discuss the impacts on the parties and further issues, including the economic appraisal.

I’ll introduce each issue and we’ll begin the questioning, and stakeholders will have the opportunity to ask questions or make comments through me. I would ask that you do not interrupt each other and that we try and keep things brief and to the point.

At the end of each session I’ll summarise any action points and at the end of the day we’ll summarise the next steps in light of what we’ve heard.

Before we continue I’m going to pause there and ask if there are any questions about the process today before we make a start on capacity. No? Okay. Thank you.

In that case let’s start on capacity, and I’m going to hand over to Rob Plaskitt to set out our current understanding of capacity issues.

ORR:

Thanks, John. Good morning, everyone. To start off this section I think we should recognise the question of what capacity is or will be available, and when it will be available, is rather complicated, with rolling stock choices, service patterns, infrastructure works, power supply issues, and other things all affecting the answer.

So we want to start by recapping where we think we are on capacity and give everyone an opportunity to comment.

We’ll start by setting out our thinking on the southern end of the route and then pause for Network Rail and then everyone else to comment. Then we will come back and pick up our thinking on the northern end of the route. And again, we’ll pause and let Network Rail and others react. And then finally for this session I’ll say something very brief about how that capacity might be used, and I’ll pick up DfT’s recent comments about the future of the ECML connectivity fund. And again, there’ll be a chance to react and comment.

So picking up the south end first, and looking at services out of King’s Cross. We understand VTEC currently uses around five off-peak paths an hour, open access operators First Hull Trains and Grand Central share something around one path an hour, making a total of six.

Our current best view is that capacity for an additional off-peak path every other hour out of King’s Cross is probably available today. We think one further additional off-peak path per hour out of King’s Cross should be available from the May 2021 timetable, assuming the infrastructure works at Werrington and Woodwalton are completed, in line with Network Rail’s enhancement delivery plan.

When I say ‘Enhancement Delivery Plan’ I’m referring to the version that Network Rail has prepared that reflects the Hendy Review.
conclusions. We spoke about this a little, some of us, before Christmas.

A further half path per hour off-peak, we think, may be available beyond this point, bringing the total capacity up to eight paths per off-peak hour out of King’s Cross, but we would want to better understand the risks to connectivity and freight before that final half path of capacity was used. For example, we’d want to be clear what an eighth off-peak LDHS train out of King’s Cross every hour would mean for reduced connectivity at places such as Stevenage or reduced capacity for heavier freight that would want to use Welwyn.

Just on Welwyn, we’ve noted Network Rail’s advice that the VTEC and TSGN franchises specify a quantum of services that may not fit over the viaduct in one particular hour. We think it’s sensible stakeholders have started thinking about how that can be resolved.

But our view is that that issue does not need to be, and probably cannot be, settled before we decide on these applications. So having a clear answer on that is not on our critical path.

I think those are the key points I wanted to make about our thinking on the King’s Cross end of the route, so I’ll just pause there, and invite, to start off with, Network Rail to comment. Is there anything in that you would like to comment on, or disagree with, or are surprised by or think we’ve missed out?

NETWORK RAIL: We’ve got nothing further to add. We agree with your statement so far.

THE CHAIR: Okay - that’s helpful, thank you. Now we will open it up then to the applicants, and then DfT. Let’s start with the applicants first. Is there anything anybody wanted to comment on on what Rob’s just said?

VTEC: We agree with some of what Rob just said. We were surprised to hear you say that there was an extra half a path an hour available now. I think that’s new information to us. Our view is the route is pretty full at the moment, and bearing in mind things like freight, which often don’t get discussed at this sort of meeting - you know, it needs extra capacity before we can fit any more trains on reliably at this stage. I think we had recognised the extra one path at May 2021, bringing it up to seven, possibly seven and a half with compromises, and I think we’d supported your comment on the eighth - going from seven and a half to eight - as a possibility, only a possibility, and it needs to be fully understood in terms of all the compromises that would entail and any impact on performance.

THE CHAIR: Okay. So your main query is around the extra half a path.

VTEC: The extra half a path now is the biggest issue for us, I think, that we don’t recognise.
THE CHAIR: Okay.

ALLIANCE: Yes, just to clarify, is May 2021 now the date for the additional eighth path, then?

ORR: I said May 2021 because it was the first timetable after the end of December 2020, which is the date in the draft Enhancement Delivery Plan for the Woodwalton and Werrington schemes.

ALLIANCE: The reason I ask that is that that’s a later date than everybody’s plans for additional services, so it actually will be delaying even the start of the additional franchise services.

ORR: Well, we’re not saying capacity couldn’t be available before May 2021.

ALLIANCE: Okay. I have one further point to make, and that is about current open access services. The common assumption has been made throughout the process that only one path is currently used by open access. That actually is not correct. There are 16 paths today which are in each direction and they currently are spread over the maximum of 14 hours a day, which realistically is the maximum that can be achieved to get a sensible service. And one of those hours is basically barred because it’s a high peak hour in each direction. So it’s 16 paths in a maximum of 13 hours, which is around one and a quarter paths. So it is more than one. It’s less than one and a half but it’s more than one.

ORR: Yes. There’s certainly at least one hour where there are two quite close together arriving in London. I concur with that.

THE CHAIR: Anything else from the applicants? No. Okay. I’ll just ask whether DfT wanted to come in at all.

DFT: I just want to echo the concerns that Andy was expressing about, and the need to clarify connectivity and the ability of other operators, including freight, to fit in amongst the mix of services, and concerns around if something happens. The nearer you get towards even seven and a half, never mind eight, the more difficulty it may be.

DFT: So we note your points around needing to understand risks to connectivity and freight. We need to understand risks to performance as well. We think that’s also very important. The current performance of the line is not indicative of there being very substantial amounts of spare capacity at the moment, and we would be concerned about that trade off as well.

THE CHAIR: Thank you. Any other points before we move on to the northern end?
FIRSTGROUP: I think the only thing we would add to that in terms of the point that Simon Smith has made about performance is that I think previously as part of this whole application we’ve provided evidence as to how performance should be unaffected as a result of the applications that are being discussed. We provided that both in writing and at the previous meeting in October there was a discussion around performance.

THE CHAIR: Okay, thank you. Any other points?

VTEC: If we’re covering performance now then I’d like to just say more about that. We have very strong concerns about performance, both increasing - or particularly around this seven and a half, eight trains an hour. There hasn’t been any sort of robust recent work done by Network Rail, as far as we’re aware, on performance. The best estimate there is the figure that Fiona put in the letter of May 2015, which was 1.8 to 2 per cent impact on PPM without appropriate mitigations, which at that stage really hadn’t been identified.

We’ve done a quick look - effectively a back of the envelope calculation - and we reckon that’s worth about £160 million in lost revenue to the franchise over 10 years. That can’t be ignored. That’s a big number. So we can’t just blindly go into approving paths without understanding that 1.8 to 2 per cent better than we do today, I think, or making allowance for it.

THE CHAIR: Okay. So you’re reinforcing the points you’ve previously made about performance?

VTEC: Yes

THE CHAIR: Okay, thank you. I’m going to move us on now to the northern end.

ORR: So, turning to the northern end of the route then. The latest power supply analysis that Network Rail has produced was discussed last week in York. Several people here will have been at that meeting.

We understand from that that Network Rail has identified work, such as upgrading various feeder stations, will be needed around Doncaster and further north to meet any increase in electric load beyond today’s levels. Works in the Doncaster area, we understand, may be delivered around the end of December 2017 on current plans, but it seems unlikely the other necessary power supply enhancements will be completed much before the end of 2020, and that is subject to Network Rail working out what exactly it needs to do, and ought to do, and securing CP6 funding to do that work.

We think the Northallerton freight loops listed in Network Rail’s current Enhancement Delivery Plan, the draft Plan, for completion in March 2019, are needed to protect freight particularly if extra
passenger trains are to run between York and Newcastle. And looking at Edinburgh we agree with Network Rail’s view that no more than two and a half London to Edinburgh trains per hour could run without unduly impacting freight and local connectivity. So those I think are the two or three key points we want to make on the north end of the route.

Network Rail, how does that sound to you?

NETWORK RAIL: I’ll say the same thing as I said last time: that we agree with your summary of the situation and we don’t have anything to add to that.

THE CHAIR: Okay. Thank you. Let’s follow the same format, then, of just going first to the applicants, then to DfT, and then opening up to anybody who wants to make a comment.

VTEC: There are just a couple of things I’d just like to say. I note your comment in terms of the northern freight loops. I think it’s just worth adding that in the meeting earlier this week in York Network Rail indicated that the northern freight loops may actually be delayed to early CP6 rather than completed in March 2019, and the timescales are under review and not yet firmed up.

The second point is, noting your comments about London - Edinburgh trains, clearly since our last meeting here the franchise award for TransPennine and Northern have been made, the franchise TransPennine being awarded to FirstGroup, and the proposal within that include additional services between York and Edinburgh, and I suggest that that may need to be thought about as part of this process now, because clearly that is a new development since this process started, and it clearly has an impact on the capacity demand north of York.

THE CHAIR: Can I just ask you, David - that first comment you made about the possible change in the date, when did you say that possible change had been indicated? The power supply meeting?

VTEC: It was a stakeholder group. Ian was there - a stakeholder group looking at the East Coast Main Line Connectivity Fund where we had an update on the various schemes. The freight loops are part of the Connectivity Fund output. Network Rail indicated that whilst they’re hoping to still deliver the schemes within CP5, there is a possibility that the freight link project may slip into early CP6.

THE CHAIR: Graham, could you comment on that?

NETWORK RAIL: I think what’s David’s referring to is the piece of ongoing communication and information sharing on where we are with projects. David has articulated we share the risks. The dates in the delivery
plan are indicative, and we’ve got more work to do to demonstrate how we get to there.

THE CHAIR: Thank you.

ALLIANCE: I would agree with what David has said about the freight loops. That’s where we were, and Graham has just highlighted the position. There’s a couple of further things here. First of all the award for TransPennine and Northern really are not part of the process here. This is to deal with the applications that you have. I think that’s quite important.

The second one is that in view of the position that the DfT made clear about the possible withdrawal of funding for the CP5 schemes, bearing in mind that the electricity supply is likely to tip into CP6 can I have a view from the DfT as to whether or not the threat of withholding further investment on the route will accompany a possible award of an open access service on this route?

THE CHAIR: I’ll ask DfT to come back on that with any points DfT have in general on this. Just before we get there I’ll just see if there are any other points from applicants?

VTEC: I think there’s just this general concern about, clearly, exactly when either of the infrastructure schemes are to be delivered, as both are required in order to release the additional capacity, and to pick up on Graham’s point, the dates that we’ve all seen are simply indicative. So there’s this fundamental uncertainty prevailing throughout.

THE CHAIR: Okay. Thank you.

VTEC: One further point from me concerning Leeds - I’m assuming that Leeds counts as the north. I think we’re currently not clear about the capacity between Hambleton Junction and East Leeds for extra services via East Leeds Parkway, various people have said that there is or isn’t capacity for an InterCity type operation and I think that needs to be understood fully before a decision can be made that involves trains using that route.

ALLIANCE: On that point about capacity between Hambleton Junction and Leeds, Alliance is in discussion with Network Rail at the moment about ways in which we can help increase capacity on that section of route if that is needed. Those discussions are ongoing and we will be talking to the ORR separately about that. It’s a fairly recent development. We’re reopening discussions that we had some time ago.

THE CHAIR: Okay. Thank you. Can I ask if DfT want to come in at this point? Generally and also in terms of answering Ian’s point.
DFT: We have nothing further to add on the basic capacity issues. On the point about CP6, I think it’s way too early at this stage to comment on priorities for CP6. There will clearly be a number of competing priorities, with a number of schemes having been delayed from CP5, but it is too early at this stage to comment. In general the Department, when undertaking analysis of the case for different enhancement schemes, as we’ve set out we’d look at the benefit to cost ratio of those schemes. If the schemes facilitate the introduction of highly abstractive open access services then it is likely that the cost elements of the benefit to cost calculation, that is the cost to government element, will be quite high and that will affect that analysis.

THE CHAIR: Would anyone not at the table like to come in at this point?

FTPE: Just to provide a bit of context to the points that have already been made about franchise award. Over the next seven years we will be seeing quite major changes in our timetable that have been committed to DfT as part of the new FirstGroup franchise. We’ll see an introduction of high performance rolling stock, and as part of that the intention is to apply for additional access on the East Coast Main Line in two phases, so both north of York to Newcastle initially, and then further to Edinburgh. So as has been noted, whilst not directly relevant to the determination it’s probably quite an important context to be aware of. Those applications will be submitted for industry consultation imminently. Thank you.

THE CHAIR: Okay. Thank you.

ORR: There were just two other points we wanted to pick up in this section, one about the Hendy consultation first of all. The DfT said in its Hendy consultation, which I think is still open if anyone hasn’t replied yet, that its decisions about the connectivity fund might depend on our East Coast access decisions. Everyone, certainly the applicants, should have seen we have exchanged letters with DfT, starting to explore what that statement means.

The current position is that we think the value for money concerns that DfT have raised are relevant to our duties, but we are unclear how much weight we can reasonably give them in this kind of decision-making process in the absence of any information about: the assumptions that were originally made about value for money of the fund or individual projects within it, details of the analysis, how the analysis would change depending on the decisions we might make, and an understanding of how material those changes might be for value for money.

So we’ve asked DfT to share whatever analysis and thoughts it has on those points, and we’ve asked for a reply by 15 March. That letter only went out yesterday. We’ll be copying it around everyone in
the usual way. We didn’t want to bombard everyone with too many new bits of information just before today.

So that’s where we stand on that issue which Ian referenced a moment ago.

THE CHAIR: Can I just pause on that point? I don’t know if DfT wanted to say anything more at this stage or not.

DFT: I don’t think there’s anything more that we can say on that at this stage, other than what was set out in our letter from 19 February, which I assume that you and the applicants have seen, but to reiterate the point the original condition for the fund should be a BCR threshold of 1.5 for individual projects. That BCR threshold and the overall case of the fund itself was predicated on the assumption that the East Coast franchisee would use the additional capacity. The BCR is likely to be significantly impacted if the capacity was used by an open access operator, and therefore that threshold of 1.5 may well not be reached.

THE CHAIR: Thank you.

ALLIANCE: I’ll be very keen to see the evidence about the position for the agreement for this fund, going all the way back to well into CP4 about the BCR. It’s the first I’ve heard about it, and DfT are starting to use it now.

This fund was approved as part of the regulatory settlement as far as I’m aware, and it would appear to me that the DfT are now trying to retrospectively review a regulatory settlement for something that just doesn’t suit.

Now, in respect of a BCR in relation to investments via those approvals in the ORR, then I don’t quite see how the DfT can view this as anything other than state aid, and it’s certainly an area that we’ll be responding back to you on in relation to the consultation that’s open at the moment.

But the fact is that, going all the way back to the original meetings when this was fund was first approved, the talk then was of increasing the route availability from six to seven paths, and it is only Alliance that continued to badger and pester, as I’m sure my colleagues at Network Rail will agree, to say that there’s already seven and therefore you shouldn’t be spending any money at all if it’s only seven that you want.

And eventually we’ve got to the conclusion - which I think you’ve come to as well, which by 2021 there will be eight, which is where we expect it to be.

At that time, at those meetings - and they’re all minuted - the DfT said they wanted six paths on the route - not six and a half or seven - six paths on the route and that one of the issues in relation to this investment as well is to deliver the six paths they will need to
I regard the letters from the DfT - and I'm happy to put it into print today - as nothing more than blackmail of the independent regulator. I'd like to make the point clearly today, that we're not happy about it, it won't finish here and we'll continue to respond in the way that we think, legally, is the right way to respond.

THE CHAIR: Thank you.

ALLIANCE: Can I add as well, with the Connectivity Fund we'd like to note that the DfT has had ample option to protect its interests here. It could have looked at using the rebate mechanism. It could have looked at agreements with operators upfront. It could have looked at access options, could have looked at protecting loss. It could have looked at the levy. All these things we've raised with the DfT, and I'd like to know from the DfT, instead of it whinging about impact on Secretary of State's funds, what it's actually done to try and avoid putting taxpayers' funds at risk.

Because at the minute all it's doing is saying it's getting the taxpayer to back up the risk. It's requiring taxpayer investment in the network. What we are saying firmly is "You didn't need to do that. There's an alternative mechanism. We will quite happily pay our way." But we're not being allowed to do that. I think that's an important point, where open access are actually wanting to pay a bit more to contribute and there is a way forward through existing mechanisms. We would like to do that. The DfT hasn't made use of those.

THE CHAIR: I'll take some more points before giving people an opportunity to come back. Thank you.

FIRSTGROUP: I think the only point we have around the East Coast Connectivity Fund is in a letter we sent to the ORR last week, which I believe was copied to parties around the room.

And that goes to the point that Ian already made that the investment is required to unlock the capacity that's required for the franchise, and in doing so - in unlocking the capacity and spending that money to unlock the capacity it - by its very nature, unlocks more capacity, and Ian's already pointed out that I think everyone's come to the conclusion that there will be eight paths available.

Now, what hasn’t been picked up so far in terms of some of the points that have been made is that if a path is created and the franchisee runs what the business case was for the original franchise, which is the six plus the existing paths - the ones we talked about from Hull Trains and Grand Central, and an additional path that's available, and open access operators use that - then the overall economic benefit is likely to be higher than was originally considered in the business case. The total economic benefit of having both paths
operating is likely to be higher as a result of the investments spent. And when I say ‘total economic benefit’ I mean all economic benefit, not just benefit to the DfT.

THE CHAIR: Okay. Thank you. Any other points on that before I see if DfT want to come back?

HULL TRAINS: I have a big concern about the regulatory settlement and what is funded for enhancements, i.e. the Connectivity Fund. We’re of the view that unless that investment is predicated by a track access application of some sort to use that investment for a particular purpose, then the result of that investment is free for everybody to bid into.

It is the inability to join the dots up - and if you’re putting money forward, if you’re making an investment case for new railing stock or a new franchise and you don’t put the rights with that case then it’s not following the industry procedure and it’s giving other parties false expectations, through the regulatory settlement, of what they can actually use in terms of the network to run existing services better or new services in the future.

And I really would urge that the DfT actually starts to use the industry mechanisms rather than coming late to the party and trying to retrospectively alter things to suit a purpose which should have been more thoroughly thought through in the first place.

THE CHAIR: Thank you. Does the DfT want to come back on any of those points?

DFT: I’m not sure there’s much for us to add on that. We obviously welcome Alliance’s apparent willingness to pay its way. I think the DfT’s concerns about open access applications would be much reduced if open access operators did pay their way, but under our current charging structure - which is a matter for ORR, not for us - they don’t.

THE CHAIR: Just to check, were you referring to something specific then with that comment, Jonathan?

ALLIANCE: Yes. There are existing mechanisms including access options, and with regard to the connectivity problem, what DfT could have done there is actually engage with operators. The reason [inaudible] to do that under the organised policy up from negotiations where you can say ‘Pay your way.’

But actually the DfT is not taking advantage of existing mechanisms. All it has done is sit there and say ‘open access is going to abstract.’ But actually we want to talk to the DfT and we want to look at paying our way. We’re quite happy to do it.

The other thing is, in relation to the levy which is in the directive
but not UK law, we’ve been pushing for payment of a levy, but the DfT have sat by and not implemented the levy which would allow us to pay towards provision of PSO services, and that would reduce the burden on the taxpayer for funding the rail network.

The DfT seems to want the taxpayer to continue to fund the rail network, and that is wrong. And one other thing I’d just like to point in relation to DfT’s statement saying that in relation to investments being at risk, an important point here is that we are coming along with significant third-party non-taxpayer funded investment into the network in infrastructure and in rolling stock in two applications.

We can say the same. We can say ‘If we don’t get the access rights that’s at risk as well.’ So I don’t think that’s a valid point that the DfT are making.

THE CHAIR: Okay. Thank you.

ALLIANCE: Can I come back to - I know this meeting is not about the charging structure, but the DfT have made a point about the charging. Just to be clear, the charging structure at the moment is based on moderation of competition for entry to the market by open access. If open access is allowed free head-to-head competition with the franchise, then you can look at a different charging mechanism. The current charging mechanism is based on two different markets for paths and for getting paths granted on the network. So it’s wrong to say that open access is not paying its way.

THE CHAIR: Okay. Thank you.

FIRSTGROUP: Just an observation in that some of the submissions that are being made seem to be getting close to a submission that the decision should be made on the basis of a structure which may or may not come into place in the future. Obviously we do have a legislative regulatory regime for open access, or if necessary for tying paths to a particularly regulatory settlement then under submission.

If that is not done, then obviously there is the regulatory balancing exercise to do. But our submission would be it has to be under the rules that are there now and not on a future charging structure.

THE CHAIR: That’s right. Yes.

ALLIANCE: Can I just add something? Just at the time when we’ve got the Shaw Report, which is looking at ways to bring in third-party investment into the network, the DfT’s position which is basically threatening to withdraw funding, what sort of message does that send in terms of confidence for anybody who might want to look at investing in the network? Because if I - even completely [inaudible] denying it. I think
that the DfT needs to take that into account, that when they are coming along, saying that they can threaten to withdraw funding, it sends out the wrong message to the industry.

THE CHAIR: Okay. Thank you.

ORR: So just to wrap up on this section then, we talked a little bit earlier about the north and south ends of the route and our current views on capacity. Just looking at what might be done with that and to summarise the applications that we are considering, additional capacity could be allocated, we think, to subsets of services taken from: up to one additional hourly path for VTEC’s additional trains to Edinburgh; half an hourly path for VTEC’s Middlesbrough service; up to half an hourly path for First Edinburgh; one for Alliance Edinburgh and up to one for the Alliance Cleethorpes / West Yorkshire proposal; any additional capacity could be allocated to subsets made up from these services.

That was the last thing we wanted to say in this section. I don’t think that’s a controversial statement but I’ll just check in case anyone disagrees or thinks I’ve missed something out.

VTEC: I just think the point on the north of the route - the north of the route still requires CP6 funding.

ORR: Yes - the idea that one could take subsets of those choices and put them together and approve them is all subject to the long list of caveats we discussed earlier.

