

**Rob Plaskitt**  
**Head of access and licensing**  
Telephone: 020 7282 2072  
Fax: 020 7282 2043  
E-mail: [rob.plaskitt@orr.gsi.gov.uk](mailto:rob.plaskitt@orr.gsi.gov.uk)

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Jonathan Cooper  
on behalf of  
Grand Central Railway Company Limited  
c/o Alliance Rail Holdings  
88 The Mount  
York  
YO24 1AR

Tim Wright  
Network Rail Infrastructure Limited  
George Stephenson House  
Toft Green  
York  
YO1 6JT

Dear Jonathan and Tim

## **Directions in respect of a track access contract between Network Rail Infrastructure Limited and Grand Central Railway Company Limited**

1. On 25 July 2014 the Office of Rail Regulation (ORR) issued directions under section 17 of the Railways Act 1993 (the Act) to Network Rail Infrastructure Limited (Network Rail) to enter into a track access contract with Grand Central Railway Company Limited (Grand Central), as formally submitted by Grand Central on 10 September 2013. The contract we directed, and which the parties entered into on 1 August 2014, contained some modifications to that originally submitted by Grand Central. The purpose of this letter is to explain our decision and the reasons for it.

### **The original application**

2. Grand Central's application was for a new track access contract to replace its two contracts for its Sunderland and West Riding services (the previous contracts), both of which were due to expire on the Principal Change Date (PCD) 2016. Grand Central applied for a contract until PCD 2026, saying that it needed to secure the rights for a further ten years in order to take a long-term lease on its existing fleet of Class 180s and on some additional Class 180s, which would replace its High Speed Trains (HSTs).

In addition it intended to spend £5.2 million on enhancements to the Class 180s, and a further £2.6 million on station enhancements at Hartlepool.

3. Compared with the previous contracts, the key changes were:

- all services to/from Sunderland would have firm rights (one previously had firm rights only to/from Hartlepool);
- all trains would have arrival and departure interval protection to/from King's Cross in place of just departure time ranges for some trains; and
- all trains, rather than just some, would have Maximum Journey Times (MJT) protection, and with some shorter journey times.

### **Network Rail's initial position**

4. Initially Network Rail objected to the application, its key concerns were:

- the contract should contain a committed financial sum, rather than an investment in specific committed schemes;
- there should be a break clause, as per the previous contracts, if Grand Central did not proceed with the planned investment;
- Network Rail wished to be involved in a three-way discussion with Grand Central and ORR about the terms of the proposed contract;
- rights should be limited to "quantum only" - namely passenger train slots, calling patterns and specified equipment;
- specifically the time-banding of the service intervals was restrictive and too narrow, and whilst a case for time-banding could be made when Grand Central only ran six trains per day, it was not appropriate for a business running 18 trains per day;
- specifically MJTs were not appropriate (several of them could not be met in Grand Central's December 2013 timetable), and would unduly constrain the timetable review proposed for December 2016;
- several of the services currently operated by Grand Central did not have the specificity of rights sought in the application; and
- Grand Central had not adequately demonstrated why these rights were now a commercial requirement.

5. Grand Central responded to these points and advised it would be meeting Network Rail to discuss the specification of access rights and the termination clauses. This discussion resulted in a revised draft contract agreed between the parties which was submitted to ORR on 5 November 2013 (see paragraph 20).

### **Initial industry consultation**

6. Prior to submitting the application to ORR Alliance Rail Holdings Limited, Grand Central's sister company, carried out the usual industry consultation. In response, First Greater Western Limited said that it had no objection. Substantive comments were received from the following consultees:

*DB Schenker Rail (UK) Limited (DB Schenker)*

7. DB Schenker said it was unclear from the application form the extent to which the parties did not agree on the level of flexibility required for the access rights, but felt that the flexibility of +/- 30 minutes sought by Grand Central was greater than the level previously agreed for regular timetabled passenger services. This observation is no longer applicable to the revised draft contract.

