

1 March 2000

Tom Winsor
Rail Regulator
Office of the Rail Regulator
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Dear Tom,

The Regulator's Consultation on Model Clauses for Track Access Agreements

1. The sSRA warmly welcomes the consultation process for model clauses and believes that their introduction will play a significant part in establishing the framework for the development of the railway over the next 10-20 years.
2. 2. Renewal and development of the infrastructure is one of the most important keys to a successful railway. To this end, the sSRA believes:
 - Railtrack needs to be a responsive, competent and knowledgeable network operator in all its dealings with its customers; and
 - the industry contractual and regulatory instruments need to contain a presumption in favour of development.
3. On 1st February 2000, we forwarded to you both our initial formal response and a more detailed confidential response to your consultation paper. We have since had an opportunity to consider other industry responses, both written and at your seminar. We have been impressed by the scope and quality of the responses.
4. Those contributions demonstrate that there is a need for model clauses to address serious weaknesses in the current track access contracts. The seminar also led us to the view, *which* we have since discussed with you, that this process cannot be rushed if we are to have fit for purpose track access contracts.
5. Attached to this letter is a more detailed response to your model clauses consultation paper published 7 January 2000. However, because of the difficult issues raised in a number of areas, our thinking is still developing, informed by other participants in this consultation. It should, therefore, be taken as a further Working Paper of the sSRA's current position. We are happy for the Paper and this letter to go on the public register.
6. The remainder of this letter highlights some of the themes which we believe should both inform and shape the substance of the model clauses. The themes are:

The need to specify clearly the extent and quality of the access rights which are to be granted to TOCs by Railtrack

7. The access rights contained in Schedule 5 must protect the Passenger Service Requirement and additional service commitments placed on franchise operators through their franchise agreements, with particular regard being had to quantum, journey times, calling patterns and frequency. There is also a strong case for templating the various other expressions of access rights, so far as possible, in the interests of clarity and consistency.
8. However, a balance needs to be struck between providing certainty to investors and allowing for the development of the network over a long period of time. There has to be a recognised and fair process to vary access rights in order to accommodate major enhancements and other developments of the network through amendments to the timetable, rules of the route and rules of the plan. Administrative procedures and financial incentives may have a role here.

The need to specify clearly and unambiguously the parties' respective obligations

9. The sSRA believes that Clause 6 needs to be strengthened to contain meaningful standards and outputs. We would favour aligning the obligations in Clause 6 more closely with the obligations placed on Railtrack under condition 7 of the Network Licence. For bankability reasons, the sSRA, whilst acknowledging the industry's interest in a commercial purpose clause, believes that the mischief at which such a clause is aimed, might be better addressed by a clear and unequivocal statement of the extent and quality of the access rights being granted.

Securing the optimum use of network

10. The key to success is not simply a matter of creating new capacity, but also ensuring that we make the best use of the capacity we have. To achieve this, Railtrack needs itself to understand and then be able to demonstrate to its customers the capacity of its network so that it can give a commitment to deliver that capacity without overselling (or, indeed, underutilising) the available capacity. Railtrack, as steward of the network has a responsibility under Access condition D to optimise the timetable, taking into account the various demands placed upon it. Again the sSRA believes that the specification of access rights is critical to this optimisation.

Avoiding ossification of network by a cumbersome and unbalanced network change procedure

11. Access condition G needs to protect the interest of train operators while at the same time facilitating the expansion of passenger and freight services in line with government policy. While legitimate reasons for challenging a network change proposal must be properly protected, this must not be at the expense of beneficial network changes proceeding. Proposals must be properly validated, which means greater transparency and provision of fit for purpose information. We need to move away from the "horse trading" which characterises the practical operation of condition G, towards a system of published compensation tariffs. Finally, the process itself must be made more expeditious.

Securing the development of the network "as a network"

12. The sSRA believes that it would be counter-productive to become overly intrusive in the way in which Railtrack carries out its network obligations, In particular the sSRA,

conscious of its objective to secure the development of the network would not want to support measures that might lead to the "balkanisation" of the network. Accordingly the sSRA believes that local output statements should be seen as a means of communicating comprehensive information rather than being a commitment to deliver specific local outputs at a given time.

13. I should say something about the franchise replacement process and how we see the introduction of model clauses impacting upon that process.

14. While we wish to have the model clauses settled as quickly as possible, it is apparent that full consideration and development of the ideas received back from the industry may not be deliverable within the timescales originally set. The sSRA would therefore propose a new timetable for taking forward model clauses as follows:

- the Regulator's provisional conclusions with outline of contents of each clause, after discussions with sSRA, no later than the middle of May;
- settled and agreed clauses by summer 2000.