ALLIANCE: Just one quick question. At the last hearing I raised the issue about access to Middlesbrough, and we were talking earlier about capacity. I know there was some follow up. I think Network Rail did take the issue away and have a look at whether it would be possible to run an intercity or IEP train into Middlesbrough. Has that been looked at? If you’re still looking at the Middlesbrough application then is it possible to run an IEP into Middlesbrough? Does Network Rail have a view on that?

NETWORK RAIL: We haven’t looked at this in any further detail at this stage, so we can’t comment on it.

THE CHAIR: Okay.

ALLIANCE: Rob just said that the Alliance West Yorkshire application was, in round figures, one path per hour. Actually it’s significantly less than that. It’s nine trains a day, which is slightly more than half but significantly less than one. And I know we’re talking in broad figures about whole paths and half paths, but bear that in mind, that it isn’t a
whole path.

ORR: Yes, we accept that and I think Chris made a similar point earlier about the dangers of rounding. We are alert to that.

THE CHAIR: Yes. That's a good point. That covers all we wanted to cover on capacity, unless anybody else has got any other points. So let's now move on to talk about the different aspects of the economic appraisal. We're going to start by focusing on the set of issues around demand modelling before lunch, then after lunch go onto the impact on parties, so for example the impact on the Secretary of State's funds and on other open access operators, and then we'll move onto other aspects of the economic appraisal: for example the treatment of infrastructure costs and sunk costs.

ORR: Just to set out a bit of context so that we can try and work through the issues here in a simple sequence. I think that it's clear that central to the evidence that we have on revenue and economic impacts that we're going to use for our decision making is the CH2M report.

As you know, we've commissioned that report. It's been circulated and it has been accompanied by Systra's work to audit CH2M Hill's analysis. Separate to that, DfT has circulated an updated version of the SDG report that it has commissioned, and there was a helpful note there as well which responded to the views that SDG and DfT had received on an earlier draft.

So there's a lot of material here but I think it's really important that we try and progress on the basis that those reports have been widely reviewed, have been read by parties, and that there is no need necessarily here to summarise the detail of the approaches that each of those individual reports have taken.

Further, I think it's worth noting that quite a large number of points have been made about the CH2M report. I think it's helpful that you have set those out in writing, and we will review and reach a view on those points.

We do not intend to discuss each individual one of those points at this meeting. There obviously is not the time to do that and I don't think it would make the best use of the time we have. Rather, can we please focus on those issues where we think that discussion in this forum could add significantly to the available evidence?

I would therefore ask all parties to avoid simply repeating the material that is set out clearly in their reports or that has been previously submitted to ORR in writing.

Reflecting this, we propose to structure the session around a subset of issues. As I've noted, these issues are the ones where we think that discussion and debate here today in this forum could add significantly to the available evidence base.

So we're going to structure the discussion around a list of
issues as follows, which reflects the sequencing in the CH2M Hill report annexes.

We’re going to start off with Annex B, which is the MOIRA modelling. In particular here we’re going to talk about the options that have been modelled, and our intention here is to pick up some issues relating to the specification of the FirstGroup timetable, and some characteristics of the FirstGroup service in that section. So we will turn to that one first.

We will then turn to Annex C, which is the fares overlay. That includes the issue of competitive response, and we expect to spend a reasonable amount of time on that point.

We’ll then turn to Annex D, which is the competition overlay, and then Annex E, which is the gravity model, before finally turning to Annex F, which is the crowding model. And our intention here is to talk about some of the technical issues associated with some of the proposed services, and there is also the related issue of crowding for Middlesbrough.

So if we follow that structure we think that also provides us with an opportunity to discuss the underlying reasons for the differences between the CH2M and SDG reports, so we’ll pick those up as we go through. And obviously then there’s an opportunity for more general comments after we’ve gone through that.

So if people are with me so far, I think that means that we should turn to annex B. So that’s the Moira modelling and options. And I’ll start off with a bit of context and a couple of questions.

ALLIANCE: I’d just like to make a point. I’m not quite sure what relevance the report from one of the interested parties – the SDG report - is, and whether it’s more relevant than the report from AECOM, which is our work, and the report from FirstGroup in relation to their work.

It really is a concern for me. I made that quite clear I think in our response to SDG. It was of interest, but it’s their work, so why are we interested in their work? And it is a concern because you seem to be taking that into account, and we’re going to discuss it publicly, but the work that the others have done, which you wouldn’t normally put in a public domain anyway, we can’t discuss. So I think the SDG report is an irrelevance in relation to what’s going on here today, and I’m quite disappointed if you do end up actually giving it any credence whatsoever in this forum.

THE CHAIR: Well, the report has been tabled and I do think it’s quite important that we understand the differences between the different reports. But there’s nothing stopping everybody chipping in with the pieces of information or evidence that they think are particularly relevant in addition, so we’re not stopping anybody chipping in. But I think it’s quite important that we do explore the differences.
ALLIANCE: I mean, you would expect me to disagree with that. As I said, this is a report from a group that’s got a serious interest in what happens here, as we made quite clear; as indeed did FirstGroup in relation to their input. So it’s a biased report. It’s clearly a biased report, and as a result I just cannot see that it has any relevance, and I actually think it’s a real issue if it’s discussed here today as being relevant to an independent decision.

THE CHAIR: Well, it’s a piece of analysis, and ultimately our board has to decide what weight they place on different pieces of analysis. But given the purpose of the hearing, which is trying to shed more light on the issues, I do think it’s relevant. But I would urge you at any stage, if you’ve got issues you want to raise, then - you will do.

ALLIANCE: I understand your position, John, and you’re Chair. I fully understand that. But we have been consistent. Our response to the report was consistent in what we said. When we sent in our comments we made it quite clear we were just sending it to you, not for any internal discussion.

So, we may input at any time. But I’d just like to be recorded as saying our real concern that this biased report is being used in this forum.

THE CHAIR: Okay. Thank you.

DFT: We clearly disagree with that characterisation of the report as biased. What we tried to do is in the interest of constructive engagement with this process, to try to assist the ORR with its decision-making, not only prepared a detailed piece of analysis, but also shared that detailed piece of analysis on an open basis with all of the applicants.

We then prepared and provided a further note which reflects the points that have been raised by the applicants. We think it is an incredibly important for the ORR to consider that report. I think that we’ve acted in an entirely procedurally proper way, and in a constructive way and an open way. So we want to also put that on the record alongside Ian’s comments.

ALLIANCE: Okay. If this was a fully inclusive report we would have been consulted prior to the preparation of the report, not after the report, as indeed would our colleagues at FirstGroup. So, I’m sorry, I don’t accept that you’ve actually done something that’s independent and fully inclusive.

THE CHAIR: Okay, I think we’re going to note the disagreement on that. Thank you both. But I am going to stick to the structure that we have set out, and we will move on now to the MOIRA model.
ORR: Okay, so this is focused on the issues covered in Annex B of the CH2M report, so MOIRA modelling and the options.

So I will repeat the comment I’ve made; there are obviously a lot of comments on the MOIRA modelling and we don’t propose to go through those all here. But there is a particular issue related to the FirstGroup application and the options that have been modelled that we’d like to pick up.

As you’re familiar, we’ve been considering the issue of the overtake manoeuvre and the modelling of that, and the extent to which we think that is likely. Our current team view is that we think that is unlikely to be timetabled in practice. Reflecting this, CH2M have tested a further option, which is number 15 in their report, that removed that overtake.

We’ve been thinking further about that option, and one thing we would like to explore is the extent to which we think that option, as modelled, may still overstate the journey time that would be achieved in practice. So, if it is really to be clear there, we think that the actual journey time achieved may be shorter than the one that we have modelled.

We think that implies that there is a risk that the modelled results may understate abstraction. So actual abstraction may be higher than that which is modelled in option 15.

We also think that there is a risk that in that circumstance, because that faster service is more attractive, that may lead to further crowding effects and/or that that would give FirstGroup a strong commercial incentive to adjust fares, i.e. to increase fares in response to that better offer that is delivered to the market.

So that’s the context. I think just before I turn it over to First, I think two particular questions come out of that thought process. I think the first is whether FirstGroup in particular have got any comments on whether you think option 15 is a reasonable reflection of the journey times that would be achieved in practice.

And the second question is, have you got comments on those effects: so the likely impacts in terms of abstraction, crowding and fares?

FIRSTGROUP: I’ll make a couple of comments and then my colleague will probably make a more detailed comment. Just to answer your question in terms of, first of all, whether option 15 is something that should be tested, i.e. with no overtake manoeuvre - yes.

I think as we’ve said before - without wishing to go over ground before - when we submitted the timetable, that was done to demonstrate that our proposal could be pathed on the railway. When the timetable process then happens and once a train is on the graph and it has a path, as the timetable is developed that path often improves and it may not require overtaking in future. So we understand why that’s being tested and that’s okay.
In terms of your points about crowding and whether that as a result of a slightly better journey time we would change our position in terms of commercial offer, then I think dealing with the second one first, that’s not what’s going to happen.

We’ve been very clear about the type of business that we are proposing. It is new. It is innovative. It’s not done currently. We’ve made commitments in our application and discussions that we’ve shared with the ORR about the fares that we are proposing to offer. Those have been made and we are going to stick by those. That’s the purpose of our business model, it is to offer a low fare.

Our service models have been primarily based on reservations. Using the systems that we’ve got, people will be able to reserve up to a few minutes before departure, so if they want to travel on the train and then they will be able to book minutes before departure and pay the fare that we are proposing.

And I think just before I hand it over to my colleague, I would just like to say if you think that as a result of our proposal that will lead to crowding, then we’re obviously very pleased by the fact that you think our service is going to be very popular and our business case clearly works very well. So as a result of that we’re quite happy.

FIRSTGROUP: I don’t think I’ve got much more to add other than to say that we’ve also tested the same scenario as CH2M Hill, and we’ve come up with a similar result in terms of the relativity between those two options. We think it represents a sensible sensitivity test for this issue.

ORR: Okay, that’s very helpful. I guess the particular thing I’d just like to come back on is that I understand your point that that’s the business model you’re launching today, or proposing to launch today, but if we are in a world where you achieve faster journey times won’t your commercial imperative be to change that business model? I guess that’s the nub of the issue.

FIRSTGROUP: I don’t see why. That’s the bit I’m struggling with. I understand that today on the railways, if you had two services, generally how it works, I could understand why you might say ‘Well, if the train’s going faster and faster and they’ve become the fastest train and they’re going to be the most popular train’, but I don’t think either that you’re proposing that they are the fastest train. Actually what they would have is a similar journey time to Virgin’s service.

So I think that’s all you’re suggesting is that Virgin would still have services that they’re proposing to be trains to Edinburgh. We would be running five trains in one direction and five in another. So we’re not running every hour.

We know what we’re offering in terms of the available seating capacity, and we are marketing and we are proposing the service, and we’ve made those commitments in writing and in part of our proposal
that we’ve submitted to you. We’ve made those commitments about the fare that we will charge.

FIRSTGROUP: I think the other thing to add as well is that the objective is to compete with the low fare airlines and coach operators as well, so in terms of the commercial pressure, if prices were to rise then you lose that competitive position with those other operators, and therefore we’re more likely to stick to the business model we set out.

FIRSTGROUP: And that’s the last point - really it is not a model based on journey time. We haven’t submitted this based on journey time. We haven’t asked for journey time protection or anything like that. We are proposing to operate this service to compete with other modes of transport: air and coach. That’s where we would generate our business from.

THE CHAIR: Any other points before we move on?

ALLIANCE: I fully agree with the points that Chris was making earlier. I think I don’t really understand how First will manage demand. I think the only way that they could do it would be making the trains reservation only so you cannot board unless you have a reserved seat, otherwise the trains will be flooded. And the only way that that can be enforced in the railway that we have is by having a customer service assistant at every door checking everyone’s reservation before they board the train. And that clearly has both cost implications and clearly time implications, because I can see some very long dwell times at Newcastle while that takes place in the southbound direction.

I’d be interested, in the context of that, to know what the actual capacity of these trains is, but I’ve also got a slightly more general point, which is about MOIRA. MOIRA, as I think we all recognise, is a very useful tool for understanding the generalised journey time implications of proposed services, but it is very sensitive to the precise ordering of trains on the graph. So if you have two trains to the same destination to pass one after the other nearly all the demand will be on the first train.

I mean, that’s logical and what would have happened at the time that MOIRA was constructed, when BR was the monopoly provider of rail services. In the world that we now have, with open access, it’s likely if you have two trains going to Edinburgh or Leeds or wherever, one open access, one franchised, departing a few minutes apart, some people will make a choice not on which goes first but on which has the costs and quality combination that they prefer.

So in reality, whether an Alliance service, for example, is just before a VTEC service, or a VTEC service is just before an Alliance service, won’t make as much difference as MOIRA would suggest. And I think that’s something to consider in looking at the MOIRA results for all these applications.
THE CHAIR: Okay. Thank you.

ORR: We’re going to pick up the capacity point next, but picking up the reservation point would be helpful.

FIRSTGROUP: Yes, I’m probably going to repeat myself, but it is the point again that the fares that we are proposing, if you want to purchase that fare you will get it with a seat, so it’s reservation-based. Clearly if somebody has an inter-available fare and there is room for them to travel on the train then they can travel on the train, but they won’t purchase that fare at the reduced rate.

Our dedicated fare for our service is based on reservation, as we’ve identified in our business plan that we have submitted to the ORR.

THE CHAIR: Okay. Thank you.

VTEC: I’d like to largely agree with what Simon and Chris were saying. We have very severe concerns about the journey time. It’s both the undertaking and the journey time that’s been assumed. Compared with our journey time we reckon it’s about 10 minutes slower than it needs to be. If you put those two together and model it just in MOIRA it more or less triples the abstraction you’d expect from the service, and that is a very significant change to the base service.

We’ve actually got independent advice on what FirstGroup would be able to be likely to achieve in the event that both parties had rights in 2020 or whenever. We’ve got Tony Crabtree to produce a report, looking at the Network Rail decision criteria, and it’s quite clear that if we both came in with equal rights we’d both get broadly equal journey times, so you could expect that in that circumstance there will be much more abstraction.

When you put that abstraction together with the relatively short trains, and the fact they will be very attractive to interavailable tickets, their services will be massively oversubscribed. So a rational operator would do one of two things. They’d run longer trains and thereby increase the abstraction or they’d put the prices up.

I imagine the easier option would be to put the prices up, and they’ve become more of a direct competitor to us than a coach and air competitor, as the original business plan said. And there’d be nothing to stop them doing that, and what rational operator wouldn’t do that?

THE CHAIR: Okay. Thank you.

FIRSTGROUP: I just think I need to come back, because of a number of these points that are being made, and made directly about our proposition. I suppose what I come back to saying is that the commitments that
Clearly everybody thinks that our business is going to be a huge success, which is good news, and I’m looking forward to the decision that’s coming. But having said that, and all joking aside, we’re proposing to run five trains a day in each direction, not two trains an hour in each direction. Virgin will be operating two trains an hour from London to Edinburgh in each direction.

We’re not running in the peaks. We’re an off-peak service. We’re targeting the air and coach market. Our business model works on the trains on which we are proposing, and I don’t think I can say anything else because if I do I’ll start repeating myself again.

THE CHAIR: Okay. Thank you.

ALLIANCE: I hear what Russell is saying about they’ve got a policy where it’s going to be low fares. I think the concern from our side is it’s really that enforcement, particularly on journey times, which drives revenue, but also about how the ORR would enforce low fares.

Because I don’t think you could actually do that. We’ve raised this before but I think it needs to be said again, that you’ve got nothing really you could do. Russell says what he’s going to do, but actually he could do anything that he wants in the long term.

THE CHAIR: Thank you.

DFT: So there’s been some discussion that FirstGroup would be targeting the air market and the coach market, and not the train operator. I think that’s ignoring the fact the air market is not a completely separate market. All of these applications, regardless of which is granted, will be seeking to compete with air travel on the London to Edinburgh flow - there’s been significant changes in their market share over time as prices have changed and the service quality offered by the different operators have changed. So I don’t think you can look at those as separate markets.

Specifically on the timetable point, I think it’s critical that ORR undertakes its assessment on a realistic, central case scenario for the timetable, and from what we’ve heard the scenario in which the FirstGroup service is overtaken and is much slower is not a realistic central case. Thank you.

THE CHAIR: Thank you. I’m going to move us on again. Have you got anything to say on that, Chris?

ORR: I may have misheard. Just to clarify some things you said, Andy. So I think you said that you think that the journey times could be 10 minutes faster than option 15 journey times?
VTEC: Yes.

ORR: That's very helpful. There's some other points that relate to the FirstGroup application that, given that we've talked about this area, it would be useful to pick up.

Largely these are the points that were raised in our January technical note relating to the proposed service; issues such as seating, the early morning service and coach competition. I was just going to again play back what we think currently about some of those issues.

We've started to touch on this already, but there's the issue of the modelling by SDG of the higher density seating. We have had a conversation with FirstGroup about the seating configuration and the density of that seating, and our current view is that the proposition - comparing standard class with the standard class on the likely Virgin service - is for a comparable level of comfort.

On the basis of that, we think on the point of whether there should be an adjustment relating to the quality of service, we think that the current treatment by CH2M is appropriate because we think that there is reasonable basis to believe that for standard class there will be a comparable service level.

The second point is relating to the early morning departure. This is the issue around the extent to which it is realistic to expect significant numbers of passengers to be on the 5.30 departure from King's Cross, given the different surface access options available at that time of day.

We have looked at this issue. The MOIRA modelling does model a lower number of passengers for that departure; that is one relevant point. The modelling results don't suggest that there are large numbers - or comparable numbers, I guess, if that's the phrase - on the 5.30 as there are on later services.

But we do recognise the difficulties in terms of surface access. But I think in general terms we don't see that the modelled results need significant adjustment to reflect the difficulties in reaching King's Cross at that time of day. Noting that that service, when it first stops at Stevenage, is stopping at a more convenient time for access at those later stations.

That's the second observation. The third one, related to coach competition, is the issue around whether the PDFH elasticities are reasonable or whether we need to make a further adjustment in respect of coach competition.

Again, we think that those elasticities are drawn on evidence from the market that has coach competition in it, and we'd also note that we don't think that the orders of magnitude here are particularly significant in terms of the effects of coach competition in terms of the results. So on that basis again we don't think that there is a need to make a particular adjustment to the modelling results in respect of coach competition.
FIRSTGROUP: I don’t particularly have much to add to those. We’ve already put on record and had those discussions with you in meetings and submitted them, so you would expect me to say that we would expect there to be a benefit in terms of our competition with coach, and we believe that’s there, so you might expect me to say that.

And on your other points you might also expect me to say we’re comfortable with your approach on the other two points.

THE CHAIR: Thank you.

SDG: I’d particularly like to go back on seating layouts. That’s evidence we’ve provided. We haven’t seen the detailed planned layout of the trains that FirstGroup are proposing, but we don’t understand how they’d be able to fit the quantity of people they think on those trains without using more airline style seating and significantly less two plus two and table seating.

Although there’s limited evidence on passenger seating preference there was a study undertaken which found that passengers did prefer the option of a table and the ability to sit with a group, and we included these values in our appraisal.

And we think this is quite a conservative estimate, the impact of going to that kind of seating structure, because the study was based on commuter routes. We think that people would have a stronger seating preference when they’re using a long intercity service, perhaps with business colleagues or with their family.

THE CHAIR: Okay. Thank you. Russell, did you want to come back on that?

FIRSTGROUP: I haven’t got a set of detailed plans to hand out so you can see the difference, but the trains are similar in that we’re proposing to use the AT300, the Hitachi product, which effectively is the same trains for IEP. I’ll give a little bit of detail; there will be slightly more airline seating, but not significantly. There will still be tables on the trains. The class 800 that exists and is currently under construction for the intercity express program for both Great Western and East Coast, their standard class coach is 26 metres long and has 88 seats, standard class seats.

Now, if you did five times 88 you’d get to over 400, but clearly there are driving vehicles so some of the coaches will have that – but all of those coaches that have the 88 seats in them have tables. They have airline seating but they have tables as well.

Our standard class coaches will have both tables and airline seating, and the pitch of the seats will be similar - the same as their current standard product.

I could make another point that there are currently Mk III coaches in operation on the railway network today, on those routes,
that are 23 metres long, so they're shorter and they have 84 seats in
them. So you could say the 88 seats in the 26 metre coach has better
pitch than today. And our pitch, as I've just said, will be similar to
those standard IEP layouts that are in the public domain, that have
been seen.

THE CHAIR: Okay. Thank you.

ALLIANCE: Surprisingly I agree with Lucy on most of what she’s said here this
morning. A couple of things here, that the operator with 84 seats in
the Mk III, is FirstGroup. Grand Central operates 64 seats in a similar
vehicle. And part of our proposal to go to Edinburgh, of course,
acknowledges the fact that most of the people flying early in the
morning, whichever way, are business people, and therefore the
importance of the seat space and some privacy will be the overrid-
ing factor for us.

And I think - I know you've got the information as well. You will
see from our own fares structure that because of the number of
services we offer and the availability throughout the day we're almost
offering as many seats at a similar price to what FirstGroup are
advertising, right across the day. And so I think that’s quite an
important point.

But for us, in a nine-car train, we’re looking at around about 500
seats. I still don’t know how many seats we’re talking about here in a
FirstGroup train, but I do understand from Hitachi’s plans initially that a
normal VTEC train, which admittedly will have first class, is around
about 330. So I’d still be quite interested to know the actual density of
the seats.

And one other thing: I’m assuming from what’s been said that
there are no operator-specific walk-on fares for this service, but I’d just
like to be sure that that's actually going to be the case. So if you
haven’t pre-booked it’s interavailable or nothing?

THE CHAIR: Okay. Thank you.

ALLIANCE: Not on the issue of seats density, but on the other two points that Chris
made. A 5.30 departure in the morning - clearly access costs will be
high at that time of day, although granted the lack of congestion,
access time may be low. But if you’re paying £20 quite easily for a taxi
fare to King’s Cross that rather undermines the advantage of
FirstGroup’s low fare offer, even assuming that in reality it’s
deliverable. So that is a consideration.

