ACCESS DISPUTE RESOLUTION RULES
ADP 35, 36 AND 38 CONCERNING MANAGED STATION EXPENDITURE

NETWORK RAIL'S SKELETON ARGUMENT

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Network Rail submits:

1. Legal basis of the Claims

1.1. The Claimants' references are not particularly specific as to the legal basis of their claims in relation to insurance and staff costs, (and also in relation to station cleaning costs, maintenance, and refuse disposal concerning which they no longer consider there are any disputes of principle). Network Rail reserves the right to make further submissions should the Claimants' submissions put forward a basis of liability which is not dealt with herein.

1.2. The Claimants state merely that costs which were not QX have been charged to QX.

1.3. While First claims only in respect of the accounting year 2007-8, Govia claims in respect of "all relevant accounting" years which Network Rail takes to mean all years in respect of which a claim can be made.

1.4. The Claimants presumably allege:

(i) breach of contract in that Network Rail has failed to make an adjustment under ISAC condition 39.1;

(ii) breach of contract in that Network Rail has failed to permit any or any sufficient inspection of books records and accounts under conditon 38.1.

(iii) breach of contract in that Network Rail has failed to keep accounts under condition 40;

(iv) breach of contract in that Network Rail has failed correctly to apply condition 98 in apportioning QX and non QX expenditure;

(v) breach of contract in that Network Rail has failed correctly to minimise costs under condition 99;

(vi) they are entitled to restitution for the return of monies paid because of mistake.

1.5 The claims for breach of contract are subject to restrictions under Condition 71.1 which prohibits claims unless notice of claim has been given within 6 months of the facts giving rise to the claim first became known by the claimant or could with reasonable diligence have become known.

1.6 Further the right to an adjustment is subject to restrictions as to the period during which an adjustment may be sought prior to the completion of the inspection under condition 39.1.

1.7 Lastly any claim for restitution for the return of monies paid because of mistake is not a claim for breach of contract but would in Network Rail's submission be overtaken by the contractual right subject to the restrictions contained in condition 39.1.

1.8 In relation to the right to adjustment under condition 39.1 Network Rail maintains its assertion that the there is a right to adjustment only in respect of any Accounting Year or Half-Year commencing not earlier than 18 months prior to the date on which the inspection is completed. However, it accepts that there is thereafter no time restriction in which the discrepancy must be notified and repayment made that is to say for the adjustment to take place.

1.9 Network Rail submits that a refusal to make such a payment which is properly claimed would give rise to a claim for breach of contract, and that claim would itself be governed by the provisions of condition 78.1 and would have to be commenced under condition 53.1.

1.10 In its Statement herein Network Rail accepted that the parties could vary the 18 month period for the inspection by agreement. While no specific agreement was ever articulated between the parties, Network Rail accepts that its ongoing provision of accounting information to First and Southern means that in respect of the inspection for the year 2006-2007, the inspection was for the purposes of these proceedings extended by agreement so as to mean that the right to adjustment in relation to that year is not prevented by the restrictions contained in condition 39.1 or condition 73.1.

1.11 Network Rail however, maintains its arguments as to what can properly be claimed under the condition 39.1 process as set out in paragraph 14.9 of its Statement herein.

1.12 The effect of this concession is that to the extent that the matters now to be referred to expert determination are concerned, if they are restricted merely to accounting discrepancies, then Network Rail does not seek to challenge their referral.

1.13 However, Network Rail maintains its assertion that in respect of all other breaches of contract, (other than breach of contract for the failure to make an adjustment as set out above), the effect of condition 73.1 is to prevent any claim other than relating to an accounting discrepancy being made, for instance as to what is or is not properly categorised as QX, as set out in paragraph 14.13.1 to 3 of Network Rail's Statement herein.

2. RIDR R6.5/16

2.1 The Claimants have referred to a determination of the RIDR Chairman, namely RIDR R6.5/16 (Attachment 1). That reference decided that Network Rail could treat amounts in respect of third party claims as QX only if the claimant's injury or loss did not result from any failure on Network Rail's part to perform an obligation.

2.2 Network Rail argued that the effect of Condition 39.1 is to give WAGN six months from the end of an accounting year within which to complete an inspection under Condition 38 and to seek a reduction of the amount shown in the certificate for that year.