*Department for Transport (DfT)*

8. DfT welcomed the stability and potential savings that could be realised by securing a ten-year contract, as recognised within its own latest franchise propositions. Furthermore, whilst it had concerns over the potential financial impact on the taxpayer of increased open access passenger operations in their current form, it recognised that this application was to extend current rights.

9. It sought clarification on the performance arrangement between Network Rail and Grand Central, and confirmation that Grand Central would deliver a comparable trajectory of operational performance to that of franchised operators on the route, in order not to adversely affect the performance of the route as a whole.

10. DfT said it would be helpful to know at what point Grand Central would propose to give a firm commitment to implement its investment proposals and, in turn, what contractual mechanism would be employed to ensure that any such commitments would be delivered. It also asked what additional/alternative investment might be undertaken if the planned work at Hartlepool did not proceed.

11. Finally, DfT sought assurance from ORR, Network Rail and Grand Central that returns on the investment made by taxpayers in the new InterCity Express Trains and in the Control Period 4 (CP4) and CP5 infrastructure enhancements would not be jeopardised by the approval of the application.

12. Whilst East Coast's PPM target in year five of CP5 is 88%, Grand Central's is 84%. Reviewing Grand Central's performance through CP4, Network Rail considered 84% was achievable and largely sustainable. Its strategy was to return Grand Central to the historical levels of punctuality, which it suggested was 84%, by addressing the things that have caused the current downturn in PPM, which is largely to do with the overhead line equipment, track and possession reliability. This appears to be a reasonable target in the circumstances.

13. A provision has been included in the contract so that the duration is shortened if the planned investment, or acceptable alternative investment, is not undertaken. Duration of the contract and the investment conditions are discussed further in paragraphs 28 to 32 and 37 to 38.

14. On the basis that this contract allows Grand Central to continue running its current services with improved rolling stock, we see no reason why this would adversely impact on

the investment in the new InterCity Express Trains and in the CP4 and CP5 infrastructure enhancements.

*East Coast Main Line Company Limited (East Coast)*

15. East Coast noted that (at that time) we had yet to publish our conclusions of our On-Rail Competition consultation. It said that no new rights for open access operators should be granted until we had done so and that the whole charging regime should be overhauled. It said that it believed the East Coast Main Line (ECML) was capacity constrained and that, given the competing future aspirations of operators and significant investment required (and committed) by the Government in CP4 and CP5, it did not believe that the current charging regime, whereby operators such as Grand Central only paid marginal costs, was fit for purpose. It repeated its view that no new contract for any passenger operator should be entered into on the basis of the operator only paying variable track access charges. It also argued that the Not Primarily Abstractive (NPA) test should be applied whenever new access rights were sought.

16. We subsequently issued our final determination on our charging policy for CP5. In particular, it confirmed the continuation of our policy that open access operators would only pay variable track access charges. In relation to the NPA test, our policy is that we only apply the test when open access operators first apply for track access rights for a particular service. We do not repeat the test when they seek to renew the rights for that service, which is the case here.

*First/Keolis Transpennine Limited (TPE)*

17. TPE said that as the rights being sought were to reflect current services, it had no objection to the principle of their continuation. However, it referred to our approval of the first supplemental agreement to its own track access contract, which included a defeasance provision which could be applied in the development of the May 2014 timetable. It said it would not expect any rights achieved through this application to cause its rights to defease. In the event, the May 2014 timetable was developed without the need to use the defeasance provision.

*Freightliner*

18. Freightliner said it was supportive of the application and appreciated the importance to non-franchised operators of long-term contracts with firm rights to underpin investment. It queried the apparent disconnect in the application form between the statement that the new contract was for ten years, and the contract commencing in December 2014 and ending in December 2026. In response Grand Central clarified the position. Duration is discussed further in paragraphs 28 to 32.

*Passenger Focus*

19. Passenger Focus posed some questions on specific aspects of the application, which were answered by Grand Central, and said that it had a presumption in favour of the

competition brought by open access operators because of the benefits they bring to passengers. By definition passengers would have a choice and, for some, improved access to services which they did not have before. ORR had shown that the competition generated by open access operators had led to passengers benefitting from lower fares, whilst its own National Passenger Survey (NPS) also showed open access operators recording high levels of passenger satisfaction. It believed that the proposed new contract was a sensible and realistic approach, and so it supported the application.