15. We hope you consider this revised timescale, albeit still challenging, realistic. We will, of course, work with you in order to enable you to meet that timescale. The sSRA looks forward to taking this project forward with you to a conclusion which is the best possible for the industry.

I am copying this letter to train operators, Railtrack, ATOC and the PTEs.

Terence Jenner
Executive Director The Solicitor

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02 March 2000

Dear Tom

The Regulator's Consultation on Model Clauses for Track Access Agreements

As discussed at our FRSC meeting yesterday, I now attach sSR.A's more detailed Working Paper in response to the latest stage in your model clauses consultation process.

This working paper is an attachment to Terence Jenner's letter to you of 1 March. As mentioned in this letter, the sSR.A's thinking in relation to model clauses is still developing and this Working Paper is indicative of the sSR.A's current position. We are happy for this paper to go on the public register along with Terence Jenner's letter of 1 March.

Yours sincerely,

Philip O'Donnell

SSRA WORKING PAPER ON MODEL CLAUSES

1 March 2000

This working paper reflects the sSRA's current views on model clauses having seen the responses of the industry to the Regulator's consultation document and having attended the Regulator's seminar. This paper is provided to facilitate further discussions on the model clauses and is not a formal policy statement of the sSRA's position.

Introduction

The SSRA welcomes this review of track access agreements and the overall content of the document and questions raised. This paper covers the sSRA's current views in relation to freight and passenger services as the consultation raises predominantly similar issues.

What the operator is buying, and what are his and Railtrack's obligations?

Commercial Purpose

SSRA recognizes that a 'commercial purpose clause' may be useful where there is a dispute over the interpretation of particular clauses in a contract and the original intention of the parties becomes a relevant consideration. There may also be an argument that where scheme design is at an early stage, and there is the possibility of the outputs and infrastructure design changing (as in PUG-2), or where contracts are intended to be of a long duration, a 'commercial purpose' provision which describes the overall intention of the parties to the contract may be desirable.

However, there is a risk that a commercial purpose clause may dilute and obfuscate what would otherwise be clear and unambiguous obligations, thereby undermining the bankability of the agreement as a means of securing favourable external financing. There is also a risk that depending upon how tightly the commercial purpose clause is drawn, the clause maybe capable of different interpretations at different times, enabling a party to resile from other obligations in the agreement.

The SSRA believes that the better approach would be to strengthen Clause 6 and other operative provisions of the agreement as necessary to define precisely and comprehensively the obligations of the parties, thus minimizing the chance of disputes over contract interpretation. It is also considered that the operative provisions relating to the obligations of the parties should be contained in one part of the agreement to avoid questions as to which clause takes precedence. A specific 'commercial purpose clause' would require negotiation and alignment with the obligations agreed within the main body of the agreement and poses the risk of additional time and complication in the contract negotiation process.

In conclusion, the risks of including a detailed commercial purpose provision in the standard access contract need to be considered and, on balance, SSRA does not favour its inclusion. A properly drawn Clause 6 should obviate the need for such a clause.

Standard of performance of obligations

SSRA believes that the provisions in relation to standard of performance of obligations are relatively weak in the track access agreements and merit improvement. The parties should be expressly required to meet minimum standards of competence and SSRA would support a requirement for a higher standard than that implied by the Supply of Goods and Services Act 1982.

The example of the typical commercial contract provision included in the consultation document, i.e., that 'each party shall as with due efficiency and economy and in a timely manner, including in all respects with that degree of skill, diligence, prudence and foresight which should be exercised by a skilled and experienced' network operator or train operator, may be appropriate for inclusion in track access agreements. It is noted that Licence Condition 7 requires that the Network Operator acts in accordance with 'best practice' and presumably the Regulator will have regard to this condition in setting access charges.

Basic access rights

SSRA is strongly of the view that management of the network for multiple users by Railtrack means that absolute access rights would not be desirable. Railtrack require flexibility in access rights for timetabling purposes and maintenance work etc. From a strategic point of view, it is important that a degree of flexibility of use is retained to facilitate development of the network.

Proper specification of access rights is critical to network optimisation. The access rights in Schedule 5 need to be set out clearly and SSRA believes that it would be appropriate to rationalise the myriad ways of expressing access rights currently contained in Schedule 5 and to move towards a templated approach for describing these rights. This should make the task of identifying extra capacity and potential conflicts easier. SSRA supports the point made by ATOC and operators that the access rights must protect the PSR and any additional service commitments placed on the franchise operators through their franchise agreements.

