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25 April 2008

Dear Neil,

**APPEAL UNDER REGULATION 29 OF THE RAILWAYS INFRASTRUCTURE (ACCESS AND MANAGEMENT) REGULATIONS 2005 – RAIL FREIGHT CHARGING SYSTEM AND LEVEL OF ACCESS CHARGES FOR THE HIGH SPEED 1 RAILWAY**

Thank you for your letter dated 4 April 2008 on the above matter and for arranging the subsequent meeting at your offices on 14 April 2008 to enable English Welsh & Scottish Railway Limited ('EWS') explain to the Office of Rail Regulation ('ORR') the circumstances surrounding its appeal dated 25 March 2008. I also thank you for your letter dated 17 April 2008 allowing EWS an extension of a week to respond to the contents of your 4 April 2008 letter.

The purpose of this letter is:

- to confirm the matters set out in regulation 29(2) of the Railways Infrastructure (Access and Management) Regulations 2005 ('the Regulations') upon which EWS's appeal is based; and
- to supply further supporting information that EWS wishes ORR to take into account when considering the appeal.

**1. Matters upon which EWS's appeal is based and other related information**

1.1. EWS's appeal concerns the High Speed 1 Railway ('HS1') and is made pursuant to regulation 29 of the Regulations and in particular the matters set out in:

- regulation 29(2)(d) '*the charging scheme and charging system established in accordance with regulation 12*'; and
- regulation 29(2)(e) '*the level or structure of infrastructure fees, the principles of which are prescribed in Part 4 and Schedule 3, which it is, or may be, required to pay*'.

1.2. EWS made its appeal because it feels aggrieved and frustrated that after discussing the issue of the charging system and the level of charges in respect of

<http://www.ews-railway.co.uk>

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rail freight on HS1 with Network Rail (CTRL) Ltd ('NR (CTRL)') and the routes owners since 2006, it is still no further forward in obtaining certainty and visibility on what the charges for rail freight will be and whether or not they will be affordable.

- EWS understands that the infrastructure manager, allocation body and charging body is:

Network Rail (CTRL) Limited.  
40 Melton Street  
London NW1 2EE

- EWS understands that the owners of HS1 are:

in respect of Section 1 (Cheriton to Southfleet Junction/Fawkham Junction);

CTRL (UK) Limited.  
3<sup>rd</sup> Floor  
183 Eversholt Street  
London NW1 1AY

and in respect of Section 2 (Southfleet Junction/Fawkham Junction to St Pancras International);

Union (Railways) North Limited  
3<sup>rd</sup> Floor  
183 Eversholt Street  
London NW1 1AY

1.3. EWS also understands that for the purposes of regulation 12 of the Regulations, the Secretary of State is responsible for establishing the charging framework for HS1.

## ***2. Other Information EWS wishes ORR to take into account when considering the appeal***

### *Background*

2.1. EWS is rapidly developing its plans to facilitate a substantial increase in the operation of Trans-European rail freight services to and from the UK through the Channel Tunnel. The announcement made by EWS on 22 November 2007 regarding the launch of an integrated network of intermodal services between Belgium, Germany, Italy and the UK was the first step towards this goal. HS1 provides a European high-gauge route into the United Kingdom, which will

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encourage modal shift from road to rail in line with UK Government and European Union policy and in furtherance of a sustainable freight transport system.

2.2. Before EWS could operate rail freight services on HS1, however, it will need to undertake and complete essential modification work to its relevant locomotive and wagon fleets to make them compatible with the operating systems used on HS1. These modifications represent a substantial investment and given the time it will take to complete the project design, development and fitment programme, the decision by EWS on whether or not to proceed should have been made a long time before now. However, this decision is being delayed because EWS currently has no confidence that the access charges for rail freight services on HS1 will be affordable due to the lack of a proper charging system and an affordable level of infrastructure fees.

#### *Chronology of relevant events and supporting information*

2.3. A chronology of relevant events with supporting information is contained in Annex 1.

### **3. Subject matter for the appeal**

3.1. Since 2006 EWS has had many meetings with NR (CTRL) and the route owners regarding EWS's concerns over the charging system and level of charges for rail freight on HS1 and has entered into much correspondence on the subject (see Annex 1). This includes expressing its concerns and aggravation in response to the route owners' consultation process on its prospective statement of the levels and principles of access charging for HS1.

