Structure of Charges Review

Phase 3 Consultation – November 2021

Structure of Charges Review – Phase 3 Consultation

1. Background

HS1 Ltd has the 30-year concession from the Secretary of State (SoS) to own, operate and maintain High Speed 1 (HS1), the UK's only high-speed railway, as well as the stations along the route: St Pancras International, Stratford International, Ebbsfleet International and Ashford International. As asset steward HS1 is expected to determine the long-term renewals and enhancements required on the HS1 assets and is subject to economic regulation by the Department for Transport (DfT) and the Office of Rail and Road (ORR).

Network Rail (High Speed) is our contractor for maintaining and operating the railway infrastructure and three of our stations, St Pancras International, Stratford International and Ebbsfleet International. HS1 Ltd's railway infrastructure has physical connections with Eurotunnel, the DBS freight depot at Dollands Moor and the Network Rail classic railway at Ashford, Ebbsfleet, Ripple Lane and domestic lines north of London.

The train companies currently operating on HS1 are Eurostar, who operate the international train services to Europe and Southeast Trains Limited (SETL), who operate domestic services to Kent. East Midlands Railway and Thameslink are also serviced by HS1.

DB Cargo operate freight services on the HS1 route. DB Cargo, Direct Rail Services (DRS), Freightliner and GB Railfreight operate freight services utilising the Ripple Lane Exchange sidings which is currently part of the HS1 asset.

As we set out in our initial consultation HS1 provides a direct "Green Gateway" rail link to Europe so a key strategic aim from this structure of charges review is to encourage greater network usage to both lower costs overall as well as promoting the sustainability of rail in the longer term. These aims need to be balanced with the certainties the concession structure provides which is the basis of the private sectors acquisition of the asset.

Since the initial consultation closed, we have reviewed the constructive and detailed responses from our key stakeholders. A summary of which is included in Annex A.

HS1 has also concluded its review of approaches adopted by other infrastructure managers to identify potential opportunities for reform within the context of the current contractual and regulatory framework. We have also worked with NR(HS) to understand in more detail the relationship between their direct and indirect costs, as well as take forward work to better understand the impact different trains have on the network.

The proposal in this consultation document is based on a combination of this work and is set out to inform stakeholders of HS1's proposed next steps and scope of work – the majority of which will feed into our work for PR24. Given the broad set of stakeholders that use the HS1 asset and the role of the DfT and the SoS in public policy decisions relating to rail infrastructure **HS1 has focussed this paper on matters where it has the direct ability to take decisions.** In several areas, we have identified issues that would require a change in approach from DfT and collaboration across a few parties in the HS1 system. It is not possible for HS1 to take these forward (for example renewals and Thameslink Box)– and at this stage these matters are not being taken forward. We look forward to working with our customers to prepare for and manage processes that require decisions by DfT as part of the PR24 process.

2. How are we undertaking the review and consulting stakeholders?

We set out our plans to conduct the review in 4 phases as set out below.

Phase 1 and 2 of the review are now largely complete and this document sets out HS1 response and proposed next steps. This document comprises Phase 3 and sets out options which will form part of the PR24 process as well as bringing forward a series of immediate actions in 2022 which will feed into that process.

- Phase 1, initial consultation: We are launching the review with **this initial consultation** to set the scene for the review and seek early views on the issues that stakeholders believe are important. **[COMPLETE]**
- Phase 2, optioneering: We will hold workshops or meetings with stakeholders and develop options for changes to the charging regime. We anticipate that this will take place from July to October. **[COMPLETE]**
- Phase 3, consultation on proposals: We aim to issue a second consultation in November 2021. It will set out the findings from the optioneering discussions, put forward proposals and seek stakeholder views on the proposals. **[THIS DOCUMENT]**
- Phase 4, conclusions: We aim to issue conclusions to the review by February 2022 and commence a charging model rebuild, some contractual amendments if required and feed into preparations for PR24. **[ON TRACK]**

3. Current charging regime

As we set out in the initial consultation HS1 Ltd's charging framework was established in 2009 by the DfT in the Concession Agreement. Under the framework, track access charges and station charges are levied on passenger train operators (TOCs) and Freight train operators (FOCs) that use the HS1 infrastructure. The charges are set to recover the costs that HS1 Ltd directly incurs in operating, maintaining and renewing HS1 and the long-term project costs incurred from the initial construction and long-term operation of HS1. There are 3 broad types of charge:

- Investment charges (long-term project costs from initial construction);
- Track access charges (ongoing operations, maintenance and renewal), and
- Station charges.

The following table provides a summary of the main charges currently levied by HS1 Ltd. The remainder of this paper sets out proposed changes to various elements of the regime consistent with the scope of the review.

