Rail Delivery Group

Review of Charges: Station Charges

November 2015

Contents

1. Executive Summary

1.1. Purpose of this document

The purpose of this document is to present the findings from the Rail Delivery Group's (RDG's) review of station charging. It also explains the background to RDG's work, and how it fits into RDG's wider Review of Charges work programme.

1.2. Scope of this document

This report explains the current structure of station charges and sets out our approach to the review. It describes our assessment of the current station charges regime and identifies the advantages and disadvantages of potential changes to the regime, which seek to deliver better value for money for stations users and taxpayers.

The focus of our work has been on station charges, where the Office of Rail and Road (ORR) has regulatory oversight. However, our work has inevitably touched on station charges outside of ORR's remit.

1.3. Industry context

The GB rail industry continues to experience significant change. At the time of writing this report, there are a number of industry reviews taking place, e.g. Shaw report on the longer-term future shape and financing of Network Rail, which could lead to change in the way that rail infrastructure is delivered. Additionally, the Summer Budget 2015 confirmed that the government would introduce a new approach to station redevelopment and commercial land sales on the rail network.

Our work does not seek to pre-empt the outcomes of any industry reviews or proposed changes to stations. However, we have considered different station operating models in our review and our findings should be applicable even if there are reasonably significant changes to the operation, management and/or ownership of stations.

1.4. Key messages

The findings of our work on station charges are explained in the rest of this report. However, our key messages are that:

- railway stations are an **important part of every passenger's journey**;
- **station charges matter** because they affect the way that Network Rail and train operators work together to deliver the service that customers expect at stations;
- station charges currently recover the costs of maintaining stations in their existing state. They **do not encourage challenge of what is there now** and they are generally treated as uncontrollable costs. Charges should become a stimulus for challenging the current approach to stations and whether money is being used as well as it can be, for passengers;
- whilst improvements can be made to station charges, there are limits to what they can achieve. Reform of charges is **not a substitute for industry leadership**; and
- a robust and consistent station **charging framework is increasingly important as ownership and management of stations becomes more diverse**. Train operators need to be clear about who is accountable for each station, how they will be charged for using a station, and what they can expect in return.

1.5. Current approach to station charging

Network Rail is responsible for the maintenance, repair and renewal (MRR) of most of the stations it owns. The Station Facility Owner (SFO) is responsible for the day-to-day management and operation of the station. For the majority of stations, the SFO is a franchised train operator. However, Network Rail is the SFO for a small number of its larger stations – these are called 'Managed Stations'.

For around 200 Network Rail-owned stations, franchised train operators are responsible for both MRR and day-to-day operation. There are also a very small number of stations that are owned and run by third parties.

So that stations owners and SFOs can recover the costs of running stations, train operators contribute towards these costs, through a set of station charges, in relation to how often they call at that station.

Specific charging arrangements vary depending on the type of station that a train operators calls at. However, broadly, there are charges that recover: operating costs; MRR costs; and also the costs of past investments in stations, where these were promoted by train operators or other third parties.

1.6. Approach to review

As part of RDG's Review of Charges, we set up a small working group of representatives from passenger operators, Network Rail, ORR and RDG's Policy team to focus on station charges. These individuals were nominated by members of RDG's Stations Strategy Group.

The findings in this report have been developed, primarily, through a series of discussions with the working group between June and October 2015. The assessment of options for changes to station charges was supported by Cambridge Economic Policy Associates (CEPA).

Our review of station charging has taken place alongside RDG's wider work on charges and incentives and we have maintained a clear link to the rest of RDG's charges and incentives work programme.

2. Introduction

2.1. Purpose of this document

The purpose of this document is to present the findings from the Rail Delivery Group's (RDG's) review of stations charging. It explains the background to RDG's work, and how it fits into RDG's wider Review of Charges work programme.

2.2. Scope of this document

This document sets out:

- why RDG has reviewed station charges;
- the approach we have taken to reviewing station charges;
- the current station charging regime and approach to station management;
- our assessment of the current approach to station charges; and
- a review of potential changes to station charges to deliver better value for money.

Although this work has taken into account different types of station ownership models, we have not set out any views on the most suitable model.

2.3. Rail Delivery Group

RDG seeks to improve services for rail users and deliver better value for money for taxpayers. It was set up in 2011 to bring together the owners of Britain's passenger train operating companies, freight operators and Network Rail to provide leadership to Britain's rail industry.

RDG's mission is to promote greater co-operation between train operators and Network Rail through leadership in the industry and by working together with governments, the supply chain and stakeholders. RDG is committed to the long-term health of the railway but also recognises the need to see improvements in the shorter term.

RDG's current work programme spans 14 different areas, with each area overseen by dedicated 'Working Group' made up of industry representatives.

2.4. Background to the RDG Review of Charges

Purpose

RDG's Review of Charges is an industry-led review of the charges and incentives regime, for use of Network Rail's infrastructure. It considers how charges and incentives might operate under several alternative 'States of the World' (or industry scenarios). This work forms part of RDG's Contractual and Regulatory Reform Working Group (CRRWG).

This project has provided an opportunity for train operators (passenger and freight) and Network Rail to work together to clearly set out their own views on the appropriate structure of charges and incentives, prior to ORR communicating its own work for PR18 at the end of 2015.

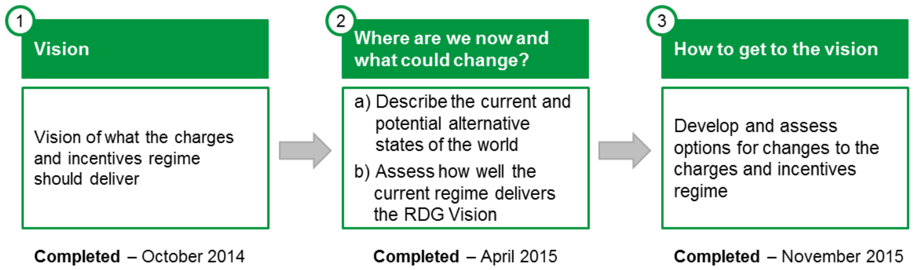
Additionally, this project sought to improve the understanding of charges and incentives across the industry and to provide sufficient time to consider charging and incentives issues for the next control period.

The time horizon for our review was 2029, i.e. the end of Control Period 7. However, we have given particular focus to the next Control Period (CP6).

Approach to the review

RDG's Review of Charges was made up of three phases:

Figure 2.1: High level plan for RDG Review of Charges



The outputs described below are all published on RDG's website[1].

Phase 1: RDG Vision for charges and incentives in the long run

The RDG Vision sets out RDG members' views on what the charges and incentives regime should deliver in the long run. It provided the framework against which various options could be assessed later in the review.

The majority of the work for Phase 1 was completed between April and September 2014. It was the product of a number of workshops that brought together views from a wide range of industry stakeholders.

During Phase 1, RDG also produced a user guide which set out to provide an overview of the regulatory charges and incentives mechanisms that are in place in the GB rail industry in CP5.

Phase 2: Assessment of the current regime and States of the World

This phase was a stepping stone to developing options for changes to the charges and incentives regime in the next stage of the review. It built on the RDG vision for charges and incentives, and was made up of two parts:

1. Current and potential alternative states of the world: we described the current environment in which charges and incentives operate within (the 'State of the World') and developed a number of alternative States of the World, in which it can test options for changes to the charges and incentives regime.

2. Assessment of the current charges and incentives regime: we assessed how well the current regime delivers RDG's vision for the charges and incentives. This assessment set out the elements of the regime that work well and also those areas where there were gaps. The findings were developed, primarily, through a series of industry workshops, facilitated by L.E.K. Consulting (International) Limited, between January and March 2015.

Phase 3: Options development and assessment

The final phase of work sought to develop and assess options for changes to the charges and incentives regime. It was made up of three main elements:

1. *Factors that impact the form and/or the effectiveness of the regime*: we identified the main institutional, policy, economic and practical factors that should be considered by policymakers when proposing changes to the regime.
2. *Impact assessment*: informed by the previous phases of work, we selected 22 options for changes to the charges and incentives regime. For each option, we assessed how the option performs against the RDG vision for charges and incentives, in both the current, and alternative, States of the World.

   We then undertook further analysis of seven of the options, where we thought ORR was likely to consider the option in PR18 or because that option performed well in the initial assessment. Where we have considered options for change, this should not be taken as RDG recommending that any, or all, should be implemented. Instead our work is intended to inform industry debate on reform.
3. *Station charging*: whilst station charges were not identified as a priority area for RDG's Review of Charges during Phase 2, industry representatives wanted to ensure that RDG's work provided sufficient coverage of stations charging. Therefore, we set up a series of dedicated meetings, with industry representatives, to consider potential improvements to this area of charging. The findings of that work are set out in this report.

[1] This is available at: http://raildeliverygroup.com/what-we-do/our-work-programme/contractual-regulatory-reform/review-of-charges.html.

2.5. RDG's work on stations

Context

Great Britain has in excess of 2,500 railway stations with over 1.6 billion passenger journeys made each year. Stations provide access to rail travel for the majority of people living in Great Britain, with over 85% of the population living within five kilometres of a railway station[2].

RDG's Vision for Stations

In April 2014, RDG set up a dedicated working group to look at how the industry should evolve its approach to the development and management of stations – The Stations Strategy Group (SSG).

A key output of the working group was to set out RDG's thoughts for a future vision for stations that recognises they are more than just building assets or a place for people to access rail services – 'RDG's Vision for Stations'. The time horizon for RDG's Vison for Stations is 2030. The vision recognises that stations have the potential to regenerate communities, support local identity and also be a test bed for new technologies to support and create an experience that attracts even more people to use Britain's railway.

RDG's Vision for Stations is the next step in establishing a strategy for realising that vision. That document sets out RDG's vision for Great Britain's stations and nine principles that RDG's considers should shape the approach to their successful evolution.

The overarching vision for stations is *"… for Britain's stations to be places which are inclusive and welcoming, and which encourage everyone to travel by rail. This vision will be enabled by those working at the station, by the innovative use of technology, and by the involvement of the communities which stations serve."*

RDG's Vision for Stations was launched at RDG's Second Stations Summit, on 20 October 2015, following consultation with a broad range of industry stakeholders over summer 2015.

RDG's work on station charges

The charges that train operators pay for using stations are not explicitly addressed in RDG's Vision for Stations. Whilst stations charges represent a relatively small proportion of Network Rail's total revenue, these charges matter because they affect the way that Network Rail and train operators work together to deliver the service that customers expect at stations.

Phase 2 of RDG's Review of Charges identified areas of the charges and incentives regime, where there were the most significant gaps with RDG's vision for charges and incentives. Whilst station charges were not identified as a priority area for RDG's Review of Charges, industry representatives wanted to ensure that RDG's work provided sufficient coverage of station charges.

