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16 May 2014

Addressee list in Annex D



Dear colleague,

Consultation on implementation of CP5 capacity charge for new open access operators

1. The purpose of this letter is to consult on the approach we take to implement our PR13 decision on the capacity charge for new entrant open access operators (OAOs), which we outlined in our final determination¹. If you wish to comment on any of the proposals in this letter, please do so by responding to Alex Bobocica by **1 July 2014**.

2. The consultation consists of this letter and annexes which explain the options we considered when developing our proposed approach. A list of addressees is contained in Annex D and we will also publish this consultation on our website. We will consider the responses to this consultation, and publish a decision letter by 5 September 2014.

3. In the remainder of this letter we:

- (a) recap on our final determination decisions on the capacity charge for new entrant OAOs;
- (b) propose the threshold at which capacity charge wash-up rates² are payable instead of CP4 equivalent capacity charge rates³;
- (c) explain how this threshold would be converted into a monetary baseline to go into Schedule 7;
- (d) explain the approach that should be followed when calculating CP4 equivalent capacity charge rates for a new entrant OAO; and
- (e) propose how we will define new entrant OAO.

¹ This is available at: <http://www.rail-reg.gov.uk/pr13/PDF/pr13-final-determination.pdf>.

² Capacity charge wash-up rates are equivalent to the CP5 capacity charge rates for franchised operators that were calculated by Arup for Network Rail as part of the PR13 recalibration of the capacity charge. The final report is available at <http://www.networkrail.co.uk/WorkArea/DownloadAsset.aspx?id=30064786027>

³ CP4 equivalent capacity charge rates are rates that are equivalent to the capacity charge franchised passenger operators would have paid for running services over a particular part of the network in CP4.

4. The proposals in this letter are specifically for CP5 and do not relate to work on charges that is being carried out to prepare for CP6 and beyond, such as the RDG review of the structure of charges.

Final determination decisions

5. In our final determination, we recognised that existing OAOs are unlike franchised passenger operators⁴, in that they are fully exposed to changes to the charges and incentives that are made at periodic review. We therefore concluded that existing OAOs will pay CP4 rates for their existing services (with any anomalies corrected⁵) and CP5 rates for any additional or new services. Contractually, the CP5 rates (as calculated by Arup in Network Rail's PR13 recalibration) are referred to as wash-up rates due to the way the formulae in the track access contract work.

6. We also concluded in paragraph 16.201, page 592 of our final determination on how the capacity charge should apply to new entrant OAOs. We said:

“New entrant OAOs will pay CP4 rates on services below a threshold (set to provide broadly equivalent treatment with existing OAOs) and CP5 rates above the threshold. This approach is to ensure that we are treating existing and new entrant OAOs in the same way, as required by European law and our section 4 duties.”

7. In our 30 September 2013 consultation letter⁶ on the contractual provisions for implementing options for the capacity charge in CP5, which preceded our final determination, we provided a more detailed proposal:

“For new OAOs, services below a threshold would pay CP4 rates; any train mileage above the threshold would pay CP5 rates; we would define the threshold as part of PR13 to be equivalent to that of existing services for the smaller of the two main existing OAOs, which at the time of writing is Hull Trains.”

8. We did not receive any objections to our proposal that the threshold is equivalent to that of existing services of the smaller of the two main existing OAOs, Hull Trains.

9. In summary this means that in CP5, new entrant OAOs will pay:

- (a) for services below the threshold: capacity charge rates that are the equivalent to CP4 rates; and
- (b) for services above the threshold: capacity charge wash-up rates, levied via a year-end wash-up;

⁴ Franchised operators pay CP5 rates on all their services but are protected through their franchise agreements against changes made to the charges at periodic review

⁵ Corrected CP4 rates were calculated by Network Rail for existing OAOs operating on the East Coast Main Line because, during the process of recalibrating the capacity charge in PR13, anomalies were discovered in the CP4 rates for these services, which meant that different operators using similar parts of the network with similar services had been subject to significantly different tariffs during CP4. The methodology is explained in the cover note to Network Rail's draft determination consistent price lists <http://tinyurl.com/luz3tqt>

⁶ This is available at <http://orr.gov.uk/what-and-how-we-regulate/regulation-of-network-rail/how-we-regulate-network-rail/periodic-review-2013/pr13-consultations/implementing-pr13-capacity-charge>

where the threshold is set to be equivalent to that for the Hull Trains' services as of the end of CP4.

