4th Floor
Northern House
9 Rougier Street
York
YO1 6HZ

Joanna Whittington
Director
Railway Markets and Economics
Office of Rail and Road

Telephone ✂
Email ✂

Dear Joanna

PR18 Reviews of Schedules 4 and 8 of Track Access Contracts

Thank you for the opportunity to attend the stakeholder event in November, which we found very useful, it's always good to have the opportunity to meet up with fellow industry colleagues and to share experiences.

Following the event please see below Northern Rails response to the effectiveness of the current regimes together with examples and some suggestions of ways we think the regime can be even more effective and provide the correct incentives for Network Rail and the industry.

Yours sincerely

Liz Hudson
Assistant Track Access Manager

Schedule 4, the Possessions Regime

1. The purpose of Schedule 4

Schedule 4 is designed to incentivise Network Rail to plan its engineering efficiently and in a timely manner. Northern believes that these principles must remain at the heart of the regime and welcomes the opportunity to be able to debate this as part of the Periodic review process (PR18).

2. The level of compensation received by Operators

We have recently undertaken an exercise in order to assess the formulaic compensation we received in relation to Type 1 54 hr weekend possessions. Our analysis has uncovered that where we generally have large passenger numbers on heavily utilised routes the compensation we receive fails to cover our costs. Northern Rail recognises that the regime is designed on ‘swings and roundabouts’ principles, however, we have concerns that prolonged weekend disruption on high volume routes into key urban centres presents a significant cost risk to us.

Sustained Planned Disruption provides operators with a mechanism for full cost recovery in these circumstances; yet our analysis has shown that the thresholds for triggering this mechanism are currently set too high. Northern believes that as the triggers are set at service group level for an operator such as ourselves it becomes virtually impossible to prepare a robust claim under these provisions. We would ask that ORR reviews this mechanism as part of the PR18 process.

One area that isn’t incorporated into the compensation regime is the provision to compensate or provide a good will gesture to regular travellers and season ticket holders in times of prolonged disruption. The risk to an Operator is that customers will find alternative transport methods and don’t return once the service has returned to normal. As a regional operator Northern relies heavily on its commuters for revenue.

3. Notification discount factors

Northern believes that the notification discount factors are currently acting as a perverse incentive, as they incentivise Network Rail to plan possessions in advance to get them at a cheaper rate. We often find that Network Rail books up possessions to secure them at a cheaper rate without fully understanding the work content, and more importantly before they have engaged their contractor. Once contractors have been engaged we often find that the access footprint requirement changes and Network Rail then requests additional late notice access which places additional cost and resource burdens onto operators. The industry needs to explore ways in which the regime can incentivise Network Rail to plan its access strategy right first time in order to eradicate perverse behaviours and late notice change.

4. The Access Charge Supplement (ACS)

ACS is payable by franchised operators in return for full Schedule 4 compensation and the regime is designed to be financially neutral over the control period. The value of the ACS is based on assumed maintenance/renewals volumes. This in turn relies heavily on ensuring that possessions are booked in the most efficient manner, this poses a financial risk to both Operators and Network Rail as the overall financial position is not known until the end of the control period.

In order to alleviate some of the risk it may be beneficial to review the baseline Schedule 4 costs during the control period in order to assess the volume of ongoing renewal and maintenance work.

5. The Sustained Planned Disruption mechanism

Under part 3 of Schedule 4 if an operator reasonably believes that Sustained Planned Disruption (SPD) has occurred, compensation can be calculated on the basis of actual revenue losses and costs (rather than formulaic).

However in order to trigger SPD, the routes affected have to be under the same Service Group and for a regional operator such as Northern it becomes impossible to trigger, as our routes affected by the disruption are often included in more than one Service Group. The costs trigger for SPD is also unwieldy as this looks at cost across the whole business. Given the vast scale of our operation it becomes impossible to trigger on cost and extremely resource hungry trying to build a case.

The thresholds appear to be set very high which also makes this compensation mechanism inoperable, and we would argue that there needs to be a review of the current mechanism, .This is even more critical given the amount of engineering work that is currently underway in the North of England. Northern Rails view is that the operator must not be put in a position where it is subsidising Network Rail's investment programme and taking on a cost risk for Network Rail's efficient delivery.

During 2014 and in to 2015 Northern Rail were subject to a significant number of late notice possession requests (which were all under 54 hours) due to Network Rail's inability to plan its enhancement portfolio effectively. Our rail replacement costs were significantly more than the compensation we received given these routes are heavily utilised commuter routes into Manchester. These possessions caused considerable disruption & inconvenience to both us and customers over a much longer period of time than was initially anticipated when the original access footprint was agreed.

Due to the nature of our services and the number of service groups we have we were unable to trigger the Sustained Planned Disruption mechanism. We would therefore argue that sustained planned disruptions thresholds be set at a route level as opposed to a service group level.