Description of charge	Approx. annual value (£m)	Who sets the charge	Passenger (P), Freight (F)*
Investment Charges			
Investment Recovery Charge (IRC). This is a fixed charge to recover the initial capital cost of building HS1.	175	Concession Agreement with DfT	P
Additional Investment Recovery Charge (AIRC). To recover the cost of route enhancements. Currently the only enhancement is that for GSMR.	1	ORR	P
Track Access Charges			
Traction electricity charge. Actual costs are passed through to operators.	20	HS1 Ltd	PF
OMRCA1: for directly incurred operations, maintenance, and renewal (OMR) costs that vary with traffic.	14	ORR	PF
OMRCA2: for the avoidable long-term OMR costs on a long run incremental basis.	10	ORR	PF
OMRCB: to recover common long-term OMR costs.	56	ORR	P
OMRCC: to recover common pass-through costs that are outside of the control of HS1 Ltd	19	ORR	P
Station Charges			
Station Long Term Charge (LTC): to recover repair and renewal costs at the 4 stations.	9	DfT	P
Station qualifying expenditure (QX): for actual operating and maintenance costs at the 4 stations.	32	HS1 Ltd	P
Approx. total annual charges income assumed at PR19 (i.e. does not reflect the impact of the volume re-opener or actual revenue received during the pandemic)	£336m		

*References to freight in this table relate to conventional freight services. High-speed freight services do not currently operate on HS1.

4. Investment Charges

The purpose of the IRC is to recover the initial construction costs of HS1.

IRC is charged based on chargeable journey time on HS1: the chargeable journey time excludes time for stopping at stations. IRC is paid quarterly in advance. There are adjustments for additional services operated as a result of subsequent spot bids and services which could not be operated for certain reasons e.g. cancellation by HS1. IRC is capped at £69.57 per minute per train, in February 2009 prices. The cap is indexed every 6 months by RPI, and at February 2020 prices is £96.09 per minute per train. The IRC cap and indexation were set in the HS1 Concession Agreement and are not subject to review. HS1 is permitted to discount below the IRC cap: the HS1 discount policy and the IRC discount schemes currently in operation are described in the HS1 Network Statement[1]. With the exception of these discounts the IRC charge is currently set at the cap for both domestic and international passenger services. Traditional freight services are not charged IRC.

As set out in the initial consultation IRC itself is not part of the scope of this review. However, as part of the review HS1 looked at how discount schemes have been applied by other infrastructure managers, particularly in Europe to consider what options there may be moving forward. We used external review to validate and support our findings.

Like HS1, DB Netze, SNCF Réseau, Eurotunnel and Network Rail (amongst others) all apply financial discounts to facilitate new services. The key distinction is that discounts must be linked to new services that can be identified as such – and not for services that may have ceased and are seeking to be re-run. Further – new services are not considered those which are delivering incremental growth on existing routes.

[1] Network Statement: https://highspeed1.co.uk/media/x31jse0d/hs1-network-statement-2021-final-26-may-2020.pdf

There was a mix of discount types – some being time limited (as with HS1's discount policy) with others being more permanent in nature. The review confirmsthat longer term discounts are typically associated with state owned infrastructure managers.

Typically, HS1 discounts are significant with up to 75% reductions in IRC on a time limited basis and this was generally better or in line with discounts offered by other infrastructure managers. Although the take-up of discounts by operators is not as easy to identify it appears that the take up of discounts is relatively low. Specific to HS1 it was noted that there are no formal growth discount processes in Belgium and the Netherlands. This is for a variety of reasons including existing congestion on routes and that incentives can be provided by changes to the mark-ups applied to track access charges. This highlights that the effectiveness of overall discounts HS1 can provide and the impact this will have on route economics generally, particularly on new routes is significantly influenced by other parts of the network,

Having said that, although discounts are traditionally only offered for 'new routes' there is an opportunity as we recover from the pandemic to consider how discounts can be used to incentivise the recovery for pre-existing services and we welcome proposals from operators on how HS1 might take this forward with you.

With this is mind HS1 does not propose amendments to the HS1 Discount Policy currently other than the inclusion of discounts for Highspeed freight – noting we have been working with both our major operators to consider discounts in the last two years. We would welcome applications for discounts on new routes, and to discuss how discounts might be applied to incentivise recovery on existing routes that are considerably underutilised. We are happy to discuss how the application for, and execution of discounts through the process can be made as seamless as possible for our operators.

5. Route Specified Upgrades and ERTMS

Specified upgrades, also known as enhancements, are funded on HS1 via an Additional Investment Recovery Charge (AIRC). HS1 currently levies and AIRC to recover the costs of a specified upgrade to the GSM-R network that enables amongst other things – in cab signalling.

