



OFFICE OF RAIL REGULATION

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Approval of the Track Access Contract between Network Rail Infrastructure Limited and GB Railfreight Limited submitted under section 18 of the Railways Act 1993

Introduction

1. The Office of Rail Regulation (ORR) has today approved the terms of the above track access contract (the contract) submitted to us by Network Rail Infrastructure Limited (Network Rail) under section 18 of the Railways Act 1993 (the Act) on 23 October 2007, and has directed Network Rail to enter into it. Having considered the terms of the contract and after consulting Network Rail and GB Railfreight Limited (GBRf), we have made certain modifications to the contract, and this letter sets out the reasons for our approval of the contract in its modified form.

Our statutory duties and criteria and procedures for approving track access applications

2. In considering track access applications, we must ensure that our decisions are consistent with our statutory duties under section 4 of the Act. In some cases, the different duties will not all point towards the same conclusion and we therefore are required to balance all of the relevant duties in coming to a decision. Our published criteria and procedures document for the approval of freight track access contracts¹ (criteria and procedures document) outlines the process of how we process track access applications, including how we discharge our section 4 duties. We adhere to this document when considering all track access applications.

¹ *Criteria and procedures for the approval of freight track access contracts: third edition*, Office of Rail Regulation (2006) available at <http://www.rail-reg.gov.uk/upload/pdf/289-frghtcp3ed.pdf>.

Statutory requirements for approving long-term track access contracts ('LTAC')

3. In considering the contract term we must take into account the requirements of Regulation 18 of the Railways Infrastructure (Access and Management) Regulations 2005.² The Regulations refer to framework agreements having in principle, a term of 5 years, with agreements of between 5 years and 10 years being justified by the existence of commercial contracts, specialised investments or risks. Framework agreements of longer than 10 years may only be made in 'exceptional cases, in particular where there is large-scale, long-term investment, and particularly where such investment is covered by contractual commitments'.³ Our policy regarding LTACs⁴ establishes that we will approve freight access contracts, with a term of up to 10 years, providing that the applicant demonstrates it can fulfil one or more of the relevant criteria referred to above.

Consultation

4. In line with our policy to consult as widely as possible, we invited comments from other freight and passenger operators that might be affected by the proposed contract, as well as Department for Transport (DfT), Transport Scotland, Transport for London, the Welsh Assembly Government and passenger transport executives. Following our consultation process, we received one substantive response from English Welsh & Scottish Railway Limited (EWS), raising issues that required addressing by the parties.

5. We also held discussions with the parties in considering the application and the parties' responses to our preliminary observations letter. The parties' responses to those preliminary observations have been taken into account by us in reaching our decision regarding the proposed contract.

The Contract

6. The contract gives GBRf permission to use Network Rail's network to operate freight train services. At the parties' request, the contract will commence on 18 June 2008 (after the expiry of GBRf's existing access contract) and we have directed it to expire on the Principal Change Date 2016. While the terms of the contract are based on the model clause freight contract,⁵ GBRf proposed several changes to the freight model contract, including amendments to certain definitions and deletion of certain conditions precedent.

² Available at http://www.rail-reg.gov.uk/upload/pdf/SI3049_A-MReg05.pdf.

³ *Railways Infrastructure (Access and Management) Regulations 2005*, regs 18(8)-(9).

⁴ *Long-term access contracts: final conclusions*, Office of Rail Regulation (2005) available at <http://www.rail-reg.gov.uk/upload/pdf/240.pdf>.

⁵ *Freight model contract* available at <http://www.rail-reg.gov.uk/upload/doc/freightmodcontract-dec05.DOC>.

ORR's Consideration

ORR's initial observations

7. On 5 December 2007 we wrote to the parties seeking comments on the issues raised in the application. On 6 December 2007 we discussed with GBRf our requirement for the provision of further information in order to justify the application for a LTAC. GBRf and Network Rail responded separately to our initial observations letter on 17 December 2007 and 20 December 2007 respectively. Our initial observations and the parties' responses are outlined below.

Term of the directed contract

8. The parties sought a LTAC commencing on 18 June 2008, the day after GBRf's current access contract expires, and expiring on the Principal Change Date 2017, which is approximately 9.5 years from the anticipated date of its commencement. In support of the request, GBRf asked us to consider the investment it had made in leasing various locomotives and wagons, its investment in infrastructure developments, and various commercial contracts with customers that varied in length between 1 and 10 years. GBRf said that these investments and contracts, in justification for a LTAC, were in line with our LTAC policy and the criteria and procedures document. GBRf also stated that it believed that the application was in line with recent decisions made by us regarding the approval of LTACs for EWS and Freightliner Heavy Haul Limited. Network Rail did not dispute the term of the contract.

