



PR18: Schedule 4 - Proposal not to pursue a range of schedule 4 issues in PR18

December 2016

This document has been published alongside [‘Improving incentives on Network Rail and train operators: A consultation on changes to charges and contractual incentives’](#).

Policy	Incentives - Schedule 4
Policy area	Potential changes to the schedule 4 regime that we are proposing to de-prioritise for the PR18 review
Background	<p>Schedule 4 relates to planned disruption on the network ("possessions"), which is needed to undertake maintenance, renewals and enhancements. It is intended to:</p> <ul style="list-style-type: none">• Reduce the risk train operators bear with respect to planned possessions by compensating them for the financial impact they incur (which is outside of their direct control); and• Incentivise Network Rail to limit the level of service disruption as a result of possessions. <p>For most possessions Schedule 4 is a 'liquidated damages' regime, for which the compensation is determined by the formulae specified in the contract, with different formulae for passengers and freight. Train operators can also claim bespoke compensation for severe or long-lasting disruption.</p> <p>Franchised passenger operators pay an Access Charge Supplement (ACS) and in return receive compensation under the liquidated damages regime. This includes both revenue loss and cost compensation. Currently no open access operators choose to participate in this regime. Aside from the ACS, the costs of Schedule 4 compensation for passenger and freight operators are ultimately met by the government through its funding of Network Rail.</p> <p>The amount of compensation a freight operator receives depends on</p>

the degree of disruption, with payments being higher for late notice possessions.

Which of the PR18 outcomes does this charge/incentive deliver against?

Outcome: The network is available.

Description of outcome:

- *Taking effective decisions around possessions, mitigating the overall impact on end users*
- *The impact of delay on train operators, passengers and freight customers is minimised*

Problem under consideration with the current charge/incentive

In response to our November 2015 stakeholder letter (“the November 2015 letter”) stakeholders raised a number of issues with the existing Schedule 4 regime. The RDG review of charges also highlighted a number of areas where improvements could be made. In addition to “*Incentives created by NDFs*”, “*Approach to ACS calculation*” and “*Bespoke compensation*” ([these areas are presented in separate notes](#)), stakeholder feedback included the following areas for improvement:

- *Liquidated damages passenger train operator cost compensation* - the existing arrangements do not compensate passenger train operating companies (TOCs) for all of the costs they face as a result of planned possessions. Compensation includes the cost for bus replacement and costs associated with the number of train miles operated. Compensation does not include any compensation for costs associated with, for example, train planning, management and publicity;
- *Liquidated damages freight compensation* - the existing compensation arrangements do not cover all the costs incurred as a result of possessions and may significantly undercompensate freight operating companies (FOCs) for the overall impact on their businesses;
- *Cancelled possessions* - when a possession is planned (e.g. for a proposed strike) but later cancelled, a passenger train operator may recover costs but not revenue losses;
- *Scope of incentives* - Schedule 4 does not incentivise Network Rail to fully take into account the end user and wider societal impacts when planning possessions; and
- *Encouraging joint working on timetabling* - the Schedule 4 regime does not encourage industry to work together to declare amended timetables. This issue was highlighted especially in the context of bad weather.

What is the scale of the issue & who is impacted?

As set out in our initial consultation on PR18, given limited stakeholder and ORR resources, we need to focus on areas where the review can make a significant impact on outcomes for passengers, freight customers and those providing funds to the railways. Accordingly, we have focused our efforts on making improvements to the Schedule 4 regime only in the areas where they can deliver the most value.

We recognise that any inaccuracies in the Schedule 4 regime are likely to reduce its effectiveness in terms of its intended impact on Network Rail and train operators. However, our approach to addressing these issues needs to be proportionate. Therefore, in considering the issues that we have identified with Schedule 4 we have looked at the:

- available evidence on the scale of the problem; and
- ease and effectiveness of the potential solutions available.

Based on our initial assessment of these issues, we are proposing to take forward those issues which we think will have the biggest impact on the effectiveness of Schedule 4, notably *“Incentives created by NDFs”*, *“Approach to ACS calculation”* and *“Bespoke compensation”*. We have assessed the prioritised issues in the separate notes.