### **A revised draft contract**

20. Following the further discussions between Grand Central and Network Rail mentioned in paragraph 5, on 5 November 2013 we received a revised draft contract which had been agreed between the parties. Grand Central advised that the main changes were in relation to interval protection, journey time protection and investment.

21. Network Rail confirmed that Grand Central had agreed to remove the departure time/interval ranges and replace them with a quantum split between peak and off-peak, combined with footnotes in Table 2.1 of Schedule 5, saying that this greatly increased Network Rail's flexibility to produce timetables which could adapt to incremental change and make efficient use of capacity, whilst giving Grand Central a degree of commercial certainty.

22. Network Rail said that both parties had agreed to move from their initial position on MJT protection. It recognised the unique make up of Grand Central's journey times, which contained a considerable amount of pathing time, and was satisfied that the level of flex was sufficient for Network Rail to timetable effectively.

23. Network Rail advised that Grand Central had agreed to the inclusion of a break clause should the investment conditions not be met, and confirmed that Network Rail would now be willing to support the application. However, for the purpose of expediency, the application would remain a section 17.

### **Further industry consultation**

24. We advised the parties that a further industry consultation would be required on the revised contract which was undertaken by Network Rail. Three responses were received.

#### *DB Schenker*

25. DB Schenker raised a number of minor queries, in particular whether the service intervals for the Sunderland and West Riding services were linked. Network Rail confirmed that they were not and answered DB Schenker's other queries.

#### *Department for Transport*

26. DfT said that it had nothing to add to its response to the original consultation.

## *Passenger Focus*

27. Passenger Focus said that passengers would be pleased by Grand Central's commitment to carry out a full interior refresh and reconfiguration of the Class 180 fleet by the end of 2017, as the upkeep of Grand Central trains scored 78% satisfied or good in the latest NPS, seven percentage points less than the average for long-distance services. It concluded that it had supported the initial application because of passengers' views, as indicated in the Spring 2013 NPS scores, and also supported the revised application.

## **Issues considered by ORR**

### *Duration*

28. Grand Central explained that it needed a long-term track access contract to enable it to secure its existing fleet of Class 180s on a long-term basis, lease two additional rolling-stock sets to standardise its fleet (currently a mix of HSTs and Class 180s), and invest £5.2m in refurbishing its rolling stock. This would deliver operational and performance benefits as the additional sets could be used to strengthen services in busy periods, provide spare sets during the refurbishment period and allow Grand Central's West Riding and North East routes to be operated as one integrated service group.

29. Grand Central also advised that it planned to invest a further £2.6m in infrastructure improvements at Hartlepool station by bringing back into use the disused platform. It said this would deliver benefits to Grand Central's passengers as well as helping to relieve capacity constraints on the route as a whole. Should it not prove possible to produce a viable scheme to bring the platform back into use, Grand Central said it would invest a similar amount to improve retail or passenger facilities and car parking at Hartlepool and/or other stations served by Grand Central.

30. Under The Railways Infrastructure (Access and Management) Regulations 2005, access contracts of longer than five years must be justified by the existence of commercial contracts, specialised investments or risks. In reaching our decision we considered the scale of the investment proposed by Grand Central, the degree to which these investments are likely to be sunk, and the additional costs and passenger benefits.

31. Grand Central submitted, on a confidential basis, an investment appraisal setting out its investment plans, expected return on investment and payback periods. We assessed Grand Central's appraisal and considered the costs, benefits and timescales to realise these benefits to be reasonable. Based on the information supplied we consider that Grand Central is making a substantial investment in refurbishing rolling-stock and improving station facilities to the benefit of passengers and that there is a reasonable probability that this investment is sunk.

32. Based on our assessment we considered a contract length of seven years as reasonably necessary to support the investment in rolling-stock. We are satisfied that without this length of contract there are risks that this investment would not go-ahead in its entirety or on the terms necessary to maximise passenger benefits, to the detriment of

passengers. However, because Grand Central intends to invest additionally in station infrastructure, we consider that a longer payback period of ten years is reasonably necessary to support this additional investment. We therefore decided to approve a contract length of ten years and, because the investment is planned to take place from 2016, we considered it reasonable that the contract extension should start from this date.

