

ORR Periodic Review 2013
Consultation on Schedules 4 and 8
Possessions and Performance Regimes

28 January 2013

Introduction

ATOC provides a national voice for Britain's passenger train companies, helping to create, inform and shape the rail environment in Great Britain. We bring together all train companies to preserve and enhance the benefits for passengers of Britain's national rail network, which jointly we do by providing the following key services:

- A central clearing house for the train operators, allowing passengers to buy tickets to travel on any part of the rail network, from any station, through the Rail Settlement Plan
- A customer service operation, giving passengers up-to-the-minute information on train times, fares, reservations and service disruption across the country, through the National Rail Enquiries (NRE)
- A range of discounted and promotional rail cards, cutting the cost of travelling by train for groups including young people, families, senior citizens and people with disabilities
- Operational and engineering expertise, promoting safety, setting standards and encouraging excellence across the sector.

ATOC's mission is to work for passenger rail operators in serving their customers and supporting a safe, reliable, attractive and prosperous railway.

ATOC Viewpoint

ATOC is pleased to provide its response to ORR's important consultation on how the Schedule 4 and 8 possession and performance regimes will operate in the next control period. The punctuality and reliability of train services is clearly a key driver of passenger satisfaction and it is crucial that the regulatory framework for the industry as a whole creates the correct incentives and behaviours to deliver the appropriate standards of service.

We are pleased with the general direction set out in the ORR's consultation including the on-going commitment to retain the overarching framework provided by Schedules 4 and 8 as liquidated sums regimes. We agree with ORR that these perform an important function in a way that is more efficient than the alternatives.

Moreover, the existing arrangements are well-understood and we believe generally drive appropriate behaviours across the industry. For those reasons, train operators are not persuaded of the need for significant change to the existing policy framework, although they do fully accept the need for recalibration. Setting new benchmarks will be an essential process for the start of CP5 and we consider that some tweaks to the detail of the schemes may be necessary.

As with any systematised model of this nature, there will be areas at the margins where improvements in calibration will deliver closer alignment with actual revenue effects, but train operators do not consider that there is overall misalignment in the current process or that the structure is any more biased to 'over compensation' than it is to 'under compensation'. Thus, in our view the focus for the remainder of the PR13 period should be on fine-tuning the current arrangements rather than overhauling or further reviewing the over-arching principles.

That having been said, ATOC draws attention to the emerging alliances between train operators and Network Rail, recognising that they may result in requirements to modify and develop transmission mechanisms in the light of changes to relationships between industry parties. In that regard, we consider that there may be significant merit in Network Rail and train operators having the option to agree bespoke performance and possessions compensation arrangements in their track access contracts, subject to regulatory approval. Additionally, it will be important for the schedule 4 and 8 regimes to be robust to any possible future changes to franchise agreements.

In summary, ATOC welcomes the detailed work that ORR has carried out to review the current arrangements for the Schedule 4 and 8 regimes. We remain committed to working with ORR including through the industry steering group to improving the current approach such that incentives across the whole industry are better aligned to minimise delay impacts and continually improve performance for passengers.

Transparency of possession management

1. What are your views on whether or not passengers and freight customers adequately consulted on the planning of possessions? What activity currently takes place?

In our view there is room for considerable improvement in the way that the industry as a whole, and passengers in turn, are consulted on the planning of possessions. Research has consistently demonstrated that passengers and freight customers are particularly concerned about train punctuality as well as the impact of both planned and unplanned disruption. Part D of the Network Code requires Network Rail to propose possessions within the Engineering Access Statement. Train operators take a number of steps to inform customers about changes to rail services. However, operators are constrained by paucity of detailed and accurate information made available by Network Rail with regard to the possessions it plans to take.

We consider that there needs to be an holistic review of the quality of the information that Network Rail provides to the industry, in order to inform the discussion of how that information is then provided to customers.

2. What are your views on whether we should encourage Network Rail to consult with passengers and freight customers in the planning of its possessions?

As a general rule, we see enhanced consultation around possessions planning as a good thing. However, train operators own the relationship with passengers and it is right that they should represent passenger's interests with respect to possessions planning. Operators are invariably best placed to assess the implications of engineering access and to explain this to passengers in terms that they understand.

