



# Department for Transport

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## Mode Shift Revenue Support and Waterborne Freight Grants Schemes

As you may be aware the UK Government has completed a spending review for the period April 2016 to March 2021. This has confirmed funding for England for the continuation of the mode shift revenue support (MSRS) and waterborne freight grant (WFG) schemes. Both schemes also have European Union State Aid clearance to operate across the United Kingdom until March 2020.

The funding envelope for the schemes for the years 2016/17 to 2019/20 (inclusive) has been set at approximately £16m per year for England, compared to levels of actual expenditure between 2010/11 and 2014/15 averaging about £18m per year.

Total UK Government Spend -MSRS and WFG	2010 to 2015 Outturn	2015 to 2020 Forecast / Indicative Budget	of which 2015/16 Forecast	2016 to 2020 Indicative Budget
£m	88.9	83.3	20.55	62.6

DfT intends to invite applications for the MSRS and WFG during the next few weeks for the period up to March 2019 (as there is a three year limit on MSRS contracts and for a WFG). There will be continued opportunities for applications through the life of the schemes, probably at a frequency of about three times a year.

The Department is considering two administrative changes to the MSRS scheme in England, but which could impact on rates for cross border flows. These are:

- (1) to increase the assumed wagon utilisation rates for port-related intermodal rail freight in the MSRS scheme; and
- (2) to offer MSRS applicants (for all types of flow) the choice between:
  - a. a contract for up to twelve months; and

- b. a longer contract with no early exit penalties, period negotiable but not beyond March 2020, with an automatic reduction in grant rates after twelve months of 10% and a further 5% (to total 15%) after twenty four months.

The attached note seeks views and evidence to inform decisions about the possible changes by 1 February 2016.

Yours sincerely

A handwritten signature in black ink, appearing to read 'Duncan Price', with a horizontal line underneath.

**Duncan Price**

## **Note: Proposed Administrative Changes to the Mode Shift Revenue Support Scheme in England**

### Background

The grant schemes involve four types of traffic, with the MSRS scheme applying to the first three listed and, because of different State Aid rules, the WFG scheme applying to the fourth:

- port-related intermodal traffic, where containers are transported by train from or to ports;
- domestic intermodal traffic, where containers are transported by train within Great Britain;
- certain bulk traffic of commodities transported by rail and inland waterways within Great Britain. Intermodal (container) traffic rail freight services using the Channel Tunnel to and from Great Britain is also considered as a bulk commodity;
- coastal shipping between ports in the United Kingdom.

Decisions related to Scotland and Wales are devolved, so on some flows more than one Government makes funding decisions. This note relates to England only. However the Department will ensure the Scottish and Welsh governments are involved in the consideration of any changes to the administration of the MSRS scheme.

The principle of the grant schemes is that they take account of the effects of road freight mileage not captured in commercial transactions, net of similar effects on rail and water. This includes valuing the effects to road freight on congestion for other road users, as well as accounting for the external effects of the road freight movements, including greenhouse gas emissions, air pollution, noise, public safety and movement-related taxation. This principle continues and these benefits will be valued in the same way as when the schemes for April 2015 to March 2020 were finalised early last year.

For the grant schemes to be effective for their public objectives they need to be supporting traffic that would not operate on railways or water anyway. So in addition to the benefit test, the scheme also considers whether flows could run commercially or not. For flows that appear unlikely to run commercially, there is a ceiling on the financial support available, which prevents the support exceeding the assessed commercial gap. This ceiling is particularly important for flows that are close to being commercially viable for rail or water.

The recent increases in inter-modal traffic are suggestive not only of a sound economy but also of a competitive rail freight sector, particularly for some port-related flows. Investment has been made in routes allowing larger and longer trains and this has been reflected in the grant rates payable. Investment is also being made in wagons to allow the more efficient loading of trains. More routes now operate without grant and DfT aims to encourage that trend further.

The Department is therefore proposing two operational changes to the MSRS scheme.