To ensure that there was sufficient focus on this area of charges, we set up a series of dedicated meetings, with industry representatives, to consider potential changes that could be made to improve station charges.

This report sets out the findings from the series of meetings and the analysis that we carried out as a result of those meeting discussions.

Scope of RDG's work on stations charging

The focus of this report is station charges that are regulated by ORR, which includes:

- Stations Long Term Charge (LTC) for both franchised and managed stations;
- Qualifying Expenditure (QX) management fee for managed stations; and
- Station Facility Charges.

[2] Source: RDG's Vision for Stations, available at: http://raildeliverygroup.com/what-we-do/our-work-programme/stations.html.

Whilst some station charges are not set by ORR, our review has considered the way that regulated station charges interact with these other money flows. Therefore, the scope of our review also includes:

- QX charges for both managed and franchised stations; and
- Stations Lease income.

The following areas are not within the scope of this work:

- station planning. Whilst some of the observations in this report touch on planning issues, we consider the focus of our analysis to be the role of charges and incentives at stations;
- assessment of appropriate ownership structure and operating models for stations. Whilst we have considered the role of station charges for different types of stations (e.g. managed, franchised and third party owned), we have not set out any views on the most suitable model; and
- depots charges. These charges were not included in the scope of this review.

2.6. Industry context

The GB rail industry continues to experience significant change. At the time of writing this report, there are a number of industry reviews taking place, e.g. Shaw report on the longer-term future shape and financing of Network Rail, which could lead to change in the way that rail infrastructure is delivered. Additionally, the Summer Budget 2015 confirmed that the government would introduce a new approach to station redevelopment and commercial land sales on the rail network.

Our work does not seek to pre-empt the outcomes of any industry reviews or proposed changes to stations. However, we have considered different station operating models in our review and our findings should be applicable even if there are reasonably significant changes to the operation, management and/or ownership of stations.

3. Current approach to station charging

3.1. Scope of this section

This section sets out the current station charges that apply across the GB rail network, and how charging arrangements vary depending on the way that a station is run and managed. We discuss the range of charges that operators pay to use stations and how this may vary for:

- Managed stations;
- Franchised Short-Term Lease Stations;
- Franchised Long-Term Lease Stations; and
- Third party owned stations.

3.2. Background

Network Rail is responsible for the maintenance, repair and renewal (MRR) of most of the stations it owns. The Station Facility Owner (SFO) is responsible for the day-to-day management and operation of the station. For the majority of stations, the SFO is a franchised train operator. However, Network Rail is the SFO for a small number of its larger stations – these are called 'Managed Stations'. There are also a very small number of stations that are owned and run by third parties.

So that stations owners and SFOs can recover the costs of running stations, train operators contribute towards these costs, through a set of station charges, in relation to how often they call at that station.

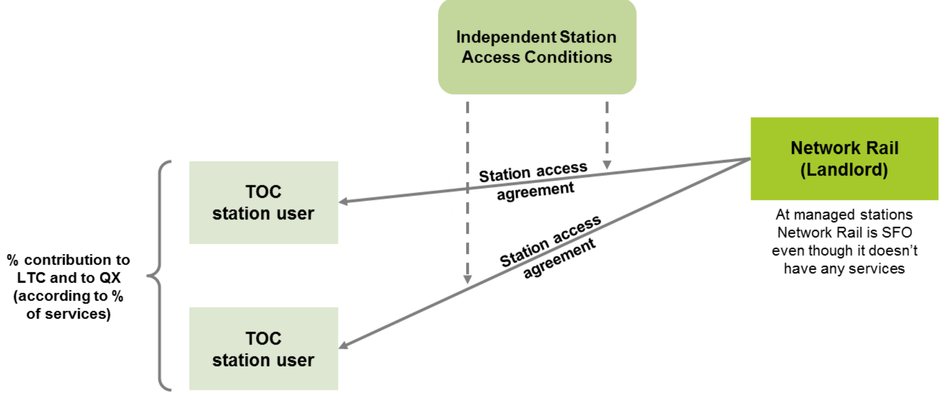
3.3. Approaches to operation, management and ownership of stations

In this section, we have summarised the four main approaches to the operation, management and ownership of stations. Station charging arrangements differ across these types of stations.

Managed Stations

Managed Stations are some of the biggest stations across the GB rail network. There are currently 18 Managed Stations, which include Birmingham New Street, Glasgow Central, Kings Cross, Euston and Leeds City[3]. Figure 3.1, below, sets out the current approach to charging at Managed Stations.

Figure 3.1: Current approach to charging at Managed Stations



Network Rail is responsible for the MRR of a Managed Station. It is also the SFO, which means that it is responsible for the day-to-day management and operation of the station.

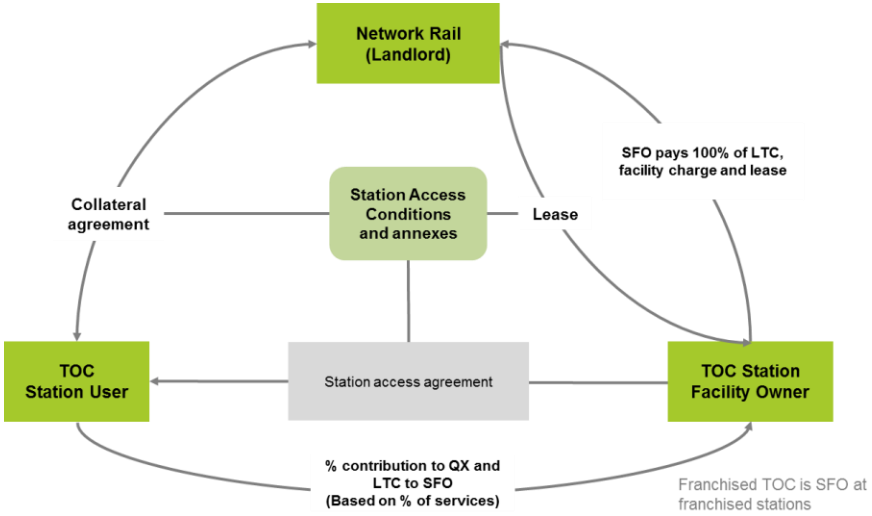
Station access agreements govern the charges that train operators are required to pay to Network Rail, as SFO, to use the station.

[3] A full list of Managed Stations is available at: https://www.networkrail.co.uk/managed-stations/.

Franchised Short-Term Lease Stations

The majority of railway stations in Great Britain, around 2,250, are Franchised Short-Term Lease Stations. At these stations, franchised passenger operators have a short-term lease for operating the station. Figure 3.2, below, sets out the current approach to charging at Managed Stations

Figure 3.2: Current approach to Franchised Short-Term Lease Stations



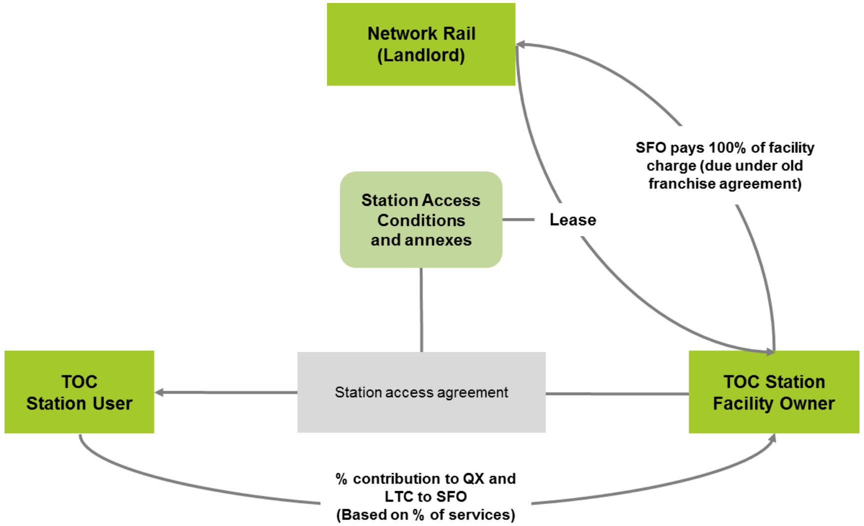
Network Rail is responsible for the MRR of the station. However, a franchised operator is the SFO, which means that it is responsible for the day-to-day management and operation of the station.

The Station Lease governs the charges and lease payments that the SFO needs to pay to Network Rail, as station landlord. Train operators stopping at the station then pay the SFO a share of Station LTC and QX charges, based on the number of its services that stop at the station (based on a percentage of total services that use the station).

Franchised Long-Term Lease Stations

There are around 200 stations in Great Britain that are managed by franchised passenger operators on a long lease, normally a 99-year or 125-year lease.

Figure 3.3: Current approach to Franchised Long-Term Lease Stations



Until recently, Network Rail was responsible for the MRR of all its stations. However, since 2012, some franchised operators have taken over the responsibility for MRR, in addition to the day-to-day management and operation of stations, where they were SFO. These franchised operators have a full repairing lease and only pay a peppercorn rent to Network Rail. However, they also pay existing facility charges relating to these stations, to Network Rail.

Reflecting the change of responsibilities, at PR13 ORR did not determine Station LTC for these types of stations[4].

[4] At that time, Greater Anglia was the only franchised operator that operated this type of station.

Train operators stopping at these stations, continue to pay the SFO a share of LTC and QX charges, based on the number of its services that stop at the station (based on a percentage of total services).

Third party owned stations

There are currently, only a small number of stations across the GB rail network that are owned by third parties. Examples include Southend Airport Stations, owned and managed by Stobart Rail, and Fishguard Harbour Station which is owned by Stena Line. At these stations, the owners are generally also responsible for the MRR and day-to-day management and operation of the station.

Train operators using these stations have bespoke station access agreements, which are negotiated and agreed on a station-by-station basis. Therefore, charges paid by train operators at these stations are not necessarily consistent with the station charges paid for using Managed and Franchised (Short-Term and Long-Term Lease) Stations.

3.4. Description of station charges

Train operators pay a range of charges (regulated and non-regulated) to use GB rail stations. The main charges are:

- **Station Long Term Charge** (regulated) covers maintenance, repair and renewal (MRR) costs at stations;
- **Qualifying Expenditure (QX) Charge** (part-regulated) reflects the day to day running costs of providing services and amenities at the stations;
- **Facility Charges** (regulated) recovers Network Rail's capital expenditure on enhancement schemes promoted by station and depot operators; and
- **Station lease** (non-regulated) covers Property Rent, e.g. retail car park income, and represents a share of income received in 1994-95 (with subsequent RPI inflation increases).

We set out further details of each charge in the rest of this section.