3.2. This dialogue and correspondence culminated in a joint meeting between senior members of the owners of HS1, EWS and the Department for Transport ('DfT') on 14 January 2008 where it was agreed, amongst other things, that the owners of HS1 would send to EWS and DfT a programme outlining the work they are doing to assess what the level (or levels) of the charges for rail freight should be.

3.3. Now more than three months after that meeting, EWS is no further forward in obtaining confidence that charges for rail freight on HS1 will be affordable. The owners of HS1 have recently informed EWS of the terms upon which they have engaged consultants to undertake a freight study to determine the strategy and appropriate charging for rail freight. This work is not expected to be submitted to DfT until the end of April 2008 and then some time after that a consultation document will be issued to interested parties on the conclusions.

3.4. EWS feels aggrieved and frustrated that it still has no certainty or visibility of a proper charging system for rail freight on HS1 or what level the charges will be. This is particularly unsatisfactory given the considerable amount of time the issue of the charging system and level of charges for rail freight on HS1 has been

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discussed, and given that there is no indication of when the route owners' further consultation document will be issued and, more importantly, when the actual charges for rail freight on HS1 will be published.

3.5. Whilst EWS remains committed to developing a rail freight option for HS1, it cannot proceed with its planning and investment decisions, which includes securing EU Marco Polo funding, until it is confident that charges for rail freight using HS1 will be affordable. As EWS considers that there continues to be no proper charging system in place for rail freight using HS1 that meets the requirements of Part 4 and Schedule 3 to the Regulations, this confidence is severely lacking. Furthermore, it appears clear that the uncertainty caused by the lack of a proper charging system and robust level of charges will continue for some considerable amount of time yet.

3.6. This is unacceptable and is severely affecting EWS's ability to plan its future business with a reasonable degree of certainty. This is why on 25 March 2008, EWS decided that it had no other option but to lodge an appeal to ORR pursuant to regulation 29 of the Regulations.

**3.7. EWS requests ORR to investigate these matters with a view to directing those responsible to establish and publish a proper charging scheme and charging system for rail freight services using HS1 in accordance with Part 4 of the Regulations along with a level of infrastructure fees that meet the requirements of Part 4 and Schedule 3 of the Regulations.**

3.8. EWS understands there are proposed to be three elements to the charging system for rail freight on HS1 for the use of infrastructure. These comprise a usage charge, a 'mark-up' on the usage charge and an investment recovery charge. EWS sets out below its concerns over each of these elements in turn along with it requests ORR to determine:

#### *Usage Charge*

3.9. EWS understands that the freight usage charges for HS1 have been proposed to be at a level that is 80-90% higher than the average levied on the UK domestic network. Rail freight will not be able to afford usage charges that are almost twice those levied by Network Rail Infrastructure Limited, which are already amongst the highest in Western Europe. EWS fails to understand why rail freight usage charges for HS1 are proposed at such a high level. In this regard, EWS has sought supporting information from NR (CTRL) concerning the charging model for HS1. Whilst some of the information asked for has been supplied (see Annex 1) some has not yet been released. Without full information, it is difficult for EWS to ascertain for itself whether or not the usage charges have been set in accordance with the relevant provisions of Part 4 and Schedule 3 to the Regulations.

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**3.10. EWS requests ORR to determine whether the usage charges for rail freight using HS1 have been set at the cost that is directly incurred as a result of operating such services.**

*Usage Charge – ‘Mark Up’*

3.11. EWS understands that, as currently proposed, a ‘mark-up’ of 10% is to be applied to usage charges for rail freight on HS1. EWS also understands that this 10% ‘mark-up’ is a notional figure and that the owners of HS1 are currently undertaking a market analysis to assess whether or not a ‘mark up’ can be justified and, if so, at what level it should be set. Whatever the outcome of this further analysis, if rail freight cannot afford to pay for the basic level of usage charges, which is almost twice that it pays for use of the UK domestic network, it would not be able to afford a further ‘mark-up’ in addition.