## Proposal 1: Consideration of Commercial Costs

The 2014 review of the schemes indicated that in the event of the grant schemes stopping (which would have happened if they had not received State Aid approval) or being phased out, based on an analysis restricted to the predominant category of supported freight (intermodal) that a significant proportion of the flows would have been retained by rail.

During the 2014 review the assumed utilisation per unit of space on port-related intermodal trains for containers was reduced to reflect the widespread use of wagons with a loading length of 60 feet and the increasing predominance of 40 foot containers over 20 foot containers at ports. This assumed utilisation affects the commercial costs assumed for rail freight in the grant scheme.

Since the review there has been a major increase in the intermodal port-related traffic supported by the MSRS grant. This is suggestive of better market conditions for this sector of rail freight and a better climate for forward investment in wagons adapted better to intensively use the space available on trains.

So, for port-related inter-modal flows it proposes to amend the wagon to loaded container ratio used (and sought) for costing purposes within the MSRS scheme. Specifically the Department proposes to increase the assumed utilisation of wagon space from an average of 1.25 containers per 60 foot wagon to 1.333. This is equivalent to assuming that on average one eighth of a train's loadable length is unused due to the wagon-container size consistency problem, rather than one sixth. This represents a productivity gain. This assumption would still be lower than the equivalent used for the 2010 to 2015 scheme.

To illustrate the impacts of such a change a revised table of maximum grant rates is attached at Annex A, but please note that these are rates from an adjusted MSRS model which assumes the change would apply to all flows, not just those in England.

The existing MSRS model also assumes that 10% of containers transported are not loaded and there are no significant back hauls. Neither of these assumptions is proposed to be changed.

The effect is to remove or reduce grant for a number of flows which the previous cost model indicated were close to commercial operation. The previous model indicated these flows were the least vulnerable to being lost to rail and back to road if grant support were withdrawn.

With an un-amended scheme and if current trends continue, it would be likely that some high value flows (with benefit to cost ratios of between about 4:1 and 3:1) would not be supported and many would be lost to rail, because of the expanding number and volume of eligible flows. So the Department considers the proposed change to the scheme would secure more traffic for rail overall.

**Q1: Please comment on the DfT proposal to increase the assumed wagon utilisation rates for port-related intermodal rail freight.**

The assumed container to wagon utilisation rate for the 2015 to 2020 scheme for domestic intermodal rail freight is higher than the 1.33 already and no change is proposed.

Bulk flows in the MSRS are considered on a case by case basis, with evidence collected about the rail or water costs compared to road transport comparison costs. A number of flows have operated with grant for several years. The current contracts expire in March 2016. With funding for MSRS secured to the end of the State Aid clearance in 2020, DfT will examine systematically all bids for continued support and for new flows, including to ensure productivity gains on rail and water are being secured.

WFG schemes last for a maximum of three years, with a decreasing public funding profile to help lead them to commercial viability. The consideration of forecast costings will continue in the same way as now and there will be no re-examination of the existing WFG contract which continues past March 2016.

**Q2: Do you have any comments on the proposed operational approach to costs in relation to domestic intermodal and bulk flows eligible for the MSRS scheme and the WFG scheme?**

#### Proposal 2: Multi-Year Contracts and the Option of Variable Grant Rates

Secondly because of the timing of State Aid clearances and the spending review, MSRS contracts for financial support were only agreed for a maximum of a year in 2015/16. DfT wishes to return to multi-year contracts in MSRS, as was the case in the 2010 to 2015 scheme.

Experience during 2015/16 suggests there is a risk, when there is a high level of demand, that established contracts consume the vast majority of the available budget and exclude later good and high value proposals. Market conditions in the 2010 to 2014 period meant that this risk was generally not realised, but recently it has only been managed by using under-spend from elsewhere in DfT's budgets. This risk would be magnified by the return of multi-year contracts in MSRS.

The cost modelling for the MSRS scheme does not distinguish between the cost overheads of adding extra volumes to existing flows (by more intensive train use or using paths on more days) compared to developing new flows, including securing for trains that have not run before. It is technically difficult to model this level of complexity of the cost structure and DfT does not propose to do so.