9. We wrote to GBRf on 5 December 2007, seeking further details to support the application for a LTAC. GBRf responded on 17 December 2007, providing further particulars of its commercial contracts and specialised investments. GBRf requested that this commercial information remain confidential.

ORR's decision

10. We have concluded that, based on the evidence provided, in particular the further evidence provided by GBRf (and referred to in paragraph 9 above), GBRf has justified a contract of longer than 5 years. However we are not convinced that GBRf has provided sufficient justification for a contract for the full 9.5 year duration. In particular, all of GBRf commercial contracts and most rolling stock leases expire before 2017, that is, during 2016 or earlier. Further, we do not regard the level and type of investment made by GBRf justifies a full 9.5 year contract. We have therefore decided to direct a contract of 8.5 years rather than 9.5 years. We feel that a contract of this duration should give GBRf sufficient certainty going forward and would not disadvantage GBRf compared to other operators (as no other freight operator currently has a contract extending beyond this date). Therefore, the track access agreement will commence on 18 June 2008 and will expire on the Principal Change Date 2016.

Service variation and cancellation threshold – Schedules 4 and 8

11. In our initial observations letter we asked the parties to advise the rationale behind the service variation and cancellation thresholds of \times instead of \times . We also asked Network Rail to confirm whether the value of \times had been agreed with other freight operators as part of agreeing the 'Disruptive Events: Managing Freight Traffic' protocol.⁶

12. In response, Network Rail stated that with regard to the contract, it is preferable from the overall impact on all operators across the network, for a new train slot to be identified and allocated to a delayed train after it has been delayed by \times , given train crew relief will be required and the path will have been lost. Network Rail confirmed that the thresholds are not currently consistent across all freight operator access contracts, and while it would prefer a consistent figure to apply to all access contracts, individual contracts can only be amended subject to the agreement of each freight operator.

ORR's decision

13. We have considered Network Rail's response and have decided, in order to ensure that Network Rail provides consistency of treatment of freight operators, to direct a contract with the level of service variation and cancellation thresholds [of] \times . We do not believe that changes proposed in the application to GBRf's cancellation threshold, in isolation, will achieve a 'level playing field'. The levels of these thresholds may be considered as part of the work that is currently being undertaken in preparation for the next access charges review (PR08).

Cordon Caps – Schedule 5

14. In our initial observations letter, we asked the parties whether they were content with the cordon caps being set at zero ('0'), given our interpretation is that if a cordon cap is set at zero, the train operator will have no right to run a train through that cordon. The parties advised that as GBRf is only seeking Level 2 rights for one flow in the proposed contract (Hull Dock to Cottam), it was not anticipated that the services would operate over a route that has a cordon. As the parties are content, the directed contract contains zero values for all cordon caps.

Rights Table – Schedule 5

15. We informed the parties that the proposed Rights Table was not in the model contract format and it was inconsistent with certain paragraphs in Schedule 5. We suggested that the Rights Table data be repopulated into model contract format, and a revised table be provided for incorporation by modification under section 18(7) of the Act. These modifications were agreed by the parties and form part of our directions.

⁶ The Protocol is an agreed process between Network Rail and a freight operator, to set out parameters about how and where to re-time late running freight services and manage these services back to the right running time, rather than to allow disruption to continue. This enables Network Rail to find robust paths for late running trains minimising further disruption, and allows freight operators to plan their resources and crew in a proactive way.

Representations by English Welsh & Scottish Railway Limited (EWS) and ORR's decision

16. EWS stated that while it had no objections in principle to GBRf's application, it did have a number of specific comments regarding the detail of the contractual terms and the proposed services in the Schedule 5 Rights Table.⁷ We are content that the response provided by Network Rail on 20 December 2007 on behalf of both parties, addresses the issues raised by EWS. We note that a redacted copy of this response was provided directly to EWS by Network Rail. Where appropriate, we have included modifications in our directions to effect changes in the directed contract, which includes a revised Rights Table.