Station Long Term Charge (LTC)

Station LTC is a regulated charge that seeks to recover the costs of the long term upkeep of station assets. It is applicable at Franchised Stations and Managed Stations. Train operators pay Station LTC based on the proportion of their vehicle departures for that station. This is calculated in accordance with the methodology set out in the Station Access Conditions. The obligation to pay Station LTC is set out in the Station Letting Conditions which are incorporated into the Station Lease.

There are differences in the way that Station LTC is calculated for Managed Stations and Franchised Stations, which are explained below:

<u>Franchised Station LTC</u>

Franchised Station LTC is payable to Network Rail by the relevant SFO for each of the stations within its portfolio. If other users (or 'beneficiaries') also call at a station, the SFO will recover a proportion of the total Station LTC for that station in relation to the number of vehicle departures for each beneficiary.

It is based on total MRR expenditure in CP5 at the level of the group of stations operated by each SFO (referred to as the portfolio of stations). Separate charges are calculated for each Franchised Station within each portfolio to reflect 35-year average spend at that station.

Individual Station LTCs for Franchised Stations are not intended to be fully reflective of the specific spend at each station within the control period. They are instead designed to represent the proportion of the MRR expenditure for the portfolio of stations that would be spent on each station in the long run (over 35 years). Therefore, it is unlikely that for an individual Franchised Station, the Station LTC revenue will be equal to MRR expenditure at that station over the five-year control period.

Franchised passenger operators that manage stations on a long-term lease do not pay Station LTCs to Network Rail, e.g. for the Greater Anglia franchise. At PR13, ORR explained that it would not determine station LTC for these stations. This was because Network Rail no longer had MRR responsibilities at stations for which Greater Anglia is the SFO, with the exception of Stratford Station. Therefore, the Station LTC, which is in the station access agreements between Abellio Greater Anglia and beneficiaries at its stations, has continued into CP5, i.e. the same charge that was in place at the start of CP4 (uplifted annually for inflation). It is therefore, for Greater Anglia and DfT to establish the station charges for the Greater Anglia stations.

Managed Station LTC

Managed Station LTC is payable by operators that use any of Network Rail's Managed Stations. Network Rail recovers the charge directly from all beneficiaries, in proportion to the number of vehicle departures at each Managed Station.

Managed Station LTC is calculated separately for each Managed Station. It is based on the annual average of long run efficient MRR expenditure projected over 100 years. This is longer than for Franchised Stations in order to even out some of the extremes of spend found at these very large facilities. These extremes are more material for Managed Stations due to the scale of renewals costs at each station and the fact that there is no possibility to average across a larger portfolio.

Qualify Expenditure (QX) Charge

The QX charge seeks to recover the cost of the day-to-day running and operation of stations. It also covers the reasonable costs incurred by the SFO for procuring or providing the services and amenities, which all users share. It is charged by the SFO to train operators that call at that station and is applicable at Franchised Stations and Managed Stations. Train operators pay the QX charge based on the proportion of its vehicle departures for that station.

There are two main parts to the QX charge:

- Fixed QX – this forms the majority of the charge and covers direct operations costs, such as station cleaning, refuse collection and disposal; and
- Management fee – SFOs are also entitled to recover indirect central costs and overheads that arise as a result of operating stations, as well as a profit element. The management fee is levied as a proportion of the fixed QX charge.

The QX charge is generally fixed throughout the control period in real terms. However, where any significant changes occur at stations, it can be re-negotiated during the control period. As it is not determined by ORR, the QX charge is the result of a negotiation between the SFO and train operators.

For Managed Stations the QX charge is negotiated for year 1 of each control period for each station. It is varied by the Retail Price Index (RPI) – x for each succeeding year, where 'x' is an efficiency target which is negotiated between Network Rail, as SFO, and train operators, and may vary from station to station.

Franchised Stations may choose to follow the same approach to calculating QX charges as Managed Stations. However, SFOs may, for example, choose not to index the charge by inflation, or could even decide to review the charge annually.

The only part of the QX charge that is determined by ORR is the management fee for Managed Stations. Whilst it is not currently part of the periodic review process, the Independent Station Access Conditions require ORR to approve the management fee for Managed Stations before the start of each control period. For Franchised Stations, the management fee is agreed between the SFO and operators using the station at the beginning of the control period.

Facility Charges

Where improvements to stations are promoted by train operators, rather than Network Rail, DfT or Transport Scotland, facility charges are used to recover the costs that Network Rail incurs from undertaking that enhancement. A Facility Charge is included in an operator's Station Access Contract (or sometimes in the lease, rather than relying on negotiated repayment terms as is necessary for other third party-promoted schemes. Facility Charges may also include a separate element for any incremental MRR costs that result from the enhancement.

Although each Facility Charge is paid by the scheme promoter alone, i.e. the SFO, station users can themselves arrange to share the costs of an enhancement through joint promotion of a scheme. Facility charges are approved by ORR[5].

Franchised Station leases

Franchised stations lease income covers Property Rent (retail car park income, along with some amounts relating to other lease arrangements) and represents a share of the income received under these arrangements. This income stream is not regulated by ORR.

Not all stations will have Property Rent as it depends whether there is any commercial letting potential at the station. This rent was set at privatisation and was an estimate (at the time) of 75% of the potential commercial income that could be generated from the station by the SFO. It is indexed by RPI each year. Property Rent is stated in the Station Lease and the obligation to pay it is set out in the Station Letting Conditions.

3.5. Current station charges income

Station charges are a significant income stream for Network Rail and franchised passenger operators that are SFOs.

Information on Stations LTC income is readily available as this is regulated by ORR. ORR's PR13 determination forecast that over CP5, Stations LTC across both managed and franchised stations would be £756m (in 2012-13 prices), excluding Greater Anglia stations.

[5] Guidelines on calculating a facility charge are set out by ORR in its 'Investment framework consolidated policy & guidelines' available at: http://orr.gov.uk/__data/assets/pdf_file/0014/5720/investment_framework_guidelines_october_2010.pdf.

Table 3.1: Forecast Station LTC income in CP5 (in 2012-13 prices)

Forecast of station LTC income (Great Britain)	CP5 total (£m)
LTC – managed stations	159
LTC - franchised stations	597

Source: ORR PR13 final determination

The QX management fee that is part of the Managed Station QX charge was determined by ORR to be 6.54% for CP5. This is made up of 1.54% to recover central overhead costs and 5.0% to reflect an appropriate level of profit to provide Network Rail with a financial return that compensates it for the financial risks it is taking in managing the stations.

Network Rail's income from QX charges is set out in Network Rail's Regulatory Accounts and ORR's assumption on QX charging income is included in its PR13 final determination. However, data on the value of QX charges at Franchised Stations is not widely available and there is no single source of information where QX charging income for all GB station is recorded.

ORR's PR13 final determination assumed Network Rail's Managed Stations QX income in CP5 would be £212m (in 2012-13 prices) for Great Britain. ORR also provided forecasts of Network Rail's Franchised Stations lease income, which was £223m (in 2012-13 prices) for Great Britain over CP5.

4. Approach to RDG's review of station charges

4.1. Overview of approach

As part of RDG's Review of Charges, we set up a small working group made up of industry representatives to focus solely on station charges. We formed this group to ensure that sufficient time and effort was given to this area of charging. The findings in this report have been developed, primarily, through a series of discussions with that working group between June and October 2015.

However, our review of stations charging has taken place alongside our wider work on charges and incentives and we have maintained a clear link to the rest of RDG's charges and incentives work programme.

4.2. Workshops/meetings

At RDG's Stations Strategy Working Group, we sought nominated industry representatives to take part in a series of meetings to discuss station charges. We held a series of meetings with the nominees, which were drawn from passenger operators, Network Rail and ORR.

The purpose of the series of meetings was to:

- develop a common understanding of the current approach to station charges;
- identify issues with the current stations charging regime; and
- consider possible options to address the issues identified by the group.

We held four meetings between June and October 2015[6].

[6] First workshop: 11 June 2015; second workshop: 8 July 2015; third workshop: 27 August 2015; and fourth workshop: 14 October 2015.

4.3. Assessment of the current stations charging regime

To identify the gaps in the current station charging regime, we considered how well the current regime delivered RDG's Vision for Charges and Incentives and RDG's Vision for Stations.

For RDG's Vision for Charges and Incentives, the working group assessed how well the stations charging regime delivered against each element of the vision, i.e. the axioms, objectives, judgement criteria and outputs. The assessment also considered whether that assessment differed for each type of station, e.g. Managed Stations, Franchised Stations etc.

For RDG's Vision for Stations, we assessed the current stations charging regime against each of its nine principles.

The assessments were qualitative, i.e. they did not provide a score or grade for each part of the vision that was then summed to provide an overall score. Instead, the assessments set out the areas of the current regime that the group thought delivered the visions and those areas where the group thought the visions were not being delivered.

The two visions were not specifically developed for stations charging. However, we considered that they provided a broad framework to develop an assessment of the main gaps in the current approach.

4.4. Development of options to address identified gaps

Informed by the assessment of the current stations charging regime, the working group identified three charging options that sought to address some of the gaps that were identified. However, it was clear from the assessment that changes to charges may not be able to resolve some of the gaps. Therefore, the group also highlighted other potential approaches of addressing the gaps.

The three charging options that were selected for assessment were also informed by the outputs of two small industry workshops in May and June 2015. These workshops, part of the wider RDG Review of Charges project, discussed a range of potential changes for the entire charges and incentives regime, which included five broad options for changes to the stations charging regime[7].

4.5. Assessment of options

RDG commissioned Cambridge Economic Policy Associates (CEPA) to support Phase 3 of the wider Review of Charges. As part of CEPA's work, it has carried out high-level impact assessments on the three station charging options that were selected for assessment.

CEPA followed the same approach to the assessments of stations charging options, as its approach to the options for other areas of the charges and incentives regime. For each option, CEPA populated a pro forma template, which required an assessment against 19 criteria, drawn from the RDG vision for charges and incentives. The assessments were largely qualitative. Each option was rated as red, amber or green, on the basis of its impact compared to the current regime:

- *Red* (-) – option is expected to have a negative impact;
- *Amber* (=) – option is expected to have an impact equivalent to the current regime; and
- *Green* (+) – option is expected to have a positive impact.

The assessments reflect CEPA's independent assessment of the three options. However, they have had the benefit of input from the working group. This input allowed CEPA to ensure that the development of the options and the assessments are grounded in the reality of the range of business models currently in operation within the rail industry.

[7] The options discussed during the workshops were: 1) including additional fixed costs in Stations LTC; 2) developing a station costs/revenue sharing mechanism; 3) regulating QX charge; 4) charging Station LTC on a portfolio basis; 5) review approach to Station LTC for stations where Network Rail no longer has MRR responsibilities.

