



PR18: Schedule 8 – Draft impact assessment on effectiveness of the Sustained Poor Performance (SPP) regime

December 2016

This document has been published alongside [‘Improving incentives on Network Rail and train operators: A consultation on changes to charges and contractual incentives’](#).

Policy	Incentives - Schedule 8
Policy area	Schedule 8 – Sustained Poor Performance (SPP)
Background	<p>The SPP mechanism under Schedule 8 is designed to provide protection to passenger operators if Network Rail's performance falls to such a level that the payments they receive under the liquidated damages element of Schedule 8 are materially less than the actual financial impact of poor performance.</p> <p>The rationale for this mechanism is that it is generally considered that operators' costs of delay rise more rapidly when the level of disruption to their services exceeds a certain threshold. The standard Schedule 8 payment rates do not account for this as they assume that the financial impact of delay rises at a constant rate.</p>
Which of the PR18 outcomes does this charge/incentive deliver against?	<p>Outcome: The network is reliable</p> <p>Description of outcome:</p> <ul style="list-style-type: none">• Network Rail delivers the optimal level of reliability for every service• The impact of delay on operators, passengers and freight customers is minimised

Problem under consideration with the current charge/incentive

In response to our November 2015 stakeholder letter, several operators expressed concerns that the current process for making SPP claims is costly, time-consuming and difficult to resolve. In particular, operators stressed the difficulty of proving revenue losses in SPP claims. Revenue losses are uncertain and hard to estimate, making them subject to dispute. In contrast, it was generally agreed that costs were easier to establish and consequently far less subject to dispute. It seems likely that the uncertainty and consequent dispute will persist in any SPP regime that includes revenue losses.

The cost of making claims may be dis-incentivising operators from doing so. This would limit both the effectiveness of the incentive that the SPP provisions provide to Network Rail to improve its performance, and the extent to which operators are held neutral to the additional losses arising from sustained poor performance.

What is the scale of the issue & who is impacted?

Industry has provided us with several case studies to demonstrate the high costs associated with making and resolving a SPP claim. Several of the claims in the case studies were initiated several years ago and are still unresolved; such claims have cost Network Rail and operators in excess of £100,000 in legal expenses.

Since the start of CP5 no operator has initiated a SPP claim despite half of all operators being eligible to make a claim. This could be because these operators have been deterred by the resource intensive process of making a claim.

Options to be considered

Option 0: Do nothing	<ul style="list-style-type: none">• The current mechanism is triggered if Network Rail's performance is at least 10% worse than benchmark over 13 consecutive periods (one year).• After it has been triggered, passenger operators can decide to make a claim for 'all relevant losses' resulting from worse than benchmark performance.
Option 1: Only include cost recovery	<ul style="list-style-type: none">• Under this option operators would only be able to claim for compensation for the costs that they incur as a result of Network Rail's worse than benchmark performance, rather than all relevant losses. That is, operator claims would and could no longer include revenue losses (and the revenue losses would instead be covered under the liquidated damages regime).

Assessment of options

Assessment of option 1 (Only include cost recovery)	<ul style="list-style-type: none">• This would remove the difficulties of operators having to demonstrate revenue losses. In turn the process for operators to make SPP claims would be simpler, which would likely increase the number of claims made.• Any operator that can prove revenue losses
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	<p>relatively easily would be disadvantaged under this option. However based on evidence from industry this does not appear to be a likely scenario.</p> <ul style="list-style-type: none"> • If operators made more SPP claims Network Rail would have a more effective incentive to ensure their performance did not fall below the SPP threshold. • Operators would also be held financially neutral to more of the impacts of Network Rail's caused delays.
Recommendation	<ul style="list-style-type: none"> • ORR recommends the option of changing the SPP regime to allow operators to only claim for costs caused by Network Rail.
Next Steps	<ul style="list-style-type: none"> • In addition to pursuing this option we will also be working with industry to improve the clarity of the contractual wording of the SPP provisions, where necessary, and to review the threshold, if appropriate.



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