As part of PR19 HS1 notes that a significant project would need to be brought forward during CP3 to replace the current signalling system which will become obsolete in the mid-2030s.

Given the obsolescence of the system HS1 believes the signalling upgrades – known as European Railway Traffic Management System (ERTMS) – should be treated as a renewal. HS1 has well established processes linked to the renewals project lifecycle to oversee the delivery of projects of this type.

The ORR determined ERTMS would be a specified upgrade to the HS1 assets because it would bring significant additional benefits even though it is the only feasible replacement for the signalling system. As a result of the ORR decision this means HS1 must now commence a process to set up and recover an AIRC – to commence basic planning and design work for the project.

Operators noted in PR19 they were concerned that the approach to forcing them to fund ERTMS was highly discriminatory. It was noted that HS1 would likely be the only asset on the continent or the United Kingdom where operators would be directly charged for its implementation. Whether or not ERTMS is a specified upgrade or renewal on HS1 would not change the need for operators to fund the activity.

HS1 is sympathetic to operator concerns and have raised these at the highest levels within ORR and the DfT who have reiterated that ERTMS should be treated as a specified upgrade.

The practical implication of this decision is that HS1 must now bring forward a specified upgrade proposal for the implementation of ERTMS. HS1 will need to break the applications down into funding applications linked to the project lifecycle. As an example, it would be impossible for HS1 to bring forward a full funding application for the project (which would be for up to £150 million) given the level of maturity we are at. Instead, we must bring forward an AIRC application to fund early design activities to feed into the preparation of full funding applications.

We are therefore taking forward two activities to ensure we remain compliant with our asset stewardship obligations under the HS1 concession:

1. **Bring forward the principles to support an initial Specified Upgrade proposal for ERTMS design activities for consideration by operators, DfT and the ORR; and**

2. **Commence high level dialogue with the DfT and the ORR on the longer-term funding of ERTMS which will need to be addressed as part of the next HS1 periodic review.**

6. Operations, Maintenance and Renewal (OMR) Charges

The purpose of OMR charges is to recover the operations, maintenance, and renewal costs for track assets (track, bridges, tunnels, signalling, earthworks, drainage, electrification, and telecommunications); station costs are recovered separately through station charges. The OMR charges are determined by the ORR at 5-yearly periodic reviews. The last review, PR19, covered Control Period 3 (CP3) and set charges for the 5 years from 2020/21 to 2024/25. The following section addresses several issues in relation to the structure of HS1 OMR Charges.

7. Renewals Costs

Under the HS1 Regulatory Framework HS1 must take a 40 year look ahead and plan for renewals required on the network. The Concession also notes HS1 must seek to recover these long-term costs.

How HS1 approaches this issue was a significant issue of debate during the PR19 process where the ORR determined that HS1 must seek to pre-fund renewals costs over a 40-year period. This approach means up to 28% of HS1's total OMR recovery is driven by recoveries for future renewals.

Eurostar noted its position was that renewals should not be funded 40 years in advance, and this is not a requirement of the concession. Such a cautious approach by the ORR is tying up large amounts of capital, with poor returns and is a significant barrier to capital funding which operators might otherwise use to invest and expand services. This is particularly more pressing given the impact of the pandemic.

HS1 and Eurostar have provided several alternative proposals to the treatment of renewals – all of which were rejected by the Office of Rail and Road.

HS1 has also offered holidays on escrow payments in the short term – however the issue for HS1 is that we cannot take the risk of underfunding escrow unilaterally without the full support of the DfT and ORR. HS1 would need assurance that it is not at risk for underfunding in the future. Under our asset stewardship obligations HS1 must ensure it delivers renewals and funds its long-term costs. Unless DfT and the ORR adopt a different approach HS1 will not unilaterally take forward renewals in a way that underfunds its escrow accounts.

HS1 was explored with DfT the potential to change the approach to renewals recovery. At this stage DfT is not seeking to change the current interpretation of a 40 year look ahead – pay ahead approach as set out by the ORR or to amend the Concession Agreement to provide greater clarity on the issue. DfT and HS1 are looking to review the Escrow Investment Strategy.

HS1 cannot take a decision is isolation because the potential remains that it is held at risk for underfunding of the escrow account that funds renewals or there is a degradation in the standard of the asset against its asset stewardship obligations – particularly at handback at the end of the concession, if insufficient funds are recovered to deliver renewals. For these reasons HS1 cannot take forward a different approach to renewals at this time.

