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Ref: ORR/RH021a

Dear Ms Sareen,

**Virgin West Coast Trains Ltd response to the ORR's Schedule 4 and Part G Possessions Compensation Regime [PCR] for Passenger Operators consultation document**

With reference to the above consultation documentation dated 8<sup>th</sup> April 2008, Virgin West Coast Trains Ltd [WCTL] hereby responds with the following comments.

**1. Introduction**

- 1.1 WCTL welcomes the opportunity to respond to the ORR's final consultation document regarding the Industry's ongoing challenge to amalgamate all possession compensation under one regime.
- 1.2 WCTL considers this an overall positive move for the Industry for those reasons clearly stated and endorsed by the ORR, on the basis that it accurately applies mostly reflective rates and robust formulae, as well as encompassing all the relevant impact thresholds likely to cover those possession requirements that can and do occur.
- 1.3 WCTL has been at the forefront of quite possibly one of the heaviest programmes of Engineering Work experienced of recent times, so we regard the proposals for change as a major step forward. However, the complexities surrounding an amalgamated approach to possession compensation are huge, but the final measures presented in this and previous consultation documentation, offers us most of the confidence necessary to cover the majority of our compensation expectations.
- 1.4 Although WCTL is currently compensated under a bespoke Schedule 4 [S4] regime, (unlike all other current franchised Train Operators [TOC]), we nevertheless understand the principles regarding the need to move to an all embracing regime. A regime however, that needs to reasonably reflect the variances within each TOC, both in terms of service provision, mileage, stations and routes served; the work being developed in association with Faber Maunsell & Network Rail, is indeed capturing most requirements.

## 2. General Comments on the ORR's Consultation

- 2.1 As we move into a new Control Period where from a personal WCTL perspective, the major West Coast work programmes will gradually be replaced by Enhanced Engineering Access (EEA) regimes, and nationally in conjunction with other ongoing Train Operator timetable and growth changes, it is understandably an ideal time as part of this Regulatory review, to amalgamate the S4 / Network Change regimes through the introduction of new methodology, that is both all encompassing as well as fair and reasonable, whilst at the same time taking the opportunity to simplify the various claim processes.
- 2.2 Since the start of the West Coast Route Modernisation Upgrade [WCRM] there has never been a 'steady state' timetable in place over the West Coast Main Line [WCML], sufficient for WCTL to rigorously evaluate the long term business affect of any S4 recalibration and modified process being introduced from the now preferred ORR start date of 1<sup>st</sup> April 2009.
- 2.3 Presently, there continues to be, protracted claim negotiations, particularly over Network Change Restrictions of Use [ROU], involving Revenue claims where a lack of nationally consistent and robust revenue mechanisms to support such claims is not available. There have also been disagreements regarding which possessions are deemed Network Change and those that are not, essentially with regard to the transparency and detail of work categories encompassed within each possession proposal.
- 2.4 However, with the majority of WCRM Network Change possession requirements expected to be completed in conjunction with the introduction of the West Coast VHF timetable prior to the start of CP4 (with currently the exception of the Milton Keynes remodelling project), combined with the venerable formulation of methodology akin with the newly proposed S4 process, we consider the risks associated with the inability to recover our costs through this new process, to be considerably reduced.
- 2.5. In terms of specific comments outlined within our initial response to the Policy group's proposals last year, regarding changes to the Revenue calculus, whilst we were one of the few Operators who wished to see an additional Notification Factor [NF] between T-12 and T-0 introduced, we understand the Industry's reluctance and concern that this may not necessarily incentivise Network Rail to deliver to T-12 timescales. Nonetheless and especially based on our current T-12 experience, our initial deliberations regarding having an intermediate NF at T-4 still stand.
- 2.6 WCTL remain concerned that the revenue calculus will still fail to capture those elements of Business Recovery for possessions that last for less than 120 hours, (and would not meet the Sustained Planned Disruption [SDP] criteria - ROTR Section 7 items for example) – it is still not clear how such loss could be recovered. WCTL belief is that there should still be some wash-up process for *ad hoc* or less than 3 concurrent months', Type 1 & 2 possessions. This is discussed in more detail within Section 3 below.
- 2.6 There is one other element which we believe may impact on the way Franchised Operators view as a fair, either individually or nationally, application of the unit rate associated with the payment of costs (not revenue) for possessions. Although, as we have clearly stated above, we welcome the step forward in terms of the proposed methodology overall, it seems that the crucial application of the resultant *Cost Rate* for EBM calculus, may not have been fully examined comparatively for long distant operators. We explore this important aspect in further detail below – Section 4 refers.