3. If we were to encourage Network Rail to consult with passengers and freight customers in the planning of its possessions, do you have any suggestions on how we might go about doing this, for example, how such an obligation would be phrased and monitored?

See comment above.

Schedules 4 and 8 overall

4. Do you agree with the SDG research findings and conclusions on whether to set Schedule 4 and 8 payment rates so they do not compensate train operators in full for the impact of service disruption due to Network Rail and other train operators? If not, please tell us why?

Yes – see response to question 5 below.

5. Do you agree that we should continue to set Schedule 4 and 8 payment rates so that they compensate train operators for the full financial impact of service disruption due to Network Rail and other operators, where we do so currently? If not, please tell us why?

ORR has said that the objective of setting payment rates below the level that would fully compensate operators would be to help encourage operators to work with Network Rail to improve performance and minimise the number and impact of possessions. However, there are a number of more important incentives at play which affect the level of co-operation between industry stakeholders including reputation, targets set by ORR and the prospect of lost revenue. Therefore, in our view, altering payment rates is unlikely to achieve the stated objective.

6. Are you of the view that there are other steps we could take to encourage train operators to have a stronger influence on the behaviours of Network Rail, in addition to those we are doing already?

We note that the ORR has proposed a number of changes to the wider regulatory framework which are designed to encourage train operators to work more closely with Network Rail. These include the development of the efficiency benefit sharing mechanism (ESBM) into route based sharing (REBS) and the introduction of a downside for train operators. Additionally, the ORR has proposed that new franchisees should be exposed to variances in the level of the variable charge and that over the longer term it wishes explore the options for exposing operators to the fixed charge. Whilst decisions on franchising reform is firmly a decision for government, all of these factors combined appear to already offer a framework that will strengthen the incentives on operators to work even more closely with Network Rail than they currently do. For that reason we consider that the current arrangements, augmented by the enhancements proposed by the ORR for CP5, are likely to be sufficient.

We recommend that instead of seeking further changes to the current regime, the range of existing and planned measures are fully explored. A step-by-step approach to the process, will give time for robust analysis of the potential benefits and costs, and reduce the risk of unintended consequences for all parties.

7. Do you agree with our proposal not to introduce the Joint Restrictions of Use concept into Schedule 4 of template track access contracts? If not, please tell us why?

Yes we agree that it would not be sensible to introduce a generic joint restrictions of use provision into Schedule 4 at this time. The industry has a good track record of working together during extreme events such as severe weather and it not clear that a joint restriction of use would improve the

current incentive structure. Additionally, we consider that defining the criteria and trigger scenarios could be problematic and a disproportionate response to the issue. While we do not support a generic solution, we are supportive of Network Rail and TOCs being able to propose bespoke arrangements to ORR where the contractual provisions are not working well in particular localised circumstances.

8. To what extent (if at all) do you think the current contractual wording of Schedules 4 and 8 is acting as a barrier to Network Rail and train operators minimising disruption to passengers and freight customers during extreme disruption, e.g. during severe weather? If you are of the view that it does act as a barrier, we welcome any specific proposals on how it can be improved.

As noted above, in our view the industry currently works well together during times of extreme disruption so we are not clear that the contractual wording of Schedules 4 and 8 systematically acts as a barrier to cooperation.

Schedule 4 passenger possessions regime

9. Do you agree that the Access Charge Supplement (ACS) should be calculated using Network Rail's revised route based Schedule 4 costs estimation methodology? If not, please tell us why?

Given the wider move to route based regulation and in light of Network Rail's new methodology for calculating the level of ACS we consider that it would be appropriate to determine ACS at a route level. However, we think that it would be sensible for Network Rail's new methodology and the outputs that it generates to be reviewed in detail by suitable industry experts and for the results to be shared with stakeholders.

10. Do you consider there is further value in Network Rail achieving greater disaggregation in the methodology of the ACS calculation and if so do you have any suggestions how this might be achieved?