5. Key findings

5.1. Scope of this section

This section sets out the main findings from RDG's work on station charges, and includes:

- summary of key findings;
- analysis of the current stations charging regime;
- options that we have considered to address the observed gaps in the regime; and
- findings of analysis.

5.2. Summary of key findings

The findings of our work on station charges are explained in the rest of this section. However, our key findings are that:

- station charges matter because they:
    - can affect the incentives on train operators and Network Rail to work together to deliver the level service that customers expect at stations;
    - provide for Network Rail and train operators to recover the costs running stations; and
    - provide a mechanism for train operators to invest in stations.
- station charges currently recover the costs of maintaining stations in their existing state. They do not encourage challenge of what is there now and they are generally treated as uncontrollable costs. Charges should become a stimulus for challenging the current approach to stations and whether money is being used as well as it can be, for passengers;
- whilst improvements can be made to station charges, there are limits to what they can achieve. Reform of charges is not a substitute for industry leadership. On their own, changes to station charges do not appear to be able to resolve some of the more significant issues that we identified;
- it is important to be clear about the purpose and calculation approach for each element of the stations charging regime to improve understanding and confidence in station charges – currently there is a perceived lack of transparency and understanding of station charges;
- whilst station charges provide a mechanism to allow for investment in stations, there are limited incentives for train operators to do this, particularly towards the end of their franchises. However, DfT are seeking to address this issue through franchising; and
- a robust and consistent station charging framework is increasingly important as ownership and management of stations becomes more diverse. Train operators need to be clear about who is accountable for each station, how they will be charged for using a station, and what they can expect in return. Stations charges do not currently do this. Additionally, this provides third party investors with confidence that they will be able to recover their investment through a clear and stable charging regime.

We explore these points, and others more detailed considerations, in the rest of this section of the report.

5.3. Assessment against RDG's Vision for Charges and Incentives

In this section, we have summarised our assessment of how well the current stations charging regime delivers RDG's Vision for Charges and Incentives. The assessment is separated into the four elements of the vision:

- the pre-requisites the regime should follow (axioms);
- the objectives that the regime should pursue (objectives);
- the fundamental criteria that should be followed when selecting charges and incentive mechanisms (judgement criteria); and

- the resulting outputs that should be delivered by the regime (outputs).

Axioms

The charges and incentives regime should be based on these pre-requisites:

System safety **|** Consistency with law **|** Funding of Network Rail efficient costs **|** Allowance for market conditions **|** A single approach for the network as a whole

Observations:

- Station charges do not create incentives that compromise safety. They act as a mechanism to allow any additional costs that result from safety improvements to be recovered from station users. Outside of the charging regime, station licences should reflect minimums safety requirements required of licence holders.
- The current charging approach is considered to be consistent with the law.
- It is difficult to assess whether station charges recover efficient costs as there is a lack of clarity of the way in which the costs are recovered for certain charges. For example, due to the methodology for Station LTC, i.e. based on portfolio of stations, the charge for MRR at a station does not necessarily recover the MRR costs at that station over the control period.
- There is no single approach to stations charging across the network. Whilst the main categories of charging are broadly consistent across the network, the approach to calculating charges varies. For example, Station LTC for Franchised Long-Term Lease Stations is no longer calculated on the same basis as Franchised Short-Term Lease Stations. This is because there no clear governance process around station charges for Franchised Long-Term Lease Stations. Third Party-Owned Stations, e.g. Southend Airport, also have different arrangements. Similarly, the approach to calculating QX charges appears to vary across the network. This issue will become more significant if additional train operators take MRR responsibility at stations.
- ORR only regulates part of the stations charging regime. It regulates Stations LTC for Managed Stations and Franchised (short-term lease) Stations, and the QX Management Fee for Managed Stations.

Objectives

The objectives of the charges and incentives regime should be:

Service cost recovery **|** Efficient whole system whole life industry net costs | Efficient long run investment decisions **|** Efficient performance management **|** Efficient use of network capacity

Observations:

- In most cases, station charges allow Network Rail and train operators to recover the costs they incur for running stations. However, there is a weak link between charges and the quality of the outputs that are delivered.
- Changes in operating costs during the control period can be reflected in updates to the QX charge so the charge should reflect operating costs. However, where station changes are not agreed by all station users, the increase in operating costs is borne only by the SFO and not shared through higher QX charges.
- Station LTC reflects the costs of a portfolio of stations rather than the forecast costs at an individual station. The charge is designed in this way to smooth out lumpy expenditure across stations but it makes it difficult for SFOs and beneficiaries to assess whether the charges they pay, at each station, represent value for money.
- Property Rent is based on outdated assumptions around retail income. They were set at privatisation and haven’t been reviewed since then, other than being uplifted for inflation (RPI).

- The current charging approach has only limited ability to flex for changes in levels of usage. For example, the allocation of charges to train operators is based on train movements. These are reviewed annually for QX charges but only reviewed when there is a material change affecting Station LTC. Therefore, there can be situations where train operators still pay for MRR costs at stations they no longer use.
- The current regime does not promote a whole-station approach to managing a station, particularly at Franchised Short-Term Lease Stations. There are potential conflicts between Network Rail and SFO teams at stations, particularly where accountabilities for certain activities are not considered to be clear. Similarly, station charges do not necessarily take into account the potential conflicts between Network Rail and SFO plans for stations.
- The current station charges provide for recovering the costs of maintaining the station in a steady state, i.e. they do not incentivise investments in stations. Franchised operators have limited incentives to invest in stations, particularly towards the end of their franchises. Franchise Long-Term Lease Stations may improve issues around clarity of accountabilities but they do not appear to improve incentives to invest given that the franchise contracts are relatively short (generally 7 to 10 years) compared to the 99-year or 125-year station leases. However, DfT is seeking to address this issue by introducing residual value mechanisms[8] in future franchises.
- There are funds that seek to address issues with incentives to invest at stations. In CP5, funds of over £200m have been made available by governments to improve stations in areas such as accessibility (Access for All), passenger information and facilities (National Stations Improvement Programme), and passenger experience (Station Commercial Project Facility).

Judgement criteria

Alternative implementation mechanisms for the achievement of the objectives should be judged according to the following criteria:

Predictability **|** Simplicity **|** Transparency **|** Low transaction costs

Observations:

- Whilst charges are fixed within control periods, there can be relatively significant increases and decreases in charges between control periods. There is often only limited explanation for these changes, even at portfolio level. However, this may in part be an issue with the level of engagement from across the industry early in the periodic review process to consider initial estimates of charges.
- Some passenger operators thought that there was not a good understanding of the costs that are included in Station LTC and QX charges, and the reasons for this. For example, some operators considered that there were issues in the recovery of costs associated with revenue generating assets. In this case, the SFO at Franchised Stations retains revenue from car parks but beneficiaries share the operating costs of these assets, via QX charges. However, at Managed Stations, Network Rail retains the income and but bears all of the operating costs of car parks.
- There is a limited understanding of how changes to Station LTC and QX charges are triggered following enhancements to stations.
- There are examples where information used to calculate QX charges has not been accurate, e.g. there have been issues with data on the amount of retail space at some stations. The presence of these errors was perceived, by some operators, to reflect the lack of challenge that some charges receive.

[8] DfT is seeking to promote long-term investment in future rail franchises through the introduction of a residual value mechanism that compensates bidders for the value of an investment that will last into the next franchise.

- At Franchised Short-Term Lease Stations, there is generally not sufficient communication of the separate Network Rail and SFO station work plans. These plans inform station expenditure forecasts and therefore, this limits the transparency/understanding of how charges are calculated.
- The current approach to calculating Station LTC, i.e. calculated on a portfolio basis, makes it difficult for train operators to understand whether the work that is planned at a particular station, and has informed the calculation of the charge, has been delivered as expected, i.e. whether the charge is value for money.
- As QX charges are negotiated between SFOs and beneficiaries, there is very limited information available about the levels of QX charges paid by train operators across the GB rail network. Therefore, operators are not able to assess whether the charges they pay are high or low relative to other operators (although they will be able to use the information from stations where they are SFOs). As QX charges reflect the running costs at stations, the view of the group was that the majority of information on QX charges should not be commercially confidential.
- Transaction costs for Station LTC are low because, in most cases, it is determined by ORR. Transaction costs for the QX charge are higher, given the need for train operators to undertake often lengthy negotiations to agree QX charges. However, the level of challenge in the QX process is considered to drive out efficiency savings.

Outputs

A charges and incentives regime based on the specified axioms, objectives and judgement criteria would result in:

Network Rail accountability **|** Non-arbitrary allocation of costs **|** Optimal traffic growth **|** Aligning industry incentives **|** Value for money for funders, taxpayers and users

Summary of observations:

- Station LTC relies on ORR determining the correct charge. There was a view that this does not create the correct accountabilities as Network Rail, primarily, has to work with ORR to agree the charge. Although there is consultation process, train operators are not as involved in this process as they are for QX charges.
- All parties respond to their own incentives. However, these incentives do not always lead to parties acting in the best interests of passengers and other station users. For example, there is a perception, amongst some parts of the industry, that the current regime leads to train operators that are focused on what passenger want and Network Rail focused on delivering targets set by governments and ORR. However, other colleagues thought that this issue reflected that stations were not as significant a contributor to customer satisfaction as other factors such as train punctuality and journey length.
- The regime does not make it clear what passengers should expect from stations and it is not clear what they do expect either.
- The charging regime does not incentivise Network Rail and train operators to improve customer experience. It generally provides for recovering the costs of maintaining the station in a steady state. Whilst train operators are often viewed as ‘owners’ of the stations by passengers, Network Rail can have a significant impact on the customer experience at stations, not just at Managed Stations.

- There is a lack of understanding / clarity about the purpose of station charges, i.e. whether they are they simply cost recovery mechanisms or intended to incentivise certain behaviours.
- The role of station charges may increase in importance in the event that there are more stations owned by third parties. For example, where there is a more commercial approach to running stations.

5.4. Assessment against the RDG Vision for Stations

In this section, we have summarised our assessment of how well the current station charging regime deliver RDG's Vision for Stations.

The RDG Vision for Stations, which is discussed in Section 2.5, has nine principles. We have summarised our observations on station charging against each principle below.