### 3. Revenue Calculus – Concern(s)

- 3.1 The lack of a 'wash-up' process for *ad hoc* Type 1 & Type 2 possessions (unlike Type 3 possession(s)) and therefore also not meeting the Sustained Planned Disruption criteria, does not enable the taking into account of the potential for revenue loss in terms of medium to long term business recovery. In other words the proposed Type 1 & Type 2 definition and payment structures reflect the fact that revenue is lost only on the day, and not over the longer term. The current S4 algorithm (which is to be continued into CP4), is based upon MRE rates which reflect the fact that passengers become more inconvenienced the closer one gets to unscheduled delay (and is obviously weighted through varying levels of notification).
- 3.2 As we move into a new era of possession management under EEA, Business Recovery could be deemed less of a problem, but the fact remains that for example, (repeated closure on weekends in only one period for non EEA standard works, i.e. the route between Crewe and Liverpool / Preston is blocked annually for normally one period during the Autumn) has the potential for a long term affect on the leisure travel market, and to a lesser degree business travel market, who may go out on a weekday but who would otherwise travel back at weekends. Such possession proposals over one period would therefore not be covered under the Sustained Planned Disruption criteria and thus not allow for business recovery to be compensated.
- 3.3 This conceptual issue is integrally linked to the level of scrutiny regarding rail travel information, which reaches its peak about four weeks before travel. One could argue that this would only affect weekend leisure travel and that the business recovery element should be weighted accordingly. However as we have mentioned above, in line with the majority of disruptive possessions occurring during the weekends, such disruption does affect ' *the return-leg*' element of those business travellers, who would otherwise travel out on a weekday but back at weekends (v.v.). If travel is not available at weekends then this business travel element is also lost.
- 3.4 WCTL initial stance regarding the need for an intermediate NF was based upon the fact that when passengers are put off travelling, then the recovery, from which a TOC recovers that income, is potentially far more difficult if changes keep occurring closer to their implementation. This is after the point at which revenue is initially lost at the first stage of awareness, thence dipping and levelling out until about the start of the T-12 period, then rising steeply once the core of potential travellers start to enquire about the possibilities of rail travel. Such a period reflects the phase when ticket purchases reach their maximum (90%), and is obviously where most passengers can be put off their journeys, once aware of the level of service disruption.
- 3.5 Although WCTL recognises that Network Rail may lose the incentive to propose possessions as early as possible if the above views were encompassed in their raw form, and that we are receptive to the proposed recommendations based on the proposed revised notification factors, we nonetheless still reserve our position in the belief that in conjunction with Type 1 & Type 2 possessions there should be nonetheless a 'wash-up' process to allow for the capture of such Business Recovery losses.

#### **4 Sustained Planned Disruption Methodology - Concern(s)**

- 4.1 Whilst the Sustained Planned Disruption payment process [SPD] caters for compensation over a 3 or 7 month period of sustained disruption, subject to equalling or exceeding certain thresholds, it still remains based on the aggregation of formulae which is based upon Revenue Loss on the day. There still remains again, the risk that business recovery will not be fully captured, similar to those circumstances outlined above in section 3.
- 4.2 There maybe circumstances when Revenue Loss compensation for repeated or aggregated possessions do not reach the various thresholds under “On the Day Revenue calculus, but if overlaid with long term Business Recovery, such losses would actually trigger the SPD process. As far as we can see there is no ability to instigate negotiations under such scenarios – we would appreciate clarity regarding such potential risk?