2.3 The RIDR Chairman held that the condition stated that only the inspection had to be completed within the six month period and establishing whether there has been an overcharge, and if so of how much, happens "upon or following" the inspection and is a separate stage for which there is no time limit.

2.4 Further he decided that there was no apparent reason why the nature of the contract should require that the time limit for inspection in Condition 39 be strictly complied with and it was therefore necessary to look to the surrounding circumstances and in particular, how each of the two parties would be affected by time being, or not being, of the essence.

2.5 He decided that question in accordance with the dicta of Lord Simon in United Scientific Holdings v Burnley BC (1978) AC 904 (Attachment 2)that,

> "Time will not be considered to be of the essence unless (1) the parties expressly stipulate that conditions as to time are to be strictly complied with; or (2) the nature and subject matter of the contract or the surrounding circumstances show that time should be considered to be of the essence..."

2.6 A consideration suggesting that time was of the essence was that Network Rail had a legitimate interest in limiting the time within which charges might be challenged so as to give certainty of income streams.

2.7 However, other considerations suggested that it was not namely:

(i) While condition 39 recognised the possibility of adjustment in Network Rail's favour, for all practical purposes the clause operated solely for the benefit of Network Rail by placing a constraint on the Station User and not on Network Rail.

(ii) The onus is on Network Rail to calculate the charges accurately in this first place and they have all the relevant facts.

(iii) The Station User might have to inspect a large amount of material in a limited time.

(iv) The Station User might in practice have little more than four months in which to make an inspection.

(v) The Station User's compliance depended on Network Rail's ability to respond to inquiries which could not be guaranteed.

2.8 Balancing these considerations the Chairman concluded that time was not of the essence for completion of the inspection under Condition 39.1 of the ISACs and that the TOC's ability to dispute an item included in a year end certificate was not conditional upon its having completed its inspection within the period specified in that Condition.

2.9 Further he held that the TOC's remedy in restitution for a payment made under a mistake would, if the requisite requirements for the same were met, allow a claim to be made in respect of years within the relevant period of limitation.

3. Criticism of RIDR R16.5/16

3.1 Network Rail submits that this Ruling is founded on a misapprehension as to the nature of Condition 39.1.

3.2 Clause 38.1 gives the User an entitlement to inspect at any reasonable time upon reasonable notice to the Station Facility Owner. There is no time restriction on the right to inspect.

3.3 Clause 39.1 states that there is to be an adjustment to the amount of Residual Variable Charge,

"...in respect of any Accounting Year or Accounting Half-Year commencing not earlier than 18 months prior to the date on which the inspection is completed.."

3.4 The right to receive an adjustment is prima facie restricted to the situation where an inspection has taken place and only in respect of an Accounting Year or Half Year commencing not earlier than 18 months prior to the inspection being completed.

3.5 As stated in paragraph 14.9 of Network Rail's Statement herein Network Rail submits that the purpose of the inspection is to permit a TOC to satisfy itself that the level of the Residual Variable Charge ("RVC") accords with the Best Estimate given and to identify where discrepancies exist but no more.

3.6 This is supported by the reference to the finding of discrepancies and the making of repayment within 5 days of the notification of the same in condition 39.1. Plainly this must be a reference to a self evident accounting error, or blatant misallocation, rather than a questioning of the adequacy of accounting evidence in accordance with the conditions, or the meaning and applications of the definitions for instance of repair and maintenance.

3.7 It is further supported by the system in which the right to inspect and seek adjustment exists. The provision of the Best Estimate, the quarterly meetings checking progress against the estimate under condition 81.1(3)(P), and the production of the Half Yearly and Yearly Certificates of Residual Variable Charge all suggest that the discrepancies are to be identified within the parameters of the details set out by the Best Estimate. The Best Estimate is itself required by condition 32.3 to include a detailed breakdown of the Total Variable Charge in sufficient detail to enable the Passenger Operator to make an assessment of the charges proposed, the method of the calculation and the costs of the amenities and services in question. No allegation has been made that the Best Estimates are inadequate or unsatisfactory.

