Schedule 8 performance regime

ORR factsheet

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Purpose of this document

This factsheet provides an overview of the key elements of the Schedule 8 performance regime for both passenger and freight operators. It is intended to provide a useful reference for industry to assist with engaging with the PR23 process and responding to our consultations.

The rest of this document addresses the following questions:

- **What is the purpose of Schedule 8?**
- **What is 'delay attribution' and what role does it play in the Schedule 8 regime?**
- **What are 'benchmarks' and how are they calculated?**
- **What are 'payment rates' and how are they calculated?**
- **What is the 'star model'?**
- **What are 'caps' and what role do they have in the Schedule 8 regime?**
- **What changes were made to the Schedule 8 regime during PR18?**

We have published this note alongside our initial consultation on the PR23 Schedule 8 performance regime. This guide focuses exclusively on the existing structure of the Schedule 8 performance regime for CP6; our initial views about how this structure might change in PR23 are discussed in our initial consultation. For a more detailed breakdown of the performance regime and the methodologies behind its component features, please refer to ORR's CP6 Performance Regime Track Access Guidance.

If you have any queries about the information contained within this note, please contact Will Holman (Will.Holman@orr.gov.uk), Senior Economist at ORR.

Schedule 8 performance regime

Background to Network Rail's 'Schedule 8' performance regime

Network Rail's performance regime is contained within Schedule 8 of track access contracts (for both freight and passenger services). A performance regime is a legal requirement, as set out in the Access & Management Regulations 2016.

The passenger, freight and charter sectors have different Schedule 8 regimes, reflecting the differing nature of the services operated.

What is the purpose of Schedule 8?

The performance regime has three key functions:

1. To reduce train operators' exposure to losses that arise from delay and cancellations that they cannot control, by compensating them for losses incurred as a result of delay. This reduces their level of risk from operating and investing in the industry. The original intention of Schedule 8 was that, for franchised passenger operators, this ultimately reduced the cost to taxpayers by reducing the risk premia that firms include in their franchise bids.
2. To provide Network Rail with financial incentives to reduce the delay they cause to train operators.
3. To provide operators with financial incentives to reduce the delay they cause to other operators.

How does Schedule 8 work?

Schedule 8 payments are based on attributed delay, benchmarks and payment rates: if a party causes more delay than its benchmarked amount, it pays an amount equal to the excess delay multiplied by a payment rate.

Payments are determined formulaically (instead of requiring parties to negotiate actual losses for each delay), as a function of a payment rate and how actual performance compares to a benchmark level. This formulaic system reduces the administrative and legal costs that would be incurred if parties were required to make a claim for each individual incident.

Schedule 8 also contains a Sustained Poor Performance (SPP) mechanism to protect passenger operators in the event of Network Rail's performance falling to such a level that the payments passenger operators receive under the liquidated damages element of Schedule 8 are materially less than the actual financial impact of poor performance. In these circumstances, on a case-by-case basis, the mechanism allows for additional revenue and cost compensation to be payable.

There are different benchmarks and payment rates for delays caused by Network Rail and for delays caused by operators. Likewise, the freight regime and passenger regime use different measures of delay.

Cancellations

In the passenger regime, each cancelled stop is deemed to be equivalent to a certain number of delay minutes, which reflects the disruption that passengers face as a result of each cancelled stop. The 'deemed minutes late' arising from cancellations are added to the lateness arising from delays when assessing performance against benchmarks.

In the freight regime, the 'cancellation sum' compensates freight operators for cancellations to their services caused by Network Rail. The cancellation sum Network Rail pays is determined by whether the rate of cancellations caused by Network Rail is above or below a cancellation threshold. The cancellation threshold is based on the historical normal rate of cancellations.

TOC-on-TOC vs TOC-on-Self delay

Freight operator performance is directly measured on the basis of how much delay they cause to other operators, and the amount they pay is based on that measure.

However, in the passenger operator regime, due to historical data limitations, the delay that passenger operators cause to themselves ('TOC-on-Self' delay) is used as a proxy for the delay they cause to other operators ('TOC-on-TOC' delay), with the payment rate reflecting this calculation. As a result, the Schedule 8 regime does not provide passenger operators with a strong incentive to reduce the delay they cause to other operators above the incentive it provides them not to delay themselves.

Delay attribution

What is delay attribution?

Delay attribution is the process by which Network Rail and the industry provides data on the causes of delays, such as a signal failure or late train crew, and the scale of impact this has on railway operations and on passengers and freight end users.

Network Rail is responsible for identifying whether responsibility for incidents causing delays is attributed to Network Rail, to the operator or in some limited circumstances to both parties jointly. Operators are able to challenge this attribution and present alternative evidence, and can ultimately dispute attribution if they wish.

Delay attribution is guided by the Delay Attribution Principles & Rules (DAPR). Changes to the DAPR can be made by its governing body, the Delay Attribution Board, on which ORR and DfT are observers. ORR must approve changes to the DAPR.

Delay attribution provides the key inputs to the calculation of Schedule 8 payments, specifically equivalent delay minutes caused to a given operator by either Network Rail or another operator.