8. Split between direct and indirect charges.

The Railways (Access, Management and Licensing of Railway Undertakings) Regulations 2016 (the "2016 Railway Regulations") requires HS1 to set access charges at the cost that is directly incurred as a result of operating train services (a rule often referred to as the "Charging Principle"). There are two exceptions to the Charging Principle, the first being a mark-up the market can bear (which is not presently applied by HS1) and the second being higher charges set on the basis of the long-term costs of HS1 (the "Long-term Project Costs Exception").

HS1 levies IRC on the basis of the Long-Term Project Costs Exception – i.e. the long-term construction costs of HS1.

HS1 levies OMRC on the basis of:

1. The Charging Principle in respect of direct costs – i.e. those costs that are directly incurred because of running trains on the network and relate to the wear and tear caused by traffic. These costs mainly apply to rail maintenance and renewal.

2. The Long-Term Project Costs Exception in respect of indirect costs – i.e. the long-term costs of the operational phase of HS1 incurred in order to meet the performance standards, asset condition and hand back condition of HS1 required by the Concession Agreement. These are the costs that are incurred because of

having the track assets and maintaining them in a serviceable condition as they gradually degrade with age, weather, or obsolescence. We refer to these as Avoidable Long-Term Costs ("OMRCA2") and Common Long-Term Costs ("OMRCB") in the HS1 Passenger Access Terms.

There are two main elements that determine the split between direct and indirect charges. The first is understanding the specific impact of different trains on the network – largely determined by their speed and weight. The second is to more fully understand cost causation based on a detailed review of infrastructure manager activities.

In the consultation operators had different views on how HS1 should consider our approach.

LSER was supportive of an approach that ensured operators were accurately billed for the damage their trains do to the network.

Eurostar on the other hand questioned the accuracy and understanding of the data and noted that penalising heavier faster trains would likely impact international operators significantly as these types of trains were more efficient for running international services. Eurostar also noted that they would expect greater variability in HS1 charges because of the fall in volumes. HS1 notes that Eurostar only pays direct charges on trains that run. This means Eurostar has not been charged OMRCA1 on up to 15,000 paths that it otherwise might have paid demonstrating that the cost and liability faced by operators does flex significantly as traffic volumes change. The proposed actions in this review will ensure the evidence base to drive variable charges will be based on the best available evidence.

HS1 also notes it introduced several proposals, including the decommissioning of certain electrification assets at the start of the pandemic which were rejected by operators on the basis it could impact performance and that risk could not be accepted. There is a strong link between performance and cost which HS1 is seeking to demonstrate in greater detail as part of its CP4 activities.

To take things forward HS1 has been working with NR(HS) to assess the validity of HS1's current approach – whereby HS1 uses equivalent million gross tonne kms per annum (EMGTPA). This includes the funding of two research PhD positions as agreed though the HS1 Research and Development Panel using R&D Funds to take this forward. The results of this research will take time but our ambition is to feed emerging results into the ratios used in the HS1 charging model for PR24 and will be consulted on in detail with stakeholders at that time.

Separately as part of our CP3 Commitments HS1 has been working with NR(HS) on a detailed cost causation review to understand how each NR(HS) activity relates to direct costs. The following table sets out the results of that review and potential changes HS1 would seek to make to its structure of charges in the PR24 process. It is based on the NR(HS) cost stack determined by the ORR in CP3 and shows the direct / indirect split. It then shows amendments HS1 would seek to make for CP4.

NRHS COSTS		Direct /Indirect CP3	Direct /Indirect CP4
Payroll			
	Infrastructure	20/80	28/72
	Operations	0/100	No change
	Safety and Assurance	0/100	No change
	Managing Director	0/100	No change
	Services	0/100	No change
Contribution to National Function Services		0/100	0/100
Recoveries		0/100	36/64
Plant and Vehicles			
	Plant	0/100	15/85
	Vehicle Fleet	0/100	42/58
	Tamper	80/20	100/0
	Plain Line Grinding	80/20	100/0
	S&C Grinding	80/20	100/0
	Track Recording	0/100	100/0
	Infrastructure Freight Haulage	100/0	No Change
Specialist Contractors		20/80	17/83
Materials		0/100	22/78
Security of Infrastructure		0/100	No change
Consultancy and Fees		0/100	No change
Other		0/100	5/95
Enhanced Maintenance		0/100	14/86

These splits are based on the latest analysis by NR(HS) and reviewed by HS1. As part of the PR24 process this will be the subject of extension consultation and decision by the ORR. They are presented here to show the likely changes next control period.

9. Split between international and domestic operators AND

Split between freight and passenger charges.

HS1 has considered the split between operators and is content that the current approach, based on per train kilometre and per train minute shares on the infrastructure are still the fairest and most accurate way to allocate charges.

