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By Hand

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Dear Paul

Model clauses for track access agreements

I am pleased to enclose our response to the Regulator's second consultation document of 19' April 2000 regarding the establishment of model clauses for track access agreements.

Yours sincerely

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MODEL CLAUSES FOR TRACK ACCESS AGREEMENTS

The Regulator has sought views on the matters set out below to which our response is as follows:

1. INTRODUCTIONS AND PROCESS

- *the revised timetable leading to the publication of model clauses;*

We would have preferred a longer response time:

- a) To allow sufficient time for review of the note of the seminar discussions held on 3rd and 4th May before preparation of this response;
- b) Given the interrelationship of the terms of the Access Agreements and the charges payable to Railtrack, to bring together the response on the Regulator's consultation document: "The Periodic review" of Railtrack's Access Charges: Provisional conclusions on the incentive framework;
- c) It is important that the period for consultation responses to the Model Clauses will be a minimum of 5 weeks, (while respecting the July deadline) in order to give due consideration to the drafting and to enable the affected parties to take legal advice; and
- d) If the Model Clauses are not to be complete until September the preferred bidder for the Chiltern Franchise and SSRA will be unable to take them fully into account before the expected date for signature of the Replacement Franchise Agreement.

- *whether the use of these model clauses in the new track access agreements should be mandatory and circumstances where divergence might be considered appropriate; and*

Given the multi-user railway and the interrelationship of a number of the proposals for Model Clauses with the Access Conditions (e.g. proposal for changes in the categorisation of rights) and Railtrack's licence (especially condition 7) use of the model clauses should be mandatory.

- *whether a piecemeal or big bang approach to the incorporation of model clauses into track access agreements is preferable. If a big bang approach is preferred, suggestions are sought on how this might be achieved.*

A big bang approach to implementation would be desirable both from Railtrack's perspective in dealing with its customers on common terms under a (related) common charging regime which properly reflects the risks and also from the point of view of passenger operators who will expect a level playing field.

However the reality is that operators may be reluctant to change their existing access agreements in the context of their existing franchise agreements.

Any individual or wholesale adoption of the new clauses will require SSRA's consent.

Experience from the first round of franchising (e.g. template Schedule 4) suggests that once satisfactory model clauses exist the process of adopting them can be fairly quick. However a considerable amount of tailoring will be required of each new Schedule 5 especially given a requirement on Railtrack to warrant the access rights.

The main difficulty with a big bang approach will be to tie it in:

- a) with the replacement franchising process; and
- b) with those operators who have long term access agreements (such as Gatwick Express, Virgin West Coast, Virgin Cross Country, Connex South Central) who are not within the franchise replacement process.

2. COMMERCIAL PURPOSE

- *the Regulator's provisional conclusion that a commercial purpose clause should be established which creates additional rights and obligations to deal with ambiguities and omissions in the contract;*

The aim should be for the model clauses to remove ambiguities and omissions in the contract by setting out clearly the rights and obligations of the parties. This should extend to the standards applicable to train operations and network operations and maintenance (the main areas where, traditionally, ambiguities and omissions have occurred).

The commercial purpose clause is of particular benefit where the access agreement deals with infrastructure enhancements and the introduction of new train services (as in PUG 2). It would be a retrograde step to water down the considerable benefit of the clause in those circumstance by making it too generic.

- *the Regulator's provisional conclusion that, generally, this should not go further and provide for general obligations on the parties which would operate even in the absence of ambiguity or omission elsewhere in the contract; and*

We support the Regulator's provisional conclusion that the clause should not provide for obligations which operate in the absence of ambiguities or omission. As stated above the model clauses should seek to remove such ambiguities and omissions.

