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James Osborn
Executive, Access & Licensing
Office of Rail and Road
25 Cabot Square
London
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18 August 2020

Dear James

Re: Hitachi Rail Limited - Application for Directions under Section 17 of the Railways Act 1993.

Abellio East Midlands Limited (AEM) hereby presents its response to the Application for Directions under Section 17 of The Railways Act 1993 made by Hitachi Rail Limited (HRE) in respect of Neville Hill (NL) Depot (of which AEM is DFO). AEM takes reference from both The Railways Act 1993 and the prevailing National Depot Access Conditions along with any other relevant legislation in preparing this response.

Our response will follow the format and order of the Section 17 application submitted by HRE.

1. **Introduction** – *AEM has no comment to this section.*

2. **The application**

2.1 **Title of proposed contract or amendment** – *AEM agrees* that the proposed contract is a Depot Access Agreement (non – TOC Beneficiary) between HRE (Beneficiary) and AEM (DFO) for access to and light maintenance services at Leeds Neville Hill Depot to commence on 1 April 2020. *However AEM provides the following additional information for context:*

- *A DAA has been in place between HRE and the DFO of NL Depot (initially under East Midlands Trains Limited (EMT) from 31 May 2019 and following franchise change in August 2019 under AEM).*
- *HRE have continued to enjoy access and light maintenance services at NL depot from 1 April 2020 to date following agreement between the parties whilst the Section 17 application and determination process is ongoing.*

2.2 **Contact details** - *AEM has no comment to this section.*

2.3 Licence and railway safety case - *AEM has no comment to this section.*

3. The proposed contract or amendment

3.1 **Executive summary** – *AEM agrees* that the proposed DAA is a new Depot Access Agreement on the ORRs generally approved template for the purposes of securing access to and light maintenance services in connection with the overnight servicing of the newly introduced Class 800/801 Units, built by Hitachi Rail and operated by LNER. The expected start date for the Beneficiary Depot Services is 1 April 2020 and AEM confirms that commercial terms in respect of the Beneficiary Depot Services set out in the proposed DAA are **not agreed** by the parties. *However AEM provides the following statements for context and to aid understanding of AEMs response in later points:*

- *The Abellio East Midlands (AEM) franchise commenced August 2019 replacing the previous East Midlands Trains franchise (EMT). During the mobilisation phase of the AEM franchise a DAA was entered into between AEM & HRE which did not have agreed commercial terms – this was approved by ORR and included provisions which sought to provide time to conclude commercial discussions over access charging.*

This arrangement sits outside of the standard ORR process for generally approved DAAs and should be taken into consideration here as well as the detailed history pertaining to the introduction of the Class 800/801 fleet to NL depot and the corresponding out phasing of the LNER legacy HST & Mk IV fleet.

AEM believes it to be difficult and potentially prejudicial to not understand and take account of the previous EMT franchise and HRE discussions as to scope of services required, fleet introduction time lines, delays and changes to LNER fleet cascade and ultimately the DAA arrangements reached between EMT and HRE when seeking to make a determination as to the appropriate commercial terms from 1 April 2020.

The AEM franchise contains the provision for the DFO of NL depot to be changed from 31 March 2021. As of today's date a confirming directive has not been issued to AEM by DfT that provides certainty as to the future transfer of the depot. The DFO status of NL depot has been uncertain for the duration of the time that HRE has sought to agree commercial terms with both EMT and AEM. AEM believes that the consequences of this uncertainty for it as franchisee (and for EMT previously) should be fully understood and considered within this application.

AEM recognises that any proprietary commercial or financial information pertaining application will be sought by ORR direct and as such is not included within AEMs response here.

3.2 **Terms not agreed with the facility owner** - *AEM agrees* Hitachi Rail *has not agreed* to the price proposal by the DFO for the Beneficiary Depot Services for the Minimum Level of the Beneficiary Depot Services set out in the proposed DAA.