3.12. Furthermore, EWS notes that both Eurotunnel and Network Rail (i.e. the adjacent infrastructure managers to HS 1) do not levy a ‘mark-up’ and whilst EWS acknowledges that the principle of a ‘mark up’ is permitted by the Regulations (sub-paragraph 2(1) of Schedule 3 refers), its effect should not be to exclude market segments that can pay at least the cost that is directly incurred as a result of operating the service (sub-paragraph 2(2) of Schedule 3 to the Regulations refers).

3.13. EWS also understands that ORR took account of this when forming its view in its document entitled ‘*Periodic Review 2008, Consultation on Caps for Freight Track Access Charges*’ that international rail freight could not afford to pay a ‘mark-up’. This view, of course, was expressed in the context of Network Rail’s usage charges which, as EWS has highlighted above, are already at a level which is almost 50% of those proposed for HS1.

**3.14. EWS requests ORR to determine that a ‘mark-up’ on usage charges is inappropriate for rail freight using HS1. Alternatively, if ORR considers that a ‘mark up’ is appropriate it is asked to determine which market segments can afford to bear a ‘mark up’ along with a suitable value for such a charge.**

*Investment Recovery Charge*

3.15. Given the comments made above in respect of the un-affordability of both the usage charges and the ‘mark-up’ on usage charges, EWS is further concerned that rail freight should also be subject to a further charge designed to recover investment. EWS considers that this further charge should not be levied if its effect would be to exclude the use of infrastructure by market segments which can pay at least the cost that is directly incurred as a result of operating the service. EWS considers that the proposed investment recovery charge will have such an effect and, therefore, submits that it should not be levied on rail freight using HS1.

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3.16. EWS does, however, note that the Regulations provide a mechanism for the recovery of investment in new railway infrastructure by which higher access charges may be set on the long-term costs of the project. However, it is important to recognise that this mechanism is an exception to the basic charging principle established by the Directive (i.e. charges set at the cost that is directly incurred as a result of operating the train service). Paragraph 3(2) of Schedule 3 to the Regulations provides that an infrastructure manager may only set higher charges on the basis of the long-term costs of a specific investment project where:

(a) the effect of the higher charges must be to increase the efficiency and cost effectiveness of the project; and

(b) the project could not otherwise have been undertaken without the prospect of such higher charges.

3.17. EWS believes that an investment recovery charge levied on freight would not satisfy either of these pre-conditions. In respect of sub-paragraph 3(2)(a), EWS considers that this does not apply to freight on HS1 and in respect of sub-paragraph 3(2)(b), EWS considers that there would need to be evidence to indicate that the project could not have been undertaken without the prospect of the higher charges for freight. EWS, therefore, submits that the relevant legislation reinforces EWS's view that the investment recovery charge should not be levied on freight services.

***3.18. EWS requests ORR to determine that an investment recovery charge is inappropriate for rail freight using HS1.***

Please let me know if you require any further information or clarification.

Yours sincerely

***Nigel Oatway  
Access Manager***

**Annex 1**

*Chronology of relevant events and supporting information*

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2006 - EWS became concerned over the lack of a charging system and tariff of charges for rail freight using HS1 but had hoped that these issues would be clarified in the Network Statement for HS1.

20 November 2006 - NR (CTRL) issued the HS1 Network Statement which was to take effect from 27 November 2006 (see attachment 1). Upon examination, not only were there no charges for rail freight specified in the document, EWS was also concerned over a number of other aspects relating to the charging system.

11 January 2007 - EWS responded to NR (CTRL) with its comments on the entirety of the Network Statement including its concerns and disappointment that it was no nearer to understanding the level and structure of rail freight charges on HS1 (see attachment 2).

2 February 2007 - NR (CTRL) replied to EWS's 11 January 2007 letter. NR (CTRL) thanked EWS for its comments which it was still considering and stated that it would respond in detail on the issues that EWS had raised on the HS1 Network Statement in the near future (see attachment 3).

January to March 2007 - EWS had meetings with NR (CTRL) Limited on 29 January, 19 February and 20 March 2007 to discuss a range of issues concerning HS1, including the putting in place of a long-term framework agreement for the operation of rail freight services. As can be seen from the draft Heads of Terms for this agreement (see attachment 4), NR (CTRL) informed EWS that it was still reviewing its freight charging regime so was still unable to provide any further information at that stage. In addition, the notes of the EWS/NR (CTRL) 29 January 2007 meeting also show that discussions concerning the charging regime took place (see attachment 5).