In the PR24 process HS1 will review the following splits of traffic to determine if the percentages used in the new charging model should be changed:

- percentage split of services to Ebbsfleet and Ashford by LSER; and

  percentage split of services by freight from Dollands Moor to Ripple Lane and Ashford to Ripple Lane.

10. Pass through costs

HS1 passes through several its costs such as through charges directly to operators – known as Pass Through Costs ("OMRCC"). OMRCC is levied on all operators and pertain to insurance, business rates and the cost of engineering controllers of the EMIS system that are beyond HS1's control. As part of CP3 HS1 noted it would review the costs included in OMRCC**. As part of PR24 we intend to expand the scope of OMRCC costs where HS1 has little opportunity to control those costs. We expect this to include items such as regulatory fees set by the ORR and RSSB and British Transport Police (BTP Costs) in OMRCC charges from CP4. This will give operators greater transparency in the costs imposed by key suppliers / regulators and allow HS1 to engage operators more directly as these charges are set.**

In addition, HS1 set out in the 5YAMS that we would exclude from OMRCC costs that might be incurred in relation to low value energy saving schemes until proposals were fully formed. We set out that we would seek to bring this forward during CP3. **HS1 will bring forward several proposals in the next 6 months to drive forward energy saving initiatives. We expect these projects to be low value and deliver positive financial benefits back to operators within 24 months.**

11. Other operators

As part of CP3 HS1 committed to looking at the treatment of Thameslink Box passenger on the basis a significant number of Govia Thames Railway (GTR) passengers use St Pancras International. Eurostar has raised this as an issue in its consultation response.

HS1 notes the decision to allocate costs in this manner is something that must be agreed with the DfT. At this stage DfT does not contemplate allocating costs to GTR for the use of St Pancras Station.

12. Other Incentives

As part of the review, we have considered other incentives to support growth and efficiency in several areas. This can split into four main areas:

- **use of IRC discounts:** as noted previously HS1 has reviewed its discount policy and is satisfied it is consistent with regulatory requirements and benchmarks against other infrastructure managers approaches, particularly in Europe. **Moving forward HS1 is committed to offering discounts to new routes on the network that are commercially sustainable over time and services which are considerably underutilised but as a private sector organisation will not permanently subsidise additional traffic which is a public policy matter for the government.**

- **contractual amendments:** Eurostar noted the difficulty it faces in booking a full First Working Timetable during periods of significant uncertainty as currently experienced through the pandemic. They have asked HS1 to consider options to alter the contractual provisions to protect the overall volume of firm rights whilst giving greater flexibility to change trains within that volume. **HS1 is happy to explore proposals for Eurostar in more detail moving forward but notes that this must be balanced against the firm rights exercised by other operators and will require a process to redraft the HS1 Passenger Access Terms (PAT) in full consultation with all parties including the ORR.**

- **changes to OMRC:** under the concession HS1 fully recovers its OMRC costs from operators. We have considered opportunities to introduce other charging categories to incentivise the efficient use of the assets including peak and off-peak charging and charges for long dwell times at stations. **Although there maybe opportunities to introduce amendments to OMRC charges in the future to encourage efficient use of the asset – given current capacity usage HS1 does not intend to introduce new charging categories at this time.**

- **environmental impact and operator efficiencies:** HS1 has taken strong steps to manage its carbon footprint including to purchase of 100% renewable energy to energise the network. At the same time HS1 has been able to deliver significant savings to operators with its energy purchasing strategy which has delivered significant savings. For example, the current market rate for power is over £150 per megawatts hour while HS1 purchasing has delivered rates at £50 megawatts per hour. For every £1 HS1 saves an operator this amounts to a saving of over £250,000 on HS1's overall energy costs.

    - HS1 has also been working closely with LSER to introduce regenerative braking and will be introducing metered billing on the network from next year. This will significantly improve our ability to assess operator electricity usage and more accurately align financial payments to use. HS1 encourages all our operators to move towards a metered billing approach moving forward. **Several contractual amendments to the HS1 passenger access terms will be brought forward to bring metered billing into effect.**

13. New Market Segments

Stakeholders supported the potential for new market segments on HS1 in addition to the current three – domestic, international and freight. Freight operators noted that the approach to charging of new freight market segments – such as Highspeed freight would be an important commercial consideration moving forward.

HS1 welcomes this support and will bring forward new market segments and indicative charges in its next Network Statement Consultation.

14. Station Enhancements Policy

HS1 welcomes stakeholder feedback on the Stations Enhancement Policy and the general support for taking the policy forward. There were several queries related to the definition of renewals versus enhancement along with greater detail on how the beneficiary principle would be applied in practise. HS1 reiterates that this is a high-level proposal for the HS1 Network Statement setting out the basis of the approach. The specifics of each proposal will be considered in detail and consulted on with stakeholders.