- *the benefits and risks of train operators being able to pass to Railtrack, by means of such a clause, certain aspects of their obligations to the SSRA under their franchise agreements.*

Railtrack is the indirect benefiting of very substantial payments from the tax payer which are channelled through train operators. Franchise groups are required, particularly under the replacement franchising process, to provide substantial investment which is likely to require considerable equity investment in operators. Where operators are dependent upon Railtrack's performance to meet their obligations to the SSRA it is an economically correct and equitable result that operators should be able to pass to Railtrack the risks associated with Railtrack's performance which can of course include the default termination of a franchise. If Railtrack is to share in the benefits (presumably meaning increased ride ship and associated farebox) it is necessary for the model clauses to define the standards which Railtrack is required to reach so that operators can understand at what point benefits accrue beyond those which are to be expected from proper contractual performance.

3. ACCESS RIGHTS AND CAPACITY CONSUMPTION

- ***whether there should be a template specification of access rights and what it should contain;***
The existence of templated specifications of access rights would have the benefits of
 - a) consistency;
 - b) economy and efficiency in agreeing new or changed access rights; and
 - c) easier comparison of existing and new rights e.g. in consultation on timetable development and concerning new rights.

Railtrack should be prepared to ensure that its staff and lawyers are properly trained in the use of the templates, in particular as to which are appropriate for which circumstances.

- ***whether there should be development of "tiered" access rights;***
The existing designations of rights between firm and contingent appear to work well. The characteristics of rights which are important differ from operator to operator e.g. platforming is sufficiently important for Gatwick Express at Victoria and Gatwick and for Silverlink at Euston to be part of the firm rights description. We are not aware of any enthusiasm amongst operators for the tiered rights concept.
- ***the Regulator's provisional conclusion that access rights should remain subject to the Rules of the Route and the Rules of the Plan;***
We share the Regulator's provisional conclusions that access rights should remain subject to the Rules of the Route and Rules of the Plan but only in the context that these are set as described below.
- ***the scope and procedure for reviewing the content of, and process for, establishing the Rules of the Route and the Rules of the Plan;***

Revision of the Rules of the Route and Rules of the Plan should be governed by the Access Conditions. The change process should be led by Railtrack, although operators should have the ability to require reviews. The process should involve multiparty consultation. There could be a presumption in favour of changes made for reasons demonstrated to be of good operational practice. It may however take time (or require a subcommittee to develop) good operational practice.

- ***how the issues concerning change in access rights over time should be addressed, for instance by a system of access rights which are redeemable with compensation, and the scope of any use it or lose it provision;***

the access rights of an operator can to some extent be equated with its goodwill. Involuntary loss of access rights is not something which an operator would welcome so that any public interest requirement would need to be very strong and go beyond e.g. a commercial requirement of Railtrack. Any proposal for "use it or lose it" should look not so much at the period of non use but at the reason for non-use: holding access rights for the purpose of denying access is not acceptable. However the accumulation of rights at the outset at a new franchise because they are required to meet Committed Outputs or Primary Aspirations under the new franchise agreements should not be open to challenge and Secondary Aspirations may also need to be accommodated.

The measure of compensation needs to be related to the circumstances in which the right is surrendered. Arguably compensation will need to cover the loss of benefit associated with the right and not simply the rebating of the amount payable for right through the charging mechanism.

- *the Regulator's provisional conclusion that Railtrack should be obliged to provide a capacity warranty, and to improve the assessment and transparency of capacity consumption of new access rights; and*

On analysis it is not sustainable that operators should pay fixed access charges for rights that may not exist which is effectively the case if rights are not warranted. Railtrack should be in a position to verify the rights which it grants - templating the description of rights in Schedule 5 should assist in this. Railtrack should also be able to assess the effect on compacting of the rights which it grants in order to be able to manage and operate the network efficiently.

- *the Regulator's view that these principles also apply to freight and whether there are any specific considerations in respect of freight which should be taken into account in developing the policy.*

We see no reason why these principles should not apply to freight operators.

4. OUTPUT STATEMENTS

- *the Regulator's provisional conclusion that there should be a contractual obligation to produce and deliver local output statements for individual train operators;*

We support the provisional conclusion on the basis that Railtrack should be under an obligation to produce and deliver local output statements for individual train operators. The obligation will need to be clear as to the areas to be covered in the LOS and the timing for production and implementation.