As noted above we consider that an independent review of Network Rail's approach should enable the validation of the current approach and the opportunity for the relevant experts to propose improvements for the future.

11. Do you agree that we should update the estimated bus mile payment rate based on actual amounts paid during CP4, rather than simply uplift the current rates by cost inflation? If not, please tell us why?

Yes we think ORR should update the estimated bus mile payment rate to ensure that the formula more accurately reflects actual costs.

12. Do you agree that we should continue with the current formula for calculating revenue loss compensation for cancelled train services when there are replacement buses? If not, do you have any suggestions for how we could improve this aspect of Schedule 4?

We note ORR's observation that the current formula could, in theory, generate a perverse incentive for operators to agree to possessions when alternatives might be more appropriate. In practice, operators place passenger satisfaction above marginal revenue benefit. Therefore, we consider that the current formula remains appropriate subject to an update of the component elements. This approach reflects the fact that Schedule 4 is very much an average regime designed to broadly reflect the circumstances surrounding most 'typical' possessions.

13. Do you consider the way in which the revenue loss formula compensates franchised passenger operators when using replacement buses encourages passenger train operators to run too many buses (rather than trying to run train services using diverted route, for example)? If so, please explain why you think this is the case?

We do not consider that the arrangements would lead operators to use buses rather than trains. As we explain above, operators are more concerned with improving services to customers overall by delivering consistent rail services than receiving marginal revenue benefits through the compensation arrangements. Also of some relevance to this issue is the fact that much of the compensation is shared with funders.

14. Do you agree that we should extend the scope of the protection provided by paragraph 2.9 of Schedule 4 to enable the recovery of direct costs related to amended or cancelled Type 1 possessions? If not, please tell us why?

ATOC developed this proposal and believes that a change of this nature would improve the incentives on Network Rail to consider the impact on operators of cancelling or changing possessions at short notice. We also advocate an approach under which there is more regulatory scrutiny of Network Rail's performance in regard to late changes / cancellations. This should include a review of Network Rail's performance in this respect in the Possessions Disruption Index- Passenger (PDI-P) to ensure the negative impacts of late changes to advertised possessions are adequately captured.

15. If so, do you agree the threshold for triggering a claim should be £5,000 per possession? If not, please tell us why?

We consider that £5k per possession reflects the fact that the abortive costs associated with Network Rail cancelling an individual possession might not always reach the existing Schedule 4 cost threshold of £10k and therefore

changing the scope of paragraph 2.9 to cover Type 1 possessions would not make any difference unless the threshold was lowered. Additionally, the threshold should be set above zero to avoid small claims being made where the costs of administration might exceed the value of the claim.

16. Do you agree that we should update the new working timetable notification factor to reflect changes to delay multiplier values in the Passenger Demand Forecasting Handbook (PDFH)? If not, please tell us why?

The delay multiplier for each service group is clearly central to the calculation of notification factors. In our view it would seem appropriate that the notification factors should be clearly linked to the latest evidence on customer behaviour as revealed by the updates to the Passenger Demand Forecasting Handbook (PDFH).

17. Do you have any further proposals for changes to notification discount thresholds and factors? If so, please explain your reasoning?

The proposals set out in the ORR consultation reflect discussion of these issues at S4 and 8 industry group where notification discount thresholds and factors have been considered in some detail.

18. Do you agree that we should keep the Sustained Planned Disruption (SPD) revenue loss threshold the same and uprate the cost compensation by inflation (RPI)? If not, please tell us why?

Yes we consider that this would be the most appropriate option for updating the SPD loss threshold.

19. Are you of the view that the provisions for claiming compensation under the SPD mechanism would benefit from clarification? If yes, please highlight which areas should be clarified?

From a TOC perspective there is little appetite for fundamental reform of the SPD mechanism. However we agree that the contractual wording would benefit from clarification. At present there are often differing interpretations of the provisions between TOCs and Network Rail which can make claiming more contentious and difficult to process than it ought to be.

Schedule 4 freight possessions regime

20. Do you consider the current regime appropriately compensates freight operators for losses resulting from severe disruption caused by possessions? If not, what do you consider the level of compensation should be based on?

No comment.