#### **5. Costs Calculus - Concerns**

- 5.1 WCTL has incurred over the duration of the WCRM Upgrade project, arguably one of the highest amount of costs associated with Rail Replacement Service provision of any Train Operator. Understandably this has been mostly covered through negotiations under the Network Change process, for which we therefore believe that we are in a very strong position when considering the proposed and amalgamated S4 changes and rate applications in conjunction with bus costs and the like.
- 5.2 As WCTL continues to represent one of the fastest growing Train Operators in the country, down to a combination of both growth in the business generally and despite performance levels being very challenging, the delivery of the timetable through improved rolling stock and operational management, the number of passengers travelling is exceeding all expectation, both of short & long distance journeys.
- 5.3 The volume of WCTL passengers (primarily commuter and business) based on journeys less than 85 miles in 2009 (equivalent to what we perceive as the average maximum commutable journey using a London & SE Area Operating TOC) is expected to equate to 32% of our total number of journeys undertaken. Of this, 21% of the overall total is expected to represent journeys between Milton Keynes and London. None of the other following top 14 short distance flows can match such volume.
- 5.4 Similarly, in terms of ‘*on the day*’ revenue, involving journeys of less than 85 miles, the greatest income expected in 2009 applies to journeys between Rugby, Milton Keynes and London Euston. Such revenue flows equate to 51% of all short journeys.
- 5.5 The reason for such analysis of short mileage based journeys is to highlight our concerns with the EBM rate for long distant operators who, with a proposed rate set at about £8, can, over short mileages, actually provide the same functionality in terms of journey expectation , as a London & SE Operator with a rate set at about £12.
- 5.6 Such rates are based upon data supplied by certain TOC’s including ourselves (but on the basis such data was likely to be skewed due to the massive engineering programmes taking / that had taken place), to the Policy Group last year. Although this data reflected the amount of rail replacement costs incurred between 2005/6 & 2007/8 for the various S4, Network Change and SROU situations, it represented the affect to total overall journeys.

- 5.7 This in hindsight, disguises the fact that long distant TOC's such as ourselves, do indeed provide a commuter type L&SE service (FGW between Reading/Oxford and Paddington, EC between Peterborough/Stevenage and Kings Cross being representative of other classic examples), even though the services themselves may originate from locations a great deal further away.
- 5.8 Taking all of the above points and translating them into the Rail Replacement situation, and taking cognisance that the Estimated Bus Mile [EBM] measure recognises the impact on the quantity of trains operating over it and the level of bus replacement provision required, then with the level of train service patterns (under VHF) between London and especially Milton Keynes as well as Rugby, alongside the number of journeys, in the eventuality of disruption anywhere between Rugby and London, then the higher rate should apply.
- 5.9 In the eventuality of the route between Rugby and London being disrupted, our case is further supported by the fact that the volume of passengers is higher the closer you are to London. Therefore aside from the fact that L&SE bus hire rates are higher than anywhere else in the country, the volume of people to be moved is a great deal more. This in turn, requires a greater number of rail replacement vehicles in the event of disruption.
- 5.10 WCTL has past and continuing experience regarding bus provision and it is a fact that south of Rugby the number of vehicles hired is far greater than that which would be required for example between Wigan and Warrington. If we were to accept the lower long distant rate then we would receive considerably less compensation for Type 1 and possibly Type 2 possessions (where costs come to under £10k) than other TOC's providing a similar sort of service – a possible candidate being London Midland?
- 5.11 Furthermore, there is still the issue that at certain times of day more buses have to be provided to convey passengers. Taking standard weekend possessions, there is as highlighted already, an increase in the number of passengers conveyed from 1400 on Sundays, (or Bank Holiday afternoons) necessitating an increase in the number of buses provided and thus the number of bus diagrams in place. This can be exacerbated further on those occasions when engineering work clashes with public events like football matches, shows, exhibitions and state occasions etc.
- 5.12 WCTL appreciates a formulaic approach to cover all RRP costs is very complex, and likely to have wins offset by losses, but we sincerely believe that EBM's on the route between those Viable Transfer Points [VTP] of Rugby and London need to have the higher, L&SE rate applied.