The threshold at which the higher charge is incurred

10. The threshold is intended to ensure that a new entrant OAO is treated in an equivalent manner to an existing OAO in terms of when the new entrant would pay the CP4 equivalent rates, and when the new entrant would pay the wash-up rates.

Setting the threshold

11. In our final determination we did not specify exactly how the threshold, above which a new entrant OAO would pay the wash-up rates in CP5, would be calculated.

12. We have considered the following options on where to set the threshold:

- (a) the 2012-13 Hull Trains actual mileage sourced from the Track Access Billing System (TABS);
- (b) the annual mileage value used to calculate the Hull Trains baseline⁷ published by Network Rail on 10 February 2014⁸. This mileage figure was derived from train diagram information relating to the end of CP4⁹ provided by Hull Trains;
- (c) the £ baseline value for Hull Trains published on 10 February 2014; or
- (d) the number of services operated by Hull Trains over a defined period – e.g. yearly (weekday and weekend).

13. More detail on the options is in Annex A. With options (a), (b) and (d), the threshold would need to be converted into a baseline monetary amount to go into the contracts. This is explained in more detail in paragraphs 18 to 24 below. With option (c) the threshold is already a monetary amount.

14. We are proposing to take forward option (b), which is the most transparent to implement, is well understood by operators and Network Rail and is based on data that is readily available that has already been used to set the Hull Trains CP5 capacity charge baseline. It is therefore a measure which would easily be convertible into a baseline for a new operator and, by knowing the distance of their proposed services, a new entrant would be able to consider the necessary trade-offs when considering service patterns.

15. Option (b) would allow a new entrant OAO to run the same number of train miles at a CP4 equivalent rate as Hull Trains, while allowing its contractual baseline amount to be informed by the capacity charge rates calculated for that particular OAO's services.

⁷ The baseline is a contractual term which has a value in pounds. It is calculated for each service code by subtracting {the revenue that Network Rail would have received at threshold traffic levels if the CP4 equivalent capacity charge was levied} from {the revenue that Network Rail would have received at threshold traffic levels if the capacity charge was levied at the wash-up rates}. Paragraphs 18 to 24 explain the baseline in more detail.

⁸ The list of capacity charge baselines for CP5 can be accessed at: <http://www.networkrail.co.uk/cp5-access-charges/list-of-capacity-charge-baselines.xls>

⁹ This mileage accounts for all services which were planned to run, and therefore excludes the impact of cancellations or Network Rail possessions on traffic levels during the year.

16. If a new entrant OAO introduces more than one service code, we propose that the threshold mileage is allocated to service codes in the order that the services are introduced.

17. If the new entrant OAO introduces more than one service code at the same time, we propose that the threshold mileage would first be allocated to the proposed service codes where the wash-up weekday rate is higher than the CP4 equivalent weekday rate (we expect this to be the case with most service codes). The mileage would then be prioritised so it is allocated to the proposed service code with the biggest monetary difference between the CP4 equivalent weekday rate and the wash-up weekday rate. Any remaining threshold mileage would then be allocated to the other service code(s), following the same priority rule.

Converting the threshold into a baseline

18. In principle, our PR13 decisions in relation to the capacity charge for existing OAOs could have been implemented through the price list, without using a wash-up. However, this would not have been compatible with TABS, which requires a single charge for a service code. For pragmatic reasons, therefore, we decided to implement our decision through a wash-up.

19. For the same reason, we will also need to implement our decision for new entrant OAOs through a wash-up.

20. If we decide to set the threshold for new entrant OAOs as the Hull Trains annual train diagram mileage at the end of CP4 (option (b), our preferred option, above), the wash-up approach would involve converting the threshold mileage into baseline monetary amount(s).

21. The baseline amount for each service code would determine any year-end monetary wash-up an operator would have to pay if its actual mileage in a given year exceeds the threshold.

22. The purpose of the wash-up would be to ensure that across all its services an operator is paying:

- (a) wash-up rates, equivalent to the rates calculated by Arup as part of PR13, on any traffic above the pre-determined threshold; and
- (b) CP4 equivalent rates on any traffic below the pre-determined threshold.

23. For new entrant OAOs with more than one service code and mileage above the threshold, we propose that the baseline for an individual service code would be based on an allocation of the threshold mileage, using the prioritisation approach outlined in paragraphs 16 and 17.