1. ***Customer focussed***: Incentives provided by the charging regime do not necessarily act in best interests of customers. For example, the lack of aligned incentives between Network Rail and train operators reduces the focus on delivering a positive customer experience. This is not just an issue for charges.
2. ***Intelligent use of technology:*** There are potential issues with incentives to invest in new technology because there are limited incentives for train operators to invest in stations, particularly at the end of franchises.
3. ***Seamless journey experience:*** As a result of the combination of accountabilities between train operators and Network Rail at stations – this is most significant for Franchised Short-Term Lease Stations – passengers do not always experience a seamless journey experience. This is less of an issue for Managed Stations and Franchised Long-Term Lease Stations, given that accountabilities are clearer. However, this issue seems to be more of a contractual issue, rather than a charging issue.
4. ***Reflect local needs and opportunities:*** Whilst the charging regime does allow for Local Authorities to invest in stations through facility charges, the regime does not always provide incentives for Network Rail and train operators to act in the best interests of local areas. For example, Network Rail and train operator station plans may not align with those of Local Authority.
5. ***Safe and secure environment:*** The charging regime does not appear to put the safety and security of stations at risk.
6. ***Entrepreneurial spirit:*** The regime does allow for changes in operational costs to be recovered through a revised QX Charge following investment at stations. However, the threshold for making changes to the Station LTC is £50,000, which could deter parties from undertaking certain investments at stations if they cannot recover the resulting increase in MRR costs. Whilst charges should not inhibit entrepreneurial spirit, there may be limits to the role that the charging regime can play in incentivising entrepreneurial activity at stations.
7. ***Flexible and long-term stewardship***: The charging regime does have flexibility to adapt to changes in stations, e.g. for enhancements to a station or changes to the number of different operators using a station. However, there are limited incentives for train operators to invest in their stations towards the end of the life of a franchise. However, Managed Stations and Franchised Long-Term Lease Stations have better incentives for long-term asset stewardship.
8. ***Shared industry know-how***: The charging regime does not address issues with the misalignment of incentives between Network Rail and train operators at stations. Therefore, it does not actively encourage parties to share knowledge about how to best operate stations. However, it is not clear that this should be an issue for charges to address.
9. ***Optimised network*: ** Station charges do provide for train operators to invest in stations through facility charges, which may support improvements in efficient operation of stations. However, the charging regime does not actively incentivise station improvements as it is focused on maintaining stations in their steady state.

5.5. Assessment of charges and incentives options to address the observed gaps

Whilst there are a number of potential options that could help to address the gaps in the current regime, we asked consultants, CEPA, to consider three options in more detail. These options were:

1. **Regulated QX charge.** ORR would assess and agree with Network Rail and/or operators the levels of QX charges as a revenue cap. The regulated QX charge would be set based on expected efficiency savings and be updated annually for inflation. Currently, the only part of the QX charge which is regulated is the QX management fee for Managed Stations, which cover Network Rail's central support costs and profit element.
2. **Station-by-station LTC.** Station LTC would be set for each station, based on the expected efficient MRR at each station, rather than being allocated a share of MRR at the portfolio level. Bottom-up estimates of efficient MRR would be used to set charges for each station, capturing each station's planned renewals and repair schemes, operator-specific expenditure and route-wide expenditure.
3. **Revenue sharing.** This option involves giving NR a financial incentive by exposing it to movements in operator revenues at franchised stations. As for the network charging revenue sharing option, it is likely that this would be based on passenger ticket revenues, as recorded by existing industry mechanisms.

5.6. Assessment of options

The full assessments of each of the three station charging options are presented in Annex A. However, we have summarised the findings of each assessment below.

Regulated QX charge

This option was considered as a way to improve the process for determining QX charges to provide confidence that QX charges reflect the efficient levels of operating costs at stations. It would also provide greater transparency of the costs that are being recovered through this charge.

The additional information would allow operators to benchmark QX charges across the network and help to drive greater efficiencies in station operating costs. Current arrangements for QX charges have been in place for a long time and are not transparent. This makes it difficult to determine if charges are based on efficiently incurred costs.

The current approach is consistent with maintaining station operation standards, i.e. the charge passes through the costs incurred in operating the station. Moving from the current QX charge to a capped charge (or a revenue cap) that is regulated, may introduce incentives for SFOs to reduce expenditure relative to the cap and improve efficiency.

Regulating QX would be a significant change as ORR would have oversight of QX charges that are levied by franchised passenger operators in their role as SFOs at stations.

However, by providing greater incentives for SFOs to reduce station operating costs during a control period, this may drive reductions in the quality of the station environment if, for example, cleaning or station staffing is reduced below acceptable levels. Although, services level are defined in the Station Access Conditions, which may reduce minimise this risk.

This option may improve the transparency of costs being recovered by the QX charge and provide incentives to improve cost efficiency. However, there are other ways of addressing some of the issues targeted by this option, which may require less regulatory intervention. For example, the group considered making the breakdown of QX charges for both Managed Stations and Franchised Stations more widely available and refreshing the guidelines on the costs that can be recovered through QX charges.

Should these alternative, more administrative, approaches not resolve the issues, regulating QX charges could still be considered as a viable option.

Station-by-station LTC

This option was considered as a way to improve the link between station-specific expenditure on MRR and the Station LTC paid by station users. If the LTC were set on a station-by-station basis, SFOs and beneficiaries would have a clearer basis on which to demand cost reductions from Network Rail to realise reductions in their Station LTCs.

In this option, Station LTC would be set based on the expected efficient MRR at each station, rather than being allocated a share of MRR at the portfolio level. The costs that are recovered could either be based on:

- MRR costs within the control period, which could vary significantly from one control period to the next; or
- MRR costs over a longer time period, e.g. 35 years, which could be smoothed over a number of control periods using some form of Regulatory Asset Base (RAB)-based[9] or escrow[10] approach.

Bottom-up estimates of efficient MRR costs would be used to set charges for each station, capturing each station's planned renewals and repair schemes, operator-specific expenditure and route-wide expenditure. This would require robust expenditure plans for every station across the GB rail network. Currently, such plans are not in place for each station and this would need to be addressed before being able to implement this option.

If Station LTC was based on within-control period costs at each station, the 'lumpy' nature of MRR is likely to introduce greater volatility to the Station LTC. To address this issue, a RAB-based (or escrow-based) approach would allow smoothing of charges over time while retaining transparency over costs. However, with over 2,500 stations, this will create additional data requirements and this may not be practical or proportionate for the potential benefits that could be realised.

Instead, work could be undertaken to improve the information behind the current Station LTCs to provide better information to allow SFOs and beneficiaries to challenge the assumptions at the portfolio level.

CEPA considered that moving towards greater cost-reflectivity within portfolios of stations might be a disproportionate move, resulting in greater volatility for charges at each station in the portfolio and this resulted in an overall red grading for this option.

However, in discussions with industry colleagues there were mixed views on whether a RAB-based approach would be as impractical as CEPA considered. Some participants thought that the benefits of the option could outweigh the requirement to collect and maintain station-by-station expenditure data. This option was considered to be more beneficial in a situation where there were groups of third-party owned stations and transparency over costs was of greater importance, e.g. where ORR was not responsible for regulating the charge for a portfolio of stations.

Industry colleagues also considered that this option might indirectly help to improve the existing bottom-up station planning processes. However, there was a shared view that the real issues that need to be addressed in this area may lie outside charging and relate to the way that costs are allocated and the availability and robustness of station plans.

Revenue sharing

There is currently no financial incentive to align Network Rail's MRR activities with the interests of SFOs and beneficiaries. This option involves providing Network Rail with a financial incentive to help train operators generate additional fare revenue. The revenue share would expose Network Rail to movements in train operator revenues at franchised stations. CEPA

[9] A RAB acts as a commitment to allow regulated utilities to recover the costs of their investments. Lumpy capital expenditure at a station could be financed by debt or equity. The RAB acts as a store of value of that investment which can be recovered over time through charges.

[10] Charging income would be paid into an account, potentially held by a third party, which would only be used to fund future MRR costs at a particular station.

considered that that this may be paid for by government funders rather than payments from train operators[11].

The revenue share would be based on passenger ticket revenues, as recorded by existing industry mechanisms. However, it could also be extended to station tenancy, advertising, carpark and other SFO revenues, where appropriate.

The introduction of station revenue sharing could encourage Network Rail to focus its asset stewardship activities on areas with the greatest potential to improve passengers' experience and boost ticket revenue. It would help to improve the alignment of incentives between Network Rail as station landlord and the train operators using the station. However, some operators thought that any revenue sharing mechanism should be focused on non-farebox revenue only.

There are some advantages of introducing station revenue sharing but it is possible that in cases where the benefit from doing so would be greatest, it may be more appropriate to make the franchised SFO responsible for MRR instead of Network Rail. This would remove the need for revenue sharing. However, this is solution sits outside of the charging regime. Some train operators already have been given MRR responsibility for station, including Greater Anglia and Essex Thameside. Bespoke arrangements such as alliances could also be explored at certain locations.

The conceptual benefits of revenue sharing are relatively well understood but there appears to be significant barriers to implementing this type of mechanism at a station level. Solutions outside of the charges and incentives regime appear to be better placed to resolve issues regarding the alignment of incentives at stations.

[11] This could operate in a similar way to the Volume Incentive, which seeks to encourage Network Rail to grow traffic. Network Rail receives additional money from funders if it outperforms ORR's targets but if it underperforms, it receives less money.

5.7. Recommendations to address the identified gaps

The three options that we have assessed in this report could result in some improvements to the stations charging regime, e.g. a Station-by-station LTC may help to improve the link between expenditure at individual stations and the charges paid by SFOs and beneficiaries at those stations. Whilst these options are not exhaustive, changes to charges do not appear to be sufficient to address some of the more significant issues at stations. This is because these issues are not necessarily related to the structure of charges.

Drawing on our assessment of the current stations charging regime and the assessment of the three charges and incentives options, we have set out, below, potential measures that that could address some of the issues we have identified during our work. Whilst the focus is on station charges and incentives, we do discuss some other, related, non-charging issues.

- **Understanding of station charges.** It is important to have clarity about the purpose of each charge (or money flow) at a station, e.g. is the primary purpose of station charges cost recovery or is it also intended to provide particular incentives for industry parties?

  The creation of a document (or guide) that brings together all of the information on station charges (not just regulated charges), and is agreed by ORR and the industry, would help to improve understanding of station charges amongst stakeholders. It should include important information on each charge such as: the agreed purpose; the approach to calculation; and governance arrangements.

- **Transparency of QX charges.** There is currently no central store of information about the range of QX charges that are paid by train operators. It is, therefore, difficult for beneficiaries to determine whether the charges are value for money.

  To allow train operators to benchmark QX charges across the GB rail network, the industry should consider whether it is possible to increase the transparency of QX charges paid by different train operators at both Manages Stations and Franchised Stations. This could take the form of a central repository of information covering the QX charges paid for each portfolio of stations and the breakdown of how this is calculated.

- **Industry engagement.** In the past, there has been limited engagement between train operators and Network Rail at early stages of the periodic review in relation to the calculation of Station LTC.