Stakeholders queried the difference between a renewal and an enhancement. As HS1 set out in the policy:

- **Renewal:** replacement of an existing asset with a like-for-like equivalent, or where technology has developed, the modern equivalent asset (including when the modern equivalent results in increased functionality relative to the asset being replaced).

- **Enhancement:** – Replacement of existing assets performed earlier in the lifecycle than strictly necessary (i.e. where the asset continues to perform but there are identified benefits in replacing it early); – Replacement of life-expired assets with new assets that provide significantly greater functionality than the modern equivalent; or – Introduction of new assets which results in a significant increase in functionality (e.g. capacity / output).

This is very much driven by the detail of the activity at hand and even then, there is often the potential for disagreement as evidenced by the ORR's approach to ERTMS (as an enhancement) which HS1 still believes should be treated as a renewal.

HS1 will commence consultation on its Network Statement which will include the Stations Enhancement Policy. At this stage HS1 will only make minor amendments to the policy based on current feedback from stakeholders but will address areas of detail as specific project are brough forward.

15. Freight Charges and Ripple Lane

We have considered the impact of freight as part of our work with NR(HS) to consider the split between direct and indirect charges. This means understanding whether the current approach using EMGTPA is supported by the evidence and if HS1 charges should be amended in CP4. This forms part of the scope of work noted above in relations to the split between direct and indirect costs.

A related issue for freight is the treatment of Ripple Lane charges which has been raised over a number of control periods. To operate and maintain Ripple Lane HS1 currently engages Network Rail through a management contract to deliver these services on our behalf. HS1 levies a regulated charge to recover these costs and then pass these through to freight based on volumes. As part of CP3 the ORR noted that stakeholders should consider the transfer of Ripple Lane to Network Rail who is already operating and maintaining the assets. **HS1 supports this approach and is working with Network Rail and the Department for Transport. However, as noted in CP3 the decision to transfer the asset is not within HS1's gift and will require an agreement between the ORR, DfT and Network Rail on how Ripple Lane costs should be managed.**

16. Research and Development Fund

HS1 undertook to consider its approach to Research and Development Funding as part of its CP3 Commitments. In CP3 – as part of HS1 costs we are recovering £2 million from operators to fund R&D activities. We noted that we would consider whether R&D should be considered as a renewal instead based on the ORR Determination.

During CP3 HS1 has set up a Research and Development Panel, including NR(HS) and operators to consider proposals. Governance for those activities is working well and we are monitoring expenditure closely.

HS1 has reviewed the decision and is content that R&D funding is treated as a renewal in the future. The detail of this treatment will need to be agreed with the ORR as part of PR24 – for example not treating these costs as part of the renewal's annuity so HS1 can ensure the correct allocation of costs to operators.

17. Contractual Amendments

Although major contractual amendments are not the primary focus of the review the impact of the pandemic has demonstrated that several amendments are required to the HS1 Passenger Access Terms (PAT) and Freight Access Terms (FAT). Eurostar has also noted several areas where they would like further flexibility which HS1 would like to explore.

HS1 will therefore bring forward amendments on the PAT / FAT for consultation in 2022 with a focus, amongst others, on:

- **amendments to clarify the approach to the volume re-opener process;**
- **amendments to bring into effect meter billing for traction power;**
- **amendments to clarify and improve the OMRC-C washup process; and**
- **an exploration of contractual requirements that lock Eurostar into a volume of firm rights in the First Working Timetable (FWT) but gives greater flexibility for Eurostar to amend specific paths within that volume to flex operations (noting they would not have firm rights to these amendments).**

18. Charging Model

A key CP3 commitment by HS1 was to rebuild the regulatory charging model. **We will begin this process in Spring 2022 and seek to share the model with stakeholders including the ORR as the PR24 process unfolds. The model will consider several of the proposed amendments set out in this document although the specific numbers and splits will be based on the best evidence available at the time.**

19. Summary of Next Steps with our proposals

The following section sets out a summary of our proposals and the actions we will take moving forward.