24. More detail on the wash-up calculation and how we propose that the threshold is converted into a baseline for each service code of a new entrant OAO is contained in Annex B.

Calculating CP4 equivalent rates for a new entrant OAO

25. The capacity charge wash-up rates for a new entrant OAO should be calculated using the PR13 capacity charge recalibration model produced by Arup for CP5.

26. Since no CP4 capacity charge rates exist for services not currently running on the network, CP4 equivalent rates would need to be calculated for any new entrant OAO. We propose that these are calculated using an approach that is consistent to the one used to calculate the corrected CP4 rates for existing OAOs. This made use of the CP4 and CP5 capacity charge rates for franchised operators¹⁰.

How we define new entrant OAO in CP5

27. There are two things we need to decide in order to define a new entrant OAO in CP5:

- (a) the date that a company becomes an OAO, because to qualify as a new entrant, the OAO needs become a new OAO in CP5, not CP4; and
- (b) other requirements that the company must satisfy in order for it to be categorised as a new entrant OAO.

Date that a company becomes an OAO

28. In our 10 February 2014 letter¹¹ on the publication of capacity charge baselines, we said that we approved the baselines for existing OAOs on the basis of existing services being defined as those that have access rights on or before the start of CP5.

29. Accordingly, we propose defining a new entrant OAO as one which did not have access rights for services on or before the start of CP5 (irrespective of when the services are due to start running).

Other requirements that a company must satisfy to be categorised as a new entrant OAO

30. In reaching our proposal on how to define a new entrant OAO, we have had regard to the reason behind our final determination decision to allow new entrant OAOs to pay CP4 capacity charge rates on services below a threshold, which was to ensure that new entrant OAOs are treated in a way that is equivalent to existing OAOs.

31. We have considered a range of definitions of new entrant, ranging between:

- (a) the strict definition that a new entrant OAO is one with its first ever track access agreement entered into in CP5 and no affiliation to an existing OAO anywhere in its group company structure (whether a parent or subsidiary undertaking); and
- (b) the much less strict definition that a new entrant OAO is any company with its first ever track access agreement entered into in CP5 and a company number distinct from any other OAO.

More detail on the options we considered is contained in Annex C.

32. Our proposal is between these two extremes. We propose to define a new entrant OAO as an OAO with a company number distinct from any other OAO, with its first ever track access agreement entered into in CP5, and that meets one of the following criteria:

¹⁰ The CP4 capacity charge rates for franchised operators are available at <http://www.networkrail.co.uk/browse%20documents/regulatory%20documents/access%20charges%20reviews/cp4%20charges/d%20-%20list%20of%20capacity%20charge%20rates%20for%20cp4.pdf>. The CP5 capacity charge rates are available at <http://www.networkrail.co.uk/using-our-network/cp5-access-charges/>

¹¹ http://orr.gov.uk/_data/assets/pdf_file/0012/10515/cp5-capacity-charge-baselines-2014-02-10.pdf

- (a) it is a completely new OAO with no affiliation to an existing OAO at any point in its group company structure; or
- (b) if it is affiliated in any way to an existing OAO, it does not have any service codes with more than one station overlapping with the stations called at by any individual service code of that existing OAO¹².

33. Through this definition, we seek to ensure that the implementation of our final determination decision balances the following two considerations:

- (a) we do not want a new entrant OAO that is affiliated to an existing OAO to be unfairly discriminated against relative to a completely new OAO with no connection to an existing OAO at any point in its group company structure¹³; and
- (b) we do not want an existing OAO or its owner group to create an affiliate in order to pay CP4 equivalent rates on what amounts to an expansion of its existing services or services that are very similar those it already runs¹⁴.

Contractual wording

34. Our proposal for new entrant OAOs would involve the same formulae being used as those in Schedule 7, Section 6 of the template track access contract for existing OAOs. However, we may need to make some changes to the definitions of the components of the formulae and the contractual wording.

35. If we do need to make changes to the contractual wording of the model contract, then at the same time as we publish our decision letter, we will also publish an annex setting out the differences to the track access contract that would be needed to contractualise the policy.

Responding to our consultation

36. We would welcome your comments on anything in this consultation letter, particularly in relation to our proposals on:

- (a) the threshold at which capacity charge wash-up rates are payable instead of CP4 equivalent capacity charge rates;

¹² These criteria regarding overlapping stations can be illustrated by the following examples. If there are two service codes: service code 1 stops at stations A, B and C, and service code 2 stops at B, C and D, then service code 1 would be considered as having more than one station overlapping with service code 2. If there are three service codes: service code 3 stops at stations E, F and G, service code 4 at F, H and I and service code 5 at G, J and K, then service code 3 would not be considered as having more than one station overlapping with the stations in another service code.