  To improve the accuracy of Station LTC, and to improve the understanding of the calculation of the charge, there should be a greater level of engagement between Network Rail and train operators in the early stages of the periodic review. This will help to reduce circumstances where there are significant unexpected changes to station charges between control periods.

- **Governance of Station LTC.** The governance process for changes to Station LTC for Franchised Long-Term Lease Stations is not clear. As more franchised operators take on responsibility for MRR at stations, this issue is likely to increase in significance.

  To provide consistency across the network, there should be an agreed approach to governance and calculation of Station LTCs at these stations.

- **Incentives to invest.** Changes to station charges do not appear to be the best solution to improving the willingness of train operators to invest in stations.

  The introduction of residual value mechanisms in franchise agreements, which are already being consider for future franchises, may address the issue of longer term view of investment. However, this is an issue for franchising authorities.

- **Seamless journey experience.** There is perceived lack of clarity about the roles and responsibilities of different parties that own, manage and operate stations. Also, for many stations, train operators and Network Rail do not have joint station plans in place. These issues affect the industry’s ability to provide passengers with a seamless journey experience.

  To address these issues, each station, or portfolio of stations for large train operators, should have a robust and up-to-date joint station plan, which includes a forecast of expenditure over a long time period, e.g. at least 35-years. This will support SFOs and beneficiaries in challenging proposed expenditure at stations and help to drive cost efficiencies. For each station, there should also be a clear accountability matrix which sets out the roles and responsibilities of each party involved in delivering the customer experience.

The main issues at stations appear to relate to issues with the ownership, planning and accountabilities at stations. These issues need to be resolved before we seek to optimise the station charging regime.

Annex A: Assessment of potential options

This annex includes the high-level assessments for longlist options 12-14 relating to reforms to station charging:

- Regulate station QX charges;
- Station-by-station LTC; and
- Station revenue sharing.

Option 12: Regulate Station QX charges

A qualifying expenditure (QX) charge is levied at all stations but only the management fee element at stations managed by NR is overseen by the ORR. A regulated QX charge would provide an independent challenge to these charges for the day-to-day operation of stations that are currently negotiated confidentially between Station Facility Owners (SFOs) and operators at each station.

Key characteristics

Description of option

Regulate the entire QX station charge for all SFOs to provide an independent challenge to these charges for the day-to-day operation of stations.

The ORR would assess and agree with operators the level of the entire QX charge as a revenue cap. All of QX would be set based on expected efficiency savings and be updated annually for RPI movements. This is currently only the case for the "management fee" covering central support costs and profit at managed stations where NR is the SFO.

Description of counterfactual

QX charges arise at station served by more than one operator where the SFO "off-charges" a proportion of its costs to other users based on traffic forecasts.[12] It therefore applies to a relatively small sub-set of the network. The annual charge is around £40m of the £300m charges at the stations managed by NR. [13] Except for the management fee at managed stations, the level of the QX charge is not regulated.

The principal elements of the QX charge relate to day-to-day operations expenditure to provide services and amenities at stations and include station cleaning, utilities and provision of competent and suitably trained staff.

Unlike the long term charge (LTC) for stations, QX charges are not published and there is no central information available.[14] Operators negotiate charges with the SFO under the conditions of Annex 2 of the station access conditions.[15]

NR described the process of negotiating QX at managed stations for CP5 as follows:

> *"In the course of negotiating the QX charge with TOCs, one of the principles followed is, where NR makes efficiency through its own initiative then no change will be made to the QX charge. However, where NR and the TOCs work together to jointly effect a saving then a reduction will be made to QX by an agreed amount at an agreed date."*[16]

At franchised stations, QX charges are agreed between the SFO and the beneficiaries of the expenditure, with NR (and presumably the ORR) having no visibility of them.[17] Similarly, QX is not regulated for third party SFOs, such as at Southend Airport.

Relevant factors impacting the form and/or the effectiveness of the option

- Franchising (Factors Report Section 3.2)
- Industry complexity (Factors Report Section 4.2)
- Network scope and specification (Factors Report Section 4.3)
- Data availability, measurement, and billing (Factors Report Section 4.7)

Impact on stakeholders

Changes to QX affect franchised passenger operators as station users and SFOs. NR is the SFO at

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[12] Passenger operators attending the second stations workshop on 27th August 2015 noted that it would be difficult to conduct QX negotiations based on actual traffic.

[13] NR (2013) "SBPT3278 Stations and depots income" available on the NR website here p2.

[14] CP5 LTC charges are available on the NR website here.

[15] Station access conditions and related annexes are available on the ORR website here.

[16] NR (2013) "SBPT3278 Stations and depots income" available on the NR website here p5.

[17] NR Infrastructure Limited and First Rail Holdings Limited (2010) "Reference to Access Disputes Panel in respect of interpreting the split between day to day Maintenance and Repair of Retail Telecomms and CCTV and other Retail Telecommunications Equipment at Franchised Stations" available on the Access Disputes Committee Website here p8

Option 12: Regulate Station QX charges								
managed stations. Franchised passenger operators may be SFOs under short and long leases. There is currently one independent SFO.[18] ORR stated that for CP6, if the QX charge were retained, it would like the process for approving the NR QX management fee to be better aligned with the periodic review of NR's outputs, charges and funding. The ORR indicated that this could be achieved by NR submitting a proposal as part of its strategic business plan, backed by support from the relevant train operators.[19]								
Other options that complement and conflict with proposed option								
There are no clear complementarities or conflicts with other options considered in the long list.								
Performance against criteria								
Axioms	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
System safety	=	=	=	=	=	=	=	=
	Moving from the effective pass-through of directly incurred costs to a revenue cap would introduce incentives for SFOs to reduce expenditure relative to current arrangements. Monitoring arrangements and penalties could be put in place to help ensure cost efficiencies did not come at the expense of falling standards. If it were not possible to achieve this, there is a risk that reductions in station cleaning services and station staffing might lead to small reductions in the safety of the railway system. The potential impact of this would be muted in the "specified franchises" SoW where franchisees have very little freedom to adjust service provision but NR would still be affected.							
Consistency with law	=	=	=	=	=	=	=	=
	No conflict has been identified between regulating QX and requirements from relevant regulations and laws. As QX is not currently regulated, it is not clear that the ORR currently has the powers to regulate QX but if it does not, we anticipate that it would not be problematic to acquire.							
Funding of NR efficient costs	=	=	=	=	=	=	=	=
	The full regulation of QX could put pressure on NR to uncover efficiencies in the operation of stations. However, assuming that the allowance would be set by the ORR at an appropriate level, regulation of this charge should not affect NR's ability to recover total efficient costs of providing and improving all services.							
Allowance for market conditions	=	=	=	=	=	=	=	=
	Assuming that regulation of QX would be based on cost directly incurred, as now, a regulated QX charge should have no impact on the ability of a market segment to bear the cost. While franchised passenger operators would be protected from changes until the stopping pattern changes, open access operators would be exposed to changes, suffering if regulation led to an increase in charges but benefitting from efficiencies where they are uncovered.							
A single approach for the network as a whole	+	+	+	+	+	+	+	+
	Regulating the full QX charge would provide an opportunity to align the treatment of the charge across managed and franchised stations. Currently the QX management charge is regulated for managed stations but is not regulated for franchised stations.							

[18] Stobart Rail currently operates the London Southend Airport Railway Station.
[19] ORR (2015) "NR managed stations – decision on the approval of the qualifying expenditure (QX) management fee for control period 5 (CP5)" available on the ORR website here p3.

Objectives	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
Service costs recovery	=	=	=	=	=	=	=	=
	Regulated charges would be based on efficient costs directly incurred.							
Efficient whole-system whole-life industry net costs	=	-	-	=	=	=	=	=
	Current QX negotiations provide a mechanism through which costs and standards are agreed between the SFO and users. This allows changes to be made where benefits exceed the change in costs. A regulated QX charge might be less flexible than the current arrangements but participants at the second RDG Review of Charges meeting on options for stations charging explained that the link between the level of QX charges and the level of service received was weak, and that information was treated in an unnecessarily confidential manner. This indicated that current arrangements might not be as flexible as they could be but most station users are also SFOs at their own franchised stations and have their own information against which they can challenge QX at others' stations. The only group of users without this benefit would be open access operators. However, requirements for non-discriminatory treatment should enable them to benefit from other user's negotiating power. Therefore, while the additional rigidity of the regulated charges might not have much impact in many SoWs, particularly as at least some franchised operators are held harmless to station charges, it could be noticeable in the two SoWs with less highly specified franchise agreements.							
Efficient long run investment decisions	=	=	=	=	=	=	=	=
	As indicated by the ORR's statement on QX for CP6, there is no clear link between QX and NR's wider plans. Regulating QX could allow the ORR to consider the charge alongside LTC and facility charges. A more complete analysis of the efficient costs of station investments might aid better investment decision making. It might also remove any incentive to inflate QX given its current preferable treatment compared to regulated activities. However, the materiality of these benefits is not certain in any SoW.							
Efficient performance management	=	=	=	=	=	=	=	=
	There is no clear impact of this charging approach on efficient performance management.							
Efficient use of network capacity	=	=	=	=	=	=	=	=
	There is no clear impact of this charging approach on efficient use of network capacity.							
Judgement criteria	**Current**	**Dynamic railway**	**On-rail comp**	**Specified franchises**	**Protect freight**	**Beneficiary pays**	**Capacity allocation**	**Regional powers**
Predictability	=	=	=	=	=	=	=	=
	There is no clear impact of this charging approach on the volatility of the level of charges across multiple control periods.							
Simplicity	+	+	+	+	+	+	+	+
	The QX charge is not currently well understood. Information is treated in a confidential manner and there is no central record of QX charges. A regulated tariff could be specified at a sufficient level of detail to allow understanding of its constituent elements. It could also be recorded centrally to allow comparisons across stations, enabling greater contestability.							