- *the Regulator's provisional conclusion that these should be operator-based;*

We had experience of the production of an Engineering Strategy for a single user part of the railway (LTS routes) early in the privatisation. Based on that experience we would suggest:

- a) that the LOS could operate for longer than a single 12 month period; and
- b) that in those circumstances (where consultation with other users was effectively restricted to freight) operator-based negotiations were satisfactory. However in the case of multi-user sections of the railways we question whether negotiation on a bilateral basis will be any more effective than multilateral consultation to award the lowest common denominator effect. The latter process has the benefit of greater speed and transparency.

- *the outline content of such statements and their relationship with Condition 7 and existing contractual provisions;*

If the statements are to be prepared in output rather than input terms they will need to cover such matters as:

- a) Periods when the railway (specific parts) will not be subject to possessions; and

- b) Improvements measured in terms of capacity and removal of temporary speed restrictions ride quality.

The areas described should reflect the output obligations of Railtrack within the contract generally applied to the local circumstances.

There would not on this basis be any conflict with condition 7 or other contractual provisions.

- *the desirability of and mechanism for local funders (e.g. Passenger Transport Executives) to have similar local output statements, thus avoiding reliance on the relevant operator's relationship with Railtrack, and*

No comment.

- *the applicability of the proposals to freight operators.*
We consider that freight would need to be involved in the formulation of local output statements. See our response to second bullet point of this section 4 above.

5. NETWORK ENHANCEMENT

- *whether there should be a presumption that, subject to regulatory approval, when an operator pays for capacity enhancement over and above the capacity that it is expecting to bid for in the timetabling process, it should have rights to that capacity where there is a public interest benefit;*

It is difficult to see how such enhancements can be funded by the private sector unless such a presumption applies. The references to "subject to regulatory approval" and "public interest benefit" open up additional areas of risk which private sector funders would need to assess.

- *whether and how the clarity in the timing and detail of information provision through Part G of the Track Access Conditions should be improved;*

Part G is very much a process section. As such it should have clear time period for provision of information and spell out (or provide for the spelling out of) the detail to which information is to be provided.

- *whether and how Part G of the Track Access Conditions should give more certainty about the timing of implementation of changes to the network;*

A party proposing a Network Change should be required to indicate the proposed date for completion of the change and the estimated length of time to carry out infrastructure works. The process will need to cope with refinement of this information. The information is relevant to assessment of the effect of the works, of the change, and of compensation.

Also see our response to second bullet point of this Section 5 above.

- *whether and how the position in respect of compensation under Part G of the Track Access Conditions could be improved;*

Part G needs to set out more clearly what deductions are intended to be carried by G 2.3 and G 4.3 and how future benefit is intended to be calculated.

The equivalent amendments will need to be made to Part F.

- *whether there should be arrangements in Part G for operators to be required to contribute to the cost of a project if they are net beneficiaries from an enhancement; and*

It is suggested that provisions for contributing to the cost of enhancements should be contained in Schedule 7 rather than in Part G.

If operators are to be required to contribute to the cost of enhancements, either during a central period or subsequently through the effect of the charging review the cost implications need to be acceptable to both public and private sector funders.

The position of franchise operators with current franchise agreements and that of operators under replacement franchise agreements will need to be harmonised.

- *whether the proposals set out in relation to network enhancement should also apply to freight operators.*

Yes. The appropriate funding support mechanism will need to be developed for freight operators.

6. LIABILITY AND REMEDIES

- *whether additional remedies should be available if operational performance falls below a predefined floor level and, if so, what remedies might be appropriate;*

The consequences, in terms of passenger charter compensation and liability under the current and replacement franchise agreements leading to potential termination, are extremely serious for operators. An appropriate remedy would have to be an uncapped damages claim, in order to provide a sufficient incentive on Railtrack to perform.