The other point is on the coach market. I looked at how many
coaches there are between Edinburgh and from Edinburgh and
Newcastle to London, today, and there are five daytime services from
Edinburgh and seven from Newcastle. So that’s about 700 seats, and
that's assuming 100 per cent load factor and it's assuming that
100 per cent of the journeys are end to end, neither of which are reasonable assumptions. So I do agree with you that the MOIRA elasticities do allow for coach competition.

THE CHAIR: Okay. Thank you. I'll just bring in Andy and then I'll come back to you, Russell.

VTEC: Andy Sparkes from VTEC. I just need to reinforce the 5.30 point. Our sister company runs a 5.30 from Euston to Glasgow. We've supplied the information in confidence to the ORR. But it has load factors that are an order of magnitude lower than FirstGroup are claiming, and we offer prices that are pretty similar to what they're proposing.

The point about that is not that the train is going to be empty, but the fact that if you're going to try and get 80 per cent overall the rest of the trains are going to be pretty close to 100, and you can't achieve that day in, day out, other than by significantly pricing up the busier days and thereby destroying the whole raison d'être of the service.

THE CHAIR: Thank you. FirstGroup, did you want to come back in?

FIRSTGROUP: Yes. So I'll deal with that 5.30 point. So yes, it is an early departure from King's Cross, but the key point of the service, which I think we've explained in our application and you just touched on a little bit, is that it will call at Stevenage, and the point at which it calls at Stevenage is still early in the morning, but it's around a similar departure time as the early morning flights from airports located near Stevenage, to Edinburgh, and that's the market that we are competing with. So that's actually the benefit of that service we run out of King’s Cross, because that's where the train starts. So that would offer the opportunity for people to travel from King’s Cross that early in the morning.

Both calling at King’s Cross and Stevenage means that we will have an arrival time into Edinburgh before 10 o'clock, which is a good time to arrive for meetings. So we think it will be a popular service, and that's why we proposed it.

Just coming back on the seating point, while we haven't got full final design from Hitachi I imagine in the same way that Alliance haven’t got the full final design for their rolling stock either, because our rolling stock investment is obviously dependent on decisions that are being made, but we have had discussions with Hitachi.

We have shared details. As Chris alluded to earlier we've shared commercially confidential details with the ORR as to what our seating layout will be. They will be five-car trains and they will have around 400 seats, but the exact number I can't tell you at the moment because we haven't got at the final design as yet.

THE CHAIR: Thank you. Are there any other points that wanted to raise, before we
come to a break.

ALLIANCE: It was just a question I asked about an operator-specific walk-on fare. I just wanted to be clear that there no operator-specific walk-on fares.

THE CHAIR: Sorry, yes. That was a question to FirstGroup?

ALLIANCE: To FirstGroup, yes.

FIRSTGROUP: I think I’ve already reiterated our commitment around fares and the fact that we will - the majority of our passengers and our availability will be based on having reservations that are advance-purchase fares that you will be able to book up to the moments before the point of departure. Those are the fares that we will offer. So once the train is at capacity we’re at capacity.

ALLIANCE: Sorry, that doesn’t quite answer it, actually. It’s a pretty simple question. On the day can I turn up and buy an operator-specific FirstGroup fare on that train - that’s all I want to know - or can I only buy an interavailable fare? It’s a simple question.

THE CHAIR: Do you want to answer that question?

FIRSTGROUP: Yes. Our current intention, I think as we put in our business plan which we’ve submitted, is that the operator fares will be the reservation fares.

ALLIANCE: No, not quite there yet but nearly, maybe. Can I buy an operator-specific walk-on fare for the train like I can for Grand Central, like I can for Hull Trains? Is there an operator-specific walk on fare without a reservation or do I have to buy an interavailable fare? It’s a very simple question?

THE CHAIR: Do you want to say anything else, Russell?

FIRSTGROUP: I think I’ve been clear.

THE CHAIR: Right. Okay, I’m going to leave it at that point. Chris, do you have anything else?

ORR: So that concludes on Annex B. There’s a long way to go on other things like fares next, but those are the issues that we thought would warrant discussion on Annex B.

THE CHAIR: So is there anything else on that area that we just covered?

FIRSTGROUP: Going back to the previous session, sorry. I just missed making this point before. If the request to you is effectively to take into account a
10-minute reduction in journey time based upon some material not seen, then we would wish to have the opportunity to comment on that, because it’s not something that’s come up in the work that’s been done by CH2M and certainly not even flagged by SDG. So the request would be not to take that into account.

**ORR:** Just to be clear, are you asking about the extent to which we are thinking about what would happen with a faster journey time than option 15?

**FIRSTGROUP:** The request from Andy was, yes, to take into account a 10-minute reduction in journey time based upon some material apparently put together but not seen by anyone.

**THE CHAIR:** Just to be clear, are you referring to the specific piece of work that was made earlier by VTEC?

**FIRSTGROUP:** My understanding - it may be a misunderstanding - was that there was reference to some work done by Tony Crabtree, which was the basis of a 10-minute submission. But I may have misunderstood.

**THE CHAIR:** Let me just check. Is that material that is available to everybody?

**VTEC:** The report from Tony Crabtree we haven’t shared with other people. I think we’re prepared to do that. I’ll confirm after the meeting, but we’re prepared to do that.

**THE CHAIR:** That would address that. I wasn’t aware whether everyone had seen it or not.

**VTEC:** And we haven’t shared the 10-minute journey time reduction because we only did it yesterday, but we of course are prepared to do that once we’ve had a chance to refine it a bit more.

**THE CHAIR:** Right. That would address that point. That’s very helpful.

**FIRSTGROUP:** Well, being able to come back on it would address the point.

**THE CHAIR:** Yes. I’m sure you will.

**FIRSTGROUP:** So can I just clarify? I think what Chris said in terms of option 15; option 15 was testing a journey time that was a similar journey time between the operators.

**ORR:** We’ve looked at that. Perhaps, Chris, you’re the best qualified to answer.
CH2M HILL: I think it’s important for me to make the point that all of the options and base timetables have been discussed and agreed with ORR, and all of the options and base timetables have been shared twice with applicants: once in September and once in October. The option 15 timetable is based on the journey times that we felt were reasonable based on the base timetable that had been predicated upon. Is it possible for trains with those characteristics to achieve faster journey times? Well, clearly, yes, it is.

ORR: Just to say a bit more on that. So as Chris Judge just said it was based around the timetable in your application without the overtaking manoeuvre, so when we compared it to the VTEC timetable we did find that it was slower, accounting for differences in stopping patterns, by several minutes.

FIRSTGROUP: I think that everything that Chris has said is fine, because that accords with the correspondence that you had with us when you suggested that you would do this additional sensitivity.

THE CHAIR: Thank you.

DFT: I mean, can I clarify then? It sounds like from this discussion that it’s clear that - and sorry, I’m not a train planner, but I understand from those in the room that it’s clear that the FirstGroup journey times would be faster and much closer to the VTEC journey times. So are the ORR saying that is the basis on which it will undertake its assessment of the FirstGroup application? Because at the moment there is just a sensitivity test which I think we’re saying doesn’t even reflect the journey time that you think is most likely.

ORR: Okay. So I wouldn’t characterise it as the way you’ve put it there, in that I think there is inevitably some uncertainty about the precise journey times that will be delivered in practice. I think what we’re trying to understand is what are the impacts if the journey times differ from those that we’ve modelled? And we will have to take a view on whether those journey times have a significant impact on the modelling and the likely effects. We will have to take a view on what we think is most likely.

So I wouldn’t quite characterise it as that’s our central or base scenario. I think we’re just trying to understand the scenarios further. We need to take a view on what are the impacts and what we think are the likelihood of them. More complicated, I think, than what you set out.

DFT: I mean, I guess from our point of view we think, again, it’s critical that you take a decision on what’s the most likely scenario. We accept there will always be uncertainty. But the central case that you should
present should be what's most likely. It's not sufficient from our point of view that you have a sensitivity test to show the most likely scenario. You should always have that as your base.

THE CHAIR: I think on the basis of this discussion we will decide how best to present the information. I take that point, yes. But I go with the comments Chris has just made.

ALLIANCE: It's just one point, John. If I recall correctly at the 12 June hearing, Tim O'Toole said that FirstGroup were expecting four-hour journey times for these services between London and Edinburgh. I just thought that's quite a useful point, because I imagine that drives towards what they think the business will be.

FIRSTGROUP: I think we said that it was around four hours. I think that's what everybody has said. I appreciate the journey times you are proposing for your service are that much quicker because of the investment and the journey time and the speed of the trains which you want to achieve, but we said around four hours because that's the journey time that's there, that we understand from the timetables that you produced that is around the time - around four hours is the round number, which is what it is for VTEC's application is as well.

THE CHAIR: Okay. Thank you. I'm going to take one final point from David, and then after the coffee break if there's any other point anyone wants to come back on we'll do that.

VTEC: Just to conclude the point on the fares, I think it's clear that there is uncertainty as to what fare structure FirstGroup will offer, and particularly about the fare method as well, whether there will be operator-specific walk-on fares or not. I don't think we've established what FirstGroup's plans are. There is uncertainty. I think it's just important that ORR consider the possible options and take into account the uncertainty that clearly exists.

THE CHAIR: Okay. Thank you. At that point we're going to take a break for 15 minutes. So we'll come back in 15 minutes, and if there's any further issues that we didn't pick up already we'll just have a couple of minutes to do that. Thank you very much.

(The meeting adjourned at 11.33 a.m. until 11.49 a.m.)

THE CHAIR: We're just going to have two more minutes closing out the points from the discussion before the break before we move on to the fares overlay. I just wanted to clarify one point about further work that we're doing. Could I just hand over to Rob for one minute?
ORR: Thanks John. Yes, I think we’ve touched on this but it was quite a confusing discussion.

THE CHAIR: Yes, I think it was.

ORR: We talked about option 15 as modelled by CH2M in relation to the FirstGroup application. It removes an overtaking manoeuvre that people have highlighted as unrealistic in various ways. We have ourselves noted that option 15 still leaves the FirstGroup journey times significantly slower than the equivalent VTEC services and we couldn’t think of any good reason why that would be the outcome of the Network Rail process applying the decision criteria. So, on that basis we have already asked CH2M to model a further sensitivity, building on option 15, which speeds those trains up, to be the same as the equivalent VTEC services, taking account of calling patterns. So, that’s a further sensitivity, we’ve already asked to be done independent of the work that Andy mentioned has been done for VTEC by Tony Crabtree, which I think we’d still like to see, and it sounds like it’s going to be in the same vein. Our plan is to circulate details of the new sensitivity as soon as it’s ready – which will be within a week or two, I’m sure.

THE CHAIR: Just to clarify, there are therefore two pieces of work that will be circulated round. Okay. Thank you. There were still some points left from the session. Russell?

FIRSTGROUP: I’d just like to clarify – just because David mentioned it at the end in terms of the walk-up fare – I realise that whilst I thought was being clear about what we’re offering; it didn’t come across as clear. So, just to say that, well, it’s partly what Ian asked as well. So, Ian asked: ‘Can I walk into the station and buy a fare?’ As in a walk-up fare. Well, you can walk into the station and buy one of our fares on your phone, off your app, if there’s a seat available, you can buy that fare, but you cannot go into the ticket office and buy a dedicated walk-up fare. It’s the difference between “walking into” the station and a “walk up” fare – you can walk into the station if you’re there at 5.20 a.m. in the morning and there’s a seat available and you can buy a ticket, there will be a train you can get on. That is exactly our business, as we’ve just described it. We all think it’s going to be very successful.

THE CHAIR: Thank you, Russell. If there are no other points on that area I’m going to hand back over to Chris. We’re going to continue following through the structure that Chris set out at the start.

ORR: So we’re now on Annex C, the overlay. The CH2M forecast fares competition to have quite a significant impact on more than one of the
applications that we’re considering. And there have been a number of comments that have been made around the treatment of fares. We have spent a fair bit of time on this, and walked through some of the points, but in order to move the debate forward I’m going to ask Chris Judge to talk through the fares modelling in particular and the response to some of the points that have been made. Chris?

CH2M HILL: Yes, having reviewed the responses to our report, we thought it would be useful to clarify a couple of aspects of our modelling. Number one is how we have applied the passenger demand forecasting handbook to assess the impact of changes in fares. And number two is how we have modelled the response. We have used version 5.1 of the Passenger Demand Forecasting Handbook, ‘PDFH’ for short, which is the most recently available version. PDFH states that fares analysis should be conducted separately for individual market segments. We have followed this approach and the segmentation is shown in our report. The evidence used has derived the specific spread parameter contained within the logit function in Section B 11.4 of the PDFH, which is fairly old. We acknowledge this in our report but could find no good evidence to use an alternative figure.

PDFH states that the published conditional elasticities should be modified under certain circumstances. And there are three such circumstances that it lists. Number one is whether the change in fares exceeds 10%. For most segments in our model the change in fares is less than 10%. For a small number of segments, the change slightly exceeds 10% but based on the stated PDFH elasticity modifiers, adjusting these elasticities would have no meaningful change in revenue projections.

The second criteria where one might wish to modify elasticities is if fares differ from the national average. Based on the information we have access to, we could not find evidence to suggest that in the base case for any of our options, fares do differ or would differ from the national average. We have a problem here of a lack of data relating to the fares that would be offered in the future by the incumbent operator. We received a small number of sample fares from VTEC and statements around the dependency between managing loads and the availability of the most heavily discounted fares. We’ve asked VTEC to support that with more detailed future fares data and specifically from its recent bid model which we’ve thought would have been a good source of that data. And VTEC didn’t respond to the request. So, it made us have to make more of a judgement in terms of incumbent fares than we ideally would have liked to but that’s the situation.

The third statement in PDFH around modification of fares elasticities is if the GDP per capita, as a proxy for income, differs from the national average. We hadn’t perceived significant differences to the national average for the flow served and viewed adjustment of the
elasticities with respect to the GDP as a second order consideration versus the more fundamental uncertainties which we have referenced in our report.

So, that is a brief summary of how we applied the passenger demand forecasting handbook to assess fares. I haven’t mentioned yet the competitive response element. I think it would be needed to pick that up second.

THE CHAIR: Shall we pause there for one minute before we move on to the competitive response point? Does anybody want to comment at this point? There’ll be another chance later on, after the competitive response point.

SDG: I would like to make a point about the general modelling of fares, I think, before the competitive response point, if that’s ok?

THE CHAIR: Okay.

SDG: First of all, picking up on the elasticity modifier point you just made, Chris, about the average fare. Just reading the PDFH here I think you can read it either way, but, I think you could read it that actually it’s the average fare level compared to where they were in 2007, rather than where the average fare level is now. So, it might be worth considering that. It’s also a point we didn’t consider in our analysis. So I can’t actually push that too strongly but I think it’s worth flagging that may still be valid –

CH2M HILL: To clarify – we did consider that.

SDG: Fine. Generally though I’d like to make a fundamental point about how CH2M modelled the impact of undercutting fares. And that’s the way they’ve allocated it between operators. So, CH2M, as I understand their details in Appendix C, assumes that the demand growth that would occur, due to lower fares, from one operator will accrue to both operators in the market. To us, this just doesn’t follow common sense. If a person is attracted to the railway because of lower fares, that are only valid on some services, then, surely, those people will be travelling on those lower fares – and only on the services on which those lower fares are valid. They won’t be choosing to travel on the VTEC services, at fares that were already available in the base case. If they’re coming in because of the lower fare, naturally they should be travelling on those lowers fares. And I think the fact that CH2M has not assumed this is a fundamental flaw in their approach. I understand that CH2M have put two points in in support of this – what we consider an erroneous assumption. They suggest that the example in the PDFH Section B 11.4 supports them. I’ve had a look at this example and actually it doesn’t go on to allocate the demand growth from fare
reductions to the operator. So, we think this is a bit of a stretch to say it supports their assumption. CH2M also claimed that the fact that their assumption is the only one that returns no revenue change when the fare elasticity is minus one supports this position – for the economic theorists, CH2M have said in their report, if you have a fare elasticity of one for the whole market, then the change in demand for any fare change will be equally and oppositely met by the change in yield.

So, you’d have no change in total revenue. That’s noted in CH2M’s Appendix C as a footnote in support of their argument. And we think that shows a misunderstanding of the complexity of this market. There are actually a lot of sub-markets within each of the individual markets that they will have modelled. All have different price elasticities. By offering an undercutting fare product, you are trying to attract some of the people with a different price elasticity even within a market segment within that market and so you could – even with an overall average price elasticity of minus one – have an increase in revenue or a decrease in revenue, in fact, if you had too much leakage of people moving from the VTEC product to the cheaper product when the price before was the ideaFTPE.

I think most essentially it just fails the common sense test as I mentioned before. If people are travelling because of lower fares, we expect them to travel on the lower fares.

I think this then leads to CH2M making a further fundamental error because they’re not accurately allocating demand to the operator offering the undercutting fare, they’re underestimating the load factors FirstGroup would achieve. So, our own analysis has shown that if FirstGroup did offer a fare reduction of 40% or 50% under that of VTEC that they’d achieve load factors in excess of 140%. Now, these kind of load factors are just not believable and we’ve already talked about how these are higher density trains. Whether or not you could actually fit 140% of people with seating capacity on the trains physically is quite questionable. Moving on to the willingness of people to stand between London and Edinburgh – that is not likely on a long term basis. It might be on the Friday before the Edinburgh fringe or something but they’re not going to do it on a wet Tuesday in January.

And that takes me to the other point. And I think this one was made earlier – that there are natural variations in demand. So, if you’re going to get an 140% average overall load factor, that must mean some trains are full to the gunnels literally – people sitting three a deck, on each other’s laps because you’ll have naturally some trains that are at most 100% or even below, as we’ve had some discussion about before. And, as a commercial organisation, I think Chris made this point earlier, as a commercial organisation, if FirstGroup are facing those kind of load factors and that kind of demand, they’ll naturally increase their prices, and increase their revenue, rather than just send
people away.

So, overall we think that they would end up with a much reduced fare discount than they have proposed and by the fact that CH2M are incorrectly allocating the demand from fares growth they are not coming to the same conclusion as we are.

THE CHAIR: Ok, thank you. I’m going to ask Chris to come back on those points, and in particular the allocation points.

CH2M HILL: I can only answer the question in terms of the facts of what approach we have used. And the approach we have used is exactly as is stated in the Passenger Demand Forecasting Handbook and ORR can read it.

THE CHAIR: Okay. Well, let me bring a few people in. Do you want to go in to this?

ORR: I think it’s a challenge on the CH2M methodology so it probably would be useful if Systra comments.

SYSTRA: We looked at this point very carefully and we looked at PDFH, and in fact I was the editor of this part of PDFH anyway. It is clear, it says, that the estimate there is a market share. It is clearly calibrated for the market shares. It’s the standard approach to use from the logit choice model, which is of market shares and therefore it does apply to the market shares. And you have to be careful that the parameter in it is appropriate and it doesn’t have obscure effects, silly effects, which generate extra demand for say the incumbent operator. And that we checked through as well as the checks we did during the audit. We are confident this is the appropriate way of modelling on correct economic grounds and it’s the appropriate way as specified in PDFH.

SDG: So, you’re suggesting that – say there were two operators operating right now – one reduces their fare – that will lead to increased demand for the other operator?

SYSTRA: No, it doesn’t reduce the fare – it increases the overall demand – and the percentage of demand given to each operator is according to the formula in 11.4.

SDG: So, some of it would be allocated to VTEC, in that case, then?

SYSTRA: Implicitly, it’s the wrong way of thinking of it. There’s an increased benefit to the whole market –

SDG: – because of the lower fares that are only valid on one of the –

SYSTRA: – it’s standard modelling.
THE CHAIR: Okay, let me – if we pause on that one now. I just want to bring some other people in.

ALLIANCE: Well, perhaps some surprise that I wholly agree with DfT and Lucy Kavanagh on this point. I guess not on everything else but on this point – it seems to me that implicitly, even though this isn’t – perhaps John will argue not quite the way that it operates – this is a two stage process. The first stage is that the market gets reallocated between the operators so the lower fare operator gets a higher share of the market than they would have done just on the output from MOIRA and the second stage is that the market is grown and it seems not only that it doesn’t follow a rationality test to give some of that growth to the operator with the higher fare, but also you can quite easily – I’ve played around a little in spreadsheets to do this – demonstrate that what happens if you apply it to the – if you give the full growth, say 20% reduction, the full 20% reduction – to the lower fare operator, you do end up with elasticity of minus one with no change in the overall size of the market. I’m happy to share that little spreadsheet with ORR and indeed everybody else after this session.

THE CHAIR: Okay. Thank you.

CH2M HILL: May I respond?

THE CHAIR: Yes.

CH2M HILL: We can intellectualise all we like about what the PDFH does or doesn’t mean. The fact is that it is written in black and white on how to apply this particular methodology and we have to follow this in black and white. We could talk about examples where on average somebody between 12 weeks out and the day of departure would pay slightly less when the average fare’s reduced using any particular media like the Trainline, but I would contend that it’s a complete waste of time because we have used the PDFH to the letter and I just think if we could reflect on our previous testimony in June where several members of this panel in the round, have advocated that the PDFH is the industry best practice and something that we should not depart from. So, it just seems highly inconsistent to me that we are now saying that this is flawed and we shouldn’t be using it. We’ve used it exactly to the letter.

THE CHAIR: Okay. A few more points.

ORR: Yes. So, as Chris just alluded to, this is an issue that’s been in discussion a long time. It’s something we picked up before the hearing and talked to CH2M about. And a lot of people around the room
who've got a lot of experience in fares modelling know it's very difficult and there are often rather strange things happening, so we've talked about it. We have had plenty of time to think about whether it's the right approach and we've talked it through with CH2M and of course we've talked it through with the auditors, as well, and for the reasons that Chris and John have said, we've decided it's the best approach.

SYSTRA: Can I just add - of course, this formula, in PDFH, was specifically developed in the context I think of open access operations by MVA on behalf of ORR in 2009?

SDG: At much lower levels of fare discount than are being discussed here.

SYSTRA: Yes. At relatively low levels of fare discount – I should have said that.