3.8 If an inspection were to reveal that there is no accounting evidence relating to a particular item allocated to QX, or that in the opinion of the inspecting Operator the definitions have been wrongly applied, then that is not the identification of a discrepancy giving rise to an adjustment. There can indeed be no adjustment as such because the parties will differ as to whether accounting evidence is needed and as to how the definitions apply. In such circumstances the Operator's remedy is, if it considers there is a breach of the conditions by Network Rail, to make a claim under condition 53.

3.9 The condition thereby acts as a restriction or exclusion of the right under it to an adjustment based on the inspection of a limited class of accounting records.

3.10 Further it should be borne in mind in assessing whether the commercial context of the ISAC means that it is likely that the parties intended time to be of the essence that the ISAC is a regulated agreement which the parties are obliged to enter into by the ORR. Neither party negotiated the ISAC's terms which were in effect imposed upon them.

3.11 The Determination effectively deprives the clause of any meaning in that there is no time in respect of which an inspection must be commenced or completed and there is nothing to stop an inspection being made at any time in respect of any year subject only to limitation. Further the restriction has no meaning in the sense that it is difficult to see that there would ever be a circumstance in which its breach would cause damage so as to give entitlement to redress for the same to Network Rail. It is therefore highly unlikely that it was the parties' (or the ORR's) intention that

condition 38 and 39 should be of no effect or operate otherwise than with time being of the essence.

3.12 Further, while the Station User may lose any right to an adjustment, its substantive rights arising from any breach of contract remain in being. Thus if its inspection discloses that expenditure has been wrongly assigned to QX then that would be a breach of one or more of the terms of the ISAC set out above, and subject to compliance with the notice requirements of condition 71, the Station User would be able to commence proceedings to recover the same.

3.13 In addition the right to adjustment is categorised by the RIDR Chairman as being a right to restitution. Restitution is a right which is independent of contract. Thus,

"The starting point is a fundamental one in relation to restitutionary claims, especially claims for work done or goods supplied. No action can be brought for restitution while an inconsistent contractual promise subsists between the parties in relation to the subject matter of the claim...This ensures that the law does not countenance two conflicting legal sets of legal obligations subsisting concurrently." (Mason P quoted by Seymour J in Mowlem Plc v Stena Line Ports Limited (2004) EWHC 2206 (TCC)(Attachment 3))

and,

"..the law of restitution is subordinate to the to the law of contract in that, if a contractual relationship subsists between the parties, the contractual regime will prevail." (Chitty 29-002 (Attachment 4))

3.14 Condition 39.1 gives no right to restitution, but it does provide a form of contractual restitutionary remedy subject to a limitation. The rights of the Claimants are in Network Rail's submission thus governed by the contract and not any wider consideration of mistake giving rise to a restitutionary remedy. Further the restriction in condition 71.3 as to remedies which is set out below at paragraph 4.4 would prevent reliance on any contractually extraneous remedy such as restitution in any event.

3.15 The nature of the inspection and its commercial context would tend to suggest that the restriction in condition 39 was intended to have effect and the force of the considerations taken into account by the RIDR Chairman in support of his decision is much diminished when the condition is seen in this context.

3.16 Further the result of Network Rail's interpretation represents business common sense. There is an adjustment process which must in relation to completion of inspections take place within time limits on limited material, and which excludes any wider restitutionary rights, but which leaves in being the right to claim for any breach of contract itself whether identified

by the inspection or otherwise and subject to the required notification. In Network Rail's submission R16.5/16 was therefore wrongly decided.

4. Validity of Condition 39.1 as a Limitation Clause

4.1 In Network Rail's submission condition 39.1 should be treated as clause limiting liability. As such it must comply with the requirements set out by the House of Lords in Ailsa Craig Fishing v Malvern Fishing (1983) 1 WLR(HL(Sc)(Attachment 5))

4.2 There it was said,

"Whether a clause limiting liability is effective or not is a question of construction of that clause in the context of the contract as a whole. If it is to exclude liability for negligence, it must be most clearly and unambiguously expressed, and in such a contract as this, must be construed contra proferentem...But one must not strive to create ambiguities by strained construction...The relevant words must be given, if possible, their natural, plain meaning. Clauses of limitation are not regarded by the courts with the same hostility as clauses of exclusion: this is because they must be related to other contractual terms, in particular to the risks to which the defending party may be exposed, the remuneration which he receives and possibly also the opportunity to insure." (Per Lord Wilberforce at p.966)

