

**Joint Reference to the Access Disputes Panel
Of a Dispute Relating to Vehicle Change
for Class 185 Diesel Multiple Units**

Reference ADP14

1 DETAILS OF PARTIES

1.1 The names and addresses of the parties to the reference are as follows:-

First/Keolis Transpennine Limited "TransPennine Express" A company registered in England under number 4113923 having its registered office at: Third Floor, Macmillan House Paddington Station London W2 1FG	Network Rail Infrastructure Limited "Network Rail" A company registered in England under number 2904587 having its registered office at: 40 Melton Street London NW1 2EE
Contact: Philip Hassall Position: Track Access Manager Tel: 07841 295303 Fax: 0161 228 8191 Email: philip.hassall@firstgroup.com	Contact: Tim Wright Position: Business Manager Tel: 01904 383092 Fax: 01904 383262 Email: tim.wright@networkrail.co.uk

2 THE PARTIES' RIGHT TO BRING THIS REFERENCE

2.1 This matter is referred to the relevant Access Disputes Resolution Rules Panel ("the Panel") for determination in accordance with Condition F 5.1 of the Network Code.

3 CONTENTS OF REFERENCE

The Parties have together produced this joint reference and it includes:-

- (a) The subject matter of the dispute in Section 4;
- (b) A summary of the issues in dispute in Section 5;
- (c) A detailed explanation of the issues in dispute prepared by the claimant with a paragraph by paragraph response from the respondent(s) in Section 6;
- (d) The decisions of principle sought from the Panel in respect of legal entitlement and remedies in Section 8; and
- (e) Appendices and other supporting material.

4 SUBJECT MATTER OF DISPUTE

- 4.1 This dispute arises over the interpretation of Condition F3 of the Network Code and in particular Condition F3.2 which sets out the amount of compensation which Network Rail can seek as part of the Vehicle Change under Part F.
- 4.2 This dispute also concerns whether or not Network Rail is seeking to recover costs which are already funded through the industry framework in particular the Variable Track Usage Charge (the "VTU charge") set out in the Track Access Contract between the parties.
- 4.3 Other provisions of the Network Code which are relevant include:
- (a) Condition F2.3 which sets out the contents of the notice required to be sent by Network Rail;
 - (b) Condition F2.4 which requires Network Rail to provide a preliminary estimate of costs;
 - (c) Condition F3.1 which sets out the required contents of the Formal Notice;
 - (d) Condition F3.3 which provides that the benefits of the Vehicle Change should be considered in the estimate; and
 - (e) Condition F3.4 which sets out the time for application to the Panel and the implementation of Vehicle Change.
- 4.4 The following documents are also considered to be relevant by the Parties:
- (a) Schedule 7 of the Track Access Agreement between the Parties in particular Part 2 clause 3 (Schedule 7 is attached as Annex A).
 - (b) The Office of Rail Regulation Criteria and Procedures for the approval of Passenger Track Access Contracts (Third Edition) in particular paragraphs 5.12-5.14 explaining the purpose and operation of the Variable Track Usage Charge. (Extract of paragraphs 5.12-5.14 attached as Annex B).
 - (c) The Office of Rail Regulation document "Network Code reform phase 2: Conclusions – the way forward, November 2005" in particular paragraph 3.46 (document attached as Annex C).
 - (d) The Office of the Rail Regulation document "Network Code reform phase 2: update and emerging conclusions: Network Rail's response" in particular the third paragraph on Page 10 (document attached as Annex D)

5 SUMMARY OF DISPUTE

5.1 The dispute relates to a Vehicle Change notified to Network Rail by TransPennine Express on 7 September 2004 for the proposed introduction of Class 185 Diesel Multiple Units (Class 185). (Annex E)

5.2 A vehicle change notice was issued by Network Rail on behalf of TransPennine Express on 7 February 2005 (Annex F). On 17 November 2005 Network Rail provided a formal response under Condition F3 of the Network Code (the "Formal Response") (Annex G). The Formal Response provides among other preconditions that Network Rail will accept the Vehicle Change proposal subject to TransPennine Express agreeing to : -

"Meet all costs associated with any increase in track wear and resulting increased maintenance requirements, compared to existing vehicles being used over approved routes."

And

"All costs associated with work required to the network resulting from monitoring and attributed to this Vehicle Change application."