#### *Specification of rights*

33. Around the time Grand Central's initial application was submitted in September 2013, Network Rail was also reviewing its approach to the sale of access rights and intended to apply the new approach to all access rights from December 2016. This was explained as starting with quantum rights as a base position with any additional elements of protection being agreed if the operator could demonstrate a commercial need for those added levels of protection and Network Rail had the capacity to grant them. This policy was intended to give Network Rail flexibility to make the best use of available capacity when constructing future timetables.

34. Our concern was that during the period while Network Rail was developing its new approach it had not been consistent when negotiating journey time and service interval protection with different operators. We therefore asked Network Rail to look again at all recent cases where it had agreed access rights from December 2016 onwards to ensure that it had treated all operators fairly and consistently. Around this time Network Rail also revised the terms of its Sale of Access Rights (SoAR) panel so that it would have to approve the sale of all access rights and ensure a consistency of approach across the network.

35. Network Rail engaged in further discussions with Grand Central on this point and agreed that the specification of journey time and interval protection should be subject to review from December 2016 taking account of: any future recast of the overall ECML timetable; implementation of the various infrastructure improvements; and development of the SoAR panel processes and the associated Network Rail criteria against which Schedule 5 parameters could be assessed.

36. Precisely how Network Rail's new approach to the specification of access rights from December 2016 will be applied in practice is the subject of extensive discussions with the industry through the Rail Delivery Group. In the meantime, rather than including journey time and interval protection for the duration of the contract and including a review provision from December 2016, we have inserted provisions whereby these protections expire in December 2016. This is the same approach we have taken with other operators recently who have extended access rights beyond December 2016. In due course, if the parties agree to add additional specification to the access rights, we will consider them in the usual way.

#### *Investment conditions*

37. The original draft contract did not contain a break clause in the event that Grand Central did not undertake the investment that formed the basis of its justification for a long-term contract. This omission was acknowledged and rectified by Grand Central in the revised agreed draft contract submitted in November. We advised Grand Central that in

fact two break points would be required - one in December 2019 if it was unable to secure the long-term lease on the Class 180s (in which case it would revert to a standard five-year contract), and one in December 2023 if, having secured the long-term lease, it did not undertake the further investment in the Class 180s and station enhancements by December 2018. This second breakpoint reflects our assessment that we consider a contract length of seven years as reasonably necessary to support the investment in rolling-stock, as mentioned in paragraph 32.

38. We amended the drafting of the conditions which were based on similar provisions in the previous contracts so that ORR, rather than Network Rail, will decide whether the investment conditions have been met. *Service intervals*

39. The contract contains service intervals expressed as footnotes in Table 2.1 of Schedule 5. We are not convinced that this is the clearest way to achieve this given that service intervals are usually expressed within a separate table in Schedule 5. However, as interval protection currently only extends to December 2016 and, given that the ECML timetable is unlikely to see any significant change during that period, we are content to approve the rights sought. If the parties agree interval protection beyond this date we would suggest the model contract drafting is used as a starting point.

#### *Peak definitions*

40. The contract contains a more tightly defined Weekday peak period than is normally the case and a Saturday peak period. Grand Central argued that this, combined with the service intervals mentioned above, was necessary to protect its existing service pattern because the small quantum of Grand Central services meant there was a requirement for it to have a reasonable spread of services for both commercial and operational reasons.

41. Whilst this is unusual it is not unique and, given Network Rail's willingness to agree to the provisions, we are content.

#### *Maximum Journey Times*

42. The contract contains MJTs for each train, with three minutes added to the journey times achieved in the May 2014 timetable. Grand Central justified the inclusion of these provisions by saying that it required journey time protection as a backstop to ensure that its already excessively long journeys were not extended further. It provided an analysis showing that on average its services contain far more pathing time than those of East Coast and Hull Trains over equivalent parts of the ECML, and argued that it needed MJTs on a train by train basis as a result of the wide spread of journey times across individual services.