¹³ For example, if train company A is a completely new OAO with no affiliation to an existing OAO, train company B is owned by the same owner group as an existing OAO and they both start to run open access services to somewhere that currently does not have a service run by an OAO, then we would expect both companies to be treated equally through the charges system

¹⁴ For example we would wish to avoid an owner group of an existing OAO, train company C, setting up a new OAO, train company D, to run very similar services to train company C in order to benefit from CP4 equivalent capacity charge rates.

- (b) how this threshold would be converted into a monetary baseline to go into the formula in Schedule 7;
- (c) the approach that should be followed when calculating CP4 equivalent capacity charge rates for a new entrant OAO; and
- (d) how we will define new entrant OAO.

37. Please send your comments to Alex Bobocica alexandra.bobocica@orr.gsi.gov.uk on or before 1 July 2014.

38. You should indicate clearly if you wish all or part of your response to remain confidential. Otherwise, we would expect to make it available on our website and potentially quote from it. Where your response is made in confidence, please could you provide a statement summarising it, excluding the confidential information, which can be treated as a non-confidential response.

Yours faithfully,



Robert Mills

Annex A – options considered regarding threshold at which CP5 capacity charge rates are payable

39. The table below shows the options we considered regarding the definition of a threshold for a new entrant OAO and the advantages and disadvantages of each. As explained in paragraphs 18 to 24, the threshold will be used to calculate a monetary baseline so, for example, if the threshold was train miles, then the baseline would be calculated using Hull Trains' train miles and the capacity charge rates of the new entrant OAO.

Option	Discussion
<p>Option A:</p> <p>Set the threshold at 2012-13 Hull Trains actual mileage sourced from TABS.</p>	<p>Advantages</p> <p>The data to implement this is readily available from TABS.</p> <p>It is a measure of train miles which would easily be convertible into a baseline.</p> <p>Disadvantages</p> <p>This approach would not be consistent with the approach used to derive CP5 baselines for Grand Central and Hull Trains, which were based on train diagram information.</p>
<p>Option B:</p> <p>Set the threshold as the annual mileage value used to calculate the Hull Trains baseline published by Network Rail on 10 February 2014. This mileage value was calculated using information from train diagrams.</p>	<p>Advantages</p> <p>This data is readily available and has already been used to set Hull Trains CP5 capacity charge baseline.</p> <p>It is a measure of train miles which would easily be convertible into a baseline.</p> <p>It is well understood by operators and Network Rail and, by knowing the distance of their proposed services, a new entrant would be able to consider the necessary trade-offs when considering service patterns.</p> <p>Disadvantages</p> <p>This would be an operational measure of Hull Trains activity rather than an economic measure. It would allow operators running on parts of the network where there is a greater difference between the CP4 equivalent and wash-up rates to benefit from a higher £ value baseline than Hull Trains, as opposed to option C below.</p>

<p>Option C:</p> <p>Set the threshold as the £ baseline value for Hull Trains published by Network Rail on 10 February 2014 (calculated using the Hull Trains annual train diagram mileage and the Hull Trains CP4 equivalent capacity charge rates and wash-up rates).</p>	<p>Advantages</p> <p>This value has already been validated and agreed as part of the exercise to calculate CP5 baselines for existing OAOs.</p> <p>This threshold would be an economic measure of Hull Train's activity (by using Hull Trains' capacity charge rates), rather than an operational measure. It would ensure that operators running on parts of the network where there is a greater difference between the CP4 equivalent and wash-up rates would not benefit from a higher £ value baseline than Hull Trains (as would happen with a mileage threshold which was then converted into a baseline).</p> <p>Disadvantages</p> <p>This methodology is based on the Hull Trains corrected CP4 capacity charge rates which were estimated using a methodology developed as part of the PR13 process to correct for previous anomalies in the rates. An approach using train miles (e.g. option B) would be less ambiguous and the baseline would not be based on a calculation, which has relied on assumptions being made.</p>
<p>Option D:</p> <p>Number of services operated over a defined period – e.g. yearly (weekday and weekend) – by Hull Trains</p>	<p>Advantages</p> <p>We have not identified any.</p> <p>Disadvantages</p> <p>It could result in situations of discrimination where a new entrant OAO was able to run more miles than Hull Trains at the CP4 equivalent rates, or conversely, for shorter services, fewer miles than Hull Trains at the CP4 equivalent rates. This is despite a longer service typically having a higher economic value per trip (passengers pay more to travel further) and for a given level of congestion on the network, a greater overall impact on reactionary delay.</p> <p>It could also result in situation where a new entrant was able to introduce a service similar to an existing operators' service, but which was slightly longer, and pay CP4 rates on more miles than the existing operator would be able to pay CP4 rates on if it lengthened its service.</p>