Item in Structure	Next Step
Investment Charges	Consider discount proposals for new and underutilised routes
AIRC	HS1 will bring forward a Specified Upgrade proposal for early design works on ERTMS.
Renewals Costs	Review of the Escrow Investment Strategy. HS1 is tied to the regulated approach to renewals and notes there does not appear to be a desire from DfT to consider the 40-year prefunding model at this time. This will need to be revisited as part of the PR24 process.
Pass Through Costs	HS1 will take forward proposals in CP4 to expand the scope of OMRCC charges to include a range of other supplier and regulator costs. HS1 will bring forward a number of small-scale energy efficiency proposals for consideration with operators that would be recovered through OMRCC.
Direct / Indirect Split	The splits used in CP3 will be subject to update in the PR24 process based on the methodology presented. The splits and analysis will be shared with stakeholders and consulted on at that time. HS1 will bring forward new EMGTPA calculations (if required) based on emerging evidence from our R&D activities
Split between operators	The current splits in the charging model reflect general traffic patterns. HS1 will continue to review the split between LSER services to Ebbsfleet and Ashford and Freight services patterns and provide updates in the PR24 process.
Other Operators	HS1 is no longer taking the Thameslink Box issue forward based on advice from the DfT.
Other Incentives	HS1 does not intend to introduce new incentive-based charges in CP3 or CP4. We are looking at potential contractual amendments to incentivise the booking of an FWT (see below).
New Market Segments	HS1 will bring forward new market segments in its next Network Statement Consultation and a list of indicative charges.
Stations Enhancement Policy	HS1 will bring forward its Station Enhancements Policy in the next Network Statement Consultation
Freight Charges and Ripple Lane	HS1 will bring forward new EMGTPA calculations (if required) based on emerging evidence from our R&D activities.

	HS1 continues to support DfT activity to transfer Ripple Lane to Network Rail but notes the decision is one to be agreed by DfT/ORR and NR.
Research and Development Fund	HS1 will bring forward an approach to R&D funding as part of CP4 based on approach that fairly allocates costs to different stakeholders. This will be considered in the charging model rebuild.
Contractual Amendments	HS1 will commence consultation on several amendments to the HS1 PAT/FAT in spring 2022
Charging Model	HS1 will commence its charging model rebuild in Spring 2022

Consultation response and timescale

This consultation closes on 14 January 2022. We would welcome your views on our proposed next steps and any specific comments you would like to add into:

- proposals for contractual reforms to the PAT / FAT and how this might be achieved;

- proposals to consider the rebuild of the HS1 charging model.

Please send your response by email to James Mackay, HS1 Head of Regulation and Customer Relations at: james.mackay@highspeed1.co.uk.

ANNEX A – Summary of Responses

Overview

HS1 received responses from the following stakeholders:

- London Southeastern Railways
- Eurostar International
- Rail Freight Group
- DB Cargo
- Department for Transport.

A summary of responses is provided below.

Summary of Responses

General

Stakeholders welcomed the review and recognised the unique nature of HS1 in the U.K. We appreciate the time and effort that has gone into responding to the ten consultation questions.

Operators noted the relatively high costs of HS1 driven by the regulatory and contractual arrangements that underpin the concession and welcomed activity to promote greater asset utilisation moving forward.

In relation to specific consultation questions comments were as follows.

1. **How should greater use of the HS1 network be incentivised within the current concession framework?**

All operators noted the relatively expensive nature of HS1 compared to both the conventional railway network in the UK and European networks.

While it was recognised that the structure of charges review was looking at the current contractual and regulatory framework Eurostar noted that the overall economics of highspeed rail in the UK needed to be addressed by Government because the overall economic drivers for high-speed rail were suppressing the potential for growth and recovery.

Eurostar noted that they would welcome greater flexibility in the contracts to enable operators to book a quantum of volume on the network through the timetabling process – but then have the flexibility to move train paths around within that quantum without being subject to specific paths.

LSER noted that they would struggle to be incentivised to utilise the network further given rolling stock constraints but would welcome the potential for discounts to incentivise services – particularly during off peak.

Freight noted that cost was a significant factor in their decision making and rail freight needed to remain competitive with other modes.

2. **Within the current concession framework, what aspect of the current charging arrangements works well and therefore should not be amended? What aspects do you think needs to change and why, and how would these changes impact behaviour?**

There were mixed views on the current effectiveness of the charging regime.

In relation to transparency and scrutiny - While Eurostar welcomed the high levels of transparency and oversight, LSER noted they had poor visibility of the regime and actual usage on the network.

Eurostar noted that a significant issue with the current charging regime is the degree to which costs are fixed in nature and there needed to be greater variability to ensure charges reflected the evolving economic / commercial environment faced by the industry.

Eurostar also asked that HS1 review its approach to charging for cancellations and questioned the variability of some of HS1's charges noting they would have expected NR(HS) to deliver cost savings with such significant falls in traffic.

Eurostar also questioned the approach to NR(HS) management fees which are levied as a percentage of overall costs.

Eurostar noted its position was that renewals should not be funded 40 years in advance, and this is not a requirement of the concession. Such a cautious approach it tying up large amounts of capital, with poor returns, which operators might otherwise use to invest and expand services.

Freight emphasised the importance of transferring the Ripple Lane asset to Network Rail Infrastructure Limited (NRIL).