There may be a case for protecting journey times in order to prevent these increasing gradually through amendments to the Rules of the Plan. However, we have reservations whether addressing this issue within the track access agreement is the best approach. It is questionable whether the maximum journey time is actually what parties wish to protect in practice and in any event train operators will wish to achieve the best overall timetable specification. The TOCs are currently required to challenge any changes to the Rules of the Plan that would prevent them from, delivering their pSR obligations, including journey times.

SSRA is of the view that the process for operators to agree or challenge changes to Rules of the Route or Rules of the Plan are working well at this point. Although there is a right for Railtrack to amend the rules, there is a right of appeal which is used by operators.

SSRA would not be in favour of a general 'use it or lose it' provision but there may be circumstances where elements of access rights should be subject to review or 'use it or lose it' provisions. SSRA would wish the case for compulsory purchase of paths (subject to certain protections) to be considered, in circumstances where the requirement for the paths changes or is delayed and available paths are reserved but not in use.

SSRA is not in favour of a general review of access rights over the life of the contract. This would add unnecessary uncertainty for the train operator in planning their business. However, achieving flexibility to address specific circumstances, such as major enhancements, is to be encouraged. If it is intended to change access rights without the agreement of all parties, then a mechanism to provide compensation for any subsequent loss would be necessary.

In terms of network optimisation, rights of access for operators over and above quantum, frequency and journey times are not, in general, desirable. There are examples where a higher level of service on the network would be possible if specific slots and platforms were not guaranteed. There may be a case for access rights over and above quantum, frequency and journey times to be time limited and, in these circumstances, be subject to review.

Network operation, maintenance and development

SSRA believes that the obligations of Railtrack under Clause 6 should be brought into line with the obligations on Railtrack under condition 7 of the Network Licence. Clause 6 might contain commitments to the Railtrack outputs including those in the NMS, which should include explicit track and ride quality parameters, SSRA is in favour of the inclusion of specific measurable parameters over and above the maintenance and renewal obligations. The operator needs to be able to act where Railtrack is failing to deliver enhancements. Clause 6 could also be extended to provide train operators with a remedy where Railtrack take more than the permitted Rules of Route possessions. There should be more transparency as to what information train operators are entitled to, such as a schedule of the required information and the timescales for providing.

Consistent with a presumption in favour of development, Access Condition G needs to protect the interest of train operators while at the same time facilitating the expansion of passenger and freight services in line with government policy. While there may be legitimate reasons for challenging a network change proposal, the process of challenge must not be allowed to unduly frustrate network development.

SSRA is concerned to avoid potential ransom strips and the 'horse-trading' that currently occurs and wishes to see control on levels of available compensation. SSRA believes that the industry should move towards a system of published compensation tariffs, As advised in the SSRA response to Part II of the Regulator's Consultation on the Incentive Framework, SSRA believes that processes for possessions as a result of Network Change (currently defined in Track Access Condition G) should be consolidated in Access Condition D.

In summary, improvements to Part G should concentrate on developing an expeditious process with comprehensive information to be supplied and caps on compensation.

Local output arrangements

We note that a view needs to be taken on the consistency and efficiency of the various network development initiatives and the statutory overlaps. However, the sSRA believes it would be counter-productive to become overly intrusive in the way in which Railtrack carries out its network obligations. The sSRA believes that local output statements are more appropriate as a means of conveying comprehensive information about when schemes are likely to be carried out, what that will involve in

terms of disruption to the network and if the scheduling of a scheme has to slip, the reasons for that and when it is being rescheduled.

Information

SSRA is in favour of the supply of comprehensive information to train operators from Railtrack within defined timescales. The information that operators can obtain from Railtrack should include parameters such as gauge, weight and speed restrictions, traction supply, signal immunisation, updated and freely available standard running times, route capability, proposed projects and possessions, Rules of the Route, Rules of the Plan and a fit for purpose timetable.

It is felt that information on the current capability of the network should be available to operators for no additional charge, as this information should be available as part of the access charge. However, it seems appropriate for some level of charge to be applied to operators in return for information from Railtrack on enhancements to the network. The mechanism for charging for this information is covered in Access Condition G but the appropriate level of charge requires consideration.

In terms of information from operators to Railtrack, SSRA would favour some tightening of the information submitted by operators for timetable bids.

Capacity

To avoid overselling of capacity and to encourage Railtrack to focus on the practical delivery of its obligations, SSRA believes that express assurances from Railtrack should be included in the access agreements, with compensation for operators where capacity is not delivered. Railtrack needs to fully understand its network capacity and its capability and to be able to communicate this understanding to its customers.

What happens if things go wrong?

The starting point has to be a recognition that in an industry as complex as the rail industry, things will go wrong frequently and for all sorts of reasons.