Contract Miles and ORR's decision

17. In its initial application, the Contract Miles column (of the model contract Schedule 5 Rights Table) was missing from the parties' Rights Table. As noted at paragraph 15 above, we suggested to the parties that the Rights Table data be repopulated into the model contract format, including the insertion of the Contract Miles column, and a revised table be provided for incorporation by modification under section 18(7) of the Act. Although the parties agreed to these modifications and provided a revised Rights Table including the Contract Miles column, the parties did not populate any data into the new Contract Miles Column.

18. Rather than delaying the approval of GBRf's LTAC to resolve this issue, we have included in Schedule 14 of the directed agreement an unfinished business provision which will allow the parties to negotiate and agree contract miles values and submit them to us for consent or determination. If the parties cannot agree the values, we have the power to determine them. We expect the parties to submit the proposed values to us by 1 April 2008. This approach is consistent with the unfinished business provisions directed by us in our recent Freightliner Limited and Freightliner Heavy Haul Limited LTAC decisions, and in our earlier EWS LTAC decision.

Indexation of Traction Electricity Charges – Schedule 7

19. In the application, the parties sought to amend paragraph 2.7.4 of Schedule 7 of the model contract to enable them to apply to the indexing of the published or determined value of Index Electricity Costs by calendar year, rather than by financial year as proposed under the freight model contract. The parties raised concerns that the values relating to financial year ending on 31 March cannot readily be published or determined for application the following day. It was therefore proposed that a provision similar to that used in the model passenger contract be used, resulting in the percentage change in the index for the year ending 30 June being used for the calculation of the traction electricity rate from the following 1 April.

⁷ Submission from EWS available at: http://www.rail-reg.gov.uk/upload/pdf/s18-GBRF_EWS_resp.pdf.

20. In our initial observations letter of 5 December 2007, we asked the parties to provide further information to justify the reason for this exception to the formula contained in the freight model contract. In its response of 20 December 2007, Network Rail reiterated that given there is a time delay before the values are published, the parties proposed a solution which provides consistency with the passenger model contract arrangements, and solves the time delay problems by using values published or determined for the period ending on 30 June, in the year before the 1 April that the indexation takes effect.

ORR's decision

21. While we understand the parties' concerns in relation to this matter, in order to ensure that Network Rail provides consistency of treatment of freight operators, we have directed the inclusion of the provision previously approved for GBRf in its existing access agreement, i.e. calculation by financial year. This issue is being considered as part of our current review of the charges and performance section of the criteria and procedures document and ongoing review of the freight model contract. This issue may also be considered as part of the work that is currently being undertaken in preparation for the next access charges review (PR08).

Access charges review

22. During the time that we have been considering this application, preparatory work continues to be undertaken (involving the railway industry) on the preparations for the next access charges review and the formal process under Schedule 4A to the Act (as amended by the Railways Act 2005) has also been initiated. The consultation process has been ongoing for PR08 for some time and the review was formally initiated on 28 February 2007 when we served a notice under paragraph 1C of Schedule 4A to the Railways Act 1993.⁸ This notice was served on both the parties.

23. This notice was served at the same time as we published a document entitled 'PR08 Advice to Ministers and Framework for Setting Access Charges' (the February Document).⁹ This document explained in detail why (following consultation and taking into account the consultation responses we had received) we had concluded that there had been a material change in circumstances since October 2001 entitling us to carry out an access charges review of any or all part of freight access contracts on the basis of the re-opener contained in paragraph 3.1.1(c) of Schedule 7 of the freight model contract. Consistent with this conclusion, this provision (i.e. paragraph 3.1.1(c)) is included in the contract that is being directed. This is the same provision that is included in all other freight access contracts.

⁸ The *Review Initiation Notice* is available at http://www.rail-reg.gov.uk/upload/pdf/PR08_note-of-proposal.pdf.

⁹ The February Document is available at <http://www.rail-reg.gov.uk/upload/pdf/316.pdf>.

24. We have also required an acknowledgment to be inserted in paragraph 3.1.3 of Schedule 7 of the contract. We explained the reason for this acknowledgement in Annex B of our February Document. In summary, this acknowledgment addresses the technical timing issue that at the time the Review Initiation Notice was served although GBRf was a party to one access contract, it has subsequently entered into a replacement track access contract and it is this contract which will be in place during the period when the conclusions of PR08 will take effect (i.e. CP4).