THE CHAIR: Thank you. Let me just bring Bobby in.

VTEC: Just – we will have further points to make on this – but just coming back on some of the points that have already been made. First of all, we would contest some of the statements that CH2M have made about whether or not it would be appropriate, given the criteria CH2M have mentioned, whether or not it would be appropriate to apply elasticity modifiers in these circumstances. I don't have any evidence to hand but we can provide further evidence.

And the second point is that for the PDFH Chapter B, 11.4 methodology we have been discussing, my understanding is that the calibration of the spread parameter and it is specifically mentioned in that section – it applies to the walk-up fare differential. Therefore, it is not the spread parameter and the situation, it is not necessarily appropriate, and it casts uncertainty over the methodology, the fact that it is being applied now, in a sense where a lot of the fares being offered are advance purchase fares.

THE CHAIR: Ok, thank you. It's quite clear, there are quite a few differences of view here so can I just ask people: have you got any further additional points that haven't already been raised rather than simply repeating points?

ALLIANCE: Mine's quite a simple one, John, I think. I'm not a great lover of models, as Simon will probably tell you, because if modelling always gave you the answer, we wouldn't be sat here today because it would be very easy for you to run. But I think Chris said this, the PDFH, as well, is based on industry best practice, and I believe Simon when he tells me and John that that's probably the case. But we've heard today this is not industry practice. This is a completely new type of structure. The only time I can ever remember the railway having fully reservable trains is holiday trains in the southwest, when I used to work in the
southwest, but based upon quite expensive fares, at the time. Now, this is completely different. I cannot get on this train unless I’ve pre-booked it on the telephone, as I’ve been told – unless I’ve pre-booked it on the phone, I can’t get on the train. Now, you show me anywhere in PDFH based on BR and anything that’s happened since privatisation where what we’re talking about now has actually happened before. And that’s why I think I have to agree with what Lucy and Simon have said: this is just counter-intuitive. It just doesn’t make sense. If I have to ring up to get a ticket for £25, but can’t get that ticket for £25, and have to pay £150 to travel with someone else, then, how does that £25 become split up – it just doesn’t work. And if I have to pay £125, I’m not going to go, because I will have had to have booked it beforehand.

The other thing is – and I think this is a passenger point of view – I turn up at the last minute with an inter-available fare and every seat is sold on the 5.30 a.m. train in the morning, how do I get decent value for money on the basis that I’ve got to stand up? And I thought the whole idea of inter-availability – and one of things you dealt with some years ago with Platinum Trains – because they sponsored something very similar – is that you actually exclude a piece of the market, so it is quite important.

THE CHAIR: Ok, thank you.

VTEC: I’m going to find myself agreeing with Ian. I think Chris Judge himself, or CH2M themselves say in the report that this is a highly complex area to model – ‘stretching the frontiers of current forecasting research’ – and I think it’s been stretched to breaking point here. You can’t safely make a decision relying on PDFH applied perfectly (whether or not we can agree that it has been applied perfectly). But even if it has, if it’s produced some implausible results and we shouldn’t be looking at them. We’ll come back to this later but some of the results are way outside current industry experience.

THE CHAIR: Ok, on that, I think all those points have been quite clearly made so I think on that basis we should move on. Simon?

ALLIANCE: I think we’ve discussed this question of whether all the growth from lower fares should be applied to the operator who has the lower fares and I think there is clearly different points of view on that point, but I think we ought, more broadly, to recognise that the ORR has little ability to influence the level of fares that are actually charged, given that fares modelling is inevitably an area of risk in the overall assessment process. There are weaknesses apart from the point we’ve been discussing with the modelling framework that is available but given the limited role that the ORR has, I don’t think that those weaknesses are fatal. So, I don’t think we need to spend a lot of time
arguing about things like elasticity modifiers – although, it’s an
interesting technical discussion. What I do think are the two issues
that are of – well, I think there are three issues – a) it’s an area of risk
generally in your decision-making; secondly) who gets the benefit from
one operator charging lower fares, which we’ve discussed; and the
third, which we’re just going to go on to, is competitive response.

THE CHAIR: Ok, thank you. One final point on this. Simon?

DFT: I think, regardless of the PDFH issues, you need to step back and
think about this in terms of common sense. So, we’ve heard earlier
that the FirstGroup service is likely to have about the same journey
times as the VTEC service. FirstGroup say that they will have the
same types of trains with about the same seating configuration. So,
we can take them on their word on that. Load factors, once we get
into the 2020s, are expected to be very high on the East Coast, in any
scenario, and so the trains are likely to be very busy. So, if there’s a
lot of demand, you’ve got about the same journey times and about the
same trains, why wouldn’t you charge pretty much the same fares?
It’s just common sense. That would be their commercial incentive. If
they did charge much lower fares, their trains would obviously be very
busy, but why would they?

THE CHAIR: Ok. I think we have registered there, there’s a set of technical issues
and a set of what I think various people have called common sense
issues. So, I think we’ve all noted that. Can I move this on to the
competitive response point now? And then we’ll wrap up anything else
at the end.

CH2M HILL: And there’s a link between what we have just been discussing and the
competitive response point.

THE CHAIR: Yes, indeed.

CH2M HILL: I’d just like you to flag that our report acknowledges clearly the key
uncertainties in our work. And our view on those uncertainties is
driven by a number of things, including our knowledge of PDFH, our
knowledge of current yield management practices, discussions with
the independent auditor, discussions with stakeholders and also
stakeholders’ responses to our October 2015 methodology report.
And we have been clear to state that the key uncertainties are: not
having access to VTEC’s fares strategy for the future, the age of the
evidence used to derive the PDFH spread parameter, and the absence
of advice in PDFH on how to derive a competitive fares response.
We’re clear on that.

In terms of the competitive response itself, common sense
economic theory and evidence from a great many industries would
suggest that when one organisation is faced by a new entrant which reduces the price, the other organisation would seek to compete on price. Nevertheless, PDFH does not offer us explicit advice on how to develop a competitive response scenario and we have therefore developed our own scenarios. The report is clear that these scenarios do not come from PDFH. We have assumed that VTEC would seek to offer the empty seats on the services that operate immediately before and after a new entrant’s services for the same price as the new entrant. We recognise that this is an assumption so we conduct a sensitivity test where the discount offered is halved. And in our model, that’s the equivalent of offering the full discount on half the number of empty seats. That’s what we’ve done.

THE CHAIR: Okay.

ORR: In terms of one of the issues, I think Chris set out clearly there that what general evidence tells us about what happens when there is competition on the route, where there was less competition before. So, to try and turn this to some specific issues, we are more interested in the debate around the magnitude of competitive response rather than whether we think there is one or not. Against that background – the magnitude of competitive response – I think that some of the arguments VTEC have put forward on competitive response point towards the role of airline competition. I think it’s useful to be clear on that – is it correct to understand your position is that the strength of that competition with airlines is such that, before any entry, the VTEC / airline competition is sufficiently strong that the addition of additional rail services and the addition of more rivalry, won’t make a difference to your price – or a significant difference to your price? And is that airline competition sufficiently strong to mean that the additional capacity and the additional rivalry on rail will not cause a significant competitive response?

VTEC: Yes, I think that’s absolutely right at Edinburgh, between Edinburgh and London certainly. We are already competing with Ryan Air at £9.99. First Group at £25 is not going to make a lot of difference in that, in our pricing. And anyway, as we’ve just heard, the train’s going to be stuffed to the gunwales. We might as well just accept that we’re going to lose people and carry on as before because the main competition is Ryanair.

I think the other point to make about this is the Leigh Fisher report is very valuable evidence in this area. That has found no evidence, historically, of competitive response. Now, you might say that there must be some there and, yes. Maybe, maybe not. But the point is that if there was any there, it wasn’t big enough for it to be able to appear out of the statistical noise. So, it must have been relatively modest.
And most important of all, what they found is that even with whatever competitive response that has been there historically, the NPA ratio was still around the 0.3 threshold. Not these incredible numbers of 0.81 or 1.5 that are coming out of the CH2M analysis. So, whatever competitive response is there, is not making a significant difference to the NPA ratio.

ORR: So, let's take those in turn. I think your comments on airlines are quite clear. Am I right then – you’re saying that the entry by alternative services, those additional six services, every passenger that you lose, you will attract from the airline market without having to lower your fares?

VTEC: No, no. We would have a net loss of passengers but –

ORR: Net loss of passengers – I’m trying to understand. If your position is you’re competing ferociously with the airline market –

VTEC: Yes.

ORR: That also implies that a small change in your fares will attract passengers back from the airline market?

VTEC: Yes.

CH2M HILL: I had understood that the number of heavily discounted tickets that you currently offer on Anglo-Scottish services is constrained by overcrowding. So then I don’t understand how you can further compete with the airline market by lowering fares.

VTEC: What we do today, we monitor airline fares and that all goes into our revenue management software and we monitor that on a daily basis. So, we have fares at these levels that we’re talking about today and in a lot of these cases they’re not all sold. There are times of the day where we do have busy trains but that isn’t reflected in higher fares but across the piece, there are fares today at these levels and they’re not sold. So, to say that putting these fares in will attract more from the airlines is just – doesn’t feel right to us.

ORR: So, if I’m understanding you correctly, you’re saying that the entry by a competitor will mean that you have fewer passengers travelling?

VTEC: That’s right.

VTEC: Yes.

ORR: Why wouldn’t you then change your fare strategy and compete to
attract those back? Or a proportion of them back? So, you’re facing lower demand for your service – is your position that you’d maintain your fares and wouldn’t respond to that entry?

VTEC: Well, I think you’ve got to take into account the fact that we’re providing a set number of services a day within the market you’ve got a load of air services every day – there’s 48 air services. This was back in, at the end of 2014 – there were 48 air services per day between Edinburgh and London. You’ve got to ask yourselves, is five additional rail services going to make such a difference in the competitive market that either ourselves or indeed one of those airlines will change their pricing. You’ve got to ask a view on that. In my mind, five additional services out of a total of 75, 80 services a day, that’s not going to be significant. So, what I’m saying is: we will continue to face significant competition from the air services on that route – and they are essentially the price leaders in this market. And that is the case in the base case as well as the cases that you’re testing.

ORR: So, I guess what I’m trying to understand and trying to make sure is that we are being consistent in how we are understanding the nature of the competitive constraints in this market. So, what I’m hearing you say is you’re competing actively with the airline market.

VTEC: Correct.

ORR: So, if that is the case, that means that as you change your prices passengers will switch.

VTEC: Yes.

ORR: So, we then combine that thought with your own view you think you will be competing for passengers with any new service.

VTEC: Yes.

ORR: So, passengers would switch from your service to an alternative service?

VTEC: Yes.

ORR: Surely you would then adjust your fare strategy in response to that change and compete passengers back from both the new rail service and from the airline market?

VTEC: But it would be very marginal because the price setters in this market are the airlines and the competition that we would see in the market
from First Group would not significantly change the competitive tension that we already face and face in the base case with the airlines. So, the airlines do act as a constraint already. That was found by the CMA back in February last year. So, they do already provide significant competitive tension and they – because of the level of services that they provide, they lead on pricing on the route.

ORR: Okay.

VTEC: I think the issue is not: Can we win back passengers? The issue is: does it change the revenue maximising fare for VTEC? And I think that answer would be: Not a lot. Because airlines are the price setters.

THE CHAIR: I just want to see if anyone else wants to come in?

ALLIANCE: The impact may be marginal with, competing with the FirstGroup application, five relatively small trains a day. With the Alliance application, which is a much larger number of much larger trains, then one would expect the competitive response would be a much more significant impact on the market. One would expect there to be a much greater affect. And while I’d agree with the points that Chris Hemsley’s been making, that makes it rather strange that the one application where competitive response has not been modelled is in relation to the Alliance Edinburgh application, where what we have consistently said is that we believe that because the service is faster and very high quality it should be capable of attracting a fare premium. But we haven’t assumed that in our revenue forecasting and indeed CH2M Hill haven’t assumed it in their revenue forecasting. And the reason that we say that is because we believe in the real world there would be a competitive response from VTEC and therefore the net result will be that our fares will end up on average at around the current VTEC level. And their fares will end up significantly lower. And we do think that it’s a weakness in the work that’s been done to date that that hasn’t been taken into account.

THE CHAIR: Ok, thank you.

FIRSTGROUP: I was just going to make a point on the competitive response in general and a point, because Andy Sparkes referred to the Leigh Fisher Report – I think it’s just important that we are very clear about what the Leigh Fisher Report found – so, on page 18, it says: ‘This finding does not represent conclusive evidence there has not been a competitive response, merely that we have not identified conclusive evidence of one’. And the report, the primary objective of the report, wasn’t actually to evaluate historical yield and fares data, it wasn’t to determine whether there had been a competitive response. And that’s clear in the report. So, the report didn’t say: There isn’t a competitive
response and there hasn’t been one.

THE CHAIR: Can we give Chris Judge a chance to come back?

CH2M HILL: It was just a point of principle on the fares response on fares that we’ve modelled for Alliance and Edinburgh service. If the proposition is not to compete on fares, as we understood it, with the incumbent, then it’s not a thing we can model in terms of trying to assess what the incumbent competitive response on fares would be, by definition, there’s no fares competition. If you’re asking me to reflect on the advice the report gives to ORR, I think it would be reasonable for ORR, given the level of abstraction in this case, to reflect on what the impact might be on the income of the incumbent operator and how the service might develop on that basis.

THE CHAIR: I would like to bring a few more people in. Lucy?

SDG: Yes. I think we would agree with VTEC that there wasn’t any evidence found in the Leigh Fisher Report of competitive response and also that they’re constrained by the airline market. But even if there was some competitive response, as Andy Sparkes said, because the Leigh Fisher Report found that there was not conclusive evidence, it implies that if there is some competitive response in the market, it’s relatively small. We think that CH2M are probably overestimating the impact of competitive response in terms of price reduction because of the formula they’ve used to determine what the fare reduction might be on VTEC. So, CH2M seem to have made up a formula for this purpose. There’s not an industry standard approach. They’ve invented something. It’s not very well documented what they’ve invented. We’ve tried to puzzle through their Appendix C to work out what they’ve tried to do. Having puzzled through it and tried to work out what they might be trying to do, we think they’ve made two errors in this formula. One of which is the weighting. We’ve said that in our letter. But the other one is that they seem to consider total empty seats on the VTEC service. I think that’s what Chris said a bit earlier, whereas, surely, you should only consider the additional empty seats that are additionally empty because the service has competition? Because surely if in the base case it was in VTEC’s commercial interest to fill the empty seats on their service, they would be doing so, and pricing accordingly. You should only be considering the extra empty seats that are available because of the additional competition. Now, we’ve taken a simple example, as we haven’t got the exact numbers that CH2M have used. Correcting these two errors, and the most significant one is to consider all empty seats, would actually take the assumed VTEC fare reduction from 8.6% to 2.5%. So, it’s a significant difference to the fare reduction that would be assumed for VTEC and that’s even if you accept that the formula that CH2M have
created for this purpose is the correct one which, we haven’t actually
seen any evidence behind that; any evidence that would be the fare
that would be undertaken. So, I think that’s a key point. Even if there
is a competitive response we think the scale of it is being inaccurately
estimated. And I think Chris alluded that they’ve already done a
sensitivity of halving that. We have a concern – we’ve heard a lot of
sensitivities of things where the modelling probably isn’t quite right.
We’re reminded that actually the central case is a combination of these
sensitivities. And if you test each of them as an incremental
sensitivity, you’re not really reflecting where you actually should be in
totality. So I think that would be my point on that.

THE CHAIR: Okay. Thank you. Did you want to come back Chris?

CH2M HILL: We do, yes, please John. Given that the accusation is that there are
errors manifest in the report, I feel I probably should. And just as a
general point, the whole report has been verified by an independent
auditor. That applies to everything we’ve done. The report is clear
that PDFH did not offer advice on how to develop a competitive
response scenario. It is clear that they are our assumptions, based on
our own understanding of yield management practice and what would
be likely to happen or could be likely to happen in the advent of the
competition as it’s described in our report. We have reviewed
stakeholders’ responses on the issue and whilst we do not necessarily
agree with the approach that’s suggested, or the algebra that
underpins that approach, we have conducted some preliminary
investigations into the magnitude of the response using the suggested
approach, and the revenue impacts, to us, appear to be within the
range of the scenarios that we have presented in our report.

SDG: We wouldn’t even accept that the formula’s appropriate in the first
place.

CH2M HILL: So, your suggested approach I think is that the competitive response is
based on the total number of additional seats. So, we have also
checked using that approach. That’s what I’ve just described.

SDG: We were saying that what your formula seemed to be doing, there was
a fundamental error. I don’t think we were saying that was the
appropriate approach for estimating the fare reduction for VTEC. So, I
just wanted to make that clear.

THE CHAIR: Can I just ask on that point; did you want to come in at all John?

SYSTRA: Nothing much more to add to what Chris Judge has said. Yes, we
looked at this element of it. We recognise the extent of competitive
response is a judgment call to some extent. It was a reasonable
model but you can take alternative views which is why we’re comfortable – it’s important to do sensitivity tests and, yes, the ORR will need to take this decision on which is the central case to have it, in terms which it recommends to its Board.

THE CHAIR: Ok, thank you. John?

FIRSTGROUP: Yes, just a quick one really. So, the Leigh Fisher work was inconclusive around whether there was a competitive response or not. There is another study that’s listed in Leigh Fisher’s work that looks much more specifically at on-rail competition from 2009, commissioned by ORR. And that study looks at the relationship between competition in journey growth and yield growth and that concludes that Hull Trains and Grand Central – and there is evidence of passenger growth and slow yield growth. So, I think it’s clear when you look at all of the evidence of what’s happened historically that there has been competitive response from the introduction of open access services.

THE CHAIR: Okay, thank you.

VTEC: Yes, so, just coming back on competition. It’s clear from the CMA conclusions that there is effective competition today with the airlines. I’m just wondering –

ORR: Are you referring to the merger decision?

VTEC: Yes.

ORR: It is important to be quite clear what the legal basis for that merger decision is. It’s that there is no substantial lessening of competition. I went back and read the references. I don’t think they’ve said that there was effective competition. Not that they said that there’s ineffective competition, either.

VTEC: Okay.

ORR: So, I think the issue of how strong airline competition is still to play for. I don’t think the CMA is – it’s just not written in its answer for that analysis.

VTEC: So, on the basis that there is competition, I’d just like to understand: Does the model include some airline fares?

CH2M HILL: So, the model that we use in the air market overlay, which looks at fares competition between rail, and in terms of fares, we included a cost that’s a proxy for airline fares.
VTEC: And then in the context of the competitor response discussion, what assumption have you made in terms of the response that the airlines will make to FirstGroup’s cheaper fares?

CH2M HILL: ORR gave us some specific instructions on what to include on that airline competitive response and they’re documented with our report.

ORR: So, just to add to that, we looked at that issue and we saw, just as you talked about earlier, that there are lots and lots of airline services and their fares are – some of the fares are very much lower than being offered by rail and we thought it was reasonable that airlines would not lower their fares in response to the FirstGroup service.

THE CHAIR: I can see it’s going to be tricky to move this one on. I’ll bring in Andy first –

VTEC: Yes, we’ve talked a lot about whether or not there’ll be a competitive response and how to model it. I think we need to really look at the results that come out on competitive response because there’s this concept of negative abstraction that comes out in the report and makes a fundamental difference to the NPA ratio. I mean it’s just beyond comprehension. I can understand that there’ll be a bit of reduction of that abstraction from a competitive response but not a negative. It just doesn’t make sense.

And the other thing to say is that when you look at the difference between the different sensitivities that CH2M Hill run, what you get is effectively an implied demand elasticity to price of minus two, which is roughly double what you’d normally expect in our industry which suggests that the model has well and truly been taken beyond the bounds of what is possible to model accurately using PDFH because these numbers are incredible.

THE CHAIR: Right, we’re going to give Chris a chance to come back on that response and we’ll listen to Russell’s point and then I’m going to give Chris Hemsley a chance to make a final point. Then I am going to be moving on to the next section.

FIRSTGROUP: It’s a point relating to whether or not there’s scope for a competitive response. Obviously, time has moved on since the application. We put our application in a year ago. And actually during that time we’ve done some analysis and research on available information and having looked at the average fare over a four-month period – the same period following the franchise change with VTEC and today – so, during the same four-month period – the average fare of London to Edinburgh offered by VTEC had gone up by 7.5%. It’s gone up by 9% to Newcastle. So, the proposition that we had to start with is now that
much lower than VTEC’s is now. And we would argue that in fact provides scope for a competitive response from VTEC with its fares as it is now because its fares are now higher than they were before – without any competition.

THE CHAIR: Ok, thank you. Chris Judge, do you want to come back on Andy’s point?

CH2M HILL: I think the accusation was some kind of error, from Andy. We haven’t seen the base data that supports the calculations in VTEC’s response to ORR so we can't replicate the calculations but it looks to us as if it doesn’t follow the PDFH methodology and therefore we believe it has been completed in error but until we see the data that sits behind it, we can’t possibly comment on it.

VTEC: I don’t think I’m saying it’s an error. I’m saying that you’ve probably applied it perfectly right but maybe you’ve misclassified some of the demand. But the result is implausible so, whether or not it’s in error, it’s not credible. If it was credible, we would be out there in the market reducing our fares now. If we were a rational operator, we could compete with ourselves to bring the price down and have lots more lovely demand. And as a rational operator, that’s what we would do in the base case. And that should be taken into account of in the base case, not as part of the option.

CH2M HILL: Andy, you’ve previously stated to us that you can’t reduce your fares because you’re overcrowded. And, just, again, to make the same point, our elasticities are from PDFH inputs and outputs and our work has been independently audited. The methodology has been audited. The calculations have been audited.

THE CHAIR: Right, those points are similar to the ones we’ve had before of the modelling versus perceptions of the outcomes of the modelling. I’m going to stop us there. Are there any further points you’d like to make, Chris?