Any system of remedies must also recognise, however, that Railtrack is to be one of the principal drivers of investment in the industry and that whatever system of remedies is put in place should not undermine the bankability of the agreement as a means of securing favourable external financing.

It is generally recognised that what we have at the moment represents an unsatisfactory choice between performance regime based remedies and the generally impractical option of terminating the agreement. The sSRA believes that the track access arrangements require a system of remedies which is both comprehensive and effective and which is consistent with those objectives. The remedies should not exacerbate the failure, either by prohibitive cost of enforcement or in terms of giving rise to undue delay.

Liability - operational performance

SSRA recognises that, as currently the only remedy for poor or substandard performance, Schedule 8 is inadequate. It is complex to enforce and as a remedy it cannot be described as comprehensive. In particular, it is probably inadequate for persistent non-performance or poor performance. Schedule 8 should not be perceived

as a charter for poor performance on the basis that the price of poor performance is less than the price of performing.

The sSRA believes that there is an important place for a properly formulated performance regime in relation to operational performance. A performance regime does provide a focus for performance related issues and, because remedies for inadequate performance are expressly stated, this should encourage transparency and certainty. If properly put together, a performance regime should keep costs down while providing a quick and effective remedy. A performance regime could also be said to be consistent with the whole model clauses approach, which is to template obligations where possible rather than having bespoke contracts.

Schedule 8 has to be overhauled so as to make it

- less complex
- easier to enforce
- a more effective remedy.

If these criteria are met, the sSRA believes that for the majority of claims, the performance regime will still represent the most appropriate means of incentivising output as well as providing effective remedies while at the same time avoiding overbearing costs.

However, the sSRA is also sympathetic to ATOC's view that where possible, remedies should be performance based. In relation to persistent failures, other remedies could be available which are performance based. Specific performance is discussed in more detail in the next section.

The sSRA further believes that where access charges relate to a service which was bid for and accepted but that service is not included in the timetable, so that Schedule 8 does not apply in any event, there does need to be particular redress. The sSRA believes that, with a rationalised Schedule 5, Railtrack should be in a position to give a capacity warranty so that whatever access rights are sold, those rights are then timetabled.

Liabilities - breaches which do not lead to train delays or cancellations

For breaches which are not operational failures causing train delays or cancellations and where the Schedule 8 regime would not apply in any event, there is a compelling case for having available to the beneficiary the normal remedies available at law, including where appropriate specific performance.

Network enhancement obligations and maintenance obligations are, by their nature, input based. The means of rectifying the breach should be more readily apparent than might be the case in a purely output based arrangement. In these circumstances, the sSRA agrees that a performance regime is less appropriate. For lesser breaches and breaches where it is inappropriate to order specific performance, the sSRA would favour a system of liquidated damages. Appropriate liquidated damages would engender certainty and be consistent with the necessity for reciprocity as between Railtrack and the operators in terms of remedies available.

For key obligations, however, there could be an entitlement to claim damages at large and/or seek specific performance.

Non-money remedies

In relation to "self-help" remedies, those available to operators through station and depot access contracts may be desirable. However, in relation to the track there are difficulties. The operator would need to ensure that it was acting within its safety case in pursuing any self-help remedy

Turning to specific performance, in the case of infrastructure enhancement and the carrying out of maintenance obligations and where operational failures can be directly attributed to a failure to carry out obligations, there may be significant advantages in having the remedy of specific performance available. This is particularly so where the marginal cost of delay may be small to Railtrack when compared with the bottom line benefit to Railtrack of deferring the capital expenditure (or paying liquidated damages). The sSRA recognises that damages do not necessarily address the underlying problem and that damages in any case will almost certainly not compensate adequately for persistent failure.

However, specific performance is a discretionary remedy. It will not always be granted. A court (or even an independent expert) may determine that it is not feasible for Railtrack to be compelled to carry on with the contract.

In order for specific performance to be available, the obligations and the criteria for assessing whether the obligations have been carried out will need to be very clearly expressed. This should not present a problem in the case of an input based contract. Further, although specific performance may not be awarded where constant supervision is required it may be possible to link the remedy to arbitration or expert determination on the basis that engineers will be used to monitor performance against milestones and can provide constructive suggestions as to how the aspirations of the parties may best be met.

Events of default and remedies

The sSRA would support a broadening of the remedies available on the occurrence of an event of default. The events of default also need to strike a better balance between the parties. The sSRA is generally not supportive of the train operators being able to withhold payment of access charges, as opposed to abating access charges in appropriate circumstances.

In looking at model clauses generally, regard needs to be given to Contracts (Rights of Third Parties) Act 1999.