Proposed option

1. We consider that option B is the most appropriate way of ensuring that a new entrant OAO is treated in an equivalent manner to an existing OAO.

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2. It is the most transparent to implement, is well understood by operators and Network Rail and is based on data that is readily available that has already been used to set the Hull Trains CP5 capacity charge baseline. It is therefore a measure which would easily be convertible into a baseline for a new operator and, by knowing the distance of their proposed services, a new entrant would be able to consider the necessary trade-offs when considering service patterns.
3. Option B would allow a new entrant OAO to run the same number of train miles at a CP4 equivalent rate as Hull Trains, while allowing its contractual baseline value to be informed by the capacity charge rates calculated for that particular OAO's services.
4. While option C has the benefit of being the same as the Hull Trains baseline in monetary terms, it would also mean the baseline would be based on the calculation of the Hull Trains baseline, which relied on assumptions and at the time of being made was only intended for use as the Hull Trains baseline. It is also a less straight forward threshold measure to understand than option B and our final determination decision referred to the threshold being set at a level to be equivalent to that of existing services for the smaller of the two main existing OAO. This lends itself more to an operational based measure, such as option B, rather than a monetary one, such as option C.

Annex B – converting the threshold into a baseline for each service code

1. As discussed in the main section, in principle, our PR13 decisions in relation to the capacity charge for new entrant OAOs could be implemented through the price list. However, this is not compatible with TABS, which requires a single charge for a service code. For pragmatic reasons, therefore, we propose implementing our decision through a wash-up. This is consistent with our approach for implementing our decision for existing OAOs.
2. The wash-up represents the monetary amount an OAO pays Network Rail at the end of the year if its actual mileage in a given year exceeds the threshold. The formula for the wash-up for existing OAOs as outlined in Schedule 7 is:

$$\text{Wash-up} = (M_{te} - B_{te} - A_{te})$$

3. In this formula, A_{te} is Network Rail's estimate of the revenue it is owed in relation to the particular service code for the year t in accordance with the main capacity charge formula (i.e. not the wash-up) in Schedule 7 of the open access TAA¹⁵. This is in effect the amount obtained by applying the CP4 equivalent weekday and weekend rates, as set out in the List of Capacity Charge Rates, to actual traffic within the year.
4. M_{te} is Network Rail's reasonable estimate of the aggregate revenue it would have been entitled to receive during year t for a specific service code if, in the main capacity charge formula, the weekday and weekend capacity charge wash-up rates were used instead of CP4 equivalent rates.
5. B_{te} is the baseline value in pounds (defined below).
6. The purpose of the wash-up is to ensure an operator is paying wash-up rates, equivalent to the rates calculated by Arup as part of PR13, on any traffic above the pre-determined threshold. Consistent with our final determination, each baseline is defined such that its respective wash-up is equal to zero if traffic is at threshold levels.
7. We propose that the same formula for wash-up would be used and, with our preferred threshold option B (the annual mileage value used to calculate the Hull Trains baseline), the baseline for each service code of a new OAO would be equal to:
 - (a) the revenue that Network Rail would have received at the threshold traffic levels if the capacity charge was levied at the wash-up rates (i.e. the new full CP5 rates as calculated by Network Rail using the tool developed by Arup as part of the PR13 recalibration exercise);
minus:
 - (b) the revenue that Network Rail would have received at the threshold traffic levels if the CP4 equivalent capacity charge was levied.

¹⁵ This is the formula at the beginning of section 6 of Schedule 7 (pages 121 to 122) of the document: 'Review Notice: Open Access Passenger Operator Track Access Agreements' (http://orr.gov.uk/data/assets/pdf_file/0006/5874/pr13-review-notice-open-access.pdf). A_{te} is equivalent to K_t in this formula.
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8. The baseline value of each service code would determine any year-end monetary wash-up an operator would have to pay if its actual mileage in a given year exceeds the threshold.