Benchmarks

What are benchmarks?

Benchmarks represent the average level of delay that is expected to be caused to a given set of services by Network Rail (Network Rail benchmark); or by a given set of services to those of other operators (operator benchmark, proxied by delays to the operator's own services). Benchmarks are expressed as delay minutes per train movement.

If Network Rail and an operator perform at their respective benchmark levels, no payments are made through the regime. If Network Rail or an operator cause more delay than their respective benchmark, then they make payments through the regime. Conversely, if Network Rail or a train operators cause less delay than their benchmark they receive bonus payments.

The use of benchmarks is in part designed to minimise expected money flows within the Schedule 8 regime. Benchmarks are set such that, under assumed conditions, expected Schedule 8 payments would be zero. In practice, actual delays caused will normally differ from benchmark for both Network Rail and operators; actual payments represent the net of these effects.

How are benchmarks calculated?

Benchmarks are set (or 'calibrated') at the time of each periodic review for the duration of the next control period. Benchmarks are fixed for the duration of the control period.

Passenger regime

Separate benchmarks in the passenger regime are set for each service group (collection of train services), expressed in terms of average minutes of lateness.

Passenger operator and Network Rail benchmarks are based on historical average performance. The Network Rail benchmarks are also adjusted to take into account Network Rail's performance trajectories set for each train operator by ORR in the periodic review final determination.

Freight regime

The Network Rail and operator benchmarks in the freight regime are defined in terms of minutes of delay per 100 miles. Both Network Rail and freight operator benchmarks are the same in relation to all freight operators.

Freight operator benchmarks are based on average past performance over a five-year recalibration period while Network Rail benchmarks are based on a mix of past performance and regulatory performance trajectories, as per the passenger regime.

Can benchmarks be changed during a control period?

The passenger regime allows for a recalibration of the regime during a control period in some limited circumstances. During a control period, either party can propose a recalibration of benchmarks. If the parties agree, they need to seek ORR's approval. If they do not agree, then either party can refer the matter to ORR, and ORR will decide whether and how to determine the matter.

What are payment rates and how are they calculated?

Payment rates represent the expected financial impact of a given unit of delay. The types of financial impact that are taken into account when calculating payment rates vary for each regime.

Payment rates in the passenger regime

Payment rates in the passenger regime are based on the relationship between disruption and changes in long-term farebox revenue (obtained from econometric analysis) and the average number of passengers estimated to be travelling on affected train services.

There are separate Network Rail payment rates for each service group. The Network Rail payment rate for compensation to (and bonus payments from) train operators is based on the assessed marginal revenue effect (MRE) of poor performance to that service group. The MRE is the modelled change in revenue for that service group resulting from a one-minute change of performance minutes (a measure of lateness and cancellations) across the recalibration period. The Network Rail payment rate calculation converts the MRE for that service group into the modelled change in revenue for a one-minute change in performance minutes for a single day.

Payment rates take no account of compensation payments made by operators to their passengers or changes in operating costs as the result of delay.

Payment rates in the freight regime

As in the passenger regime, payment rates reflect the expected average financial impact of delay on freight operators. The Network Rail and freight payment rate in the freight regime are uniform across all freight operators.

What is ‘the star model’?

All payments under the Schedule 8 regime are made through a ‘star model’ with Network Rail at its centre. Under this star model, all Schedule 8 payments are made bilaterally between Network Rail and operators, with no payments flowing directly between operators. The advantage of this approach is that there is not a need for contracts between individual operators.

The star model must be carefully calibrated so as for Network Rail to be left financially neutral for disruption caused by operators to one another.

Schedule 8 is calibrated to map delay for each combination of perpetrator (service group causing delay) and victim (service group affected by the delay). This is intended to ensure that TOCs’ payments for causing TOC-on-TOC delay match the likely compensation paid by Network Rail.

What role do caps have in the Schedule 8 regime?

Incident caps refer to the caps freight operators may opt to ‘purchase’ from Network Rail as an access charge supplement in their performance regime. Incident caps limit operators’ performance regime liabilities for lateness and cancellations caused to other train operators from individual incidents. As a result, caps protect freight operators from the risk of significant costs arising from incidents.

Annual caps (or ‘annual liability caps’) refer to the reciprocal annual caps between freight operators and Network Rail on the liability they face under the Schedule 8 performance regime. These provide freight operators with some certainty about the maximum liabilities they could face.

Annual caps are intentionally set at a level with a low likelihood of being reached, to ensure that they do not routinely limit the incentive to improve performance.

What changes were made to Schedule 8 during PR18?

In PR18, ORR removed the pre-existing annual adjustment of freight and charter operator benchmarks. The decision was based on the benefits of simplification and the potential improvement in signals to operators.

ORR also considered but ultimately decided not to pursue in PR18:

1. changing the measure of passenger operators' performance;
2. restricting the losses eligible for compensation under Sustained Poor Performance provisions to cost only;
3. incorporating passenger compensation arising from Network Rail caused delays into the formulaic Schedule 8 payments; and
4. removing the annual traffic adjustment to FOC benchmarks.