AEM responses to the points included in HREs application under this section are outlined below:

AEM does not agree with HREs assertion that The Depot Facility Owner's price/charge for the Minimum Level of Beneficiary Services will be 'uplifted' for the period 1 April 2020 to 31 March 2021. AEMs pricing proposal to HRE for the period 1 April 2020 to 31 March 2021 reflects the changing cost base of, and usage by, beneficiaries of the depot.

The introduction of the Hitachi Class 800/801 fleet to NL depot has a different set of access and light maintenance requirements to that of both the AEM & LNER legacy fleets. As a result of this and the fluid nature of the out phasing of the LNER legacy fleet AEM is burdened with a depot cost base that has increased whilst the volume and mix of units to be processed continues to be subject to change and uncertainty.

AEM (and EMT as its predecessor) have maintained a transparent and open approach with HRE from the outset of the Class 800/801 introduction project that any adverse depot cost implications to AEM of the East Coast route fleet changes could not be absorbed by AEM and would be priced into any access charges applied to their & LNERs use of the depot in this defined DAA period.

Discussions with HRE have always provided notice that AEM has limited ability to reduce the costs of the NL depot within the period the 1st April 2020 to 31 March 2021 (this being the last 12 months of AEM as DFO per the East Midlands franchise agreement) and that there would be an increase to their costs due to the reduced number of beneficiaries to the depot. It is for this reason that AEM disputes that assertion by HRE that AEMs prices/charges for this period have been 'uplifted' as this indicates an improved contribution by beneficiaries to AEMs costs.

AEM believes that in providing transparency and dealing openly with HRE about the unique and complex current arrangements of the NL depot, the uncertain future and the constraints this places on its ability to significantly reduce the costs of the depot renders the arbitrary comparison of costs against other depots offering similar facilities within the same region of the United Kingdom irrelevant in the context of the application. HRE has not provided any quantifying evidence within the application to validate the use of the chosen comparative depots or depot service rates. AEM does not therefore accept that the comparative information provided by HRE in Enclosure 3 is of a suitably detailed and validated nature to be used in the determination sought. For the reasons noted above and in the belief that the current operating arrangement of the NL depot result in a unique cost base AEM will not reference the data contained in Enclosure 3 within this response outside of that to which AEM is author and requests that Enclosure 3 is disregarded when considering the application.

AEM responds to HREs consideration stated within this section that the proposed charges may exceed the cost to it as DFO of providing access to its service facilities and/or the supply of services within those facilities (plus a reasonable profit). And that Hitachi Rail has not been able to satisfy itself based on information provided that the charges are offered on a non-discriminatory basis with absolute refutation to the inference proffered by way of this statement by HRE.

AEM has conducted all discussions with HRE in the process of seeking to reach commercial agreement to the services requested with a core ethos of transparency and openness. AEM has sought, since the franchise commenced, to provide suitable information to HRE that clearly explains the context of the cost base at NL, the risk factors AEM has had to consider, an analysis of the direct, indirect and overhead pertinent to the depot and details of lease cost changes to the NL depot on commencement of the AEM franchise. All of this

information is significantly in excess of that which would normally be provided in the course of commercial discussions and is at the limit of what AEM consider should be disclosed

under the ORRs guidance issued in connection with the Railways (Access, Management and Licensing of Railway Undertaking) 2016 at paragraphs 3.4 and 3.6 noted below:

'3.4 Paragraph 1 (6) of Schedule 3 of the 2016 Regulations requires that the charge imposed for track access and supply of services within these service facilities must not exceed the cost of providing it, plus 'a reasonable profit'. We expect the service provider to be able to demonstrate how charges reflect the cost of providing access to its service facilities and/or the supply of services within those facilities, if requested'.

'3.6 Service providers may publish their charges in different ways, but we expect them to be open and transparent about charges for services'.

