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Principal Economist

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Dear Freight and Charter Schedule 8 Recalibration Working Group,

Final decision: The level of freight operator exposure above the incident caps

1. Network Rail and freight operators disagreed about how the Schedule 8 incident cap regime should operate. In light of this disagreement, you asked us to determine the matter.
2. On 19th April, Network Rail sent us its proposal that freight operators should be exposed to 30% of the Schedule 8 costs of the disruption that freight operators have caused above their Incident Cap. On 11th May, freight operators sent us their proposal that the regime should not be changed, i.e. that they should not be exposed to any of the Schedule 8 costs associated with minutes of delay above the relevant incident caps.
3. On 10th July 2018 we wrote to the Recalibration Working Group setting out our decision and the rationale for it. We decided that the existing 'no exposure' provisions should remain in CP6, but that Network Rail could offer, in addition, an incident cap regime which offers some exposure in exchange for a lower ACS, if it wished to do so. This letter reiterates that decision and the rationale for it.

Network Rail's proposal

4. Network Rail argues that the current regime removes the financial incentive on operators to mitigate the effects of delay they cause once an incident breaches the cap. Network Rail suggested that exposing freight operators to some of the Schedule 8 cost of the disruption they cause above their Incident Cap would encourage freight operators to reduce the minutes of delay they cause above the caps.
5. Network Rail proposed that freight operators should be exposed to 30% of the Schedule 8 costs resulting from disruption caused above their Incident Cap.

Our response

6. This is not a dispute about how a contractual parameter ought to be recalibrated – it is a dispute about how the regime ought to function. That being so, we consider this to be a policy issue, rather than a recalibration issue, the latter being the proper focus of the Recalibration Working Group.

7. Given the late stage that the periodic review was at when we received these submissions, the threshold for approving proposals to change Schedule 8 (or any) policy was very high. For us to have approved a change to existing policy that does not enjoy full industry support, the benefits of that change would need to have been extremely clearly demonstrated. Network Rail's proposal did not meet this condition, so we could not support it.
8. Network Rail is correct that when a freight operator causes a delay that exceeds its incident cap Schedule 8 no longer provides the operator with a financial incentive to mitigate the delay. However, exposing freight operators to the cost of minutes above the incident cap will only lead to better outcomes if freight operators are able specifically to reduce the number of minutes of delay they cause above the incident cap in response. Freight operators strongly deny that they have such an ability, and Network Rail's submission provides no evidence to support the claim that the incentive that its proposal would provide to freight operators is something that they are able to respond to effectively.
9. Additionally, the level of exposure that Network Rail proposes (i.e. 30%) is arbitrary. No argument is put forward as to why this level is more or less appropriate than some other level.
10. Given the late stage of the review, the fact that this proposal relates to a matter of policy and not recalibration, and the fact that Network Rail has not clearly evidenced the benefits of this proposal, we decided that Network Rail's proposal should not be adopted; in particular, freight operators should still be able to select an incident cap which protects them from the Schedule 8 cost of all minutes above the cap. However, if Network Rail wishes to offer, in addition to the standard regime, an incident cap regime which offers some exposure in exchange for a lower ACS, it may do so.

Yours faithfully,

A handwritten signature in blue ink, appearing to be 'Deren Olgun', written in a cursive style.

Deren Olgun