3. **What role does the level and structure of access charges play in determining whether and the extent to which operators run services? How important are they and why?**

All operators noted that price remained the principle determining factor in whether to run services.

LSER also noted that the level of the charge impacted consideration of vehicle use as this has a direct impact of allocations under the Stations Long Term Charge and Stations Qualifying Expenditure.

4. **HS1 coordinates its activities with other IMs. For current and potential new entrants for international services, how can HS1 access charges be set in a way that is coordinated with Eurotunnel and related IMs in continental Europe (e.g. France, Belgium, the Netherlands)?**

Eurostar welcomes work with HS1 to coordinate routes and timetable planning but noted the ongoing challenges it faces opening new routes like Amsterdam. About charges Eurostar noted there was significant potential to use the HS1 discount policy more to incentivise them to open and grow new routes.

Freight notes that end to end journey costs were a key consideration and HS1 and more work should be done to understand how to set charges at an affordable level, including discounts. It would be important to understand how charging principles would apply.

5. **Should we carry out detailed analysis and cost modelling to make charges that recover directly incurred costs, namely the OMRCA1 variable charge, more cost reflective for different types of vehicle?**

There were mixed views on this issue.

LSER noted that variable charges were important as was the incentivisation to operate lighter trains that reduce track wear and tear. LSER noted HS1 could consider the approaches of other infrastructure managers including Network Rail.

Eurostar did not support further analysis in this area because the was an insufficient understanding of cost variability to accurately attribute costs to different train types. Eurostar noted the level of argument and time required to make charges was likely to be disproportionate to any benefit that would create an incentive for operators.

Eurostar also noted international operators were typically locked into larger heavier trains and HS1 should be set up to primarily focus on delivering this efficiently. Eurostar noted incentivising lighter trains may lead to perverse incentives such as high-volume shorter trains which would lead to a less efficient use of the asset.

Freight noted they only have one trainset type at this time, so any review was unlikely to have significant impact on them.

6. **How should renewals be reflected in charges in a sustainable and fair way?**

Eurostar referred to their previous comments on the approach to renewals. (Question 2)

LSER commented on the importance of incentivising operators to deliver more energy efficient approaches to their operators.

Freight welcomed the approach to renewals at the last periodic review and noted that this may need to be reviewed in the event a highspeed freight services commenced on the asset.

7. **Should the IRC discount policy be amended, and if so, how?**

Eurostar, Freight and LSER did not comment on this issue although LSER and Eurostar did reflect on discounts in response to other questions.

8. **Would it help support traffic growth on HS1 if HS1 Ltd developed new market segments, such as for sleeper services or high-speed freight? And if so, how should HS1 Ltd do that?**

LSER noted they would need to be satisfied the introduction of highspeed freight would not cause performance issues on the network – particularly because there is a perception freight fails more often. This should not impact passenger services.

Eurostar welcomed the potential for new market segments but did not have a view of markets HS1 might consider

Freight noted highspeed freight was a relevant market segment to consider but noted it would be unlikely to be attractive commercially if HS1 levied IRC on the segment.

9. What options do you think exist for promoting competition on the route? What are the barriers to entry? Is it technical, financial, depot access, or is it modal shift?

Eurostar emphasised that overall infrastructure costs and the ability to respond to their market in a more flexible way were important. Eurostar noted that technical and depot access issues could be challenging but were able to be dealt with through legislative requirements.

Eurostar also noted the importance of modal shift and that policymakers should be doing more to level the playing field between different transport modes – particularly as railway is a green option.

LSER noted that any domestic competition would fundamentally alter current operations and raise a number of technical and operational issues.

Freight noted a limited choice of locomotives but stressed this did not appear to be a barrier at this time.

10. Is the proposed phasing and suggested timeline for the review appropriate and is CP4 the right time to make any changes to the charging regime that may result from this review?

Eurostar noted reform was urgent and changes to the structure should be brought forward as soon as possible.

LSER was comfortable for the proposal to bring into effect structure of charges amendments at the commencement of CP4.

Freight provided no comment.

11. Any other comments you wish to make?

Eurostar noted that there needed to be reforms to the treatment of the Stations Long Term Charge. GTR should not be excluded as growing passenger numbers from their operations were contributing to the costs of St Pancras. Eurostar believes their exclusion is inconsistent with charging regulations.

Eurostar also noted that there was a fundamentally different approach to NRIL in relation to contributions from station retailers whereby NRIL invested commercial income back into the station to lower overall costs. Eurostar noted that the HS1 approach should be subject to review.

The funds collected from the renewals element of OMR charges are paid into a separate escrow account each quarter which can only be used for the funding of renewals.