AEM as a franchised UK rail operator and a limited company is subject to a range of regulatory and legislative requirements including external financial audit and franchise reporting to DfT. Additional AEM undertakes externally led process reviews and audits which support the governance of all internal authorisation and validation processes. Internal processes within AEM provide for 'separation of activities' to meet requirements that proposal, review and authorisation of business activities are suitable assigned within its organisation.

3.3 Departure from ORR's template depot access contract - *AEM has no comment to this section.*

3.4 Duration of contract - *AEM has no comment to this section.*

4. The expression of access rights and the consumption of capacity

4.1 Benefits - *AEM has no comment to this section.*

4.2 Adequacy - *AEM has no comment to this section.*

4.3 Franchise obligations – *AEM has no comment to this section save to the statement by HRE that the services required of the NL depot are similar services currently provided by the Depot Facility Owner to LNER in respect of LNERs outgoing fleet. AEM asserts that whilst the services required by HRE in respect of the Class 800/801 fleet sit under broadly similar categories as the LNER outgoing fleet there are distinctly different requirements both in VMIs and depot operations in delivering the services. The depot has needed to undertake significant process re-engineering and increases in depot resource to be able to facilitate the differing needs of the fleets.*

4.4 Public funding - *AEM has no comment to this section.*

4.5 General guidance - *AEM has no comment to this section.*

5. Charges – *AEM refers the reader to its response to section 3.2 above. In addition and for context AEM can confirm that the charges proposed to HRE under the proposed DAA for the period 1 April 2020 – 31st March 21 have been determined in accordance with standard business practice and is outlined below:*

- *Following provision of scope, volume and phasing of services required from HRE AEM utilises appropriate modelling tools to forecast the cost to AEM taking into account:*
 - (i) *The existing resource and capacity of the depot and the current utilisation.*
 - (ii) *The evaluation of further resources required to provide the services.*
 - (iii) *Any process re-engineering that could be incorporated to improve delivery of services, drive efficiencies and manage direct costs.*
 - (iv) *A review and determination of indirect and overhead costs of the depot against the revised requirements*
 - (v) *An evaluation of the level of risk/uncertainty in the requirements against the resources that will need to be employed/utilised*
- *The resulting modelling is peer reviewed for completeness, accuracy and technical robustness. Where necessary (e.g. when introducing new services or a significant change is happening) the modelling will be reviewed and authorised by the finance leadership team.*
- *A pricing proposal is developed by commercial contract and regulatory contract professionals from the modelling to include determining the appropriate offer structure to a beneficiary and a reasonable profit to AEM. This is reviewed and authorisation by functional directors and where necessary by the Finance Director.*

6. Enhancement

6.1 Enhancement details – *AEM has no comment to this section save to the assertion by HRE that The work carried out has had no adverse implication for existing Beneficiaries, but provides additional potential opportunities for the Depot Facility Owner to provide services to future Beneficiaries cannot be quantified or validated in any way here as the enhancement works undertaken by HRE only bore reference to the requirements of their Class 800/801 fleet and were distinct rather than generic in nature. As such AEM requests that the HRE assertion referenced above is disregarded when considering the application.*

6.2 Enhancement charges – *AEM has no comment to this section.*

7. Other

7.1 Associated applications to the ORR - *AEM has no comment to this section.*

7.2 Supporting information – *AEM has no comment to this section save to the inclusion by HRE of Enclosure 3. AEM refers the reader to its response to section 3.2 and requests that Enclosure 3 be disregarded when considering the application.*

7.3 Side letters and collateral agreements - *AEM has no comment to this section.*

7.4 Confidentiality exclusions – *AEM agrees with the submission contained within this section by HRE and similarly requests the same confidentiality exclusions.*



This concludes AEMs response to the Application for Directions under Section 17 of The Railways Act 1993 made by Hitachi Rail Limited (HRE) in respect of Neville Hill (NL) Depot (of which AEM is DFO).

Yours sincerely

[Redacted]

Commercial Regulatory Access Manager

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