Transparency	+	+	+	+	+	+	+	+
	QX charges are currently calculated based on principles set out in Annex 2 of the station access conditions. The current direct cost incurred approach is quite simple but there is a lack of transparency regarding the negotiations between SFOs and users, the resulting value of charges and the corresponding service levels. One open access passenger operator noted that the lack of transparency potentially hid cross-subsidisation of SFO services, with station beneficiaries paying for services that only benefit the SFO, such as carparks. A regulated QX charge might require more steps and econometric analysis but the resulting outcome should be more transparent.							
Low transaction costs	-	-	-	-	-	-	-	-
	Regulating QX would create a greater regulatory burden for SFOs and the ORR during the periodic review. This would require the development of detailed cost estimates ideally backed by evidence and gathered at station level from a combination of NR and passenger operators. While this may not be a large increase compared to the scale of current activities, it may be disproportionate for the size of QX. Regulating QX would reduce the need for passenger operators to negotiate directly with SFOs. However, the overall net impact is likely to be an increase in transaction costs.							
Outputs	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
NR accountability	=	=	=	=	=	=	=	=
	Regulating QX has the potential to make SFOs more accountable to their customers. While they currently negotiate charges with users, the scope to contest assertions on efficiency and the link between charges and service levels is weak.[20] Regulation could help challenge SFO's assertions and create a level of transparency sufficient to create a link between costs and outcomes.							
Non-arbitrary allocation of costs	=	=	=	=	=	=	=	=
	There is no clear impact of this charging approach on the arbitrariness of cost allocation.							
Optimal traffic growth	=	=	=	=	=	=	=	=
	There is no clear impact of this charging approach on traffic growth.							
Aligning industry incentives	=	=	=	=	=	=	=	=
	Greater transparency of the basis of QX charges and the rights they convey could facilitate greater co-operation between SFOs and station users to improve efficiency and adaptation to evolving needs. The scope for this to be achieved is greatest in the "dynamic railway" and "on-rail comp" states of the world but regulating the charge could create a barrier to achieving such outcomes. Therefore, the impact is expected to be neutral in all SoWs.							

[20] Southeastern (2010) "Review of arrangements for establishing access charges for CP4" available on the ORR website here.

Value for money for funders, taxpayers and users	=	=	=	=	=	=	=	=
	The QX charge is based on costs incurred, not ex ante efficient costs. The lack of information on these charges is a barrier to understanding whether there is a significant difference between these two and whether they are justified in the detail. The reason for QX not being fully regulated is not clearly articulated in ORR documentation. However, its current treatment may be well aligned with the objective of ensuring that SFOs do not reduce QX costs such as cleaning or station staffing. These are important for customers' experience and cost reductions, which more rapidly translate into passenger experience than renewals or enhancement expenditure on stations. It is uncertain whether regulating QX would increase value for money. It depends on the degree to which costs are not currently efficient but also on the ability to enforce standards during the review period if it were regulated. Therefore, without further information available, this option is marked as neutral across all SoWs.							
Summary	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
	=	=	=	=	=	=	=	=
	The current approach is consistent with a no compromise approach to station operation standards but current arrangements have persisted for a long time and it is difficult to determine if charges are based on efficiently incurred costs. Regulating QX would be a big change for this type of expenditure on stations so without being able to determine if the current approach fulfils its objectives, it is difficult to recommend such a change. Despite this, outside this review there may be value in a more root and branch review of the regulatory regime for stations beyond charging and investigation of non-charging reforms to more directly address areas of concern indicated by participants at RDG station charges workshops. For example, areas for further investigation might include the potential to make the level and breakdown of QX charges more publicly available, and to refresh the guidelines for the allocation of costs such as new ticket gates. Should an approach such as improving the transparency of QX charges be taken forward and it is found that costs are both inefficient and that greater transparency does not facilitate greater efficiencies, regulating QX could be an option to consider.							

Option 13: Station-by-station LTC
The long term charge (LTC) for the use of franchised stations is set to recover NR's maintenance, renewal and repair costs (MRR) for each franchisee's complete portfolio of stations during the price control period. A station-by-station LTC would ensure that the charge for each station within the portfolio also reflects expenditure at each station, providing a clearer basis for franchisees to challenge these charges at each location and to improve the understanding of what the charge is designed to deliver.
Key characteristics
Description of option
NR is generally responsible for the MRR of station buildings and Station Information and Security Systems (SISS).[21] It charges franchised station facility owners (SFOs) holding station leases a regulated LTC. This charge is used to recover the cost of MRR across the portfolio of stations included in each franchise contract.[22] Setting the LTC station-by-station would be a move to increase its transparency to SFOs and users building upon and perhaps helping to develop existing station-by-station asset management plans. This would enhance their ability to contest its level at each location. Charges would be set based on the expected efficient MRR at each location during the price control period rather than being allocated a share of MRR at the portfolio level. Bottom-up estimates of efficient MRR would be used to set charges for each station, capturing each station's planned renewals and repair schemes, operator-specific expenditure and route-wide expenditure.
Description of counterfactual
The current LTC is recovered as individual station-specific charges but as described by NR, "franchised station LTCs are in effect set at the portfolio level."[23] For CP5, LTC charges were set in a "top-down" manner, where the ORR determined efficient MRR expenditure for each portfolio of stations. The portfolio-level charge was then allocated to each station based on modelled expenditure over the forthcoming 35-years. The first five forecast years included bottom-up estimates for certain costs. The forecast for the subsequent 30 years was top-down. Under the current LTC, total portfolio MRR is recovered through charges in the same period it is incurred even if the benefits of such expenditure span multiple control periods. However, the application of the charge across a portfolio of stations, serves to smooth-out the recovery of the expenditure at each station over a longer period of time.
Relevant factors impacting the form and/or the effectiveness of the option
• Franchising (Factors Report Section 3.2) • Industry complexity (Factors Report Section 4.2) • Network scope and specification (Factors Report Section 4.3) • Data availability, measurement, and billing (Factors Report Section 4.7)
Impact on stakeholders
A station-by-station LTC would affect franchised and open access users of franchised stations by making the charges at individual stations more volatile, although the sum of charges paid might be unchanged. It would similarly affect NR as the station landlord at particular locations but not across the portfolio. Temporary increases in charges at individual stations to recover lumpy expenditure (assuming no other mechanism is put in place to smooth the charges) could encourage open access operators to avoid stations requiring significant works during a particular review period.

[21] RDG (2014) "Charges and incentives user guide" available on the RDG website here p20.
[22] Where a franchisee has full repairing station lease agreements for the portfolio (such as the current arrangements for the Greater Anglia franchise), Network Rail does not collect a LTC.
At managed stations.
[23] Network Rail (2013) "Explanatory note and draft price lists for CP5 franchised and managed station Long Term Charges" available on the Network Rail website here p5.

Option 13: Station-by-station LTC

Other options that complement and conflict with proposed option

There are no clear complementarities or conflicts with other options considered in the long list.

Performance against criteria

Axioms	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
System safety	=	=	=	=	=	=	=	=
	There is no clear impact of this charging approach on system safety.							
Consistency with law	=	=	=	=	=	=	=	=
	No conflict has been identified between setting a bottom-up station-by-station LTC and requirements from relevant regulations and laws.							
Funding of NR efficient costs	=	=	=	=	=	=	=	=
	No impact has been identified from moving to a bottom-up station-by-station LTC on the ability to fund NR's efficient costs.							
Allowance for market conditions	=	=	=	=	=	=	=	=
	No impact has been identified from moving to a bottom-up station-by-station LTC on the ability of a market segment to bear the cost.							
A single approach for the network as a whole	+	+	+	+	+	+	+	+
	The LTC at managed stations is currently calculated on a bottom-up basis. Moving to a bottom-up station-by-station LTC for franchised stations would align the approaches across the different station groupings.							
Objectives	**Current**	**Dynamic railway**	**On-rail comp**	**Specified franchises**	**Protect freight**	**Beneficiary pays**	**Capacity allocation**	**Regional powers**
Service costs recovery	+	+	+	+	+	+	+	+
	The move to a bottom-up station-by-station LTC would result in more cost-reflective charges for each station. The portfolio-level charge would remain at the same level of cost reflectivity.							
Efficient whole-system whole-life industry net costs	+	+	+	=	+	+	+	+
	The LTC is seen to encourage the maintenance of the "as-is" state and encourages like-for-like replacements even in cases where not required.[24] The portfolio-based nature of the LTC creates a disconnect between the actions required at station-level to reduce costs and the charges that SFOs pay. When a cost-efficiency is realised, it is difficult to identify if it is an absolute saving that could be passed on through charges or if it has allowed greater expenditure to be incurred elsewhere within the portfolio. If the LTC were set on a station-by-station basis, SFOs would have a clearer basis on which to demand cost reductions from NR to realise reductions in the LTC. These benefits could be realised in any SoW except where the franchises are more highly specified.							

[24] RDG (2015) "Review of Charges Phase 2b: Assessment of the current charges and incentives regime" available on the RDG website here p36.

Efficient long run investment decisions	=	=	=	=	=	=	=	=
	A bottom-up station-by-station LTC would serve to provide greater transparency on charges within the review period. It is not clear that there is a direct link to the quality of long-run investment decisions beyond greater pressure from SFOs and users to reduce costs.							
Efficient performance management	=	=	=	=	=	=	=	=
	There is no clear impact of this charging approach on efficient performance management.							
Efficient use of network capacity	=	=	=	=	=	=	=	=
	There is no clear impact of this charging approach on efficient use of network capacity.							
Judgement criteria	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
Predictability	-	-	-	-	-	-	-	-
	Station charges do not currently include a RAB or other mechanism (e.g. escrow accounts) to recover historic expenditure over time in line with the benefits it delivers.[25] Instead, long-term forecasts are used to smooth the cost of lumpy station-specific investments. For the LTC charge to capture expenditure incurred during the control period at both the portfolio level and at each station, the station charge would need to reflect expenditure only during the review period rather than a longer time horizon. Consequently, the station-level charges would become more volatile than at present. However, this would not affect the volatility of the overall portfolio charge paid.							
Simplicity	+	+	+	+	+	+	+	+
	LTC is currently recovered on a station-by-station basis so a bottom-up station-by-station LTC charge would not necessarily be more complex than current arrangements. In fact, removing the long-term forecast components could make the charge more tangible and readily understandable.							
Transparency	+	+	+	+	+	+	+	+
	A bottom-up station-by-station LTC would be more transparent at the station level. It is possible that a tighter link between expenditure and charges might encourage greater involvement from stakeholders at the right times to improve the station planning process and to improve their knowledge of station plans.							
Low transaction costs	-	-	-	-	-	-	-	-
	Greater transparency over LTC at the station level might lead to more challenges from beneficiary operators when agreeing charges at each station.							
Outputs	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
NR accountability	+	+	+	+	+	+	+	+
	Greater transparency of the LTC at station level might make NR more accountable for its activities at each station.							

[25] It is not expected to be practical to introduce RABs for each of the c. 2,500 stations on the network.