21. Do you consider that the current regime appropriately incentivises Network Rail to reduce the amount of disruption faced by freight operators due to possessions? If not, how do you think incentive effects can be strengthened?

No comment.

22. If Schedule 4 compensation payment rates for freight operators were increased, should this be funded by government? If so, please explain why you think this should be the case? If not, please tell us why?

No comment.

Schedule 8 passenger performance regime

23. Do you agree that we should keep the current Schedule 8 contractual wording in relation to what train operators can claim for under the SPP arrangements? If you do not agree, do you have any proposals for alternative wording?

As regards the scope of SPP claims we consider that clarification would be helpful however would stress that there may be instances where a TOC incurs additional costs/losses over and above direct revenue loss – for example as a result of management decisions in direct response to periods of prolonged poor performance – and that in defined circumstances these should be capable of being claimed.

24. Should we continue with the SPP threshold set at 10% or increase it? If not, please tell us why?

Yes we believe the current threshold is appropriate and do not support ORR's proposal to increase the threshold for a number of reasons:

- Only four claims have been made under SPP in the whole of CP4 to date. We do not consider this constitutes evidence of a widespread or routine 'claiming culture' and certainly does not undermine the integrity of Schedule 8 as a liquidated damages regime. It also suggests that transactions costs relating to SPP are not as high as Network Rail has suggested.
- While TOCs may have the right to trigger SPP, they often do not make a claim. This is largely because the only demand forecasting methodology that is acceptable to Network Rail is the same as that which forms the basis for schedule 8. Thus if a TOC suffers from a prolonged period of poor performance the compensation will probably

work out to a sum close to that derived using the Schedule 8 formula anyway. Unless a TOC has incurred additional costs (e.g. having to operate buses for a sustained period) there may be little extra to claim. This is borne out by the fact that, while many TOCs have technically breached the SPP threshold, few appear to have claimed.

- An important reason why an increasing number of operators have been in SPP territory is due to the fact that Network Rail has not met its CP4 regulatory targets for performance. We do not believe that failure by Network Rail to deliver against its performance targets should now be used as a justification for increasing the SPP threshold; the focus should be on ensuring Network Rail delivers, and is incentivised to deliver, the performance trajectory that has been agreed.
- We do not consider that the current SPP threshold creates perverse incentives to make claims or undermines collaborative working. As already noted, the number of CP4 claims is small which does not support the view that there is an excessive amount of bespoke claiming. As regards collaborative working, TOCs have engaged fully in the PR13 process to date and have shown a great willingness to ensure the Schedule 8 regime remains fit for purpose going into CP5. While we recognise the importance of working together, Network Rail remains a monopoly infrastructure supplier and in this context SPP provides an important contractual backstop where Network Rail has not delivered its performance obligations.

25. If we increase the SPP threshold, what are your views on the level we should set it at?

See comment above.

26. Do you agree that we should leave timings of Schedule 8 payments unchanged, with payments due within 35 days following the end of each four-week accounting period? If not, please tell us why?

Yes we agree that there should be no change to the timings of Schedule 8 payments. In our view, the evidence to support a time delay is not compelling and introducing a payment delay would be likely to introduce unnecessary complexity without significant benefit.

27. Do you agree that we should keep the circumstances in which Network Rail and train operators can propose amendments to Schedule 8, appendix 1 via paragraph 17 the same? If not, please tell us why?

Yes in our view Paragraph 17 is required to handle legitimate mid-control period changes to Appendix 1 such as those that might arise from a major timetable change or the emergence of new information which materially affects the calibration of the scheme. The evidence from previous control periods is that there has only been one notification of a disputed proposal via paragraph 17 – this might tend to suggest that the current arrangements are not being widely misused.

28. Are there any specific areas of paragraph 17 where you are of the view the drafting needs to be made clearer? If not, please tell us why?

We recommend that the wording of the paragraph is considered further by the industry steering group.

29. Are you content for us to remove the passenger charter element of the Schedule 8 performance regime? If not, please could you tell us why and whether you would like us to take any alternative course of action?

Yes, we think it would be appropriate to remove this element of the regime.