2 March 2007 - As it was now over three months since the issue of the HS1 Network Statement, EWS wrote a further letter to NR (CTRL) expressing its continuing concern and disappointment that there was still no visibility of the charges NR(CTRL) proposes to levy on freight services using HS1 (see attachment 6).

w/c 5 March 2007 - NR (CTRL) gave a presentation to Rail Freight Group members on its proposed charging regime for rail freight services using HS1 (see attachment 7). At this presentation, NR (CTRL) advised that its usage charges for a typical rail freight service would be more than twice the amount levied by Network Rail on the UK domestic network (i.e. £9 per mile compared to £4 per mile). In addition, NR (CTRL) advised that it was in the process of determining a suitable 'mark-up' on the rail freight usage charge.

14 March 2007 - EWS received an e-mail from NR (CTRL) containing its responses to certain questions posed at the RFG presentation the previous week. Attached to the e-mail was further information concerning the inputs used in its

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charging model along with a tariff of HS1 usage charges for rail freight (see attachment 8).

*26 March 2007* - EWS received a letter from NR (CTRL) concerning its proposals for a 'mark-up' to the rail freight usage charges for HS1 (see attachment 9). NR (CTRL) proposed that there should be a nominal 10% 'mark-up' on the usage charge for night-time operations until December 2009 when, by then, it may be in a position to realistically assess a rate of return that the market can bear. No 'mark-up' was provided for daytime operations as this had yet to be determined.

*20 April 2007* - EWS responded to NR (CTRL) with its comments on the proposals for a 'mark-up'. In summary, EWS considered that NR (CTRL) was not entitled to levy a 'mark-up' on freight traffic with the possible exception of ESI coal or spent nuclear fuel as it had not demonstrated that its proposals met the requirements of paragraph 2(1) of Schedule 3 to the Regulations (see attachment 10).

*24 April 2007* - EWS responded to NR (CTRL)'s 14 March 2007 e-mail expressing its concerns that the usage charges seemed excessive as they appeared to be around 80%-90% higher than those levied on the UK domestic network. To aid its understanding, EWS requested further information about the charging model (see attachment 11).

*April to September 2007* - EWS had further meetings with NR (CTRL) on 24 April and 12 September 2007 to continue discussion of the various issues concerning HS1.

*1 June 2007* - NR (CTRL) responded to EWS's comments on its 'mark-up' proposals stating that it considered its 10% 'mark up' to be reasonable, transparent, non-discriminatory and efficient when compared to adjacent infrastructure managers,. NR (CTRL) also confirmed that the 10% would also apply to daytime rail freight operations (see attachment 12).

*17 September 2007* - NR (CTRL) responded to EWS's 24 April 2007 letter. Whilst NR (CTRL) had provided answers to most of EWS's questions, it indicated that it was not prepared to share certain information at that stage (see attachment 13)

*25 October 2007* - CTRL (UK) & Union Railways (North), the owners of HS1, issued a consultation document regarding their joint prospective statement of the levels and principles of access charging for HS1 in advance of the formal Network Statement consultation by NR (CTRL). Again there was no real detail on the charging system or level of charges for rail freight services. The document merely restated that the charging basis for freight services needed to reflect the obligation in the 2005 Rail Regulations to ensure the competitiveness of international rail freight. Accordingly, it is proposed that access charges for rail freight services will be limited to a recovery of an equitable apportionment of

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operating, maintenance and renewals costs plus a margin which is currently subject to discussion with the rail freight industry (see attachment 14).

*26 October 2007* - Department for Transport ('DfT') issued a consultation letter concerning a proposal for the owners of HS1 to levy an infrastructure recovery charge on both passenger and freight operations. However, the document stated that the investment recovery charge for passenger services is unlikely to be appropriate for freight services, but government believes that a lower investment recovery charge for freight services may be viable, and would permit the owner of HS1 to set such a charge. It was also suggested that to ensure investment returns were maintained at appropriate levels, the level of the investment recovery charge could rise and fall depending upon usage (see attachment 15).