The parties' differences over the other preconditions in this Formal Response dated 17 November 2005 (Annex G) have been satisfactory resolved.

5.3 TransPennine Express believes that:

- (a) these costs are not a proper precondition of agreeing to establish a Vehicle Change,
- (b) the industry framework is designed on the basis that maintenance costs due to the operation of services are paid for by operators under track access charges, principally in this case the fixed track access charge and the VTU charge set out in Schedule 7 of the parties' Track Access Agreement and are not therefore properly dealt with under Part F;
- (c) by imposing a pre-condition that additional costs be paid before agreeing to Vehicle Change, Network Rail are in effect attempting to change the basis of charging for access to the Network approved by ORR

5.4 TransPennine Express also believes that the benefits of change have not been considered and that it is entitled to have this consideration.

- 5.5 Network Rail believes that
- (a) The underlying principle should be applied that a proposer of a change bears the cost of that change;
 - (b) More work needs to be done in this case to establish what additional costs exist ;
 - (c) The ability to recover additional track wear costs is a reasonable pre-condition of Network Rail's agreeing to the proposed Vehicle Change;
 - (d) Payment of these costs would not involve additional or duplication of costs already included in the VTU charge set out in Schedule 7.

6 EXPLANATION OF EACH ISSUE IN DISPUTE WITH RESPONSE

6.1 TransPennine Express Argument

- 6.1.1 TransPennine Express believes Network Rail is funded to provide the infrastructure over which the TransPennine Express services are operated. This funding provides for all the costs of maintenance of the track as assessed and determined by ORR during periodic Access Charges Reviews through a combination of grant, fixed track charge and VTU charge.
- 6.1.2 TransPennine Express is committed to paying fixed track charges and VTU charges under the terms of its Track Access Contract with Network Rail. This obligation is part of the standard industry framework approved by ORR. As part of the overall charging framework it is designed to compensate Network Rail for maintenance and other costs arising from the usage of rolling stock during the franchise.
- 6.1.3 Charges for track access are made according to the terms of Schedule 7 of the Track Access Contract between TransPennine Express and Network Rail. Paragraph 3 of part 2 of Schedule 7 sets out the VTU charge. The charge is calculated by applying the variable charge rate for each type of Vehicle calculated according to a formula approved by ORR to the actual miles each vehicle type runs.
- 6.1.4 The formula for variable charge rate is based upon characteristics for each vehicle type including average loaded weight, speed, axles, axle load and unsprung mass. It is the result of significant investigation and research within the industry and by consultants which has been periodically reviewed as part of access charge reviews and other consultations by ORR.

6.1.5 A new variable charge rate is established for new rolling stock approved by ORR and applied to all TransPennine Express' usage of the new vehicles. TransPennine Express will not have permission to use the new vehicles except subject to payment of the new variable track access charge rate as approved by ORR (and continued payment of the fixed track access charge). This is the industry approved and agreed means of compensating Network Rail for wear on the basis of the impact of operation of the vehicles which are actually used on the Network.

6.1.6 At the time of the last access charges review ORR consulted on "Vehicle characteristics in the variable usage charge model." The consultation document (6 August 2003) noted that (paragraph 6):

"Usage charges were derived from the 'top down' usage charge model which the regulator developed at the time of the last periodic review with his consultants Booz Allen Hamilton and which was consulted upon at that time. An aggregate amount of the variable element of Railtrack's (now Network Rail's) maintenance and renewals expenditure of a given volume of services was allocated through the model to different vehicle types. That Allocation is based on the vehicle characteristics... and followed research into how the various vehicle characteristics affect the level of network wear and tear and therefore impact upon maintenance and renewals cost incurred by Network Rail."

6.1.7 The cost of maintenance caused by the operation of trains is therefore a matter which is dealt with in the industry by a system of allocation of total costs between vehicle use on the basis of specified characteristics. This is undertaken by ORR following industry discussion and consultation on the basis of judgement informed by the available research. It is not appropriate to seek to separate out and assess costs of a specific change in vehicles from this global charging mechanism and to attempt to impose a specific indemnity for track wear in relation to such a change. To do so would be to place Network Rail's specific assessment above the methodology consulted with and approved by the industry and potentially to provide Network Rail with additional or duplication of funding for maintenance beyond that deemed appropriate by ORR.