30. Do you agree that we should not change the way train operator cancellations to their own trains are treated under Schedule 8? If not, please tell us why?

In our view, this is not a sufficiently material issue to warrant a change to the current arrangements.

Schedule 8 freight performance regime

31. Do you agree that we should keep the Network Rail payment rate the same, but uplifted for inflation? If not, please tell us why?

No comment.

32. Do you think that the current Network Rail payment rate accurately reflects the financial impacts incurred by freight operators as a result of Network Rail caused delays to freight trains? If not, please tell us why?

No comment.

33. Do you agree that we should re-examine the evidence base for the Network Rail payment rate with the freight industry and Network Rail in CP5, and if necessary adjust the rate to reflect cost and revenue impacts on freight operators due to Network Rail caused delays? If not, please tell us why?

No comment.

34. Do you agree that we should keep the Network Rail cancellation payments the same but uplift them for inflation? If not, please tell us why?

No comment.

35. Do you agree that we should update the congestion factor used in the calculation of adjustments to the freight operator benchmark, in order to take into account of evidence being collected as part of the update of the capacity charge? If not, please tell us why?

No comment.

36. Do you agree that the Network Rail £ per delay minute payment rates used in the calculation of the freight operator payment rate should be weighted by third party freight operator delay affecting each service group? If not, please tell us why?

No comment.

37. Do you agree with our proposal to continue to set the bonus payment rates at 50% of the level of the compensation payment rate? If not, please tell us why?

No comment.

38. Do you agree with our proposal not to require Network Rail to offer incident caps in return for an access charge supplement? If not, please tell us why?

No comment.

39. Do you agree that incident caps are something that could be provided by the private insurance market if Network Rail were not to offer incident caps at a reasonable price? If not, please tell us why?

No comment.

40. Do you agree that we should continue to allow operator specific annual liability caps? If not, please tell us why?

No comment.

41. Should we continue to set reciprocal annual liability caps for smaller and new freight operators? If not, please tell us why?

No comment.

42. Should we continue to set reciprocal annual liability caps in instances where Network Rail and freight operators cannot agree on the level the cap should be set at? Or are caps on annual liability something the private insurance market could provide if no agreement is reached?

No comment.

Compensation for charter operators

43. Do you agree that a separate charter operator payment rate should be calculated using the same methodology used to calculate the freight operator payment rate, but based on delays caused by charter operators to other train operators? If not, please tell us why?

Yes we agree on the grounds that we consider that an important principle of the regime should be that charter operators pay the appropriate rate for any delay that they cause. Therefore the delay that charter operators cause to other train operators should be used to calculate a charter specific payment rate. This should result in a charter operator payment rate that better reflects the actual impact of delays caused by charter operators to other train operators.

44. Do you agree with our proposal not to require Network Rail to provide incident caps to charter operators on the basis this currently results in a subsidy to charter operators? If not, please tell us why?

Yes we support this approach. As set above, we consider that charter operators should have appropriate incentives to minimise the delay that they cause by providing compensation which reflects the cost of delay. Therefore, removing the requirement for Network Rail to offer incident caps to charter operators should help to achieve this. Incident caps should not be used to protect charter operators from risk relating to their own performance – that is not the purpose of Schedule 8.

45. Do you agree that incident caps are something that could be provided to charter operators by the private insurance market? If not, please tell us why?

We do not have visibility of the private insurance market in this area but it does seem to us that train performance risk is something that is well understood and it, therefore, should be possible for charter operators to find means of hedging this risk without the use of incident caps.

46. Are you content for us to set the Network Rail payment rate in the charter operator performance regime so it is the same as the

Network Rail payment rate in the freight performance regime? If not, do you have any proposals on how we should update it including on the evidence we could use?

Ideally, there would be a separate Network Rail payment rate for charter operators to reflect the impact of delays on the long term revenue. However, in the absence of data on this issue it would seem sensible to use freight as a proxy by setting the Network Rail payment rate for charter operators so it is the same as the Network Rail payment rate under the freight regime.

47. Are you of the view that there are any other areas of the charter Schedule 8 performance regime that should be amended?

No comment.