*26 October 2007* - EWS responds to NR (CTRL)'s letters dated 1 June and 17 September 2007 concerning the infrastructure costing model and the 'mark up' on usage charges. As well as making detailed points, EWS stressed that it remained committed to developing a rail freight option for HS1 but could only continue to do so if it was confident that track access charges will be affordable. As it had now been provisionally allocated Marco Polo funding from the EU to assist its investment in the necessary vehicle modifications and testing required to obtain the appropriate safety and operational clearances, it was keen to engage in joint discussions with NR (CTRL), the owners of HS1 and DfT as soon as possible (see attachment 16).

*23 November 2007* - EWS wrote to DfT expressing its continued concerns in respect of the charging regime and level of charges for rail freight on HS1. EWS set out its concerns and stated that before it considered its option to pursue an appeal under the Regulations, it believed there was value in having joint discussions with DfT, NR (CTRL) and the owners of HS1 to see if its concerns could be addressed in order for its plans and investment decisions to develop rail freight services on HS1 to continue in earnest (see attachment 17).

*21 December 2007* - EWS responded to DfT's consultation on the proposed investment recovery charge. EWS stressed that it was already seriously concerned over the un-affordability of the usage charges along with the 'mark-up' on those usage charges let alone the introduction of yet another charge for rail freight. EWS set out its reasons why it considered that the levying of an investment recovery charge on rail freight would not meet the requirements of Schedule 3 to the Regulations. It also set out its belief that such a charge, in any case, were it to rise and fall would not allow rail freight operators on HS1 to continue to plan their businesses with a reasonable degree of assurance. EWS again stressed its keenness to engage in joint discussions with DfT and the other relevant parties as soon as possible (see attachment 18).

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*21 December 2007* - EWS responded to the consultation by the route owners on their joint prospective statement of the levels and principles of access charging for HS1. EWS repeated its concerns over the three proposed charging elements (i.e. usage charge, 'mark-up' and investment recovery charge') and its consideration that the latter two elements did not conform to the provisions of Schedule 3 to the Regulations. Again joint discussions were requested as soon as possible (see attachment 19).

*14 January 2008* - A joint discussion on EWS's concerns regarding the charging system and level of charges for rail freight on HS1 was held between EWS, DfT and the owners of HS1. EWS explained its concerns over the usage charge, which appeared too high compared to those applying to Network Rail's UK domestic network, the usage charge 'mark-up' which appeared not to be based on any research into what the rail freight market could bear and the investment recovery charge which it considered should not be levied on rail freight at all. It also stressed that the totality of the charges were in any case unaffordable. The route owners stressed that it was keen to accommodate rail freight on HS1 but charges had to be set at a commercial rate which could be different for each market segment. The route owners also outlined the work they were undertaking to assess what level (or levels) the charge should be and once this work was complete, sometime after March 2008, proposals would go to the industry for consultation. With a view to speeding up EWS's ability to obtain a price for access to HS1, EWS undertook to provide the route owners with an indication of those market segments in which EWS intends to operate services on HS1. In return, the route owners undertook to provide to EWS and DfT a programme outlining the work they were carrying out along with timescales for completion.

*17 January 2008* - EWS received a letter from DfT confirming the actions arising from the 14 January 2008 meeting (see attachment 20).

*25 January 2008* - EWS wrote to DfT on 25 January 2008 setting out its view as to the nature and jurisdiction of the appeal process open to EWS under the Regulations as a difference of opinion had arisen on this issue at the 14 January 2008 meeting (see attachment 21).

*12 February 2008* - EWS wrote to the owners of HS1 with its list of market segments it undertook to provide at the 14 January 2008 meeting (see attachment 22).

*13 February 2008* - EWS received an e-mail acknowledgement of EWS's 12 February 2008 letter from the owners of HS1. The e-mail also indicated that the information had been passed on to Intermodality who had been engaged to conduct a study into rail freight segmentation and charging (see attachment 23).

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*18 March 2008* - EWS received an e-mail from the route owners containing a proposal for a freight study they were conducting to determine the strategy and appropriate charging for rail freight on HS1. The owners of HS1 indicated that the final report would be delivered by the end of March 2008 which they would then consider to inform their own Final Draft Report for submission to DfT by end of April 2008. The report would then be written up and form part of the route owners' 2<sup>nd</sup> prospective consultation paper (see attachment 24).

*25 March 2008* - EWS submitted its letter of appeal concerning the charging system and level of charges for rail freight on HS1 to ORR pursuant to regulation 29 of the Regulations (see attachment 25).

End.