- *the circumstances in which the right to seek specific performance might be an appropriate remedy;*

Specific performance in this context needs to be defined. We consider that this should be a remedy available to the Regulator with an appropriate procedure for speedy referral and an adequate enforcement power behind the specific performance order.

The remedy would appear to be appropriate only where the works required can be carried out safely and without undue disruption to operators - any such disruption would have to be adequately compensated.

- *what the liabilities of the parties should be in the event of a breach of other obligations under the agreement and the nature of any limitations on liability;*

It is assumed that train delays and cancellations will continue to be dealt with through a liquidated damages regime within a revised Schedule 8. Outside that area it is necessary to distinguish the different obligations in the access agreement and to decide whether there should be individual caps on the amount which can be claimed for different heads of claim (including under indemnities) or whether there should be an overall cap. From an operator perspective it needs to be recognised that the remedies of suspension and termination are of illusory value, given the obligations in the case of passenger operators to continue to provide services, and in the case of freight the commercial imperative of the business. It would be reasonable to expect that the

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access charge would not be payable in cases of material break. The consequences to franchise operators of breach of the franchise agreement which may be caused by or contributed to by Railtrack default are extremely serious and need to be recognised in any assessment of liquidated sums or caps. It is difficult to identify circumstances (outside those already dealt with in Schedule 8) where breach by an operator could have such severe consequences for Railtrack. Therefore it would not be appropriate to apply the same overall limitations of liability to Railtrack as for operators.

- *the Regulator's provisional conclusion that no force majeure provision should be incorporated;*

The industry appears to have accepted the no force majeure concept in relation to operations. However this may not be appropriate in relation to enhancements related to Committed Outputs of an operator.

- *whether the suspension arrangements in the current agreements are adequate in the event of an operator breaching its safety obligations;*

It is considered that suspension is a very severe penalty for the operator, given that the operator continues to pay for access, suffers through the farebox and is subject to penalties under the franchise agreement in these circumstances.

- *the potential impact on the risk faced by Railtrack and operators and the implications (if any) for their costs Of finance and for the feasibility of innovative financing options; and*

To the extent that the model clauses increase the potential liability of operators these new risks will need to be taken into account and the position of operators with existing franchise agreements, those with replacement franchise agreements and that of freight operators taken separately. The position of Railtrack will similarly need to be analysed. The public sector funders need to consider what they would be paying for under the new charging regime and therefore whether any additional risks are in fact being undertaken by Railtrack.

If for example, the industry cannot afford the cost of a regime under which Railtrack can be required to accept the consequences of causing or contributing to the termination of a franchise it must be asked whether private sector investors in a franchise (whether debt or equity) should be expected to take that risk.

- *whether there are any special factors in respect Of freight.*
Freight is dealt with in the above responses.

7. OTHER ISSUES

- *whether parties other than Railtrack and train operators should have contractual rights established through track access agreements;*

This appears to be a complicated way of creating rights which are not essentially track access rights. However, given the difficulties which we understand that train manufacturers have had in reaching contractual terms with Railtrack, there may be benefits to the industry as a whole in adopting this idea. The concerns of private sector funders should be met at least in part if the track access agreement is assignable to them supported by a Direct Agreement with Railtrack.

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- *whether there should be a model clause providing for standard of performance and, if so, whether it should be in the form of the draft provision reproduced above;*

There should be an express standard of performance. The draft provision is helpful but may be interpreted in the context of the domestic railway in Great Britain. It may be desirable to refer to international practice or that of or the Western European rail Industry.

- *the regulator's provisional conclusion that a model clause should be established relating to the reciprocal provision of information;*

This would be useful. The basis of charging for provision of information (e.g. cost recovery) needs to be clear.

- *whether an operator's rights under its track access agreement should be assignable to a financing institution; and*

This would be helpful. It is assured that such an assignment would be supported by a Direct Agreement between the financing institution and Railtrack. The conditions which the Regulator is proposing would in any event be requirements of the access agreement.

- *the applicability of these proposals to freight operators.*

These provisions should also apply to freight operators.