6.1.8 TransPennine Express will be required to pay variable track usage charges on the basis of the rate for the Class 185 and therefore believes the costs Network Rail is seeking to recover as a precondition of its acceptance of this Vehicle Change are properly the subject of Schedule 7 (and if there is any dispute the Schedule 7 dispute resolution process). They are not a matter of Vehicle Change under Part F and it is inappropriate for Network Rail to attempt to require an indemnity in relation to any additional costs it may incur (and for which it will be funded under the agreed track access provisions) as a condition of Vehicle Change.

6.1.9 TransPennine Express is aware that Network Rail has recently engaged in the ORR consultation on Network Code Reform phase 2. In its response to the update and emerging conclusions document Network Rail state at page 10:

"We also consider there needs to be greater clarity about the relationship between Part F and Variable Track Usage (VTU) charges for when new vehicles are introduced to the Network. There is potential for these vehicles to cause more costs than those recovered by the VTU charge, and therefore we would appreciate a definitive statement about whether or not we can recover these additional costs through Part F." (response attached at Annex D)

6.1.10 In response ORR's "Conclusions – the way forward" document states (paragraph 3.46):

"Finally Network Rail said that it would be helpful to have greater clarity about the relationship between Part F and VTU charges. If Network Rail is correct that there is potential for new vehicles to cause more costs than those recovered by the VTU charge, then Part F could be an option for enabling these additional costs to be recovered. We have discussed this with Network Rail and have not seen convincing evidence that there are any such additional costs that are not already covered by other elements of the contract. Accordingly, we do not propose any changes to Part F. However Network Rail may wish to consider providing further information to support their view and justify further revisions to Part F."

6.1.11 It is clear from this response that:

- (a) VTU charges are designed to compensate Network Rail for additional track wear and maintenance;
- (b) Currently, Part F is not intended to provide for recovery for additional track wear alleged by Network Rail ("*Part F could be an option for enabling...*");
- (c) ORR is willing to consider whether Part F should be extended in the future to provide for such recovery;
- (d) ORR has so far not seen any compelling evidence that such an extension is necessary;
- (e) ORR therefore does not intend to make such a change.

6.1.12 Network Rail therefore appears to be trying to use Part F in a manner in which it is not intended to be used to obtain additional income which is intended to be recovered through other contractual mechanisms.

6.1.13 If Network Rail believes it is not being appropriately funded by operation of the combination of the grants it receives, fixed track access charges and ORR approved VTU charge, TransPennine Express believes the appropriate action is for Network Rail to raise this with ORR at the next access charges review. In the meantime Network Rail is already being funded for track wear and maintenance, will receive a revised VTU charge to reflect the new rolling stock characteristics and should not seek to claim further costs from TransPennine Express.

6.1.14 The issue is potentially far reaching as:

- (a) It could be applied to every future rolling stock introduction across the Network.
- (b) The value of compensation which Network Rail may claim as a precondition to each and every future Vehicle Change is currently unquantifiable, potentially significant and may prove difficult to assess or dispute. The difficulty in predicting such costs will introduce uncertainty into the industry charging regime (see d below)
- (c) The decision could introduce a change in Part F outside of the current review process and consultation headed by ORR and consequently without (or contrary to the conclusions of) balanced consideration and discussion with the whole industry.
- (d) A change in the basis of charging for access of this type would introduce uncertainty into the charges regime and would therefore change the basis on which operators bid for franchises. Currently franchise agreements contain protection for operators for changes to the charging regime on the basis of No Net Loss No Net Gain. Changes to the charging regime of this sort (introduced outside of a charges review by the actions of Network Rail in refusing to agree a Vehicle Change unless an indemnity is provided) will not qualify for the Franchise Agreement protection and will therefore fall upon operators.

6.1.15 TransPennine Express believes the Formal Response provided by Network Rail is inadequate and contains conditions which are not properly the subject of Vehicle Change.

6.2 Network Rail Argument

6.2.1 As a general point Network Rail believes that the Vehicle Change was proposed under the version of the Network Code which applied before the current version and that reference to individual conditions should strictly be to those former conditions; but Network Rail does not think that in this particular case that this makes any difference to the substance of the argument.

6.2.2 With reference to the TransPennine Express Argument as detailed in paragraph 6 Network Rail would respond as follows.