9. The baseline for a service code would be calculated through the following formula:

$$\text{Baseline} = \text{allocation of threshold weekday train miles} * (\text{weekday wash-up rate} - \text{CP4 equivalent weekday rate}) + \text{allocation of threshold weekend train miles} * (\text{weekend wash-up rate} - \text{CP4 equivalent weekend rate})$$

10. As stated in the main section, if the new entrant OAO introduces more than one service code at the same time, we propose that the threshold mileage would first be allocated to the proposed service codes where the wash-up weekday rate is higher than the CP4 equivalent weekday rate (we expect this to be the case with most service codes)¹⁶. The mileage would then be prioritised so it is allocated to the proposed service code with the biggest monetary difference between the CP4 equivalent weekday rate and the wash-up weekday rate. Any remaining threshold mileage would then be allocated to the other service code(s), following the same priority rule.

11. In practice, for the purposes of this calculation, for each service code, the threshold will also need defining in weekday and weekend mileage respectively. We propose that for each service code, the threshold mileage is apportioned across the weekday and weekend mileage in such a way that in both cases it forms the same proportion of total mileage.

12. The example below shows how the threshold mileage would be allocated across a new operator's service codes if more than one service code was introduced. The numbers in the example are illustrative.

Example

Table 1: Threshold mileage (in practice this would be Hull Trains' threshold mileage, however these numbers are illustrative only)

	Weekday miles	Weekend miles	Total miles
Threshold	50,000	10,000	60,000

Table 2: New operator's proposed service mileage and split of mileage between weekdays and weekends:

	Weekday	Weekend	Total	% weekday miles
Service code 1	33,000	8,000	41,000	80%
Service code 2	27,000	5,000	32,000	84%

¹⁶ It has recently come to light that this formula would not deliver the intended result in instances where the CP4 equivalent rate is higher than the wash-up rate. This is due to the appearance of negative values within the formula. We expect instances of the CP4 equivalent rate being higher than the wash-up rate to be the exception to the rule and are currently reflecting on how the formulae would need to be designed in the event this occurs.

Allocation of threshold mileage for new entrant's service codes


This assumes that 'Service code 1' is the first one introduced or has priority over 'Service code 2' based on the priority rule outlined in paragraph 11, above.

The threshold mileage is allocated to each service code on a total basis (i.e. without taking into account the split between weekday and weekend mileage). The percentage split between weekday and weekend miles of the new operator's proposed services (Table 2) is then used to allocate the total threshold mileage across weekday and weekend, as shown below.

	Threshold miles allocated (total)	% of mileage on which CP4 rates are paid	% weekday miles	Weekday threshold miles	Weekend threshold miles
Service code 1	41,000	100%	80%	33,000	8,000
Service code 2	60,000 – 41,000 =19,000	19,000/32,000 = 59.4%	84%	19,000 * 84% = 16,031	19,000 * 16% = 2,969

Annex C – options considered regarding the definition of a new entrant OAO

1. The table below shows the options we considered regarding the definition of a new entrant OAO and the advantages and disadvantages of each. The options ranged from being very tightly defined to more flexible.

Strictly defined			Less strictly defined
<p>Option 1 – completely new operator with no affiliation to an existing OAO at any point in its company structure</p>	<p>Option 2 – operator with a new company number and a new track access agreement but with certain restrictions.</p> <p>Geographical restrictions could relate to:</p> <ul style="list-style-type: none"> - % of mileage over the same track sections as existing services of affiliated companies - % of mileage within the same NR operating route as existing services of affiliated companies - number or % of stations in common with the existing services of companies affiliated with the operator. <p>Other restrictions could relate to the proportion of a new entrant OAO that is owned by the owner group of an existing OAO</p>	<p>Option 3 – any operator with a new company number and a new track access agreement</p>	
<p>Advantages</p> <ul style="list-style-type: none"> • Clear simple definition, reducing the risk of loopholes 	<p>Advantages</p> <ul style="list-style-type: none"> • Mitigates some of the discrimination risk associated with option 1 • Reduces the risk associated with option 3 that an existing OAO or its owner group could set up a new 	<p>Advantages</p> <ul style="list-style-type: none"> • Allows companies with a degree of affiliation with existing OAOs to introduce new services as a new entrant, and therefore unlikely to result in discrimination between an OAO with 	