ORR: I think it’s just worth making one more point, because we’ve talked a lot about the modelling. I think it’s just a point that Simon made earlier that I think we need to step back here and make sure that people are giving us a consistent story about how they think competition works today and how competition will work post-entry. And I’m not quite sure that I’ve got that clear understanding in my head. I think it would be helpful if people could explain to us how they see the market operating today and the impact that entry have. I think it’s worth people being really clear think about what impact they think a new rail service will have on pricing, on passenger switching and also fares policies. My understanding is you have dynamic pricing – so if you lose passengers
in the airline sector, prices automatically fall. That’s what happens. So, I think it would be really helpful if you could explain in a narrative form how they see entry playing out in terms of effects, using that kind of competition language. We’ve got the modelling. I think we’ve got all the evidence on the modelling. I think we just want, in as plain English as possible, how you see that competition playing out.

THE CHAIR: Right. Okay. I apologise, I’m going to move on at that point. Just following through Chris’s earlier structure, we’ve now reached air competition.

ORR: Yes, on the air competition overlay I don’t think we have a particular need to talk about this any further. We’ve talked about the more general issue of air competition quite a lot already so I think there is more if it’s a specific issue that CH2M and Systra just pick up relating to the checks that have been carried out on the model itself.

THE CHAIR: So, this is in relation to specific questions that people have raised, wasn’t it?

ORR: Yes.

CH2M HILL: So, if you could give probably 20 seconds on the model itself and then invite Systra to comment on the checks that they made. So, the model uses an approach that’s recommended in the PDFH, which is commensurate with the available data to us. The logit model which is the approach uses reasonable component costs and parameter values. It’s calibrated using the CAA data and national passenger survey data. Nothing more to add than it was reviewed as part of our full modelling suite.

THE CHAIR: John?

SYSTRA: Just a short statement. Effectively, yes, the first stage of it is the journey time competition with air which uses the well-documented PDFH approach. Perhaps not as well-documented as it should be but it’s a PDFH-compliant approach. And, yes, we checked that thoroughly. The fares element isn’t in the PDFH and requires an alternative approach. We looked at the generalised cost logit choice model that CH2M developed. The whole approach seems sensible. We did not look at the individual data behind the calibration but we did look at the resulting parameter values and confirmed that they appear to be fair and time parameters that were consistent and the applied elasticities were plausible. And we have audited the model and its detailed processes.

THE CHAIR: Ok, thank you. Does anyone want to –
VTEC: Can I just ask, is there anything you've heard today that makes you want to go back and just think about your audit again?

SYSTRA: Are you specifically asking about the air competition overlay?

VTEC: I'm thinking about your audit report in general I suppose, as we're halfway through the section.

THE CHAIR: I think that would be an issue for us but I don't mind John giving a view.

SYSTRA: Well, it's clearly an issue for ORR if they want us to look at anything again. And if, I think it's actually an issue for CH2 whether they think that elements that they wish to change. And if they wish to change some elements, then we will look at what they change and say whether we agree with their change. And indeed, it's actually been a collaborative audit, so we might discuss it between ourselves. There's certainly, when we're talking about the air competition, there's nothing I've heard — well, we haven't heard anything really — which would make me want to change at all in that area.

THE CHAIR: Ok. Thank you. Any points in this area? Simon?

ALLIANCE: Not on the journey time issue. I think the way that has been modelled is not quite how I think we would suggest is ideal. But I think it's reasonable. In relation to fares, as we've been saying consistently since last June, there is a major issue of transparency here. None of the applicants except for FirstGroup who created the model in the first place have seen this model so there is a serious issue of transparency. And I think that's the point that both VTEC and DfT have made. And we just don't know whether it produces consistent results. An easy sensitivity test that could be done which would either increase confidence or not, depending on the result, would be to put into the generalised cost model that's been used for fare competition, for example, the journey time in the Alliance application, and see if it produced a similar change in the market. If it does, then we can be confident that the model works in a sensible way. If it doesn't, then it raises an issue that ought to be considered by everybody.

THE CHAIR: Ok, thank you. Do you want to come back?

CH2M HILL: Just a very brief response. The model's calibrated to current load shares.

ALLIANCE: Yes, but it doesn't necessarily have elasticity to generalised costs which are consistent with the PDFH curve.
CH2M HILL: The PDFH curve is, so, if we’re talking specifically about the fares element of the model, the PDFH curve is with respect to journey time and not with respect to fare.

ALLIANCE: Yes, I know but you’ve got a generalised, I’m sorry to – I’m just trying to get this clear – as I understand the model that you’ve used for fares competition in the airline market works on generalised costs. And what you do is, if you have an operator with a lower fare, you reduce the generalised cost by an appropriate amount and you see the effect that has on market shares in the market. Given it’s a generalised cost model, you could, equally well, reduce the generalised cost by the equivalent number of generalised cost minutes and see if that produces a similar change to what the PDFH curve does. If it does, fine. If it doesn’t, it raises questions about the model.

THE CHAIR: Shall we come back to that? Let’s have a think about that and come back to that. We’ll talk about that one afterwards. Let me bring, Russell, did you have a point to make?

FIRSTGROUP: Yes. All I was going to say about the air rail model is, yes, we’ve provided some information and we’ve provided that under a confidentiality agreement with CH2M and as we’ve just heard the report’s been independently audited in a collaborative way but it has been audited. If it’s helpful, clearly, and you would expect me to say this, and I would say this, the model that we had when we first produced it for our business case and our business model that we provided to the ORR is ours and it’s commercially confidential but we would have no issue with, if it’s helpful, with Systra, providing under an NDA, to review it as well. And CH2M Hill have got the same access so we’re assuming that as a result of the independent audit it has already had that treatment but we would be happy to provide it.

THE CHAIR: Let’s reflect on that then. I’d like to discuss that with colleagues, I think. Okay. Are there any other points on this overlay air competition?

VTEC: Yes, I think it’s important to note a number of technical concerns we have specifically with the fares part of this overlay. I understand what John said when he said that within the scope of the audit he has looked at the outputs, the model, he’s looked at the elasticities, and I think your words were that they appear ‘sensible’ or that they appear ‘plausible’. With logit models it’s important to bear in mind that appearing sensible and appearing plausible is no guarantee that it’s an effective model especially when it’s only been calibrated against two specific examples where there is also uncertainty about the GJT effect. Systra have been unable to verify the problem in the source data due
to confidentiality restrictions although that may also be an issue that
your point made but also we are concerned that the airfares that are
an input to the model are estimated from airline websites. That is not
an accurate way of calculating the average yield of airline fares.

Secondly, access and egress costs have not been included. The
times have, but access and egress costs have not been included.
Real car parking costs do not appear to be factored into account in the
model. No mention is made of quantifying an average trip length
which is an important determinant of overall car parking costs. And as
I have mentioned before, the model has only been calibrated based on
Newcastle and Edinburgh, and there is no mention of validation of the
approach being undertaken on other routes.

Now, the overall point I am trying to make is that with this logit
model, there will be a high degree of sensitivity to very small changes
in input and so therefore there is huge uncertainty, particularly given
these flaws, over the output.

THE CHAIR: Okay, thank you. I think we'll probably just have to register these
points now, at this stage, given the time. So, unless there's anything
else anybody wants to put on the record about that particular air
competition overlay, I was going to move us on to the next area which
will be the gravity model.

ORR: Okay, so the main issue in terms of the comments that we've made
around this area, relate particularly to the views on the suitability of the
gravity model. Again, there's lots of material that's been set out about
the detailed assumptions and again I'd urge you not to repeat those
here. They have been set out so we can pick that out then. But I think
it is worth making a couple of observations before we do take some
comments on the gravity model.

We have reviewed the arguments that have been set out on
the suitability of the gravity model as an approach. In principle, we find
these arguments more informative than debates around precisely what
WebTAG and PDFH say. This is all clearly set out. We don't need to
rehearse those arguments here today.

Further, I think it's useful to emphasise here that the real issue
as we see it is whether the gravity model adds anything to the
evidence base or not. I don't think anyone is arguing that the gravity
model is a perfect model. Neither are the alternatives. Rather, it has a
set of advantages and disadvantages, much like MOIRA does. And I
think all parties have set out their views on what those advantages and
disadvantages are. I think in the interests of time; we should focus our
questions around two things. One is I think it will be useful if people
have this view, to set out whether they think that the gravity model
adds nothing to the evidence base or whether it is right for me to
characterise the debate as around how much weight to place on it.

The second one, I think, is a debate around the specific
circumstances where the gravity model may perform less well. So, are there particular locations, particular circumstances, where we think that the gravity model might perform less well. Those are two areas where we could have a more fruitful discussion rather than rehearsing the debates that I think are all well set out previously.

THE CHAIR: Ok, thank you, Chris. Who anyone like to come back on those two questions?

FIRSTGROUP: I’ll just go first for a change. And this is in the context of the FirstGroup application rather than the other applications. So, the application of the gravity model is one way to approach the process problem. There are different demand models that could be used. And there’s also a very simple bit of analysis that could be used by anyone to assess the demand uplift, which is trip rate modelling. And we didn’t use a gravity model for Morpeth when we assessed the case for Morpeth but using the alternative approach to the gravity model and taking into account the catchment area and abstraction we came up with a very similar result to the gravity model that CH2M Hill produced. So, I think, in principle, we don’t have any objection to the application of the gravity model in the specific situation of a location like Morpeth.

THE CHAIR: Thank you. Simon?

ALLIANCE: I think the most important point is to recognise that PDFH doesn’t fully reflect the changes in the market that will occur when towns get a new through service to London or a radical enhancement to their service. Whether it’s a transformational change or new journey opportunities, PDFH explicitly isn’t applicable in those circumstances. It’s referenced several times in PDFH that it’s not really applicable where there’s more than a 20% change in generalised journey time. There are also debates around the effect of interchange and so on which have been considered at some length. Clearly, there are a number of ways that one can look at this. The gravity model is one. The station choice and growth model that John Segal developed in 2009 for ORR is another. There are other approaches that one could use. But, I think it’s important to emphasise that this should be a significant part of the decision making process. So, I think that answers the first part of Chris’s question.

In relation to the second half, I think we don’t have any particular concerns about the application of the model and the effects that it has and we agree with the point that in most cases the amount of overlap with existing services is relatively small and therefore the gravity model is a reasonable tool.

The one place where we don’t think that that is the case is Middlesbrough because Eaglescliffe, the existing Grand Central service at Eaglescliffe, and the proposed VTEC service at
Middlesbrough, are serving, effectively, the same catchment area. They’re both serving the Greater Middlesbrough / Redcar type area. Grand Central draws its demand at Eaglescliffe from across that area. VTEC will draw again from across that area. Clearly, Eaglescliffe will have a greater advantage in the immediate vicinity of Eaglescliffe. VTEC will have a greater advantage in the immediate vicinity of Middlesbrough. But given the nature of the highway network in practice the two are competing at the same catchment area. And in that circumstance, we think the gravity model isn’t appropriate – and trying to find hermetically sealed catchment areas doesn’t work well.

THE CHAIR: Thank you.

SDG: I was going to go on the general approach and I think you’re probably going to go into a bit of detail about areas of abstraction.

I think first of all we don’t consider that there is a need for something above PDFH. We’ve set that out. I won’t rehearse those arguments again, as you requested. But I do think it’s important to note that PDFH 5.1 has significantly higher GJT elasticities than previous versions of PDFH. So, the situation is different in the base case. The GJT elasticities are 50% higher so even if previously there could have been an argument around the gravity model we think that it’s in a different position now and in fact the recommendations in PDFH about whether you would need to have something separate for large changes in GJT also changed between those two versions. So, I just wanted to flag that.

We also have issues with the kind of form of the model chosen and how it works. So, effectively, the model is implicitly assuming that subject to population size and wage, the changes in the size of the number of journeys are related to the GJT we have between an Origin / Destination pair. I think this is conflating cause and effect because the rail industry has developed over a number of years the train service it offers and so operators will have put on good services with a low GJT to markets that are strong, where there’s a strong underlying demand that isn’t picked up in the three variables in the gravity model. So, I think there’s something underpinning that that really needs to be understood and I think it would be overstating the GJT elasticity because it’s not fully gathering that information together. So, it’s saying that – I’m sure VTEC will say this – that they put the best service on to their strongest markets, I assume? And others have done that historically.

THE CHAIR: Ok, thank you. Let’s bring Andy in.

VTEC: I think there are two issues here. One about where it’s appropriate to apply an additional model and secondly about what additional model to apply.
I think in all the situations we regard a gravity model as inappropriate because a gravity model cannot model the abstraction. It has to be an overlay to the gravity model as I understand it. I know CH2M have done some of that now since last summer but we still think it is woefully inadequate. If you look at our current demand for places like Leeds, it’s widespread across the entire area there that East Leeds Parkway would serve so we think that the abstraction is underestimated by more than a factor of two – at East Leeds Parkway, probably at some other stations.

I think Simon’s point about not applying an additional model, (I wouldn’t argue for a gravity model but an additional model) at Middlesbrough is slightly perverse. Eaglescliffe vs Middlesbrough is very similar to East Leeds Parkway vs Leeds. So, if it’s one, it’s got to be the other, surely. They are very similar – we don’t even know where East Leeds Parkway is going to be yet, of course, but they’re probably a very similar distance apart. They serve the same roles.

So, I think that’s the two points. One is never a gravity model but in some cases an additional model I’d accept but if you’re going to do it, Middlesbrough and East Leeds Parkway are similar, and they should be treated in the same way. And one thing that comes out of the gravity model is that Middlesbrough, which is a large city of about 130 to 140,000 people gets half the increase, uplift in demand, than Morpeth does, which is a small northern town of 14,000. Okay, with a big catchment area, but so has Middlesbrough.

THE CHAIR: Ok, thank you. Do you want to come back to all that, Chris?

CH2M HILL: I will respond, I will just try and raise new points rather than –

THE CHAIR: Yes.

CH2M HILL: So, in terms of the catchment area analysis, a couple of things, we based our analysis on true origin data of passengers provided by VTEC. So, for example, in the case of East Leeds Parkway, we have, I hope, a good understanding of where VTEC’s current passengers live, whether they access the network at Leeds or at York or some other location. We asked Grand Central for the same information specifically relating to Eaglescliffe and Grand Central said that they didn’t have that information available, so the assessment at Middlesbrough is necessarily based on a combination of catchment populations, drive times to Eaglescliffe and to Middlesbrough and also the implied catchment areas of stations of similar characteristics. So, we had to do that.

Just reflecting more generally on the gravity model, just to take a step back, we used this approach not just because PDFH says it is a legitimate approach to deal with this problem but also because other industry parties had used this approach previously. For example,
Network Rail in its 2010 addendum to the East Coast Main Line Route Utilisation Strategy used a gravity model to address similar types of problems. When we devised this approach we looked in the consultation responses to that and both DfT and Virgin Rail Group submitted a consultation response which was silent on the use of the gravity model. So, we naturally assumed that they would be fine with it this time around –

VTEC: Sorry. The Virgin Rail Group isn’t a party to this application.

CH2M HILL: At the time.

VTEC: Just to clarify, we’re not part of Virgin Rail Group.

CH2M HILL: Simply, the operator of the West Coast Main Line or the parent group of the West Coast Main Line franchisee at the time.

VTEC: Separate party.

CH2M HILL: Ok. Just so we get a feel for similar organisations. So, we felt it was a reasonable thing to do.

DFT: There was a reference to us there. Can I make clear that you can’t extrapolate from our silence in response to a Network Rail consultation about something else, years ago, what our view on gravity models is. I think that’s a completely ridiculous conclusion to draw.

Also, on the point about PDFH – I understand from Lucy this recommendation isn’t in line with PDFH, using gravity model isn’t in line with the likes of PDFH –

SDG: Yes.

DFT: And I think we need some consistency here on the previous point around fares modelling, you were suggesting you should use a PDFH model, even though it was transparently producing nonsensical results. But here we’re ignoring that PDFH recommends that we don’t use the gravity model. This seems quite inconsistent.

CH2M HILL: PDFH absolutely recommends it, that you use a gravity model in this context. It absolutely recommends that. I don’t see there’s much point in us having the argument because of our remit but even if you didn’t believe me as a former Deputy Chair of PDFH or John, who’s reviewed our work as an editor of PDFH – you can read it.

THE CHAIR: Ok, thanks. We’ll stop. I’ve noticed some very different views on what PDFH is saying among the people who are practitioners and indeed experts on PDFH so it’s clear there’s a very big difference of views on
that.

Just a little bit conscious of time. I know people have got a lot of things to say. Apologies. But, we are, you’ll be staggered to know now, running a bit behind schedule so what I’m going to suggest is that we stop for lunch now. We come back at 1.45 p.m., as previously set out, 1.45 p.m., we then continue doing the crowding model which we haven’t had time to finish yet. And then carry on as before.

The meeting adjourned at 1.08 p.m. until 1.45 p.m.

THE CHAIR: So, we had one bit of unfinished business from the pre-lunch session that we’re now going to pick up on which was the crowding model. We’re going to do this in two parts. We’ll do the forecast crowding impacts associated with some of VTEC’s proposed services. And talk about the implications of the FirstGroup business model for crowding. And I think for the first one, we’re going to hand straight over to Chris Judge, aren’t we? And then we will come to Chris Hemsley for the second one.

CH2M HILL: So, reflecting on a number of the responses received by stakeholders, there have been questions raised as to why in our assessment some of VTEC’s smaller service enhancements have fairly large crowding impacts relative to the scale of the revenue impact as given by the options. This is specifically in relation to options 4, 5 and 6 which have all been modelled as increments of VTEC’s core timetables. So, in our modelling suite, positive crowding impacts have been shown to occur where the timetable changes have encouraged passengers to switch to less crowded trains. And negative crowding impacts have occurred where timetable changes have caused train loads to be less well distributed than previously. For all three options, whilst the level of revenue from overcrowding is significant in terms of the forecast revenue generation for the option, the impact is small in terms of VTEC’s overall revenue.

I’d just like to state that the crowding model we have used to develop this assessment is an off the shelf crowding model that’s been used in a number of different industry applications before. It’s been audited on a number of occasions before. I also point out that our report is clear, that our terms of reference to ORR do not include timetable validation. And we go on to state in our report that our assessment does not capture the benefits of network optimisation fully. We also state that whilst this is true of all options, it’s most likely to affect some of the VTEC options which are significant changes to the current timetable.

THE CHAIR: Ok? Thank you. Did anybody want to come in on any of those points? Andy?
VTEC: I think our main concern is the Middlesbrough option which we specifically designed – well, it was really a 50 / 50 in the business case. Part of it was to solve crowding problems that we had in our core, part of it was to serve Middlesbrough. And we’ve actually specifically designed the service to bring in five extra train sets; three of which are basically used to serve Middlesbrough and the other two of which are to strengthen services elsewhere. So, the idea that that can make crowding worse is, well, incredible to us. And I think it must be somehow we’ve found our train sets being mis-allocated in the CH2M crowding model. That is maybe our fault, maybe not. I don’t know but the results do seem incredible.


CH2M HILL: We have investigated this; we didn’t detect much of a crowding problem on Leeds services. We actually felt that the stock allocation that we modelled – your stock allocation is pretty good for introduction of the Middlesbrough service, we detected problems, some problems with moving station calls between services at York and Peterborough. I think it is, reflecting on the advice we’ve given to ORR in our report, I think it possibly is likely that a franchise operator with the ability to switch calls could solve this in the future. So, perhaps our advice should have gone a little further and said to ORR maybe you wish to consider a scenario where there isn’t a crowding dis-benefit in the Middlesbrough option, given what I’ve just said. But, the model itself seems to be working perfectly well.

DFT: Again, I think our general point to ORR is we can’t understand how this result has occurred and without looking into CH2M Hill’s model, which we don’t have the option of doing, it’s not possible for us to verify. But, again, we just have to think: is it credible? Is it credible that you run additional trains and put on additional rolling stock and therefore crowding gets worse? Clearly, it isn’t. Clearly, something is wrong. We can’t verify what it is but clearly the result as produced is incredible. It could be a problem with the model. It could be that the rolling stock allocation that’s been tested isn’t appropriate because the franchise operator has the option of running some five car IEPs, some nine cars, some five plus five – so, yes, lots of different things can be done. It can change its stopping patterns. So, either there’s a problem with the model or there’s a problem with the rolling stock allocations, or with stopping patterns, that the franchise operator clearly would change. So, as presented, the results for this model are clearly not credible or representative.

ALLIANCE: Can I just quickly come in on that? I haven’t got the facts and figures in front of me but as I recall the Middlesbrough option depends on changes to stopping patterns to Edinburgh. Is that correct?
CH2M HILL: That’s correct.

ALLIANCE: Yes. So, is that not where the crowding impacts have come? It’s not so much directly on the Middlesbrough service, although there may be additional factors coming from Middlesbrough. It’s the way that those stopping patterns will – and the fact that you’re using the Middlesbrough option to actually speed up the Edinburgh service.

VTEC: I think that is possibly how it’s come about in the modelling. The point is if we’ve got more rolling stock on the table in general, even if the initial application of it turns out to have slightly more crowding, we’d have more rolling stock available to resolve it very quickly and make sure that crowding was less than the previous option. You never know exactly how it’s going to land when you introduce a new timetable but having more rolling stock there to enable you to relieve crowding is a good thing, not a bad thing.

ALLIANCE: That option depends on using loco-hauled coaches.

CH2M HILL: In the context of CH2M’s work, I think I’ve just agreed with Andy here, having viewed the responses, we think it is probably reasonable that a franchise operator will be able to sort this out from redistributing either with rolling stock across a day or its stock capacity across the day. So, I’ve responded to that.

DFT: Sorry. Can I add to that?

THE CHAIR: Yes.

DFT: That means that results you’re currently reporting for this option aren’t representative and so shouldn’t be the basis of any consideration of that option.

THE CHAIR: Thank you. I think we should move on. Can we just go over to FirstGroup now?

ORR: First has set out its business proposition that they have in terms of the relationship between your model for booking seats, and not having significant people standing. I think that does affect how we view crowding dis-benefits in that some of the effects, such as the stress that you won’t get a seat, those affects wouldn’t likely be seen in the same order of magnitude, given the majority of passengers have a seat reservation.