7. Perverse incentives and unintended consequences

On numerous occasions possessions have been changed, which often causes a change to the type of RoU. An example of this was when Network Rail originally planned a blockade over the Easter weekend which would have triggered a Type 2 RoU claim the possession was subsequently changed to four days and became a Type 1 RoU.

This transferred a significant cost risk to Northern as we then subsequently only received the formulaic compensation, which did not compensate us fully for the rail replacement required in transporting the large volumes of customers travelling over the bank holiday weekend.

In order for Network Rail to gain the maximum discount for possessions they are incentivised to book the access they require years in advance of the delivery of the work. This can often results in operators having to agree late notice access over and above what was originally agreed as the contractor is unable to deliver the work in the agreed access footprint and these requests often come well outside of industry timescales.

We are keen to work with Network Rail to support the delivery of their enhancement portfolio, however, by adopting a collaborative approach with NwR to deliver the right solution for the industry this can often mean TOC's are exposed to a significant cost risk, and we believe the schedule 4 regime does not really incentivise the correct behaviour in order to deliver industry efficient solutions.

Schedule 8, the Performance Regime

1. The Purpose of Schedule 8

Schedule 8 in its current format is a simple and effective model for representing the formulaic impacts on the revenue impact of performance variation from forecast delivery.
It is logical for Operators to use Network Rail as a central conduit for compensation to pass through for delay impact between Operators whilst NwR maintain financial impartial neutrality.

For local service based/regional train Operators with PTE fixed based revenue streams, the impact of poor performance does not impact as greatly on the long distance revenue impact so payment rates are lower and incentives to improve the service through this schedule are not viable for either train Operator or Network Rail.

2. Network Rail payment rates

The payment rates are calculated at service group level and intended to reflect the revenue losses arising from poor performance. As mentioned above and noted from RDG's comments, the payment rates do not take in to account societal impacts efficiently nor does it take in to account the true cost on the day for the disruption recovery and the alternative transport requirements together with the delay repayment process.

The payment rates also don't take in to account any future funding agreements whereby the level of subsidy received by the operator maybe significantly reduced during the Control period.

3. Network Rail benchmarks

Northern have no issues with the methodology and logic behind the alignment of Network Rail's benchmarks to PPM.

The process of a flat line benchmark whilst easy to manage, does not allow the distinction between good or poor performance and seasonal variation. Furthermore it does not take into account the impact of network closures where a series of weekend blockades on a line of route will naturally cause a reduction in the average lateness as the average stops component is based on a perfect week.

4. Sustained poor performance (SPP)

For large operators the Sustained poor performance (SPP) process is unwieldy and difficult to trigger, the specified thresholds do not encourage its use and the revenue impact is often masked by the scale of the business and is compounded in areas where Metro style zonal tickets do not allow direct alignment of journey to ticket.

5. Operator payment rates and the star model

Northern believes that the Star Model is the most logical method for penalty and good performance payments between Operators via Network Rail without the need for numerous bilateral payment contracts and bespoke benchmarks for each possible interaction between Operators

6. Operator benchmarks

Northern believes the principle of having a fixed state of interaction impact benchmarks for Operators is a sensible one. However as with Networks Rails benchmarks it presents concerns. Consideration should be given to changes in traffic growth where new service flows are introduced, as the steady state benchmark will require increased compensation, not due to worsening performance by the operator but where they are impacted by a 3rd party.

For example if operator A introduces a new service flow part way through a control period and they adjust their appendix 1 to take this in to account, operator B will not make any adjustments to their benchmarks, however the increased traffic will cause more lateness on the network. Thus meaning that operator B will pay more compensation through to Network Rail to compensate operator A even though due to the recast of appendix 1 operator A the uplift in average lateness has been neutralised and the impact of the long run is not experienced.

7. Treatment of cancellations

Northern Rail believes the impact of cancellations should continue to be included in Schedule 8.

8 Liability caps

Northern has no comments in relation to liability caps

9. Interaction with regulated outputs and franchise obligations

As previously mentioned the regime does not support or encourage regional operators in regard to performance improvement business cases, due to the low payment rate associated with large volumes of commuter traffic in to major urban cities.

The impact of poor performance has a far greater societal impact and suppresses future growth and leisure travel which are not components of the Schedule 8 business case as noted by RDG 6.3 & 8.2.

10. Perverse incentives and unintended consequences:

Schedule 8 does not encourage improvement on routes where passengers have to use the railway as no other reasonable viable alternative exists.

It also creates a culture of managing delays based on their size and relative cost which can mean regional operators are often delayed in favour of more expensive routes.

11. Other aspects of the regime:

Schedule 8 doesn't compensate operators for the provision of alternative transport and it may be something to consider by utilising the Schedule 4 VTP framework to cover these costs.

As the industry is moving towards 'on time railway' as per the timetable and away from PPM is there a case that the threshold for delay explanation (currently 3 minutes) is lowered in line with improvements in accuracy of measurements and that the information to passengers is also subject to a tighter threshold of explanation. Monitoring points and their weightings are based on the main passenger flows in a service group, Northern Rail would question whether these are still representative or should they be more granular.