6.1.1 to 6.1.8

6.2.3 Network Rail was notified of the proposed introduction of the Class 185 on the 7th September 2004. This notification took place after ORR had undertaken the 2003 Access Charge Review. As a result the Access Charge Review 2003 did not take into consideration the introduction of the Class 185 and any potential increased track wear these new vehicles may have on the infrastructure and the subsequent additional cost in renewing and maintaining the network to the required level. In any event at this point in time we are not yet in a position to quantify these costs with out additional monitoring work so that in general there is always going to be a funding gap between the proposal of any particular Vehicle Change, constituting the introduction of a new vehicle, and the date of the next Access Charge Review 2003 which the impact is sufficiently clear to be picked up as part of the Access Charge Review 2003.

6.2.4 Network Rail can confirm that the Class 185 has been allocated a VTU Charge. The charge is calculated in accordance with the Industry model and has been approved by ORR. Whilst Network Rail accepts that the VTU charge is aimed at recovering the costs of renewing and maintaining the network, it believes that there will be additional costs and that the current VTU model and Track Access Contract charging mechanisms will not pick up these additional incremental costs flowing from the introduction of the Class 185.

6.2.5 Schedule 7 of the Track Access Contract details the charging regime, however as Network Rail will only recover the same total amount as set out in the ACR 2003 it does not reflect those additional costs that may be required to renew and maintain the network where a heavier type of rolling stock is introduced.

6.1.9 to 6.1.11

6.2.6 ORR state at para 3.46 (Annex C) in their document 'Network Code reform phase 2 : Conclusions – the way forward' dated Nov 2005 that Part F could be an option for enabling additional costs to be recovered where it can be proven that the new vehicles cause more costs than those recoverable by the VTU Charge. It seems clear to Network Rail that ORR is not projecting out of hand the proposition that VTU charges may need to be supplemented by some means to provide full recovery of all costs for Network Rail; but is simply reluctant to go further than the statement it has made in the absence of evidence that costs in excess of the VTU formula have been generated.

6.2.7 Network Rail intends to implement a monitoring regime to establish whether or not such extra costs are generated (See Paragraph 6.2.9). If they are not, then there are no further costs to the TOC other than the costs of running the monitoring regime. But if they are, then on the principle that the proposer of change should bear the costs generated by this change, Network Rail believes that TransPennine Express should be responsible for these costs.

6.2.8 Network Rail believes and has in the past claimed its entitlement to these costs as consistent with the provisions of Condition F 3.2 of the Network Code. Condition F 3.2 states:

“Subject to Condition F3.3, the amount of the compensation referred to in Condition F3.1 shall be an amount equal to the amount of the costs, direct losses and expenses (including loss of revenue) which can reasonably be expected to be incurred by Network Rail or the operator in question as a consequence of the implementation of the proposed change other than any such costs, losses or expenses which are attributable to the Sponsor improving its ability to compete with other operators of railway assets.”

Network Rail believes that the additional costs are likely to be incurred as a consequence of the implementation of the proposed change.

6.2.9 Network Rail’s Track Engineers consider that the infrastructure will be exposed to a wear and damage regime that is significantly different to that currently experienced under the TransPennine Express operations utilising Class 158 DMU rolling stock. These changes will be as a direct consequence of the new vehicle introduction. It is therefore proposed that an infrastructure monitoring regime be implemented that is capable of adequately identifying these changes, such that any emerging degradation effects can be detected and appropriate remedial actions taken to ensure ongoing safe operation and Standards compliance.

6.2.10 The potential types of additional damage are considered to be

- (i) Plain line & facing points high rail side wear and/or fatigue cracking,
- (ii) Low rail corrugation
- (iii) Adequacy/effectiveness of trackside lubrication
- (iv) Increased occurrence of rail breaks
- (v) Geometrical deterioration rate change

Of the five types of damage under consideration it is considered that items (i) (ii), & (iii) will generally be located on curves (with the exception of Switches and Crossings, whilst (iv) & (v) could occur at any location.

6.2.11 Damage Type (i), (ii), & (iii)

Infrastructure archive records appertaining to side wear, Rolling Contact Fatigue and facing points condition will be retrieved and examined. It should be noted that track locations that have existing or previous side wear and/or Rolling Contact Fatigue histories are already subject to specific monitoring and this information will be used to baseline the present extent and severity of the rail head condition at these specific locations.