## **6 Access Charge Supplement [ACS]**

- 6.1 WCTL originally agreed with the industry's view that the ACS did not necessarily provide TOC's with a reliable price signal, nor did it give Network Rail the incentive to plan its possessions more efficiently at a TOC route level.
- 6.2 However, WCTL accepts the Industry's recommendations on the basis that whilst it does not give full transparency and elements of cross-subsidy will probably continue to exist, it does nonetheless provide the industry with ongoing continuity and a nationally applied application. To introduce further complex changes at this juncture, alongside an untried new S4 regime (in whatever form is eventually taken), could give cause to potential problems including inequitable costs on franchised TOC's.

- 6.3 Furthermore, any introduction of a new type of process could be severely put at risk due to the fact that currently Network Rail's possession planning and work programme regimes, would not be currently, sufficiently reliable or stable enough when considering the application would have been applied across a whole new Control Period. This would undesirably cause constant re-adjustment of ACS values, let alone not being sufficiently steady enough for a meaningful ACS value to be calculated at an Operator level in the first place.
- 6.4 WCTL continues to consider, in the event that the ACS is absorbed within the full Fixed Track Access charge [FTA], then we would ideally seek the establishment of a process that enables full transparency regarding its financial breakdown.
- 6.5 Obviously in consideration of the effects of adjusting the ACS when traffic levels change; in terms of the financial effect then any such changes would obviously be negated through subsidy adjustments with the DfT. Equally we assume that the DfT feel comfortable that the ACS process (in whatever form it takes) is equitable? This coupled with the fact that Network Rail continues to refine the calculation of WCTL ACS charge, thereby ensuring the charge is more cost reflective and a more reliable price signal, is most welcome.

### Implementation Arrangements

- 7.1 WCTL recognised that in its current contractual position (which as stated, is subject to special provisions due to the contractual obligations of PUG2), it would be content to allow a phased introduction rather than immediate implementation. Combined with the expectation of a new Track Access Agreement being introduced for December 2008, our initial perception was that it would be preferable to use a phased approach, not only because of the changeover of TAA and short timescales between inception of such and the April 2009 commencement date, (which itself could give rise to financial and management issues both internally and with the DfT), but also because of the risks involved with a possible delay with the completion of Upgrade Engineering works specific to the WCML.
- 7.2 WCTL considered at the time, that whatever S4 process was finally introduced, it may not have adequately addressed the compensation risk appropriate to the scale of unfinished works on the WCML past the start of the new Control Period. WCTL preferred the recourse option for reclaiming all its reasonable costs, losses & expenses (including revenue loss) through the standard Network Change process until the works had been completed.
- 7.3 There is however, the possibility of introducing the VHF timetable in May 2009, this being without prejudice to the ORR's recent determination regarding the industry need to introduce the VHF timetable in December 2008, (pending any other possible potential legal & strategic outcomes), that our new (*model*) Track Access Agreement will not be implemented until such timetable is introduced in parallel. This presents an issue for WCTL only, in that we might have to continue (subject to ORR's approval) with our Bespoke S4 methodology and administration until the Subsidiary Timetable change in May 2009.
- 7.4 We had considered that with our franchise up for renewal in 2012, and the final completion of major Network Change WCML Engineering works not expected to be completed until mid 2010, it may have been of benefit to defer introduction until our Franchise change, a view shared with ATOC and other TOC's.

- 7.5 Furthermore we also considered that in the event that outstanding compensation issues (bespoke Network Change items for example) overlapped with the 1<sup>st</sup> April, then there was a need to have some form of transitional overlap (see section 8 below) to resolve overlapping negotiations.
- 7.6 However on reflection, regarding our initial thoughts put forward last year of delaying the introduction of this process to allow a staggering of the process, we can now confirm that the introduction of the 1<sup>st</sup> April 2009 is acceptable (subject to transitional arrangements). However in the event that May 2009 becomes the new date for the delayed implementation of the VHF timetable, the ORR would obviously need to take cognisance of our particular situation.