However it is likely that new to rail (or water) flows will be disproportionately represented in applications later in the life of the MSRS scheme (compared to the beginning when applications will be dominated by applications for continued funding for flows already on rail and water). For policy reasons it is important that these later applications, including for new to rail and water flows, that there remains some budget for them to access DfT funding support.

If the scheme operates as a multi-year scheme, experience from 2015/16 suggests that the first round of applications could exhaust much of the budget, blocking applications

developed later in the 2016/17 and beyond. DfT intends to manage the budget to reduce the likelihood of this, but multi-year contracts risk the budget management either leading to an underspend in 2016/17 or committing nearly all of the budget for later years.

One way of avoiding these risks would be to limit the duration of all contracts to twelve months. This would mean supported contracts would re-apply for support in competition with any new proposals during the lifetime of the MSRS scheme. This would remove some of the longer term certainty about grant funding, which DfT understands is important to the grant recipients.

The Department therefore proposes to offer MSRS applicants (for all types of flow) the choice between:

- (i) a contract for up to twelve months;
- (ii) a longer contract with no early exit penalties, period negotiable but not longer than 3 years or beyond March 2020, with an automatic reduction in grant rates after twelve months of 10% and a further 5% (to total 15%) after twenty four months.

**Q3: Do you have any comments about the proposed approach in the MSRS scheme to contracts of more than twelve months in length?**

**Q4: Would you rather the MSRS scheme operates with contracts lasting a maximum of 12 months?**

#### Timetable

Please send any comments to [catharine.parton@dft.gsi.gov.uk](mailto:catharine.parton@dft.gsi.gov.uk) by no later than 1 February 2016.

DfT proposes to seek applications for the first round of the MSRS scheme by 4 March 2016.

The administration of the MSRS scheme for the period beyond March 2016 may or may not reflect the proposals in this note. DfT intends to finalise by March 2016 and in consultation with the Scottish and Welsh Governments the administrative arrangements for the MSRS scheme beyond March 2016. If organisations considering applying for the MSRS or WFG schemes want further advice, including prior to final decisions about the details of the administrative arrangements of the MSRS scheme, they should contact the DfT team administering the grants, via [catharine.parton@dft.gsi.gov.uk](mailto:catharine.parton@dft.gsi.gov.uk).

## Annex A

Maximum Grant Rate for MSRS (Intermodal) Port following a proposed increase in utilisation rate from 1.25 to 1.33.

		Destination Zone (Inland Terminal)																	
		1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18
Origin Zone (Port)	1	0	40	51	27	23	0	0	0	0	0	15	36	54	52	27	0	63	7
	2	79	0	63	20	24	0	0	0	0	0	0	17	40	23	19	0	19	68
	3	63	66	0	65	56	87	78	0	0	0	94	55	66	66	83	0	51	12
	4	39	4	76	0	9	45	76	29	0	0	42	63	51	33	59	0	0	0
	5	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
	6	0	0	57	54	30	0	61	75	0	0	63	84	5	54	34	0	0	0
	7	0	0	0	18	73	97	0	57	49	15	81	36	0	0	0	0	0	0
	8	0	0	0	4	59	65	3	0	95	74	24	28	0	0	0	0	0	0
	9	0	0	0	0	0	38	62	89	0	89	0	0	0	0	0	0	0	0
	10	0	0	0	0	0	0	29	52	89	0	0	0	0	0	0	0	0	0
	11	17	0	49	48	21	60	14	24	0	0	0	19	88	62	55	10	6	0
	12	71	0	28	66	39	78	31	40	0	0	15	0	80	47	63	0	41	0
	13	28	6	35	44	74	0	0	0	0	0	80	79	0	52	0	48	47	19
	14	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0	0
	15	19	0	38	64	57	9	28	0	0	0	47	63	0	21	0	38	38	0
	16	62	0	0	0	0	0	0	0	0	0	25	0	48	14	38	0	133	0
	17	19	0	27	0	12	0	0	0	0	0	18	40	42	42	33	128	0	53
	18	30	68	43	8	3	0	0	0	0	0	0	17	60	35	27	0	57	0