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Aaren Healy  
Regulatory Economist  
Network Rail  
One Eversholt Street (Floor One)  
London  
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Dear Aaren

**Consent to changes to the Traction Electricity Rules to allow the billing of traction electricity using partial fleet metering**

1. We have today given our consent to a request made to us by Network Rail to proposed changes to the Traction Electricity Rules (the TERs) under Paragraph 11 of the TERs. These changes provide for the billing of traction electricity using data from partially metered train fleets for those passenger train operators that opt-in. They also reorder the TERs to give the document a more logical flow.
2. The TERs shall take effect 14 days after the date that Network Rail notifies the relevant parties under Paragraph 11.16 of the TERs, such date being within 7 days of our consent.

**Background**

3. Following the implementation of the framework for the billing of traction electricity using on-train metering in 2011, the industry developed the concept of partial fleet metering (PFM). That is, for train fleets (for specific train service codes) that are partially but not wholly metered, the actual consumption data from the metered trains is used to calculate an annual consumption rate for the unmetered fleet (which would then replace the modelled consumption rate).
4. The advent of PFM billing was a response by the industry to the relatively high cost of procuring on-train meters for trains running on the third rail DC network. The aim was to secure some of the benefits of metering, including more accurate bills and better incentives to reduce energy consumption, without the costs of full metering, and provide a stepping stone to full metering in due course.



5. In our final determination for the 2013 periodic review (PR13)<sup>1</sup>, we asked the industry to develop the contractual framework to enable billing on the basis of PFM. A significant amount of work subsequently took place, led by Network Rail and supported by the industry's Traction Electricity Steering Group (TESG).

6. On 7 September 2016, and following earlier discussions on the approach to implement PFM at TESG and informal consultation, Network Rail formally consulted the industry on:

- (a) proposed changes to the TERs to implement PFM and re-order the document;
- (b) standard wording for a supporting change to Schedule 7 of the track access contracts of those passenger train operators that opt-in to PFM to align it with the provisions in the TERs; and
- (c) the principle that, where train operators opt-in to PFM, an industry consultation on changes to Schedule 7 would not be required where the standard wording referred to in paragraph (b) above is used.

7. The consultation was extended by two weeks ending on 19 October 2016 in response to requests from some consultees wanting additional time to review the proposals. Following the consultation, Network Rail received seven responses. There were no objections to the proposals. In the subsequent industry vote on the changes to the TERs, all votes cast were supportive.

#### **ORR review of the request for consent**

8. We have been involved in the development of the PFM framework through our attendance of the TESG and in the informal consultations carried out by Network Rail on the principles of PFM and the drafting. We have no objections to the changes and indeed we welcome the implementation of PFM. We are satisfied that Network Rail has followed the required process for changing the TERs.

9. On this basis, we have given our consent to the changes to the TERs.

#### **Applications to apply PFM billing by Network Rail and train operators**

##### *Changes to Schedule 7 of track access contracts*

10. As set out in Network Rail's submission, any train operator that wishes to adopt PFM billing will need to issue an 'opt-in' notice and also agree changes with Network Rail to Schedule 7 of their track access contract.

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<sup>1</sup> Chapter 16, Final determination of Network Rail's outputs and funding for 2014-19, October 2013, available [here](#).

11. We agree with the proposal by Network Rail that such applications to us for approval and consent should not require separate industry consultation (i.e. on a section 22 application). This is on the basis that the drafting of the proposed Schedule 7 amendments and the principle of how PFM billing is to be implemented has already been consulted on. An obligation for further consultation on these issues would be duplicative and add little value.

12. However, if a party wished to depart materially from the standard Schedule 7 drafting for PFM, we would expect that to be subject to appropriate industry consultation.

13. Where an informal submission is made to us for approval under section 22 of the Railways Act 1993 to amend Schedule 7 to apply the PFM provisions, we will not require a 'Form P' application form to be submitted. Instead, Network Rail and the train operator should provide the draft supplemental agreement for review along with a covering letter that they have both signed.

#### *Process for requesting our consent to apply PFM Rates*

14. Under the PFM contractual framework, after a train operator has opted-in to PFM and specified the fleets to be subject to PFM billing (and these fleets have met the 'Qualification Threshold' of being at least 20% metered)<sup>2</sup>, Network Rail will calculate the PFM Rates using metered data from 13 previous consecutive periods. It will then give the train operator 28 days in which to dispute the calculation of the rates. Where there is no dispute, Network Rail will then submit the rates to us for our consent. The rates will then apply for 13 periods, before being updated for each subsequent year. The process then repeats, with the recalculation of the PFM Rates and ORR's consent being requested.

#### *Managing the risk of gaming*

15. During the industry discussions on the development of the PFM framework, a concern was raised about the potential for gaming by a PFM train operator. That is, the risk that a train operator seeks to gain financially by only opting-in partially metered fleets for which the PFM Rate is less than the existing modelled consumption rate, and not those where the PFM Rate is higher than the modelled consumption rate. This would impact on third party train operators in the volume reconciliation (wash-up). TESSG's 2015 policy document on PFM (which informed the design of the contractual framework) was mindful of this. It expected that, once a train operator has opted in to PFM, where any of the train operator's partially metered fleets subsequently meet the Qualification Threshold, that fleet would be given a PFM Rate.

16. We support the principle that each partially metered fleet that meets the Qualification Threshold should be given a PFM Rate. This applies immediately following a

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<sup>2</sup> Each 'PFM Fleet' corresponds to a type of rolling stock and a specific train service code.

train operator opting in to PFM, and in subsequent years, where the rates are updated. If, after initial opt-in, additional fleets meet the Qualification Threshold, we would expect these to be opted-in by the train operator. We expect Network Rail and the train operator to keep under review the fleets that have met the Qualification Threshold, so that these are opted in timeously each year alongside the recalculation of existing PFM rates.

17. When Network Rail seeks our consent to PFM Rates, we will expect it to advise us whether all the PFM Fleets that have met the Qualification Threshold have been allocated a PFM Rate (and been opted-in by the train operator). We will want to understand the train operator's justification where this is not the case. We would not expect to give our consent if we are not satisfied that there is a good reason for this.

18. TEGS will be monitoring the effectiveness of the PFM framework in due course. This may lead to proposals for modifications to the TERs if there are any issues. While it remains for Network Rail and train operators to propose changes to the TERs, we have a reserved unilateral right to amend the TERs. Should an issue with gaming arise that could affect a third party, we would consider requiring changes to address this if necessary. However, the threat of such a change should be sufficient to mitigate this risk.

19. As well as expecting Network Rail to advise us whether all PFM Fleets that could be opted-in have been opted-in, we will also need the underpinning calculations and spreadsheets to be submitted to us with any request for consent.

20. We will be amending our criteria and procedures document in due course to cover applications for PFM Rates and our expectations for these.

#### **Administration**

21. Copies of this letter and the consent notice will be placed on the ORR website.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Michael Albon', written over a horizontal line.

**Michael Albon**