43. Whilst on average Grand Central's services contain considerable pathing time, some individual trains contain very little. We would not usually approve journey time protection that is so closely related to a particular timetable. However, as journey time protection currently only extends to December 2016 and the ECML timetable is unlikely to see any significant change during that period, and given that Network Rail is satisfied that

it retains sufficient timetabling flexibility during this period, we are content to approve the rights sought. If the parties agree interval protection beyond this date we will consider any justification put forward but will not necessarily agree to similar journey time protection over a much longer period.

#### *Liability Cap in Schedule 9*

44. The existing Grand Central contracts both contain a Liability Cap of £10million, set at the minimum level for passenger operators, and the draft contract submitted to us proposed a similar cap. Whilst we are content to roll this principle forward into the new combined contract, we advised Grand Central that the figure should be updated to take into account inflation, meaning a cap of £11,338,873, to then be indexed annually. The parties accepted this amendment.

#### *Other variations from the model passenger track access contract*

45. The existing model contract is designed for franchised passenger operators and, as such, some amendments are appropriate for open access operators. The draft contract has been checked against the model contract and against the existing Grand Central contracts, and we consider that the variations from the model contract are justified.

#### *ERTMS Reopener*

46. We advised the parties that we would require the inclusion of an ERTMS Reopener, under which ORR would have the ability to insert a compensation/apportionment of costs schedule, essentially as a fall-back position in case the commercial negotiations between freight and open access operators on the one hand and Network Rail on the other did not come to fruition for any reason. In response to a question from Grand Central we explained that such an arrangement was not necessary for franchised passenger operators as the financial arrangements for ERTMS fitment to their rolling stock had already been agreed.

47. Grand Central suggested a much-revised version of the Reopener, which involves the appointment of an Expert to determine any dispute between the parties. It is drafted to ensure that Grand Central is assured that the compensation it will receive will be determined fairly, and Network Rail is assured that the ERTMS project will not be delayed by any dispute. Following some minor amendments to Grand Central's proposal, the terms of the Reopener were agreed between the parties and ORR.

#### *Periodic Review 2013 (PR13)*

48. Since the draft contract was first submitted PR13 has been implemented; therefore, we have imported into the contract the amended Schedules 4, 7 and 8 from the Periodic Review Notice and made the associated amendments to the front end of the contract. We have also inserted the correct rates in Annex C to Part 3 of Schedule 4, as one of the rates was incorrect in the Periodic Review Notice.

### *Effective Date and termination of the two existing contracts*

49. Instead of Grand Central retaining its two previous contracts until December 2016 and its new contract not taking effect until that date, the parties proposed that the new contract should come into effect upon signature and the previous contracts should be simultaneously terminated. We agreed to this and Grand Central now only has the one new contract.

### **ORR's conclusions**

50. In considering the contract and in reaching our decision, we have had to weigh and strike the appropriate balance in discharging our statutory duties under section 4 of the Act. We concluded that issuing directions in respect of this contract is consistent with our section 4 duties, in particular those relating to:

- protecting the interests of users of railway services;
- promoting the use of the railway network for the carriage of passengers and goods;
- promoting competition in the provision of railway services for the benefit of users of railway services; and
- enabling persons providing railway services to plan their businesses with a reasonable degree of assurance.

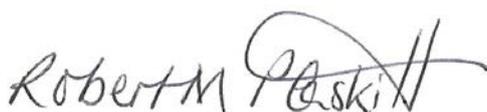
### **ORR's public register**

51. We have received a copy of the signed contract which will be placed on our public register.

### **Administration**

52. Copies of this letter and the contract will be placed on the ORR website. I am also copying this letter without enclosures to Chris Armitage at Network Rail, Andrew Murray and Keith Merritt at the Department for Transport, Nigel Oatway at DB Schenker, Phil Dawson at East Coast, George Thomas at TPE, Jason Bird at Freightliner, and John Sears at Passenger Focus.

Yours sincerely

A handwritten signature in blue ink that reads 'Robert M Plaskitt'.

**Rob Plaskitt**