So, that’s really the only thing we have to talk about because we’ve talked about the substance of what you’re offering. So unless anybody’s got anything to say?
THE CHAIR: I feel that we’ve gone through that in quite a bit of detail. I was hoping prior to lunch that we wouldn’t need to do this anymore. Is everyone happy with that? Okay. Shall we move on now – so, we’re back on now the post-lunch agenda which was the specific impacts on parties. And one of the things we just wanted to go through here was the impact on the Secretary of State of some of the options. And indeed DfT circulated some numbers two days ago I think on this. There have already been some responses. Can I invite DfT just to summarise your issues and concerns around the impact on the Secretary of State?

DfT: Ok. We circulated the numbers. Clearly, the impacts of the options on the Secretary of State depend on what scenarios are assumed for both what the open access service is and then what VTEC can still run. So, the results will be very sensitive to that. And I think we would repeat the offer we made to ORR in the past, that if there are specific other scenarios they would like us to test, then we can do that.

The scenarios we’re presenting here were those modelled in the SDG appraisal which in turn was selected to be consistent with what ORR told us that CH2M Hill was going to model so that’s how we’ve selected these scenarios. But if you tell us there are other things you’d like us to model we can test that.

So, in all cases we’ve assumed that VTEC can still run the accelerated 2014 timetable, which we refer to as the 2014 speeds timetable. That, as per what we understood that CH2M were assuming, in those scenarios, the financial impact on the Secretary of State measured over the remainder of the VTEC terms, so that’s between May 2020 and March 2023, and then up until 2033, the average per year real impact on the Secretary of State for the Alliance Edinburgh option was £132 million and that’s comparing against the 2014 timetable. Once you take into account that if this stops VTEC operating the six times an hour core timetable, the impact increases to £183 million per year. For the Alliance West Yorkshire / Cleethorpes service, the impacts respectively are £64 and £115 million per year. And for the FirstGroup Edinburgh services the impacts are respectively £52 and £103 million per year.

We’ve heard from Network Rail that – well, we heard from the capacity discussion at the start – that additional capacity might only be available from May 2021 onwards and not May 2020, as we’d heard. That was new information to us in this meeting. If the additional capacity and the open access services started in 2021, as opposed to 2020, the per year impacts would be on the Secretary of State would be slightly bigger. That is because during the franchise term, the financial impact is shared between the Department and the franchisee, whereas from the end of the term, in 2023, potentially less than two years after the additional services had started, obviously, the entire
impact would be borne by the Department. I think it’s important to take into account also that these estimates do not take into account the full potential impact on the Secretary of State.

That impact reflects the premium that we can obtain from other franchise competitions, we think it’s very likely that bidders for other long distance franchises would take into account if these highly abstractive open access applications were granted. And that would further damage the Department’s financial position.

It’s also important to emphasise that all of this would occur in an already challenging fiscal environment. DfT has to make some savings in its resource budget of 37% over the current spending review term. The spending review settlement is not set for the subsequent years as yet but it would appear unlikely at this stage that there will be a substantial increase in the budget available.

The savings to our resource budget have largely been accommodated on the basis of being able to make reasonable assumptions based on what’s happened so far on the returns we can get from future rail franchise competitions which we think would be further at risk if these applications were granted.

I think we would also highlight that DfT’s contribution to overall reducing the country’s deficit means that it has relatively little flexibility to manage risks which might crystallise and the options to manage those risks may have to include cuts to non-committed elements of transport spending. The Department is likely to have to absorb a number of other financial risks, including those arising from delays and budget over runs on the Great Western Electrification Programme and consequent impacts on the Great Western and other franchises. So, those will already be testing DfT’s ability to manage risks within its budget. So, this would be a significant additional impact on the Department which it has very limited scope to absorb.

THE CHAIR: Thank you. Does anybody want to comment?

FIRSTGROUP: I think I was a bit surprised that we were having a rehearsal of the email that was sent out yesterday given the comments that had been made previously about not going over ground that has already been established. But, fair enough. So that would mean that I would then reiterate the email that I sent yesterday in response to it. And I’m sure Ian is going to reiterate the points he made on his email that he responded with yesterday. So, conscious of saving time, I’m not going to rehearse all of those points but suffice to say, the analysis as presented, as we understand it, because it’s quite limited because it’s just an email with a table and a few words, seems to suggest that these are all scenarios where the SoSRA is triggered. Well, in the cases that have been discussed, and the capacity that’s been talked about, that we talked about this morning, the SoSRA is only triggered if there are less than six paths.
DFT: Can I correct that? Because as I’m sure Russell is aware, that isn’t true. The SoSRA is triggered if the franchisee cannot operate two trains per hour to Edinburgh and three trains per hour to Newcastle. Even if it is possible for the franchisee to operate six trains per hour into Kings Cross, the SoSRA is quite likely to be triggered. ORR made a point this morning on capacity, that there were potentially two and a half paths an hour to Edinburgh. That was news to us and we hadn’t taken into account because we were working on the basis as we understood from Network Rail’s previous capacity analysis, there were two paths an hour to Edinburgh. But I think just to make the point — that’s not what triggers the SoSRA.

Also, I think the SoSRA is almost entirely irrelevant actually. The SoSRA applies to the current franchisee period, which covers less than two years of the period in which these open access services would operate. So, the allocation of revenue risk during that term, during that two years, may be slightly different depending on exactly what operates. But really, the vast bulk of the financial impact on the Secretary of State is beyond the current franchise term.

THE CHAIR: So, you say in terms of a future franchise value?

DFT: Yes.

FIRSTGROUP: So, John could I respond to that?

THE CHAIR: Yes.

FIRSTGROUP: It would be helpful, Simon, if the information, when it’s circulated, is very clearly articulated as to what it is you’re circulating. That very brief email did not allude to all of that information.

And a couple of other points. Firstly, on the point around, you said it was ‘consistent with the SDG’ or with the SDG report. It said that there was seven and half paths not eight. So, that isn’t consistent.

DFT: No. It was consistent with the scenarios that were modelled in the SDG report which are in turn consistent with the scenarios that were modelled by CH2M.

FIRSTGROUP: Okay. But, in your letters you’ve referred to seven and a half paths, not eight. So, it is a relevant point because in certain circumstances you could have a situation where the capacity is shared across routes. We could have a number of scenarios where there are six trains, including three to Newcastle and two to Edinburgh, and then there’s another Edinburgh service and there’s other services to West Yorkshire. It depends entirely on what you’re looking at. So, I think just to present that small information is not particularly helpful.
And then to go back on your – I don’t think I’ll dwell too much on the other points that you’ve made in terms of – I’m trying to think of the better words to describe this – the way in which you’ve said that there are potential future implications on funding of the railway. I’m not entirely sure of the relevance of that in this situation particularly given that the previous reports that have been produced have demonstrated that when open access operates, there has been an increase in the service which generates overall economic benefit. But, suffice to say, as a bidder, because I think as most people understand, FirstGroup has more than just open access, we’re bidding for franchises, we’ve recently won one. We continue to bid in and we assess when we’re bidding who is there. I don’t think as a result of having open access applications approved of one group or another group, that’s going to materially change what we do in terms of our response to the bid. So I’m surprised about that.

THE CHAIR: Ok, thank you. Can I bring in Ian?

ALLIANCE: Thanks John. It is rather incredulous to believe that the impact on the Secretary of State would be more than the total amount of revenue that’s generated by a new service group. So, as I asked Enrico in my email, sending it back, it would be quite nice to see some background work on that. In particular, how, now the SoSRA’s not important, despite the fact it’s been very important until today. Looks like VTEC’s problem, it’s nobody else’s.

The issue in relation to impacts into the next franchise, the email that came also suggested there was an impact from 2020. That may have moved to 2021. Now, bearing in mind that, as you said, there’s probably no impact on the SoSRA, that’s clearly incorrect, so I don’t know why we’re being misled in that way because there cannot be any impact on the Secretary of State if the SoSRA’s not impacted, and indeed, even if it was, it was potentially for a couple of years.

Simon also referred to the fact that there’d be a threat to bidding. Well, I would have thought anybody bidding for the East Coast Main Line and our colleagues at FirstGroup did bid for the East Coast Main Line, if you’re ever going to be threatened, this was the time. Our applications have been there for two years, to run a very fast Edinburgh service and to run additional services into West Yorkshire and Cleethorpes. It didn’t seem to put off the bidders. The ones that seem to put off the bidders are the ones where maybe it’s tightly constrained and so Southwest trains, I understand, you’ve only got two bidders. But, there’s no evidence that on long distance high speed that there’s any reduction in appetite for people to try and seek to run these services.

In relation to the costs and I wasn’t aware that we were partly responsible for potentially putting a threat to the whole economy, then, as Jonathan’s pointed out earlier today, there have been ample
opportunity and offers for open access operators to get more involved in funding the network but DfT have taken every opportunity to prevent that from happening. And I can only put that down to the fact that you don’t like the implications that open access responds only to its passengers and doesn’t have to respond to the DfT and in effect this continual targeting of the best operators on the network doesn’t do the DfT any favours in relation to what we’re talking about.

So, overall, as I said in my email, the figures are fanciful; there’s nothing behind it. I mean most of the figures for our supposed revenue are included in the public domain from Chris’s report, by CH2M. So, it is, and you’ve used the word yourself, before, when we’ve talked about the report: it’s incredulous to believe that the impact on the Secretary of State could be significantly many times more than the total revenue earned by an open access operator because that just doesn’t make any sense because every piece of evidence you have – and again, Russell has mentioned it – is that open access operators drive up, and competition drives up usage of the network. And even though I don’t believe there’s no competitive response and that there’s no evidence of any competitive response, we know that there clearly is. And so passengers benefit, as well as many others.

And it is quite intriguing that for all the downsides that you show about open access operators, that VTEC’s application actually seeks to replicate the markets created by those open access operators at Sunderland, Teesside and West Yorkshire; markets that you’ve ignored in the past. And markets that now you seem to be suggesting will do nothing other than drive down the value of the entire business. Because, surely, if it’s the same for an open access operator, running those services, the same must actually be said of the franchise operator running those services.

So, it really is, as you’ve said before, a stretch of the imagination too far to believe what you’ve said. There is not one shred of evidence that you can produce that would back that up. And as a final note, if you go back, historically, to where we were in 2005, when the ORR determined that applications for the East Coast at that time, there were about 130 paths. If Grand Central and Hull Trains had not challenged Railtrack and Network Rail at the time on its ability to use infrastructure wisely, we’d be talking here about use of the sixth path, not the eighth path. And so you need to give some value to what open access manages to do in relation to the infrastructure provided. And that’s been highlighted by the CMA, and it’s something that you need to take into account. This constant badgering with nonsense figures into the public domain doesn’t do the DfT any justice. And it needs to sit back a little bit and think about the benefits that open access has brought and stop trying to protect its position with unrealistic assumptions, because that’s all they are.
THE CHAIR: Ok. Thank you. Did you want to come back on any of those points, Simon? What I was going to say, just as a general point, if one of the things that come out, I think if there’s any more detail about any of the assumptions underneath the figures, people will clearly find that helpful.

DFT: I’m sure we could do that but then similarly, I would say to ORR, it could ask its consultants, CH2M, to estimate the financial impacts on the Secretary of State of the different scenarios it has tested. CH2M Hill’s report doesn’t report that. I would have thought they would have very easily been able to calculate it. I think one of the concerns that we’ve raised about CH2M Hill’s report is it doesn’t present its results in terms of benefit to cost ratios, which would be the normal way of presenting the results of an economic appraisal. We’ve had to present these numbers partly because ORR and its consultants have not done so.

I’m slightly struggling on what Alliance have said because I didn’t really get a clear question there for me to respond to, just complaining about the fact that the Department is concerned about the financial impact of open access services. Well, of course we are. I note again Alliance saying that they’re happy to contribute towards the cost of the network but really the current charging structure is a matter for ORR. DfT has commented many times on the current structure of access charges and its concern about the fact that open access operators both don’t pay anything towards the fixed cost of the network and receive very substantially discounted rates of capacity charge which is a really significant charge on the East Coast Main Line. But, these decisions have been a matter for ORR, not a matter for the DfT.

THE CHAIR: Thank you.

SDG: Just on a point of detail -

THE CHAIR: Yes. Lucy then –

SDG: I think both the last people mentioned, have been in agreement, there’s eight paths. Am I understanding what you said at the beginning was there were definitely, probably, seven and a half, but there was significant doubt about eight?

ORR: No, that’s not what I said.


ORR: There were various constraints and if each of those were met, then we could see a total of eight paths being allocatable. But we said that in allocating the final half, over and above seven and a half, we’d need to
be satisfied on issues such as connectivity.

SDG: Yes. Thank you.

THE CHAIR: Yes. Chris?

FIRSTGROUP: Thank you. Two points of principle. One in relation to the position during franchise. And the second, after franchise.

In terms of the integrity of the bidding process, which is effectively one of the submissions, obviously what happens in a bid process is that tenderers are asked to bid a certain amount of premium for a certain amount of capacity against certain defined risks, one of which is open access risk.

In terms of equality of process, if what is being then said is that to deliver that same amount of premium, one has to take a different view of the risk or that it then requires a different amount of capacity, that is essentially fundamental and affects the equality of the bid process. So that, in our submission, should be taken into account when looking at the respective submissions.

In terms of the position post-franchise, we touched on this at the hearing in June. The starting point on arguments on impact after 2023 assumes franchise ownership of all available rights. That June exchange involved a helpful confirmation given by the Department: that it wasn’t their submission that there was effectively ‘total ownership’ to take as the starting point and as a basis for impact.

THE CHAIR: Thank you. Jonathan?

ALLIANCE: Just picking up on some of the points that Simon has made. Note that DfT is trying to make savings; has got issues over resourcing its budget; it’s got a tight fiscal budget; where we are is we wanted to contribute to that and we keep saying this to DfT and unfortunately DfT doesn’t take us up on the offer. So, on the one hand it sits there whinging about impact on Secretary of State’s funds but on the other hand it isn’t actually trying to resolve the issue. So, there is a pot of money here that can reduce that impact on the Secretary of State’s funds. We’d like to ask the DfT if their willing to engage in constructive dialogue on that? That’s one issue –

DFT: I need to say again, the charging structure is a matter for the ORR, it’s not a matter for DfT –

THE CHAIR: Jonathan, is that the point you’re making, or are you saying it’s outside the charging structure?

ALLIANCE: Absolutely.

ALLIANCE: This is not just about the charging structure and we do want to engage with the DfT constructively. We did try and do this over two years ago. And we did have some good dialogue. We want to take it further. We want to reduce the burden on the taxpayer but you just sit there, using taxpayers’ funds, saying that you’re going to get the taxpayer to enter in to a SoSRA, why you’ve done that, I do not know, because the Public Accounts Committee criticised the DfT in respect of using taxpayers’ funds for the IEP. That is a fact because – you can shake your head as much as you want. One of the issues you’ve mentioned about fixed access charges, you say that to develop an access doesn’t make a contribution there. That is true. But that’s the making of the DfT who pays subsidy and a court decided in 2005 that it would be illegal for us to pay that – for open access to pay the subsidy which you require through the fixed access charges. That is the law. It’s the DfT’s making. You continue to pay that subsidy. It’s not the ORR. It’s the DfT.

And then there’s the issue about the levy which we keep raising, which is Directive 2012/34. And this relates to how anybody can contribute to the provision of public service obligations and we’d like to do that but, again, we’ve approached the DfT, and it’s missed the boat. So, I just want to know why the DfT doesn’t want third party open access businesses contributing to the financing of the network to reduce the impact on the taxpayer?

THE CHAIR: I’ll ask DfT in a minute if they want to come back, but just on that, we just have to hold that for a minute, while I just bring Andy in.

VTEC: Yes. I think firstly, just talk about the numbers from DfT and just to reiterate that once you adjust for the fact that the DfT numbers are in mid-2020 price and demand levels and all the other numbers we’ve talked about have been at current demand price levels and demand levels, we get very similar numbers to the DfT and I’m happy to share those with you. We have shared most of them with you and with some tweaks we will share those with the wider audience. We support those as being of the right order of magnitude. And that is obviously a large number, even in current money, we’re talking about the best part of £50 million being taken out of the franchise per year for the least abstractive option on revenue. If you go back to Leigh Fisher – it’s a range – but it suggests somewhere in the mid-40s as being taken out, by all the current open access on the East Coast Main Line. So, what we’re talking about is the least damaging, of the current application as being more than everything put together so far, which is a major step to contemplate.

THE CHAIR: Ok, thank you. Unless DfT particularly want to come back anymore,
I’m assuming we’ve heard each other’s view and we’ve noted those?

HULL TRAINS: It’s very rare - I’m actually going to be supporting some things that the DfT have said but you might gather that there’s going to be a catch. The issue of funds, as far as the DfT are concerned, I am involved with them on the Great Western issue at the moment and the potential downside to the DfT, to the whole rail budget, are considerable. But in terms of letting a franchise, especially on an inter-city franchise, it can’t be right that your business assumption is there is no, or very little, open access competition. Certainly on the other side of the table, when you’re bidding, it’s something that is very, very big in terms of what you put in as your risk premium for open access. If the DfT because of its financial situation is forced to actually go down the route of assuming that so much of its revenue has to come from its franchised operator and therefore it must assume that there is hardly anything that goes off to an open access operator, I actually think that’s a bad place to be because every main line in this country, as soon as you put capacity on it, will attract open access interest. And as far as open access operators not paying their fixed charge, I sat through five days of court hearing to discuss all of this. We pay what we’re legally obliged to pay. We pay the same rate, the same suite of charges as the franchised operators pay, except for one thing – which is the franchise fixed track access charge which is a pass-through from government to Network Rail to satisfy the residual funding requirement of the infrastructure provider. It is an artificial construct. Currently, we pay a capacity charge set by the regulator in the last control period which is a mark-up on our current operations in terms of EU law. We're quite happy to do that at a price that the market can afford and it doesn’t price us off the network, which is, again, the legal position. In the forthcoming Control Period, we fully expect that the fixed track access charge will be fully extinguished and it will be up to operators to pay a mark-up on their existing operations. And we expect to pay that. In fact, that is what I said with Adrian Campbell and Brian Kogan in this very building, a few years ago – that I want to pay the exact same money as Adrian’s trains to go between London and Doncaster per path. And that’s the way that this railway should operate and we should be looking at alternative ways of providing services through whatever mechanism is being explained that do not get you into the situation where you are forced to have to maximise the entire value of an investment through a franchise mechanism because that’s the root of our problems. And please, you have to tie investment up with your track access applications so that we don’t spend all of the money coming around the table every time we have an inter-city franchise award.

THE CHAIR: Ok, thank you. I think there’s a limit to how far we can go on some of those points about structure, given what we are here to discuss today.
So, I’m going to call a halt. My apologies. As we were talking there just about open access in general, I did want to talk a bit about the impact of the applications on current open access operators and whether any of the current open access operator wanted to make any points because of the impacts on them because it has come out of some of the work that we’ve seen?

GRAND CENTRAL: Yes, there are some scenarios that may come out of the applications that have been submitted that would be pretty devastating for Grand Central as an existing successful open access operator on the network. And, at the current levels, I would go as far as to say that it would have a significant impact on our solvency. It has a wider impact as well as on the Grand Central business because obviously the markets that we’ve developed and the flows that we now serve and operate have generated a lot of jobs and wealth for the local economy which would also be affected by the lack of a local access service directly into the heart of that community. I think it’s fair to say that competition has been very successful in the East Coast Main Line and if there was a decision made that would create a backwards step for competition and for open access on the East Coast Main Line that’s an undesirable outcome, that I don’t think anybody is particularly looking for. The CH2M Hill report acknowledges the fact that it would have a significant impact on open access operators and we obviously agree with that and we don’t want to be in a position where there’s an adverse outcome from this determination.

THE CHAIR: So, you agree with the financial impacts as set out in the CH2M Hill report?

GRAND CENTRAL: We think they’re conservative but even at the modelled levels that that would make continuing to operate our current services very, very challenging.

THE CHAIR: Ok, thank you.

HULL TRAINS: Yes, not wishing to repeat exactly the same points as Grand Central, the potential effect of some of the new services on business are considerable but it appears the main effect is the VTEC timetable and if our trains are getting overtaken on every journey north and south. However, because the figures are conservative, the actual gain /loss equation really does depend on what comes out of the Events Steering Group (ESG) process. And we would like some guidance in the determination to Network Rail on the existing services both franchised and non-franchised, without fettering their overall discretion in terms of allocating capacity for best use, so that we can’t be put at a huge disadvantage in the ESG process. So, what we’re looking for is general guidance to Network Rail that we won’t be adversely impacted
through the ESG process to such an extent that we have to cease operations.

THE CHAIR: Right, just to be clear that guidance you think should come from?

HULL TRAINS: As part of the determination process, but without fettering Network Rail’s overall discretion and its duties to allocate capacity, so, effectively, not setting an agenda but setting an expectation.

THE CHAIR: Right, thank you.

GRAND CENTRAL: Can I just say, we’ve made that point to the ORR as well.

THE CHAIR: Yes.

GRAND CENTRAL: That the timetabling that would come on the back of any decision is absolutely critical to determine the financial impacts on open access operators.

ORR: Can I just check then, are you saying the kind of guidance suggested by Andy would deal with your concern about, I think you said, potentially ‘devastating impacts’ of the VTEC proposal? Or would you want more?

GRAND CENTRAL: Yes, I’m not going to say that it would satisfy us entirely but it would be very helpful.

ORR: Ok, thank you.

THE CHAIR: Thank you. Any points in terms of the impact on existing access?

VTEC: I’ve heard what both Grand Central and Hull Trains have said. I would just say that revenue impacts apply to us as well. A pound is a pound and, yes, get the point that both Hull Trains and Grand Central are small businesses, but a pound is a pound, and it can have the same impact on each operator on the network, freight and other operators.

THE CHAIR: Okay. Yes, Andy.

HULL TRAINS: Yes, a pound is a pound but there is such a thing as fair competition and the draft timetable that was produced that we have sight of actually seemed to be produced to actually put existing operators at a competitive disadvantage for a particular purpose and we believe, in Hull Trains, that was done to maximise the revenue of the East Coast bid at the expense of the existing operators by moving trains, and overtaking trains. We don’t want to see that happen. We’ve never been in that situation before where somebody has tried to effectively move us around the graph for their own particular advantage. The
ESG process should tease those issues out and deal with them. And that’s why I’ve got more confidence in the ESG process, at the end of the day. But if somebody has got that level of competitive advantage during the ESG process then that really does start to affect the future of certain operators’ businesses.