	company to run very similar services, in order to take advantage of the CP4 equivalent rates	this characteristic and a new entrant with no affiliation to an existing OAO within its company structure
<p>Disadvantages</p> <ul style="list-style-type: none"> • Could result in discrimination between a new OAO that is affiliated with an existing OAO (paying wash-up rates when introducing a new service) and a completely new entrant running a similar service (who would pay CP4 equivalent rates on some or all of mileage) • Very strict definition means could result in new operator paying CP5 rates on all mileage even if it only has very small degree of affiliation with an existing operator (e.g. owner group has 5% share). Could therefore disincentivise the setting up a new operator which has a small degree of affiliation with an existing OAO, even if this arrangement might otherwise make sense economically. 	<p>Disadvantages</p> <ul style="list-style-type: none"> • Need to be careful to reach a definition that is clear, pragmatic and achieves the right balance between avoiding undue discrimination and avoiding the risk of exploitation by existing OAOs or their owner groups. • There would be a degree of judgement involved in setting the criteria. 	<p>Disadvantages</p> <ul style="list-style-type: none"> • Very easy for an existing OAO to exploit by setting up an affiliate with a new company number and a new track access agreement, in order to take advantage of the CP4 equivalent rates. This is not consistent with the principles behind the decision in our final determination that existing OAOs only pay CP4 equivalent rates on existing mileage and pay wash-up rates on any mileage beyond this. • The end result could be little more than a regulatory hurdle/ cost, with existing operators setting up affiliate companies to run similar services, even when it would not be commercially sensible to do so in normal circumstances.

Proposed option

2. On balance we think that option 2 is the most appropriate. Option 1 could result in a new entrant OAO that is affiliated with an existing OAO being discriminated against. Option 3 would risk existing OAOs or their owner groups taking advantage of CP4 equivalent rates if they expand services in their current market, simply by setting up a new company. We do not regard this as consistent with the principles behind the decision in our final determination.

3. We considered various ways that option 2 could be implemented. We considered whether to place restrictions based on company structure in terms of the degree of affiliation a new entrant has with an existing OAO or owner group. We think in practice it would be very difficult to reach a straightforward definition due to the many ways a group of companies can be structured. Moreover, it could result in a new entrant OAO with the same owner group as an existing OAO paying a higher rate for a new service in a new market than a new entrant with no affiliation to an existing OAO would.
4. We therefore think that incorporating some geographic criteria is the best way of avoiding undue discrimination while at the same time minimising the risk of existing OAOs or their owner groups exploiting the criteria for new entrant OAOs when expanding existing services. We do not think criteria relating to % of mileage over the same track sections as existing services or % of mileage within the same NR operating route as existing services provides a good reflection of whether a service is operating in a new market or not. One of the key elements that define the market covered by a service is what stations it stops at.
5. Our proposal is to define a new entrant OAO as an OAO with a company number distinct from other OAO, with its first ever track access agreement in CP5, and which meets one of the following criteria:
 - (a) it is a completely new OAO with no affiliation to an existing OAO at any point in its group company structure; or
 - (b) if it is affiliated in any way to an existing OAO, it does not have any service codes with more than one station overlapping with the stations called at by any individual service code of that existing OAO¹⁷.

¹⁷ These criteria regarding overlapping stations can be illustrated by the following examples. If there are two service codes: service code 1 stops at stations A, B and C, and service code 2 stops at B, C and D, then service code 1 would be considered as having more than one station overlapping with service code 2. If there are three service codes: service code 3 stops at stations E, F and G, service code 4 at F, H and I and service code 5 at G, J and K, then service code 3 would not be considered as having more than one station overlapping with the stations in another service code.

Annex D – Addressee list

Abellio, Alliance Rail Holdings, Arriva Trains Wales, ATOC, Centro, Chiltern railways, Cross Country Trains, DfT, East Coast, First Capital Connect, First Scot Rail, First Hull Trains, First Greater Western, First Transpennine Express, First Group, Go ahead, Go-op, Grand Central, Greater Anglia, London Midland, LOROL, Mersey Rail, National Express, Network Rail, Northern Rail, PTEG, Rail Delivery Group, Southeastern Railway, Southern Railway, Stagecoach, Stagecoach East Midlands Trains, Stagecoach South Western Trains, Swanage Railway, Transport Scotland, Virgin Trains