	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
Non-arbitrary allocation of costs	+	+	+	+	+	+	+	+
	A greater link between the station-level expenditure and charges would allow expenditure to be attributed more precisely than if allocated across all stations within the portfolio.							
Optimal traffic growth	-	-	-	=	-	-	-	-
	Without a mechanism, such as a RAB, to allow expenditure to be smoothed over time, volatile charges might make operators without highly specified contracts avoid stations during periods where lumpy investments are being recovered.							
Aligning industry incentives	+	+	+	=	+	+	+	+
	Greater transparency of expenditure might facilitate greater cooperation between NR, SFOs and other users of stations as part of the process of agreeing LTC charges. SFOs might not be able to take advantage of greater transparency if franchises are more highly specified.							
Value for money for funders, taxpayers and users	+	+	+	=	+	+	+	+
	If greater transparency can facilitate greater accountability and pressure to reduce costs, it might be possible for the value for money of station charges to improve.							
Summary	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
	-	-	-	-	-	-	-	-
	While the current approach is somewhat complex, the use of forecast expenditure provides a relatively simple way to smooth charges at each station over time, closer in line with the benefits they provide. A RAB-based approach would allow smoothing of charges over time while retaining transparency over costs. However, that is not likely to be a practical or proportionate approach for the thousands of stations on the network. Work could be undertaken to improve the information behind the current LTC to increase its contestability at the portfolio level. However, moving towards greater cost-reflectivity at the station-level might be a disproportionate move, resulting in greater volatility for charges at each location and resulting in an overall red grading for this option in all SoWs. While participants at the RDG Station Charging workshops expressed the view that this option might indirectly help to improve the existing bottom-up station planning processes, the real issues that need to be addressed in this area lie outside charging and relate to cost allocation, information, franchising and the contractual framework (for example relating to thresholds for reopeners and the treatment of over-specified or redundant assets).							

Option 14: Station revenue sharing

There is currently no financial incentive to align NR's station maintenance activities with the interests of franchised station facility owners (SFOs) and other operators. A station revenue sharing mechanism would address that gap by giving NR an exposure to operators' ticket revenue at each station.

Key characteristics

Description of option

This option involves giving NR a financial incentive by exposing it to movements in operator revenues at franchised stations. As for the network charging revenue sharing option, it is likely that this would be paid for by government funders rather than direct transfers from operators and be based on passenger ticket revenues, as recorded by existing industry mechanisms. Where appropriate, this might also extend to station tenancy, advertising, carpark and other SFO revenues.

The introduction of station revenue sharing would encourage Network Rail to focus its asset stewardship activities on areas with the greatest potential to improve passengers' experience and boost ticket revenue.[26] This would improve the alignment of incentives between Network Rail as station landlord providing maintenance, renewal and repair (MRR) and the franchised passenger (SFO) holding the lease and stopping its trains at the station.

As for the network revenue sharing option, this option could be implemented as a station-specific volume incentive with station-specific revenue benchmarks or as part of the revenue sharing mechanisms in franchise contracts.

Description of counterfactual

There are currently no revenue sharing mechanisms specific to station charging.

Relevant factors impacting the form and/or the effectiveness of the option

- Franchising (Factors Report Section 3.2)
- Industry complexity (Factors Report Section 4.2)
- Network scope and specification (Factors Report Section 4.3)
- Data availability, measurement, and billing (Factors Report Section 4.7)

Impact on stakeholders

The implementation of this option may require coordination over risk sharing mechanisms in franchise contracts, which lie within the power variously of DfT and other devolved authorities, and vary considerably in their financial arrangements. This would be to ensure the overall effect of both the NR and franchise mechanisms was desirable.

If the mechanism required a benchmark level of revenue, it cannot be guaranteed that the form of every franchise bid would provide a suitable benchmark.

Other options that complement and conflict with proposed option

While a number of the considerations for revenue sharing remain the same irrespective of other charging options, certain charges may be more compatible than others. In particular, any broader revenue sharing mechanism would need to be adapted to avoid double counting of revenue.

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[26] RDG (2015) "Review of Charges Phase 2b: Assessment of the current charges and incentives regime" available on the RDG website here p41.

Option 14: Station revenue sharing								
Performance against criteria								
Axioms	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
System safety	=	=	=	=	=	=	=	=
	There is no clear impact of this option on system safety. It is assumed that minimum requirements for safety would need to be sufficiently strong that it would not be possible to gainfully sacrifice system safety.							
Consistency with law	=	=	=	=	=	=	=	=
	As this option relates to incentive payments similar to elsewhere in the regime, we assume that this option will remain consistent with law. **Further legal analysis is required in this area.**							
Funding of NR efficient costs	=	=	=	=	=	=	=	=
	This option might imply a slight change in terms of introducing more variability in NR funding (assuming the incentives are symmetric). However, the option has been marked as neutral, given that the change is unlikely to be material, and could be compensated by recognising the additional variability in the remuneration of the cost of capital for example.							
Allowance for market conditions	=	=	=	=	=	=	=	=
	As this we expect it unlikely that payments would be made directly from operators to NR under this option, we assume that it would have no effect on this criterion.							
A single approach for the network as a whole	-	-	-	-	-	-	-	-
	It would be difficult to apply the revenue sharing incentive outside the franchised passenger area. There may be difficulties in areas where different franchising methods are used e.g. in franchises where the operator has some responsibility for stations maintenance and renewal. Operator-specific benchmarking might have to be used, and it cannot be guaranteed that the form of a franchise bid would provide this benchmark.							
Objectives	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
Service costs recovery	=	=	=	=	=	=	=	=
	There is not a clear direct impact of this option on service cost recovery. However, a stronger incentive with both up and downside might generate some volatility in NR’s income.							
Efficient whole-system whole -life industry net costs	+	+	+	+	+	+	+	+
	Revenue sharing is likely to motivate NR to be more responsive to demand, enabling improvements in how the asset stewardship of the station can improve passenger experience and ticket revenue. However, one open access operator suggested that investigation of this link would likely show it to be very marginal and likely dwarfed by other factors.							

<table>
<tr><td>Efficient long run investment decisions</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td><td>+</td><td>=</td><td>=</td></tr>
<tr><td></td><td colspan="8">Revenue sharing is likely to motivate NR to be more responsive to demand. This has the potential to encourage more efficient long term investment decisions. However, providing effective investment incentives requires a regulatory regime that is fully aligned with that objective.

The Revenue sharing option for the current SoW has been marked neutral as the current regime has a number of features that would reduce the effectiveness of the investment incentives that revenue sharing might provide. In particular, the central planning nature of the investment decision making process. The point here is that investment incentives do not matter (or matter less) if decisions are taken centrally considering other variables.

It is also likely that the revenue sharing incentive mechanism would require regular readjustment so that overall revenues and funding remained in balance, with the effect that incentives would be blunted in the long term.

For all these reasons, only the SoWs “beneficiary pays,” where significantly less central planning could be expected, has been marked positive.</td></tr>
<tr><td>Efficient performance management</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td></tr>
<tr><td></td><td colspan="8">There is not a clear direct impact of this charging approach on performance management.</td></tr>
<tr><td>Efficient use of network capacity</td><td>=</td><td>+</td><td>+</td><td>=</td><td>=</td><td>+</td><td>+</td><td>=</td></tr>
<tr><td></td><td colspan="8">As discussed above, revenue sharing is likely to encourage NR to be more responsive to demand, especially in the short term. This has the potential to incentivise more efficient use of station assets but this requires a regulatory regime that is fully aligned with that objective.

The Revenue sharing option for the current SoW has been marked neutral as the current regime has a number of features that would reduce the effectiveness of the use of capacity incentives. In particular, the central planning and contractual nature of the timetabling process and fares policy. The point here is that network use incentives do not matter (or matter less) if decisions are taken centrally considering other variables.

The SoWs ‘dynamic railway’, ‘on-rail competition’, ‘beneficiary pays’ and ‘capacity allocation’, have been marked positive, as these would reduce certain central planning and contractual features, and thus are more likely to enable capacity allocation incentives.</td></tr>
<tr><th>Judgement criteria</th><th>Current</th><th>Dynamic railway</th><th>On-rail comp</th><th>Specified franchises</th><th>Protect freight</th><th>Beneficiary pays</th><th>Capacity allocation</th><th>Regional powers</th></tr>
<tr><td>Predictability</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td><td>=</td></tr>
<tr><td></td><td colspan="8">There is not a clear direct impact of this charging approach on predictability.</td></tr>
</table>

Simplicity	-	-	-	-	-	-	-	-
	Introducing station-specific revenue sharing mechanisms would be complex. There would be difficulties aligning it with the franchising regime, correcting other funding flows and/or charges for the potentially large change in money flows, rebasing it for specific stations from time to time, and ensuring consistency with other aspects of the railway regulatory regime. Currently there is no station-specific volume incentive that could be adapted, as per the broader network revenue charging option. Significant work would be required to calculate station-specific revenue benchmarks, as well as determining how to allocate revenue to departing, arriving and transiting passengers.							
Transparency	=	=	=	=	=	=	=	=
	There is no clear direct impact of this charging approach on transparency.							
Low transaction costs	-	-	-	-	-	-	-	-
	Given the absence of existing station revenue sharing mechanisms we anticipate significant transaction costs to establish benchmarks, the appropriate scope of revenues and to reconcile revenues from different types of passenger to each location.							
Outputs	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
NR accountability	+	+	+	+	+	+	+	+
	The revenue sharing option could be understood as a way of making NR more accountable for the results obtained by operators at each station.							
Non-arbitrary allocation of costs	=	=	=	=	=	=	=	=
	There is not a clear direct impact of this charging approach on cost allocation.							
Optimal traffic growth	=	=	=	=	=	=	=	=
	There is not a clear direct impact of this charging approach on optimal traffic growth.							
Aligning industry incentives	+	+	+	+	+	+	+	+
	There would be more aligned incentives for NR and operators, which could lead to more co-operation among them and a more seamless experience for customers. However, given a lack of information in this area, we would recommend that more detailed work to scope the materiality of the current potential misalignment of incentives would need to be undertaken before choosing to pursue this option.							
Value for money for funders, taxpayers and users	=	+	+	=	=	+	+	=
	For all the reasons discussed above, the introduction of more revenue sharing could be expected to be beneficial mostly in the SoWs that could potentially be aligned with the introduction of such charge.							

Summary	Current	Dynamic railway	On-rail comp	Specified franchises	Protect freight	Beneficiary pays	Capacity allocation	Regional powers
	-	-	-	-	-	-	-	-
	There are some advantages of introducing station revenue sharing but it is possible that in cases where the benefit from doing so would be greatest, it may be more appropriate to make the franchised SFO responsible for MRR instead of Network Rail. Although there may be some issues where a single party has more control over facility charges, this would internalise the misaligned incentives and would remove the need for revenue sharing. This option is not available for network assets due to legal requirements for vertical separation but is an option that the DfT has already implemented through the franchising regime for Greater Anglia and Essex Thameside. Bespoke arrangements such as alliances could also be explored at certain locations. A station-specific revenue sharing mechanism could be implemented within a broader revenue sharing mechanism but the additional burden of isolating station-specific effects might not be justified. Therefore, while the conceptual benefits of revenue sharing at a broader level are well known there appears to be significant barriers to achieving them at station level. Solutions outside of the charging and incentives regime appear to be better placed to resolve issues regarding the alignment of incentives at stations.							

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