25. We expect to include similar drafting in other freight operators' contracts where the same circumstances arise.

Dispute of interim statement – Schedule 8

26. We asked the parties to provide detail of the rationale behind the provision of 2 working days for receipt of an interim statement under Appendix 3, paragraphs 3 and 6 of Schedule 8. We noted that while this value is present in GBRf's existing access contract, we sought justification for its continuance in the proposed contract. The parties advised that there are rarely any instances where the interim statement is disputed and 2 working days has provided more than adequate for GBRf to respond in the past. In the light of this, we have approved this value in the directed contract.

General operational performance – Schedule 8

27. We asked the parties about general operational performance under the proposed contract, including the impact of GBRf's proposed services on other train operators and the potential risks of these services to network performance. In response, the parties confirmed to our satisfaction that these issues have been appropriately considered and processes will be initiated to manage performance. The parties advised that they intend to manage performance in the following ways:

- (a) regular performance meetings;
- (b) analysis of delay trends leading to action plans to improve performance;
- (c) use of 'six sigma' techniques to analyse problem areas;¹⁰
- (d) initiatives with end customers to deliver and present traffic on time;
- (e) ensuring smooth access/egress to/from yards;
- (f) reviewing sectional running times where these do not work; and
- (g) identifying Temporary Speed Restrictions/Permanent Speed Restrictions for remedial action.

¹⁰ A structured methodology adopted by Network Rail (from 2003) to improve process performance.

Crossrail

28. A Bill is currently before Parliament, which would enable the Cross London rail link (Crossrail) to be built. Network Rail and the Secretary of State for Transport have submitted an access option for our approval under section 18 of the Act, which would reserve capacity for the proposed Crossrail services. GBRf's application provides for the Crossrail modifications in a new Schedule 13.

29. As stated in paragraph 4.22 of the criteria and procedures document, where new access contracts contain access rights which could conflict with the access rights in any future Crossrail access option, we will incorporate in such access contracts a provision requiring the adjustment of access rights in the event of any conflicting rights, with compensation where appropriate.

30. Accordingly, we have directed Network Rail to enter into the contract with access rights for the full period of its contract with a provision which will allow the modification, with compensation as appropriate, of access rights which conflict with those in Crossrail's access option. We will determine the extent to which any modification of access rights is necessary and any compensation will be calculated in accordance with Part G of the Network Code. The Schedule includes a provision stating that the provision shall cease to have effect if the Bill fails to receive Royal Assent by 1 January 2012, which is consistent with what is proposed in the Schedule 6 (Optionholder Event of Default) of the Crossrail access option. This approach is consistent with that which we took in the Freightliner Heavy Haul Limited and Freightliner Limited applications, on which we issued directions to Network Rail in September 2007 and December 2007 respectively.

Errors and inconsistencies

31. Some minor drafting errors and inconsistencies were identified in the draft contract. The modifications proposed to address these were agreed by the parties.

Conclusion

32. In considering track access applications, we must ensure that our decisions are consistent with our statutory duties under section 4 of the Act. The section 4 duties which have particular relevance when considering this application are:

- (a) to protect the interests of users of railway services (s 4(a));
- (b) to promote the use of the railway network in Great Britain for the carriage of passengers and goods, and the development of that railway network, to the greatest extent we consider economically practicable (s 4(b));
- (c) to promote competition in the provision of railway services (s 4(d)); and
- (d) to enable persons providing railway services to plan the future of their businesses with a reasonable degree of assurance (s 4(g)).

Public Register

33. We are required under section 72 of the Act to maintain a public register, which must include, inter alia, every direction to enter into an access contract and every access contract. Please provide two copies of the signed contract no later than 14 days after the date upon which the contract is entered into, as required by section 72(5) of the Act.

34. In placing any contract on the public register, we are required to have regard to the need for excluding, so far as that is practicable, the matters referred to in sections 71(2)(a) and (b) of the Act, including:

- (a) any matter which relates to the affairs of the individual, where publication of that matter would or might, in our opinion, seriously and prejudicially affect the interests of that individual; and
- (b) any matter which relates specifically to the affairs of that particular body of persons, whether corporate or incorporate, where publication of that matter would or might, in our opinion, seriously and prejudicially affect the interests of that body.

35. When you submit the copies of the signed contract, please list any aspects of the contract which you wish us to consider excluding from our register and explain why you consider they meet the requirements of sections 71(2)(a) or (b).

36. A copy of this letter without enclosures will be sent via email to Steven Saunders at Network Rail, and a redacted version will be sent to Nigel Oatway at EWS.

Brian Kogan