"In my opinion these principles are not applicable in their full rigour when considering the effect of clauses merely limiting liability. Such clauses will of course be read contra proferentem and must be clearly expressed, but there is no reason why they should be judged by the specially exacting standards which are applied to exclusion and indemnity clauses...It is enough that the clause must be clear and unambiguous." (per Lord Frazer at p.970)

4.3 The wording of condition 39.1 is clear, is wide enough to encompass negligence, and is therefore in Network Rail's submission of effect in restricting the right to adjustment without more.

4.4 Further condition 71.3 of the ISAC states,

"Save as otherwise provided in any Station Access Agreement (including these Station Access Conditions), the remedies provided for in these Station Access Conditions and Access Dispute Resolution Rules, to the extent applicable, shall be the sole remedies available to the parties in respect of any matters for which such remedies are available."

4.5 While this too must be judged in the same way as condition 39.1, its wording is clear, it is wide enough to encompass negligence and is unambiguous.

4.6 Again however, the contract places on Network Rail an obligation by condition 81.1(2)(e) to exercise reasonable skill and care, and on both parties by conditions 81.1(D)(2) and 82.1(A)(2) to comply with their Safety Obligations which are defined to include their common law duties of care. Liability for negligence is therefore preserved but the remedy is restricted to the remedies for breach of contract under the ISAC.

4.7 Network Rail accordingly submits that the limitations contained in conditions 39.1, and 71.3 are valid and can be relied upon.

5. Breaches of Contract - Condition 71.1(A)

5.1 Condition 71.1(A) states,

"Save as otherwise expressly provided in any Station Access Agreement (including these Station Access Conditions), no party to a Station Access Agreement shall be liable in respect of any breach of as Station Access Agreement:

(A) unless notice of it is given by or on behalf of the claimant to the respondent setting out detailed particulars of the grounds on which the relevant claim is based within 6 months after the facts giving rise to such claims first became known by the claimant or could, with reasonable diligence, have become so known."

5.2 Again judged in accordance with the criteria set out above Network Rail submits that this limitation of the right to make a claim is valid and binding on the parties. As to the effect of the limitation Network Rail refers to paragraph above and 14.13 of its Statement herein.

6. Breaches of Contract and Individual Claims

6.1 Network Rail repeats the submissions made in its Statement herein at paragraphs 14.14 to 14.22.

6.2 In relation to insurance the 12% reduction concession in relation to 2007-2008 the same was given in relation to the retail areas on stations. The Claimants complain that concession has not been applied in relation to third party claims in respect of 2006-2007 and in Govia's case earlier relevant accounting years.

6.3 In fact Network Rail does not insure the third party liability of its retail tenants and therefore the same has never been part of the premium charged to the Claimants. Of itself therefore this cannot be the basis of any right or the concession to be applied to earlier years.

6.4 If the argument is there should be such a reduction in respect of previous years because under the new insurance arrangements for 2007-2008 the

insurance premium included accidents for which Network Rail was responsible and which should not therefore have formed part of the QX under RIDR R6.5/16, then as in previous years Network Rail had actually borne such costs itself within the deductible, and they had not formed part of the premium charged to the Claimants, there can be no basis for backdating the 12% or any percentage in respect of claims which were within the deductible.

6.5 In respect of claims above the deductible there is no evidence that if the premium charged the Claimants included premium for claims for which Network Rail was solely responsible above the threshold, and which should not have formed part of QX, there would have been any reduction in the premium if the same had been excluded, and certainly no reduction any where in the region of 12% as asserted by the Claimants.

6.6 Further, it would not be possible ex post facto to assess the amount of premium reduction with any degree of certainty because the policy is not a claims made policy, and therefore in relation any accounting year all claims made within the limitation period of three years are covered by the policy relating to a single year leaving aside claims which can be brought many years after the policy year by injured minors and the like. The reduction in respect of any one year would therefore be difficult to assess.

6.7 In so far as the unspecified additional items of insurance taken out, Network Rail reserves the right to supplement this skeleton if and when details of the same are provided by the Claimants.

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