This means that we propose to not pursue the remaining issues. Our reasoning to deprioritise these issues is set out in this note.

Reasons to de-prioritise

Issue 1: TOC compensation

- Our previous evidence¹ suggests that bus replacement costs (which are already compensated) form the highest proportion of TOC possession costs (around 90%); meanwhile other costs account for around 10% of total costs, and fall into two groups:
 - costs associated with the number of train miles operated; and
 - other costs associated with train planning, management and publicity.
- Based on our discussions with industry, we do not think that the proportion or scale of other costs has significantly changed; and therefore other costs associated with train planning, management and publicity (i.e. currently not included in the Schedule 4 cost compensation) continue to appear relatively small. This suggests that it could be unduly cumbersome to amend the regime to take account of them.

Issue 2: FOC compensation

- Any additional compensation would need to be funded. We do not have evidence that this is a

¹ Faber Maunsell, 2007, *Review of Possessions Cost Compensation*. A final report to Network Rail, ORR and ATOC.

	<p>funding priority at this stage, for example from either governments' freight strategies.</p> <ul style="list-style-type: none"> • We have limited information about the scale of this issue. • Unless we have good evidence on these costs, it could be unduly cumbersome to amend the regime to take account of them, not least as the impacts may vary significantly by operator and even by individual service.
Issue 3: Revenue compensation for passenger operators for cancelled possessions	<ul style="list-style-type: none"> • We have not been able to fully assess the scale of this issue due to a lack of available data on: 1) the frequency of (late) cancelled possessions; and 2) the associated revenue impacts faced by operators when possessions are cancelled. • Other reforms look likely to deliver more significant benefits than further work in this area.
Issue 4: Scope of incentives (end user impacts)	<ul style="list-style-type: none"> • The Schedule 4 regime should be consistent with Schedule 8. Work on the scope of incentives and end user impacts for Schedule 8 has focussed on passenger compensation for delays. Given the focus of Schedule 4 is on planned disruption, it would not be appropriate to incorporate those proposals directly. • We have decided not to consider other approaches to incorporating end user impacts, for either planned or unplanned delay, as part of this review owing to the complexity of doing so and the more significant scope for improvement in other areas.
Issue 5: Incentives for amending timetables	<ul style="list-style-type: none"> • This appears to be mainly an issue related to the impact of winter weather on third rail services. • Trying to address this through Schedule 4 may result in more complex arrangements that are disproportionate to the scale of the problem.
Recommendation	
Recommendation on Issue 1: TOC compensation	<ul style="list-style-type: none"> • In the absence of evidence that the omitted costs are substantial and practical to calculate, we are not intending to pursue this issue further as part of PR18. • We expect Schedule 4 to be recalibrated and encourage operating companies to engage in this process and provide any relevant evidence e.g. on bus replacement costs.
Recommendation on Issue 2: FOC compensation	<ul style="list-style-type: none"> • In the absence a clear steer from funders on their willingness to explore these issues, and in light of the likely complexity of doing so, we are not planning to consider this issue further as part of PR18.
Recommendation on Issue 3: Revenue compensation for	<ul style="list-style-type: none"> • In the absence of further data on the scale of this

passenger operators for cancelled possessions	<p>issue we are planning to de-prioritise it.</p> <ul style="list-style-type: none"> • Our work to review NDFs may help to reduce this issue assuming Network Rail is incentivised to plan its possessions more effectively.
Recommendation on Issue 4: Scope of incentives (end user impacts)	<ul style="list-style-type: none"> • We are not proposing to make any changes to Schedule 4 with respect to the scope of incentives. • Changes in this area would add more complexity to the regime.
Recommendation on Issue 5: Incentives for amending timetables	<ul style="list-style-type: none"> • We are not proposing to make any changes to Schedule 4 with respect to supporting the timetable amendments process. • We think this issue would be better solved by industry processes and collaboration.
<p>Next steps</p> <p>If stakeholders disagree with our priorities, and have evidence that supports the re-prioritisation of any of these issues, we invite them to submit it in response to this consultation.</p> <p>We will confirm our priorities in 2017.</p>	



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