THE CHAIR: Ok, thank you.

ALLIANCE: Just to add a little bit to that in relation to competitive advantage. We’re talking here about the monopoly operator, in monopolistic terms, on the route. In effect, having completely different access rights to the markets, the upstream market, and open access operators, that’s why we’re sat here today because, as it was said in court, they are chalk and cheese in terms of access to the market. So, although a pound is a pound, in relation to the development of new businesses, as you can see with VTEC’s Sunderland service at the moment which gets into London in the peak, in the morning peak, it is impossible for a monopoly operator ever, ever to fail the NPA test. So, that’s why they have such significant access to the upstream market in relation to an open access approach. So, if we’re going to have a pound for a pound then we need to get rid of the anomalies within the upstream market, access to the market. And it’s only in the downstream market where we’re actually competitive, actually where everybody does work in a competitive environment. VTEC and people before them compete very heavily with Grand Central as Grand Central does, so, you’re absolutely right. We like competition. It has to be fair competition and the difficulty we have is gaining access to the market because it does work as I’m really pleased that you’re asking the question now, it does work both ways. But the monopolistic supplier has so many benefits which was identified in the court that for it to now be complaining – having made a bid knowing exactly what the potential competition was – is maybe a little bit rich.

THE CHAIR: Ok, thank you.

VTEC: A couple of points to make in terms of the overtaking move and the VTEC 2020 timetable of the Hull Trains, we’ve dealt with that in industry consultation and we have in response said that we’d expect the timetable development process and ESG process to resolve the situation. And so we don’t expect that to be an issue when it comes to the actual timetable. There are different ways to get to the market that is touched on but I think once you’re in the market, it’s worth noting that there are significant advantages of being an open access operator and not having to pay the extra access charges and obviously not having to pay the premium which is actually significantly higher value in terms of cost base. So, you’re not competing on a like for like basis. There are also advantages in terms of fares – that you can have
dedicated walk-up fares only if you’re an open access operator. The
franchise operators are not allowed to introduce these fares – so there
are clear advantages once you’re in the market – of being an open
access operator. I don’t think those advantages should be lost.

THE CHAIR: Ok, thank you.

ALLIANCE: I’d just need to come back on just a couple of little bits there. It would
be nice to think that the franchise operators doesn’t have his own sort
of on the day walk-up slightly cheaper than an inter-available fare, but
you need to go back to Grand Central’s arrival and the instant loss as
well of an inter-available first class fare which was taken from the
marketplace. But the fact of our – we paid heavy premiums, that’s just
a factor of bidding for something – an established business – that is
your risk. The other risk that open access operators take is creating
the business from scratch and all the costs that come with that. All
have done it. Grand Central have done it. Alliance would like to do it.
There’s nothing to stop Virgin from getting in to the open access
market if it really thinks it’s that good because it does appear he really
thinks it’s that good. Or maybe it would be Stagecoach as opposed to
Virgin, whichever one. Or maybe Stagecoach Virgin or maybe each,
who knows.

ALLIANCE: But the fact is there’s nothing to stop anybody getting into the open
access market and if it really was that easy I would not be as grey as I
am today and I wouldn’t have been here – I think this is 16 years now,
we’ve been working on this. We’ve been successful with some, but it
is tortuous. And we know what franchise business is like because the
Group does it as well. But this is the exciting part because we are not
creating something that the DfT want us to do, we’re doing something
for passengers out there – and that’s really important from our point of
view.

THE CHAIR: Thank you. I wanted to broaden it out to impacts on freight. In terms
of freight representatives –

ORR: We were expecting Nigel Oatway but he sent his apologies.

THE CHAIR: Right, ok. I think we might have to follow that up further separately.

ALLIANCE: Just picking up a few points that were raised about ESG. Glad to hear
that the Virgin 2020 timetable that Phil’s quite happy for that not to be
used as a basis going forward as that is the issue due to which we are
currently staying away from ESG process, because of that very fact
that Network Rail has included work that was developed by the DfT
with Virgin and missed off all the open access operators in the
application, so we wanted to actually take part in the ESG and
hopefully that will be taken on board by Network Rail that we will get rid of preference given to Virgin services.

And then just a small point to – I hear what Stagecoach Virgin are saying about open access, it’s just again rather rich that it was last year that Stagecoach South West Trains had some open access paths approved of their own.

THE CHAIR: I must say I’m not familiar with that first point at all about exactly how the ESG is working. I don’t know how relevant it is to what we’re discussing now. Fiona, do you want to?

NETWORK RAIL: I think we do want to respond to that point.

NETWORK RAIL: Happy to. So, we did a piece of work for DfT as part of the ThamesLink Development Programme which assumes VTEC’s 2020 timetable as a proxy for what a long distance high speed operator timetable might look like on the East Coast in 2020. It was not part of the ESG process although it was shared at the ESG as a potentially useful piece of analysis. It’s not part of the ESG process.

THE CHAIR: Right, ok. I think let’s call it on that point. There was just one final question I was going to put and I think it’s a general one to VTEC. It’s come out of some of the conversations about – I mean, could the argument be put forward that, given that the prospect of open access entry was well known before the franchise bids were submitted, so, in fact the impact of any entry is reflected in your bid? Is that reasonable?

VTEC: No, I think it’s not. There’s two reasons for that really. The primary one was that – well, they’re interwoven – there was SoSRA which gave us quite a bit of comfort. And that particularly taken against what Network Rail were saying at that stage – that there were only seven paths an hour – and if you take that as gospel and put it alongside the SoSRA, that’s a pretty cast iron guarantee because obviously if there was open access, then the SoSRA would be triggered. So, that gave us a fair bit of confidence when we were contemplating how much to allow for open access in the bid – and what a reasonable allowance was. We took a lot of comfort from the combination of those two factors. Obviously, things have changed in capacity now but the SoSRA does still protect us, to an extent, depending on exactly what comes out.

THE CHAIR: So, the prospect there’d be additional capacity beyond what you’ve first thought?

VTEC: There is now, depending on seven and a half or eight paths rather than the seven paths, maybe, and we’re still not convinced about that
from a performance point of view but that's another argument. But if there are eight paths then that could allow an extra open access operator alongside us and we would not be protected by the SoSRA. But our view at the time of the bid was that we wouldn’t get open access without the SoSRA being triggered; that still left us with 20-ish percent exposed but not 100% exposed. The sort of numbers we’re talking about are big numbers. The third point, at the time of the bid, was that there were two options, two applications on the table and using a conventional ORR methodology, they didn’t pass the NPA test so we took a fair degree of comfort from that as well.

THE CHAIR: Ok, thank you. Russell?

FIRSTGROUP: I think all we’d say on that point is having re-read the ITT recently, the ITT obviously for the East Coast franchise had a specification for six paths for the franchise operator which related to the IEP business case to operate those; the SoSRA came in under certain circumstances that we’ve been through, but at the time that that work was going on it had already been established through the work that Network Rail was leading was that there were likely to be more paths available than the shared one for the current open access; six for an IEP, and then potentially one path had already been established at that point, which is quite clear in terms of the reports that have been produced afterwards. And if you back to look at the ITTSS from the time – and I think we’ve made reference to this in some of our written submissions, the ITSS has been the indicative train service specification, and the discussions that are going on around that was that there were likely to be more paths available. So, I note what Andy said, but, yes, taking into account, when you look at what’s happened, there are risks that other operators could run other services and I think it’s a point that we’ve already made – or was being discussed earlier – in response to the DfT making a point about some future franchise bids. When you are doing a franchise bid, and particularly on an inter-city route, you do look at the risks that are out there where the space is – whether or not other operators could come in and you take a judgment on that. Andy’s just confirmed that they took a judgment and they were satisfied to the certainty, I mean the SoSRA would cover them to a certain extent, not the full extent, but all of that doesn’t take away from the fact that I think it was established, it was there to be seen, that there would likely to be more paths available.

THE CHAIR: Thank you.

VTEC: I think that information was post the bid process. I specifically remember a meeting with Graham Botham and Phil Verster in Leeds just after ITT, or around about the time it came out. Phil was adamant that there was no extra capacity until the CP5 funds were spent. And
after that, there was to be one extra path. We pushed them at that stage and didn’t get very far.

THE CHAIR: Thank you. Ian.

ALLIANCE: Yes. It’s quite interesting where we are in relation to the past, because if you go back to the Programmes Board which ran on the East Coast, from the very first one, when it was said there were seven paths on the route, we said there were eight, if you’re going to spend that money, and I said that earlier on today, and I am a bit surprised, Andy, that bearing in mind the history of open access in securing and finding capacity that Network Rail consistently say is not there, that you’re confident enough to believe that there wasn’t further capacity beyond the seven.

And that also does bring me to a surprising conclusion that why have you bid for six and half? As there is already one and a quarter on the line there for open access. So, I think we’re back here to: someone’s taken, as you do, a risk, a price risk, they wanted to share that risk with the taxpayer, as we’ve just heard, and because there happens to be more capacity now, they’re just trying to fill up the capacity with services of their own to prevent the competition. And again, that’s historical behaviour from National Express before them, from GNER before that. It’s just the way the monopolistic operator always operates on the route.

THE CHAIR: Thank you. Russell?

FIRSTGROUP: Just one final point, I think this is probably bound to the point that Rob made at the very beginning about the general nature of the paths and the amount number of paths per hour that we’re talking about because if we’re talking about seven and a half, then that implies there is eight in one hour and seven in the next, so, if there’s a standard pattern timetable, there will be eight every hour. Anyhow, I don’t want to re-open the debate but clearly seven and a half means eight.

THE CHAIR: Right.

VTEC: Eight paths with compromises.

FIRSTGROUP: Absolutely with compromises, not saying there wouldn’t be any compromises, Phil, but I’m saying that seven and a half means eight in one hour.

THE CHAIR: On that, are there any more points on that area? Because I’m back to, I’m going to close the section now on impacts and I’m going to move on to the final session today around appraisal issues. So, is everyone content? Right. I’m going to hand over to Chris.
So, this session is on further issues around economic appraisal. I think there are two particular issues that we want to spend a little bit of time on. Some of this is just around clarity of treatment.

These two issues are the treatment of infrastructure cost, particularly the cost of tilt infrastructure, and then rolling stock costs, which is in particular the treatment of the IEP fleet. If I take those in turn.

Infrastructure first. I think there have been a lot of things said about this but it is probably worth being absolutely clear what’s happening here. We asked CH2M Hill to ignore the cost of the tilt operation in their report. This reflected the high degree of uncertainty about the right number to include for this cost. We agreed with parties who have emphasised that the cost of infrastructure needs to be included in any appraisal and I think it was clear from the start that that was what we were trying to do. So, that is what we’re doing.

In terms of what is the right number to interpret, it’s not just the CH2M numbers. I think CH2M’s made that very clear in their reports. So, that is a basis for this discussion.

So, in that sense, I don’t think, although I’m happy for that to be challenged, that there is actually a real disagreement about the appropriate treatment of the costs of infrastructure. If it relates to the benefits that we’re talking about it is necessary for the option, it should be in the appraisal.

I think what there is then less agreement on, and less information, is the right number to use for the costs of tilt. Now, on that latter point, I think parties have set out what they know about what that cost might be, so, again, I’m not sure that there’s much to be added from spending a lot of time debating that number. I think when we open this up further for discussion it’s worth being really clear that I don’t think there’s a disagreement on the appropriate approach. It will be an interesting debate, I think, as to what’s the right number to use.

THE CHAIR: Can I open it up?

ALLIANCE: Can I just add quickly to that? The other infrastructure investment that is proposed from Alliance, of course, is East Leeds Parkway, and that’s in our business plan and that’s very clear. And unlike the tilt option on the East Coast Main Line, for which we’ve been waiting of course for the position on power supply, which was always our position and we’ve made that quite clear. Now, that is clear that you do have a figure on them, and we can back that up with the work that Network Rail did in relation to the new station that’s proposed on that route. And that one in particular does, we believe, create capacity, not only for our services heading to West Yorkshire, but, as our colleagues at VTEC have already said they would use that station, of course, because that would also be their route into West Yorkshire.
THE CHAIR: Ok, thank you. Chris?

ALLIANCE: Can I just clarify that point Ian made on power supply? Yes, it’s right, we did make it clear the reason we did not proceed with quite an expensive study with Network Rail to determine the infrastructure costs of enabling tilt was because we believed that power supply was potentially a show-stopping issue. And I think we were vindicated in that by the latest report although Network Rail has now identified solutions to the power supply problems. They have determined that there is no capacity north of York for additional electric trains until significant investment is made in upgrading the feeder stations. And that, as determined earlier on, is dependent on CP6 funding and I think we all know that in the current environment, especially as we’ve heard from DfT how difficult funds are, how tight funds are, there must be some question about even whether that can be achieved in CP6 because power, feeder station upgrades are very expensive in terms of fitting them out to achieve that for each one. There are five, I think, that need upgrading. So, it’s not an insignificant expenditure that’s needed on power supply before additional electric trains can run to York. So, I just wanted to clarify that we’ve been waiting for that. It now seems that the earliest any further electric trains could run would be May 2021. And my own view is it’s probably later than that.

THE CHAIR: Thank you. Graham?

NETWORK RAIL: I guess if I’m being drawn into it, I maybe should clarify. We’ve been quite clear. We have not yet completed GRIP 3 on the power supply upgrade for the East Coast Main Line. That is shown for February next year and it’s at that point we would know how much that would cost and what the precise proposed solution would be.

ALLIANCE: Sorry, to come back on that Graham, but do you accept that however, whatever you do have to do that each feeder station upgrade would cost in the order of 20 million pounds?

NETWORK RAIL: Chris, I don’t know, because we need to do the piece of work first.

ALLIANCE: Surely, Network Rail has some figures? How does it work? It has upgraded feeder stations in the recent past, they must have some idea of what it costs to upgrade.

THE CHAIR: I think Graham’s refusing to speculate so I’ll move on.

ALLIANCE: Just a quick one, John, I might be able to throw some light and I think David will be able to back me up with the stakeholder meeting that we had earlier this week, although it was a generic, ordinary figure, there
was a suggestion that in to CP6 it might be a round about £100 million, I think. Is that right, David? I think that’s what was said at the time.

THE CHAIR: This relates to the power supply?

ALLIANCE: And that was a Network Rail meeting that we attended in relation to stakeholders for the East Coast. It’s not as specific, obviously, and they admitted it’s not at GRIP 3, but they believe it will be in the order of around about £100 million.

THE CHAIR: Ok, thank you.

VTEC: Yes. I’m just surprised that an application to take in the order of over £100 million a year extraction from the incumbent operator over a 10-year period, wouldn’t warrant an investment of £100,000 or £200,000 into a study to understand the indicative costs for tilt. And to say, well, we’re not going to do that until we understand what the power supply situation is, is extraordinary. The application has been on the table since December 2013. And there has been quite a lot of time to be able to do a tilt study and to understand what those costs might be.

THE CHAIR: Would you like to come back on that?

ALLIANCE: Yes, I know, there are numerous reports sat around covered in dust that Network Rail have done historically for all sorts of things on the route. The fact is, at the moment as well, Network Rail are not particularly good, and this is not a pop at Network Rail, at actually putting a price to any particular work, especially in relation to something like tilt on the route. There is not really any in-house expertise. And the fact is, unless we can sort out the power supply, then it would have been a quite expensive piece of aborted work. And we’ve made it clear right from the very beginning, with Network Rail, and here, in previous meetings, that until that was clear, it was not worth us investing that money and that seems to have been a wise choice bearing in mind where we are today.

THE CHAIR: Thank you.

VTEC: Can I just come back on East Leeds Parkway? It’s a bit of a broad point and it comes back as well to the economic assessment in terms of should the benefit of the station and the benefit to Alliance, as proposed, be reflected at all? So, just to bring to your attention the West Yorkshire Combined Authority had a Transport Committee meeting last Friday. There’s a paper which is publicly available giving an update on East Leeds Parkway Station which says that there were a significant number of issues to resolve in taking East Leeds Parkway forward and it concludes that it proposes to review options
now for the station including the location. This is a station which is not
even at GRIP zero in the Network Rail process. There must be
significant doubt as to whether it will open to the timescale that Ian is
expecting it to. And indeed whether it will actually open before CP7.
And we can talk about funding contributions but I just question whether
the benefits of this station should be reflected in the evaluation at all.

ALLIANCE: I’m not familiar with the particulars of that meeting or whether that
meeting – that was new information that was tabled at that meeting or not.

ORR: It’s new information to us as well. I wasn’t aware of that.

VTEC: I’m very happy to provide.

THE CHAIR: Ok, right. Thank you.

DFT: Just one very quick question? It’s just a question almost for you John
and to Chris. So, we accept that the infrastructure costs should be
taken into account, but there isn’t a – or at least I’m not hearing, a
number. I’m trying to understand how exactly that’s going to feed
through to your process.

ORR: Yes. There are a series of numbers around that are estimates from
parties. I think in terms of the decision making process, one of the key
things we need to establish is the extent to which that number matters.
So there are a number of scenarios where when we look at the size,
and we go into benefits and costs, this isn’t a significant swing factor.
If it is, then we’d have to decide what sort of recommendation we could
put to our Board and equally the Board would decide on whether they
had enough information to take a decision. And it’s difficult to
speculate too much on that. But I’m thinking the important thing is that
one of the key concepts is how much does it matter to the decision
because it may not.

THE CHAIR: Okay.

ALLIANCE: John, just one quick one, just to come back on East Leeds Parkway. It
is actually quite irrelevant what West Yorkshire Combined Authority
might believe because as we made it clear in our business plan, we
will fund that station. David’s quite right. If we go through the GRIP
process, we’ll probably be back here in five years still talking about this
station. The fact is Arriva has expertise in building railway stations
outside the Network Rail programme, Warwick Parkway is a classic
example on the Marylebone route. So, we mustn’t get hung up on the
fact that Network Rail’s processes take an extremely long time and
what Network Rail are seeking at the moment – and indeed what the
industry’s seeking at the moment – is real, third party investment – and that’s exactly where we come along. This is not new. It’s not something I’ve just popped in my plan. You’ve had it in our plan for over two years. And it’s something we really want to develop. Where it’s located, that’s the discussions we’ve got with Network Rail at the minute. But we do believe it unlocks some capacity on the route not only for the benefit of people that currently use the route but also for ourselves and ironically for Virgin.

THE CHAIR: Thank you. I think that probably wraps that point up? Thank you very much.

ORR: Thanks for that. And I think we now move on to the second of these, this is the rolling stock costs. Again, it’s worth being clear, we asked - because we knew there’s some uncertainty about the ‘right’ number to put in - CH2M to adopt a particular assumption in their report and it is clearly set out what they’ve done. We need to separately decide what is the right approach for the treatment of that rolling stock cost. This is something that we flagged in our technical note that we published alongside the report.

I think there are two questions here. I think the first of them can be summarised as being: How much of the IEP costs are sunk in economic terms? That is in essence an economic question, in terms of just the facts of the case. How much are sunk?

And then the second question, which is quite different in nature, is a question around: how much weight should we place on the fact these costs are sunk when we assess them against the statutory duties?

It would be worth saying a few words on both those questions separately because they’re quite different in nature.

Taking the first: To what extent are the IEP costs economically sunk, if I can use that kind of phrase?

As set out in our technical notes, we’re interested in exploring the extent to which those IEP costs are actually sunk. We’re trying to identify here both the costs that have been incurred and the extent to which they cannot be retrieved. It’s both of those things: it is an ‘AND’.

The costs have to be incurred AND they cannot be retrieved.

So, the second point here, I think, is where the debate should focus. I don’t think anyone is debating the fact that they’ve been incurred in terms of ‘a contract had been signed’. So, the ongoing issue is, whether they can be retrieved? What that really means, in terms of turning that WebTAG language into more common parlance, is: Can the Department through its action reduce that cost? They could reduce that cost in a number of different ways by redeploying the rolling stock or renegotiating that contract. DfT have made a number of points, which I think you’ve all seen, and I think neither of those strategies are without costs but the issue is obviously how much cost
might be saved through following either of those strategies to redeploy the rolling stock or to renegotiate the contracts.

It might be worth pausing there, really, in terms of that key issue of whether they are economically sunk – and those two issues of views about redeployment and renegotiation of the contracts.

THE CHAIR: Okay. Does anybody have any comments to make?

ALLIANCE: Well, certainly on the redeployment case on the East Coast Main Line because I know they have a view they can’t go anywhere else, which is rather strange for a train that’s meant to be compliant in the UK, we require eight for our West Yorkshire / Cleethorpes services.

[LAUGHTER]

ALLIANCE: There is a surplus because we haven’t ordered any because we haven’t sunk any costs yet and we’re quite happy to pick up the surplus, so that’s eight sorted. And of course our colleagues here, they want five, is it? I’m not quite sure. So there’s quite a large amount of the fleet that could be redeployed.

THE CHAIR: Ok, thank you. I’m not sure DfT have noted that offer. Russell?

FIRSTGROUP: I wasn’t going to make the same offer, I was thinking a slightly different configuration. In terms of – I suppose what we would say about it is that the original business case for those trains on the East Coast was for the six paths that were in the specification for the ITT that VTEC bid against and were successful against. So, if they were to get those six paths and that still leaves, another path - I don’t think you can retrieve those costs in the sense of that.

In terms of deployment, I would just expand a little bit on Ian’s first point which is those types of trains currently could appear in several places across the UK. And there are clearly opportunities to use them at a number of locations. There are other franchises that are coming up soon and I’m sure that those trains could be used on a number of different routes. If we were in a situation, which I don’t think we would be – of the East Coast franchise having less than six paths.

ORR: That could be quite an important point there really. So, if people are agreeing with this as a characterisation of what we’re considering here, the implication of what you said about the six paths is that this debate only matters in the scenarios where VTEC doesn’t have the sixth path. And it would be helpful if people would agree that is an appropriate way of thinking about it. And if, once you have the agreed that, the debate about sunk IEP costs is largely moot for the other options.
THE CHAIR: Can we just check that?

