

# **Access Dispute Resolution Rules**

## **Reference to ADP in respect of Certain Managed Station Expenditure Claims**

**4 September 2009**

Skeleton Submission for Hearing on 14 September 2009

**Network Rail Infrastructure Limited** (1)

**and**

**First Group Train Operating Companies** (2)

## **1 SUMMARY**

- 1.1 This reference arises out of a disagreement between certain First Group Train Operating Companies ("FG TOCs") and Network Rail Infrastructure Limited ("Network Rail"), over the treatment of insurance premiums when calculating the appropriate split between Qualifying Expenditure ("QX") and Non Qualifying Expenditure ("non-QX") at Network Rail managed stations.
- 1.2 Network Rail places insurance at the Managed Stations. This insurance covers all activities and operations at the stations both QX and non-QX. Some of the insurance coverage must therefore relate to non-QX risks and a proportion of the total insurance premiums should therefore be attributed to non-QX.
- 1.3 Network Rail admits that a proportion (12%) of the insured risk at its managed stations for the year 2007/8 relates to non-QX issues because it relates to the shared areas of the station including those used by retailers.<sup>1</sup>
- 1.4 Network Rail has identified no material changes in insurance coverage of the insurance between 2006/7 and 2007/8. The insurance proportion relating to non-QX (which Network Rail identifies as 12%) is therefore equally applicable to 2006/7 as it is to 2007/8. Nonetheless Network Rail has not applied the split to the year 2006/7.
- 1.5 FG TOCs request a determination that Network Rail is acting contrary to the requirements of the Rail Independent Station Access Conditions ("RISAC") (Part 5, Conditions 26-31) and that it should recognise that a proportion of insurance costs in 2006/7 are applicable to non-QX and therefore that the insurance costs should be reduced to reflect this split.

## **2 FACTUAL BACKGROUND**

- 2.1 The dispute concerns incorrect allocation and calculation of costs charged by Network Rail to QX in respect of those stations at which Network Rail and the FG TOCs had Station Access Agreements throughout 2006/7 (the "Stations"). It has arisen following an inspection of books, records and accounts relating to the financial year 2006/7 undertaken on behalf of the FG TOCs in accordance with RISAC condition 38.

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<sup>1</sup> Paragraph 14.19.20 of the Network Rail's submission served on 30 June 2009

- 2.2 Aspects of the certificates underlying this dispute remain to be determined by an expert. Following substantial disclosure pursuant to the Disputes' Chairman's order of 20 May 2009, the FG TOCs currently anticipate that all outstanding issues relating to the certificates can be resolved by an expert and consequently other issues raised (prior to that disclosure) in this process are not addressed in this skeleton. However, in the event that an expert does in due course identify issues of principle which he is unable to determine the FG TOCs will seek to refer such issues back to the Panel.
- 2.3 The factual background to the Reference is set out in further detail in FG TOCs document dated 11 May 2009 and is not repeated here. To summarise the issues in respect of Network Rail's failure to deal correctly with the allocation of insurance premiums in 2006/7:
- 2.4 FG TOCs position is that:
- (a) Insurance costs are included in QX to the extent that they relate to QX liabilities. However, where Network Rail elects to place insurance beyond the scope of QX liabilities (and therefore in excess of the obligations to procure insurance required by RISAC part 5 (conditions 26-31)) in order to protect itself from claims (rather than to protect the relevant train operator), the proportion of the cost associated with such additional insurance is not a cost which the train operators gain any benefit from. Indeed Network Rail are obliged to place insurance cover for their own liabilities and such cover must be non-QX. These costs fall outside QX (see Rail Industry Dispute Resolution 6.5/16) and so should not be charged.
  - (b) Understandably Network Rail has acknowledged that its premiums for all third party liabilities for the period 2007/8 should be partially allocated to non-QX, but refuses to do so for the 2006/7. Network Rail has provided no substantive reason for this refusal.
- 2.5 Network Rail has stated its position is that:
- (a) The 12% attribution of insurance costs to non-QX in 2007/8 reflects those shared areas which retail customers and passengers both used; **However,**

- (b) the application of such a split in 2007/8 should not be evidence that previous arrangements in place since privatisation were in breach of condition 98 (of RISAC). To do so would discourage Network Rail from considering improvements in the provision of QX services, or the reduction in QX charges for fear of TOCs claiming that all improvements should be backdated within the relevant limitation period; **Therefore,**
- (c) Network Rail denies that the Claimants are entitled to any further reduction in insurance costs as alleged or at all and;
- (d) the Claimants are not entitled to make a claim under condition 53 and in any event were they able to do so they would have to demonstrate that there was a breach, which is denied, and that they have suffered loss through overcharging.