## **8 Transitional Arrangements**

- 8.1 In consideration of the ORR's request for feedback on the transitional arrangements in terms of potentially preserving any existing bespoke compensation arrangements for a 6 month period after the 1<sup>st</sup> April 2009 (Para 31 refers), WCTL have the following comments, in parallel with our Track Access issue outlined above in section 7.
- 8.2 With the ongoing dispute (TTP210) relative to WCRM Upgrade works still ensuing past the deadline for this response, and in consideration of the fact that such a dispute incorporates possessions up to and including week 6 (end of May 2009), combined with the only West Coast PSN in place, (Milton Keynes & Bletchley Remodelling), WCTL tentatively express a desire to have these possessions under the associated documentation applying, be encompassed under existing Network Change compensation arrangements, but only covering up to and inclusive of Week 22 next year (ie up to Friday August 30<sup>th</sup> 2009)
- 8.3 This would then enable the completion of all WCML Upgrade work (including the now deferred Trent Valley and Nuneaton to Rugby Bi-Di introduction alongside Linespeed enhancement work on the Manchester route, as well as a major proportion of the Milton Keynes remodelling scheme, to be included under the currently robust (in terms of compensation procedure) WCRM Project / WCTL Network Change mechanism currently in place. This may indeed help Network Rail from a 'financial structure' perspective, as currently all WCRM works are paid for by the WCRM Project and not by the Territories?
- 8.4 WCTL also believe it would enable a clean break to be achieved once all the upgrade works are completed, as well as giving the new S4 process some bedding down time between the Subsidiary and Principal Timetable change dates, after which the next set of major Network Change work would arise (Christmas 2009)
- 8.5 Therefore WCTL request that all possessions (without prejudice to any resultant ADRC determinations) encompassed within documents NAUM-30, the MKC PSN and any further NAUM documents associated with WCRM Upgrade works, DO NOT form part of this new process.

## **9 Changes to the Network Code through C5 or C8 Procedures**

- 9.1 WCTL does not view any problems with the ORR implementing changes to the Network Code under those principles contained under C8; indeed it seems very prudent taking cognisance of the importance of introducing such a radical change to a financial process, that it is undertaken with the good of Industry in mind.

9.2 WCTL similarly does not see any real reason to raise any concerns with the modifications to the Schedule 4 model template. The new definitions, and the incorporation of the new procedures seem quite reasonable and nothing currently stands out as questionable.

## 10. Summary

- 10.1 It is interesting to note in Network Rail's methodology documentation, in calculating the appropriate Unit Cost for Revenue and their application of this against renewal and maintenance activity (M&R) over the next Control Period, that in adjusting the 2006-07 S4 costs (which form their baseline) to include WCML costs (which were missing due to the major engineering taking place over the route), they clearly state, that "...they would have expected Unit S4 costs on the WCML to be significantly higher than the average for the remainder of the Network, due to the high level of revenue on the route"...
- 10.2 This reasonable conclusion is applied throughout Network Rail's assumptions and methodology. Indeed their analysis highlights the fact that (page 15) S4 costs are above average on long distant, high revenue earning routes of which WCML is the primary example. This adds weight to our two arguments (see sections 3 & 4 above) in that firstly, whenever engineering work takes place on the WCML the overall revenue effect will be higher than average, and thus the increase risk of losing more revenue particularly with regards to Business Recovery compensation, as well as an increased disbursement of costs.
- 10.3 Secondly, coupled with the fact that passenger usage growth on the WCML is currently exceeding all expectation (18% average year on year), and is expected to continue growing over the next Control Period, the obvious knock on affect to Rail Replacement services as a consequence of any mainline disruption is substantial. This is why we believe that for those Service Groups and Routes highlighted in section 5 above, the higher South-East rate should be used for EBM calculus.
- 10.4 Overall however, WCTL endorses the principles contained within the new process, but would welcome further examination of the two outstanding compensative issues, as outlined above.

Yours Sincerely

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