VTEC: I think it’s difficult to say. If we had the full six paths, with all the extensions, then in that case we could use the full IEP fleet. We don’t need the 225’s for the VTEC Core, as CH2M call it. That would not use all the IEP fleet. VTEC Core plus Bradford, Harrogate, Lincoln, i.e. all the extensions, would use the full IEP fleet.

THE CHAIR: Ok, thank you.

ORR: I was just wondering, can the Department confirm? That’s right, is it?

DFT: As far as we’re aware, yes, but I think as VTEC is the expert on how its trains should be diagrammed –

THE CHAIR: Ok, fair enough. Anything else on that point? Okay. That’s helpful.

ORR: I think actually that’s quite an important rider for what I’m about to move on to, really. I think that what I’m about to say now really only follows for the case where the IEP order is not fully deployed. But I guess there are some points that have been made around how we should look at those costs.

First the issue of are they economically sunk? We’ve covered that, I think, and made some progress.

So, then there is the issue of how do we assess that issue against our statutory duties? Now, I think there are broadly two sides to this: two ways you could point to our statutory duties. I think one is that if we treated the economically sunk costs in that way – so, we actually ignore them from the appraisal – that could be seen as distorting the decision making process because it gives a first mover advantage – it’s not quite the right way of putting that – but, a sort of first mover advantage to anyone who has the resources to sink costs in rolling stock contracts. That’s one side.

The counter view, I think, is that obviously if we took that decision, it may strand some costs and impose some real costs on parties to those contracts. Those sorts of considerations would relate to other aspects of our statutory duties: such as efficiency and economy; to plan your future business; value for money; and, of course, the impact on the Secretary of State funds.

So, it appears that the treatment of this, you could argue, might differ depending on the weight you place on those various statutory duties. Now, I know this is an area where’s there isn’t a particularly scientific answer but that at least explains some of our thinking in relation to how we relate this issue to our statutory duties, which again goes to the point that it’s only relevant I think in certain circumstances for this case.

THE CHAIR: Yes, let’s pause there. Do people recognise that as a position? Ian?
ALLIANCE: Yes, this is a difficult one of course because you’re talking about two private operators investing money and therefore I’d have to question as to why it drops into the appraisal in the same way because most of the appraisal is based upon public investment, as opposed to private investment. I can see the argument for some of the costs because they’re here and the taxpayer’s behind it but like our colleagues at First we’re not expecting that fleet can’t be used at some particular time. But in relation to the cost, if you’re going to regard it as sunk, then maybe you should regard the others as sunk, even though they’re not, on the basis that the investment is completely separate; it’s really of no relevance to anybody other than the investor himself; otherwise, as you’ve rightly pointed out, and we’ve got an issue with Grand Central soon, because GC has more rolling stock than they can use, or will have soon. It then puts somebody at a significant advantage. You know, do we then go and buy rolling stock and come along and, say, well, we’ve got trains here, so, you know. I know they’re going to replace trains on another line for example but actually we’ve got some so, you know, our plan is going to be significantly better than anybody else’s plan. So, it is a real issue for you I think in respect of that. And I’m not quite sure what ultimate value this piece of work in the real evaluation of what the benefits are, is actually going to make in the long term.

THE CHAIR: Ok, thank you. Chris and then I’ll bring in DfT.

FIRSTGROUP: The first of your questions was undoubtedly an economic question. The second one is essentially, as we understand it, a legal question under Section 4. The particular criteria that you identify are probably the right ones but just taking each one of them – the criteria - in turn.

The impact on the Secretary of State’s funds. There is a synergy here, between the six paths which applies to the economic question and whether it ever becomes an issue under the legal question because if the fleet is fully utilised at six, the impact then drops away. So, it becomes academic and actually drops out of the equation as a matter of practicality.

The planning with certainty isn’t an absolute. The point probably tracks back to Andy’s point that what ‘planning with certainty’ doesn’t mean is that if you invest in the hope of getting paths later, then you’re entitled to bank that and have that taken into account as an additional decision criterion in the evaluation of Section 4 duties. That would not be a proper application of Section 4 duties.

On efficiency and economy, that is really a head which is directed to the way in which people conduct their operational business rather than a forward planning issue. And that is, in our submission, about the way in which rolling stock procurements are done rather than about an issue of comparative advantage of timing related to an
access application. So, for reasons both of principle and practicality under each of these three heads, we’re not seeing that any particular clash arises, particularly as it probably doesn’t arise anyway because the costs aren’t sunk because of the six paths.

THE CHAIR: Ok, thank you.

DFT: I just wanted to say in relation to Chris Hemsley’s laying out of the issue earlier, I actually think Chris you laid our the issue exactly right. So you’ve got this situation of “first mover advantage” which puts you in a difficult situation, in terms of whether or not you should fully treat the costs as sunk in the appraisal or if that distorts competition between the applicants. And I appreciate that that’s the trade-off that you have to look at. The point I would make, is that the only way which you could sensibly look at this trade-off is by looking at the size of the relevant costs which would normally be treated as sunk. So, to give an extreme hypothetical: If that component of the sunk costs within the application was equal to the GDP of the UK, my working assumption is that the ORR would at that point say, fine, this supersedes any strategic argument which we’re laying out on the other end, (which is in relation to the distortion of the competition). So again, I think the only way to sensibly approach that framework which you’ve articulated very well would be to start by treating the numbers as standard WebTAG / Green Book appraisal guidance suggests that you should do.

But my second point is this: to be able to do that, you need to consider the extent to which the costs would reduce if the IEPs were used for less mileage than is assumed within the contract with Agility. Now, we are happy to provide that information to you but unfortunately for some reason the ORR has refused to give the DfT the requisite assurances that the commercially confidential data that we would be passing on from Agility would not be shared with other applicants or published. And unfortunately therefore, it’s impossible for you to actually look at the numbers properly to answer the question of whether or not the extent to which the costs are sunk should supersedes the strategic arguments about the distortion of competition.

THE CHAIR: I think, sorry, to be fair, we did explain why we were unable to offer those assurances. We have exchanged letters. It’s not as if it was some gratuitous refusal. We did explain quite clearly why we couldn’t do that.

DFT: Sorry, can we?

DFT: The only other thing that I was going to add to that was I know there’s been correspondence on that. I’ve seen it in my inbox but I note that – and maybe I’ve misunderstood something – during the discussion
earlier today FirstGroup were talking about some of the data that they've provided to CH2M Hill in relation to their fares strategy. And as I understand it there is a non-disclosure agreement there. It’s not clear to me why similar assurances couldn’t have been provided to the Department in relation to the IEP mileage adjustment rates within the IEP contract.

THE CHAIR: To the best of my knowledge, we’ve not signed any non-disclosure agreements with anybody.

DFT: I may have misunderstood an arrangement that was outlined earlier.

THE CHAIR: I thought that was a reference to something to do with, a commercial arrangement with CH2M Hill. It’s not a reference to us.

DFT: Ok, then equally, we could presumably enter a non-disclosure agreement with CH2M Hill so that they could provide you with an appraisal that accurately reflected the nature of the IEP contract?

THE CHAIR: I’m not sure how that would work in practice but I’m happy to think about it. Ok, thank you.

DFT: We have other points about the appraisal that we meant to make that don’t relate to the two points that you raised about IEP, so I don’t know when is a good point to make here –

THE CHAIR: Yes. Let’s just see if there’s any more on this one and then I’ll bring you back in on that. Is there anything more on those? Simon?

ALLIANCE: I can see why Chris is wrestling with this. If you don’t take into account the supposedly sunk costs of IEP, don’t include those sunk costs in the appraisal, it sets a rather awkward precedent, in that it makes it very easy in future, where you have a situation like this, where there is a franchise operator who is, or an operator that’s bidding for a franchise, or a franchise competition is under way – and, on the other hand there are open access applications that are not yet determined – that are on the table – that the DfT could do what they’ve done. Admittedly, not for this specific reason. In the case of IEP and ordered the trains, and then told the franchise operator that those are the trains that they will use – and then say: well, that’s a sunk cost and therefore those costs should not be included in the appraisal alongside the costs of the open access operator. Because clearly no open access operator will order trains until they’ve got paths where they can use them. Arguably, the DfT shouldn’t be ordering trains before they know whether there are paths to use them but they’re in a rather more powerful financial position. They also have the potential opportunity to use them elsewhere on the network. So, I think for a fair comparison
it’s clear that the costs of rolling stock for all the applicants should be taken into account. Now, I do appreciate that you also need to take account of the possible impacts on the Secretary of State and so on, so you may then also need to do an assessment which says: well, what will happen if the franchise operator is unable to use those trains fully as a consequence of the access decisions that you make. But, I do think this is where I disagree with Enrico, that the core appraisal does need to take the full rolling stock costs of all the applicants into account.

THE CHAIR: Ok, thank you.

VTEC: Could I just? I mean this a bit out there – but the reference that you are somewhat at a disadvantage because you don’t have the resources to go out and buy some trains was wrong. You’re owned by German State Railways. You could go out and buy trains.

ALLIANCE: I could say something on this point as well but I’m going to let Simon get in first –

ALLIANCE: Yes, clearly Deutsche Bahn could afford to buy some new trains speculatively. Probably, Stagecoach could afford to buy some new trains speculatively. But neither party would do so. The DfT and indeed no other franchise operator has bought new rolling stock when that’s been part of their franchise competition, until they know that they’ve won. I mean First are in the course of ordering new rolling stock for TPE, now they’ve won. Arriva have ordered new rolling stock for Northern now that they know that they’ve won. They would have been crazy to do it beforehand. The only people who can order rolling stock in advance for a franchise are the DfT because they know that they are going to buy those franchise services.

THE CHAIR: Ok, thank you. Well, Ian, did you want to come in?

ALLIANCE: No, I’d better not.

[LAUGHTER]

THE CHAIR: Okay. Thank you. Okay. Let me just check with Chris. Chris, I think that now wraps up all our points.

ORR: Yes.

THE CHAIR: I’m now going to pause briefly to see if there’s any material – I’ll come to you in a minute, Simon – whether there’s any material points that people think haven’t been raised that they’d just like very briefly to put on the table in this area? If not, I’m going to go straight to Simon.
DFT: Thank you. I think when we’ve been looking at the appraisal results, you also have to take into account that the appraisal is the result of all the elements, including the capacity analysis, and the demand modelling that we were discussing earlier. And what was clear from the discussion earlier was that some of the fares crowding and timetable assumptions, particularly for the First Group application, in the current CH2M analysis, are simply not credible. That the First Group fares in practice would be much, much higher than has been assumed in the CH2M analysis because as a rational commercial operator, they would increase their fares so that demand and capacity were reasonably in balance. And then this has a significant impact on the economic appraisal. So, the CH2M analysis is presents NPVs for the open access and franchised operator options. In our analysis, in the NPVs for the open access options, a significant part of the positive NPV, is actually the private sector profit made by the open access operator. In our own analysis, by the mid-2020s, reflecting the fact that it’s fares will be much higher, we think, than assumed in its business plan — and really much closer to those charged by the franchise operator, we have estimated FirstGroup having an operating margin of in the region of 60%, which is, whilst it sounds ridiculously high, is actually not dissimilar to what at that point a franchised operator would be making – if it didn’t have to pay fixed track access charges or premium or capacity charges and therefore was facing the same basic economics as the open access operator was, at that point. And I think that demonstrates that the NPVs as reported by CH2M, are not a sensible way of reporting the results of an appraisal in these circumstances. WebTAG guidance is clear that in the case that public expenditure is limited and options have different impacts on public expenditure, the relevant metric to study, is the benefit to cost ratio. And NPV is only relevant where options do not impact the broad transport budget. If you do compare NPVs for options that have very different impacts on the transport budget, you really ought to be taking into account, in that NPV, the dis-benefit of whatever other bit of expenditure has to be stopped in the options that have big negative impacts on the transport budget.

So, I would encourage the ORR firstly to re-appraise all of the options taking into account the feedback today, but, particularly, the fares and timetable assumptions that have been made in respect of the FirstGroup application, as those appear to be most significantly questionable. But also, once it’s done that, to study a benefit to cost ratio – the benefits that would be achieved for the amount of public money that was sunk into each of these options rather than simply looking at the NPVs which we just think is not appropriate. Thank you.

THE CHAIR: Okay. Thank you. Lucy?
SDG: Just a couple of points to reiterate there what Simon was mentioning. Our own analysis found that the private sector benefits were in excess of the sum of the user and non-user benefits for the open access options. For example, for the First Edinburgh option we found combined user and non-user benefits were £250 million but private sector benefits were £290 million. With the Alliance West Yorkshire / Cleethorpes option, we estimate a combined user and non-user benefits of £200 million and private sector benefits of £320 million.

Now, those private sector benefits are effectively ultimately being paid for by the government.

And I just wanted to make one more point. Simon raised that the premium would otherwise be higher – if it wasn’t the case.

I just wanted to raise one other point, as Simon was saying, we’ve got doubts about the fare estimates and the crowding estimates as they relate to revenue. Those have an impact on the economic results because you’re getting economic and crowding benefits. But just today I was reflecting on what FirstGroup has said about their proposed fares structure and CH2M’s modelling approach and it occurred to me that FirstGroup has said that most of their tickets will be Advance Purchase tickets. Then I remembered that CH2M HILL actually allocate AP demand according to train capacity and just re-reading your report, you allocate AP demand just according to spare spaces on trains and then you cap the demand based on the availability of capacity, it says, in your report – both capacity and fares. So, that might be partly why you’re not getting those high load factors which lead you to think that FirstGroup wouldn’t actually offer those fare discounts. So, that’s just something to have a look at and just consider the implications of that assumption.

THE CHAIR: Okay, why don’t you come in first, Chris?

ORR: I mean in terms of the FirstGroup option, we’ve already said that we’re going to do some work there. So, we’ve said that already. I think it’s worth noting that we’ve never said that we are simply looking at the NPV. That is not our approach. We’ve made very clear that we consider all the effects, including the magnitudes of costs that we impose on the Secretary of State. I think I can understand: I’ve read WebTAG, I’ve read the Green Book. I understand what you’re saying. I don’t think the way that we’ve presented the results, but more importantly, the way that we’re going to actually use those results in our decision making is going to depend on the precise ratio that we use. The main point is we are going to look at all the effects against our statutory duties.

THE CHAIR: Chris?

CH2M HILL: So, we have run our crowding model, as I’ve said before, and for one
of the three FirstGroup options which were tested (i.e. the option where the overtaking manoeuvre in the southbound direction is removed), the model indicated to us that the load factors would not be sustained on a long term basis. So, as we stated in our larger report, back in October, we increased the fares to the point that we felt that load factors were sustainable and the discount, or the reduction in the discount offered by FirstGroup is reported. Thank you.

THE CHAIR: Thank you.

ALLIANCE: I think this is a bit like the discussion we just had about sunk costs. There are different ways of looking at the economic case. One way of looking at it is to look at the overall benefits to society from each of these applications and the resources that need to be devoted to unlock those benefits. So, a fairly classic cost benefit analysis which will give you, granted with the inclusion of infrastructure costs where appropriate, will give you an NPV, and it will give you one way of measuring BCR. And I think that is probably very important from the point of view of understanding the benefits in terms of economic efficiency, benefits to users, promoting competition, promoting use of the railway for maximising use of the railway – those types of duties. Then there is the question of the cost to government which is clearly another of your duties. And the UK Government has a very particular view of the way to undertake economic appraisal and assessing cost to government in that appraisal which is not consistent with what is done in many other countries. It’s not consistent either with the way the European Union does it. There are reasons for this. You can argue that different methods of doing economic appraisal have strengths and weaknesses but I think for a core assessment of the value to society of these applications the way that it is being done by ORR is generally correct. It may be a little conservative in terms of things like wider economic benefit, but broadly I think it’s the right approach.

I recognise that you also need to consider the cost to government, albeit, we think the cost to government, if any, will be orders of magnitude less than the DfT do because they have in our view erroneous antipathy to open access.

THE CHAIR: Ok, thank you. Russell?

FIRSTGROUP: I suppose all I was going to say is that our application – there’s a lot of information that’s contained within our application that we submitted to the ORR. And, yes, it’s our business plan and yes, it is confidential. And it is confidential for the reasons that if you read it, you would know, but it, by its very nature, I can’t describe, I can’t give you details about what’s in it because that’s our commercial in confidence IP. We think that this is a new and innovative way of providing capacity on the
network. We stand by everything that we have said in that application to the ORR and I’ll stand by what we’ve said again on our fares and the way in which we’re going to approach our operation.

THE CHAIR: Ok, thank you. Ian?

ALLIANCE: Yes. Just to say, for summing up for ourselves, our applications are the longest standing applications here. I hear what Lucy says about the value of all our services. That might be one of the reasons why VTEC have copied a number of them in the same way that National Express did some time ago. And again we must keep reminding the DfT that they have opportunities through levies etc. if they really feel that there’s an issue here about not paying the same arrangements for services.

Our applications are two-fold. One is a very early application for a record breaking, completely ground-breaking service between London and Scotland. In the same way that it was proposed 10 years ago and at that time rejected by the DfT for the franchise at that particular time.

Our service to West Yorkshire and Cleethorpes is a traditional open access service. Not one that should be difficult to measure. I’m a bit surprised that Andy believes that all these fail the NPA tests because clearly they don’t fail the NPA test; they don’t fail it through your normal measurement tools and they certainly don’t fail it through those or through our own.

And the services are designed to grow the market, niche markets into different areas – and exactly as happened in 2009 with National Express we know when we make these applications so early we run the risk of them being cloned and that’s happened. Our colleagues at FirstGroup, it was a later application – I don’t need to go through that. I can understand why the DfT get very upset about that one because that came along after the event but certainly the applications that were looked at in relation to ours were well known. One of them very traditional, apart from the fact there’s station investment which will be important in relation to releasing capacity. So, I think we’re looking here at ground-breaking, record-breaking type of service with – Andy makes a fair point that we’ve not been able to deal with as such, an undetermined amount of investment required in the infrastructure. And another one, more traditional, but opening up a market in the way that the previous franchise suggested a station on that route would open up the market. So, we’re not revisiting, or we’re re-visiting things that have been done before. We have a good track record of innovation. We have a good track record of growing the market. We have a good track record of understanding the niche markets that we develop and as a result we like to think that of the applications that you have in front of you, our applications are the easiest ones to see for their significant benefit.
THE CHAIR: Ok, thank you, Ian. I am going to start drawing things to a close and if there’s any final, very material, and I use that phrase very carefully, very material points anybody wants to make? Russell?

FIRSTGROUP: It’s only, there’s been a couple of, well, there’s been a number of pieces of new information, and new figures disclosed in the meeting today. And I’m not sure of the status of them – whether they can be fully shared. I know some of them have been referred to and said ‘more detail will be provided’.

THE CHAIR: Yes. We’ll pick up those from the transcript and we have to make sure we clarify who we think has agreed to send round what and if you disagree with us, then let us know.

FIRSTGROUP: Thank you.

THE CHAIR: So, we will pick up on that. Yes. Chris?

ALLIANCE: Chris Hanks. One thing that since lunch time, I should have picked up this morning really, I wasn’t clear, I’m not sure, whether it was made clear this morning but I didn’t pick up whether the AT300s FirstGroup are proposing for their service are bi-mode or fully electric trains. I think that is material, given the discussion we had about power supply.

FIRSTGROUP: I think as we said in our application, that they’re electric.

THE CHAIR: Ok, thank you. Right, ok, thanks very much. I’m just going to bring things to a close. I just want to say three things about next steps. First of all, we will circulate the transcript for checking and while doing that we’ll pick on that point about where we think there’s some actions or offers to circulate further information. Secondly, we will be discussing the applications at our April Board meeting. That’s in late April. And therefore, the third point is what we now need to consider in the light of this hearing is how we use the information from this hearing, the other comments we’ve received, and whether there’s any further information we need and indeed whether there’s any further analysis we want to share with all of you. It would be over the next few weeks. I think this is now about the path to get to that April Board discussion. And apart from that all I wanted to do was to say thank you very much indeed for attending. And particularly and genuinely thank you very much for the constructive way in which people have contributed to this session to date. It’s been a long and hard session but I think it’s been very productive. Thank you very much indeed.

VTEC: Excuse me. Sorry. I’d just like to make a couple of points in respect of process going forward, just following on from your helpful comments
just now. Certainly from VTEC’s perspective, we’ve really welcomed the opportunity today to participate in the stakeholder meeting and have found it incredibly useful. And just touching on the points you’ve made just now about process going forward. It’s obviously very important from VTEC’s and the applicants’ perspective that we have a fair and transparent process that leads to the best outcome for the ECML route and from that perspective we’re very conscious that you’ve got three independent reports in front of you which take quite divergent views on key issues. And we’re very conscious it’s of course for the ORR to understand the differences between those reports and to re-appraise the reports if necessary. And then take its own rational, independent decision as to what the right outcome could be, but certainly from VTEC’s perspective we would like to emphasise the need to ensure sufficient time from our perspective to make further representations to you and in particular on the particularly fundamental divergences between the experts, if there is an opportunity to put to us where you’re coming out in terms of provisional thinking and conclusions, that would be much appreciated, just to ensure that we can make appropriate representations and ensure that you have all relevant available evidence available to you to take the best decision possible.

THE CHAIR: Okay, thank you. That leans a bit to the point I was making about what further analysis we want to share with the parties. I do understand that point and we will think about how best to do that.

DFT: Could I just ask a process point? Is it your intention at the moment to invite the Board in April to take a decision? And if so, that doesn’t leave a huge amount of time if there are further iterations following the hearing. You may not be able to say exactly what your approach is likely to be to the April Board but I just want to get a sense as to what you’re thinking.

THE CHAIR: No, I was consciously not saying because my final point was about what’s the path to that discussion and how much more we would need to do before that discussion. So, there will be discussion at the Board but in terms of whether we invite the Board to make – or making a recommendation to the Board, or whatever – we haven’t decided that. I think it goes back to this point about: To what extent have we brought all the information together? And that’s what I really do want to reflect on as a result of this hearing.

DFT: Thank you.

THE CHAIR: Thank you all very much indeed. Thank you.

The meeting concluded at 3.33 p.m.