### **3 THE ISSUES**

3.1 The issues which arise are consequently limited:

#### **Splitting insurance costs between QX and non-QX**

3.2 Within the charges for insurance premiums an apportionment must be made between QX and non-QX such that the proportion of the insured risk relating to non-QX liabilities is excluded from QX.

3.3 This appears to be accepted by all parties and Network Rail have recognised its assessment of insurance premiums for the year 2007/8, and beyond, by deducting 12% of the premium from the QX costs calculation on the basis that this proportion relates to non-QX. <sup>2</sup>

#### **Year on Year improvements**

3.4 Network Rail appear to argue that efficiencies and improvements in service delivery should not be considered to be applicable to previous years. This may be true where such improvements are genuine efficiency gains. This issue of principle however does not relate to an efficiency gain or an improvement in service. It is concerned with the allocation of costs between QX and non-QX which will be substantially the same from year to year.

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<sup>2</sup> See footnote 1

- 3.5 Network Rail has provided no evidence that the insurance coverage has changed between 2006/7 and 2007/8 in any way which would affect how much is attributable to QX and how much to non-QX. The overall cost of insurance might have changed however this does not affect the shares attributable to QX and non-QX. It is not an efficiency gain simply to make the correct apportionment of costs. As such the correction should be applied to 2006/07.

### **Claim under RISAC 53**

- 3.6 This claim arises out of and is in connection with the RISAC and SAAs and is brought to the panel under RISAC 53.1. It is an issue of principle arising from Network Rail's refusal to apportion costs between QX and non-QX despite recognising that such an apportionment should be made and is being made in 2007/8.
- 3.7 Network Rail's arguments about breach and loss are not understood. Unless Network Rail correctly reduces the insurance sums charged to QX the TOCs will have to pay more than they are required to under RISAC and their station access agreements. This clearly causes them loss and would be a breach of (among other things) Network Rail's obligations under RISAC 33 and 34.
- 3.8 The refusal to split the insurance cost into QX and non-QX, and so accurately apportion costs, also has the effect of unreasonably increasing the cost to FG TOCs. This is contrary to Network Rail's obligation under RISAC 81 to minimise the cost of the operation of the station.
- 3.9 FG TOCs claim that Network Rail should apply a consistent approach to each yearly accounting period based on its own analysis for the year 2007/8. This should then be subject to justification by Network Rail as part of the inspection process and where insurance changes occur should be further adjusted to reflect the actual costs. If necessary such adjustment can be determined by an expert.

### **Exclusion of Claim**

- 3.10 Network Rail assert that FG TOC's claim is time-barred under RISAC 71.1 on the basis that details of claims in relation to all managed stations were not submitted in time.<sup>3</sup>

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<sup>3</sup> Paragraph 14.13.3 of Network Rail submission served on 30 June 2009

- 3.11 RISAC 71.1(A) requires notice of a claim to be given "... *within 6 months after the facts giving rise to such claim first became known by the claimant or could, with reasonable diligence, have become so known*". Access to the relevant information (which FG TOCs required in order to assess whether Network rail was in breach of RISAC) was either limited or refused by Network Rail. When information was made available to the FG TOCs this was only provided after a substantial delay and after proceedings had been commenced, therefore the timing of notice can not be an issue.
- 3.12 FG TOCs consider that the inspection is not concluded, particularly following the further, significant disclosure (following the Order made by the Panel on 20 May 2009) which has been made by Network Rail.
- 3.13 Network Rail's position in seeking to argue that the FG TOCs are out of time is unsustainable, given its substantial delay in providing all relevant documents.

#### **Network Rail's objections to apportioning the insurance costs**

- 3.14 None of the reasons raised by Network Rail not to apportion insurance costs between QX and non-QX in 2006/7 have any weight. Its failure to do so means the certificates for 2006/7 include a non-QX cost which should not be included (and is not included in 2007/8).

#### **4 DECISION SOUGHT FROM THE PANEL**

- 4.1 For the reasons above the Panel is asked to order that:
- (a) the entries in the certificates for 2006/07 attributed to QX for insurance in respect of all stations (at which FG TOCs have a SAA with NR) for the accounting year 2006/7 be reduced by 12% representing the split between coverage for QX and non-QX insurance liabilities and the relevant amounts be repaid to the relevant FG TOCs.
  - (b) the insurance sums charged to QX insurance be adjusted further as a result of any changes in scope of the insurance cover implemented by Network Rail by agreement in the Certificate; if agreement is not reached these adjustments are to be determined by expert determination.
  - (c) where any further issues of principle are raised by the Expert in Expert Determination proceedings in respect of the Certificates for accounting

year 2006/7 which that Expert is unable to determine such issues of principle be referred back to the Panel in this dispute.

First Rail Holdings Limited

4 September 2009