As such the above locations will be automatically considered to be candidates for the monitoring programme. In addition, analysis will be conducted to identify other curves on the network that as a consequence of their particular curvature and cant deficiency (relative to the estimated prevailing speed and declared vehicle characteristics) are now high risk sites that under previous 158 operation were known to be benign.

The physical monitoring will largely be performed using visual inspection methods in accordance with normal practice and as such this will have the added advantage of identifying any other emerging peripheral issues at the earliest opportunity.

6.2.12 Damage Type (iv) & (v)

The track geometry records for at least two measuring campaigns will be compared to previous runs and rates of deterioration computed for sites where a change is considered to be significant. An equivalent process will be applied to the data from the systematic Ultrasonic Inspection Train runs and associated rail failure records.

6.1.12

6.2.13 In conclusion Network Rail believes it is using the appropriate mechanism through Part F to recover additional expenditure which is not recoverable through other contractual mechanisms.

6.1.13

6.2.14 As the introduction of the Class 185 were proposed before the Access Charges Review 2003 it was not possible to include the Class 185 as part of our business plan submission to reflect the additional maintenance requirements and subsequent costs that this new vehicle may import upon Network Rail's infrastructure. Indeed even if we had been aware of it we would not at the stage of Access Charges Review 2003 have been able to (and still cannot) specify the amount of the extra costs involved. It is Network Rail's intention to seek to ensure that additional costs are picked up at the next Access Charges Review in 2009 meaning any such costs would form part of the regulated charging regime. However, Part F remains the appropriate mechanism to recover these costs in the intervening period until they could be input into a subsequent Access Charges Review

6.1.14

6.2.15 Network Rail agrees that this issue may apply to future rolling stock introductions across the Network, However, as the Class 185 is heavier than the current Class 158 and therefore it is vital that an assessment is undertaken to identify any additional maintenance and renewal costs that Network Rail will incur due solely to the introduction of these new vehicles. Whilst the amount of expenditure is currently unquantifiable this is purely reflective of the unknown potential damage caused by the introduction of this new vehicle onto the network and the unquantifiable costs this additional damage will lead to in terms of renewing and maintaining a safe and reliable railway. Network Rail believes the proposed infrastructure monitoring regime once completed will identify those costs that are not included in the current contractual charging regime. Network Rail does not believe that any decision would require a change in Part F as it believes that Part F is the appropriate mechanism for the recovery of any such costs.

6.2.16 This assessment would also allow Network Rail and TransPennine Express to identify the benefits, if any, the introduction of the Class 185 provides, including identifying improvements in TransPennine Express' ability to compete with other operators of railway assets and to offer an improved service to TransPennine Express' customers. Once this potential benefit was identified it would be netted off against any potential costs.

7 DECISION SOUGHT FROM THE PANEL

7.1 The Panel is requested to determine whether the conditions attached to the Formal Response are acceptable conditions of Vehicle Change which Network Rail can require under Part F.

7.2 TransPennine Express seeks the following remedy:

- (a) A determination that the proposed Vehicle Change for introduction of Class 185 be deemed to have been accepted according to the procedure under Part F without the pre-conditions set out in the Formal Response subject only to the payment of appropriate compensation.
- (b) In the event of the preconditions attached to the Formal Response are acceptable conditions of Vehicle Change which Network Rail can require under Part F, the Panel is requested to determine the amount of compensation that Network Rail should be entitled to claim, or the method by which such compensation can be calculated.

8 SIGNATURES

For and on behalf of Transpennine Express

For and on behalf of Network Rail

Signed

Signed

Print name Philip Hassall

Print name Tim Wright

Position: **Track Access Manager**

Position: **Business Manager**

Date: _____

Date: _____

9 APPENDICES AND ANNEXES

- Annex A Schedule 7 of the Track Access Agreement between the Parties.
- Annex B The Office of Rail Regulation Criteria and Procedures for the approval of Passenger Track Access Contracts (Third Edition).
- Annex C The Office of Rail Regulation document "Network Code reform phase 2: Conclusions – the way forward, November 2005"
- Annex D The Office of the Rail Regulation document "Network Code reform phase 2: update and emerging conclusions: Network Rail's response"
- Annex E Vehicle Change Notification to Network Rail by TransPennine Express dated 7 September 2004
- Annex F Vehicle Change Notification issued by Network Rail on behalf of TransPennine Express dated 7 February 2005
- Annex G Formal Response from Network Rail to TransPennine Express on 17 November 2005