



‘What is an RU compensation scheme for disruptions and how can it contribute to cost reductions?’

Schedule 4: GB’s RU compensation regime

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How to reduce access charges for rail and improve the competitive offer

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GB RU regime - Schedule 4: introduction

What are Restrictions of Use (RU) and why do we need to have the RU regime?

■ Restrictions of Use (RU):

- Restricted use of the network, typically because of engineering work that has to be carried out
- The amount of planned maintenance and renewals work inevitably means that there will be disruption to passengers and freight users

■ The objective of having a RU compensation regime is to:

- Compensate train operators for the financial impact of planned RU where operators are given restricted access to the network
- Act as an incentive on Network Rail to minimise the level of service disruption as a result of RU

■ Without regulation:

- Network Rail would not have good incentives to reduce the impact of disruption to passenger or freight customers from engineering works because Network Rail is a natural monopoly
- The regulatory response is to have the RU regime that incentivises Network Rail to ensure that RU are delivered in a way which minimises the impact of disruption to the optimal level

Why does it matter: the economic impacts of RU

- RU of passenger services has four main economic impacts:
- Short-term:
 - Passenger inconvenience: passengers usually prefer travelling by train instead of buses, therefore some passengers may choose to find an alternative or not travel at all
 - Operator cost increase: staffing, fuel, bus replacement costs and other costs to replace and/or re-route services
- Long-term:
 - Passenger welfare impact: due to RU some passengers may choose not to travel by train, especially if they experience contiguous series of RU
 - Operator loss of future revenue
- RU also have analogous impacts on freight services (e.g. additional crewing costs, impact on revenue through the loss of customers)

Schedule 4 - UK RU Compensation Scheme: intended effects

- GB RU compensation scheme – Schedule 4 of track access contracts (Framework Agreements)
 - Help to align incentives between Network Rail and train operators, so the impact of service disruption on revenue and/or costs incurred by the organisation who cause the disruption, rather than the train operator that faces the disruption
 - Provide appropriate signals so as to drive decision-making in relation to RU management, e.g. to give an indication to Network Rail on whether it is better to have a short RU but with higher engineering costs or take a longer RU
 - In its role as a compensation mechanism, Schedule 4 ensures that train operators are less exposed to risk that they cannot control than they would otherwise be

Schedule 4 regime: how does it work & how is it funded?

- Schedule 4 is a 'liquidated sums' regime, where compensation payments are largely determined by formula, set in advance
- This reduces transaction costs in the industry, because the alternative would be to negotiate the financial impact of each RU after the event
- Schedule 4 payments are funded through an **access charge supplement (ACS)** paid to Network Rail (by franchised passenger train operators in return for receipt of full Schedule 4 compensation) as well as through the fixed track access charge (FTAC) or network grant in lieu of FTAC (to compensate freight operators)
- ACS reflects that Network Rail is expected to require a certain number of RU and the amount Network Rail is expected to pay out in Schedule 4 RU compensation over the control period
- Network Rail is incentivised to efficiently plan RU in order to benefit from lower Schedule 4 payments and in that way to retain some of ACS or some of the allocated funding



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Schedule 4 regime: how does it work?

Schedule 4 passenger regime: how does it work?

- Franchised TOCs schedule 4 payments are to compensate for a combination of the following:

Loss of future revenue	Replacement bus cost	Costs or cost savings from a change in train mileage	Costs related to cancelled or late amended RU
<ul style="list-style-type: none"> • For revenue losses as a result of passengers being deterred from travelling due to RU disruption. • Compensation is based on Schedule 8 payment rates and a discount rate determined by notification discount factors 	<ul style="list-style-type: none"> • For additional costs incurred when running replacement buses the amount of compensation received is the product of estimated bus miles (EBMs) and the EBM payment rate • Different rates for London and South East and the rest of the country 	<ul style="list-style-type: none"> • TOCs may make cost savings or incur additional costs as a result of changes in train mileage operated due to RU. 	<ul style="list-style-type: none"> • Cost compensation where costs exceed £5,000

- In return for this compensation TOCs pay a pre-determined access charge supplement (ACS) to cover the costs to Network Rail of the Schedule 4 regime. This also reflects the fact that Network Rail is expected to require a certain number of RU
- Currently, no open access train operators opt to pay an ACS charge

Restriction of Use types

- There are three types of RU:

Type 1	Generally less than 60 hours in duration
Type 2	Greater than 60 hours, but equal to or less than 120 hours (excluding public holidays)
Type 3	Greater than 120 hours (including public holidays)

- Type 1 receive **only** formulaic Schedule 4 revenue loss and cost compensation (the majority of RU are of this type)
- Both Type 2 and Type 3 receive formulaic compensation **but** can also claim for actual revenue losses and costs above a materiality threshold

Passenger revenue loss compensation – notification factors

- Network Rail is entitled to a reduction in the amount of compensation it pays, depending on how early it notifies passenger operators about RU
- The discount reflects the reduced impact on passenger operators revenues where passengers receive early notice of service disruption (i.e. determined by notification discount factors which vary according to the amount of notification given to passenger operators, and the type of service being disrupted through marginal revenue effect (MRE))
- Passenger Schedule 4 CP5 notification factors for service groups, by late time multiplier

Average late time multiplier	By New Working Timetable	By 22 weeks before possession	By Applicable Timetable
4.3 or higher	40% of MRE Payable	63% of MRE Payable	85% of MRE Payable
3.4 to 4.2	45% of MRE Payable	65% of MRE Payable	85% of MRE Payable
2.8 to 3.3	50% of MRE Payable	68% of MRE Payable	85% of MRE Payable
2.7 or less	55% of MRE Payable	70% of MRE Payable	85% of MRE Payable

Sustained planned disruption (SPD)

- The SPD mechanism is designed to protect train operators from instances where there is severe disruption caused by RU over a sustained period of time or very long-lasting RU (Type 2 and Type 3 RU)
- Additional compensation for SPD is triggered when the impact of severe disruption crosses a pre-determined level at which point train operator may claim additional revenue/cost compensation above that covered by the liquidated sums payable under Schedule 4
- **Revenue thresholds** where the revenue loss compensation is either:
 - Equal to or greater than 20% of defined service group revenue over 3 consecutive periods; or
 - Equal to or greater than 15% of defined service group revenue over 7 consecutive periods
- **Cost thresholds** (2011/12 prices) where the difference between any costs as a consequence of SPD and the 'cost compensation for Network Rail Restrictions of Use' is more than:
 - £609,500 over 3 consecutive periods; or
 - £1,219,00 over 7 consecutive periods
- When SPD triggered claim, Network Rail and TOCs enter into negotiations on revenue/costs claim

Schedule 4 freight regime: how does it work?

- The Schedule 4 freight regime provides **only** cost compensation
- There are three levels of compensation depending on the notification and degree of disruption (with the possibility of compensation for actual losses for severe disruption) and higher payments made for late notice RU
- CP5 criteria for RU types and compensation rates (2012-13 prices) for each tier before and after T-12 *

RU notified before T-12	RU notified after T-12
Category 1 compensation -£300 per service	Service variation - £596 per service
Category 2 compensation - £800 per service	Late notice (service is cancelled) - £1,566 per service
Category 3 – possibility of actual costs/losses in addition to liquidated damages	Category 3 – possibility of actual costs/losses in addition to liquidated damages

* Refers to twelve weeks before the date the service is planned to depart from its origin



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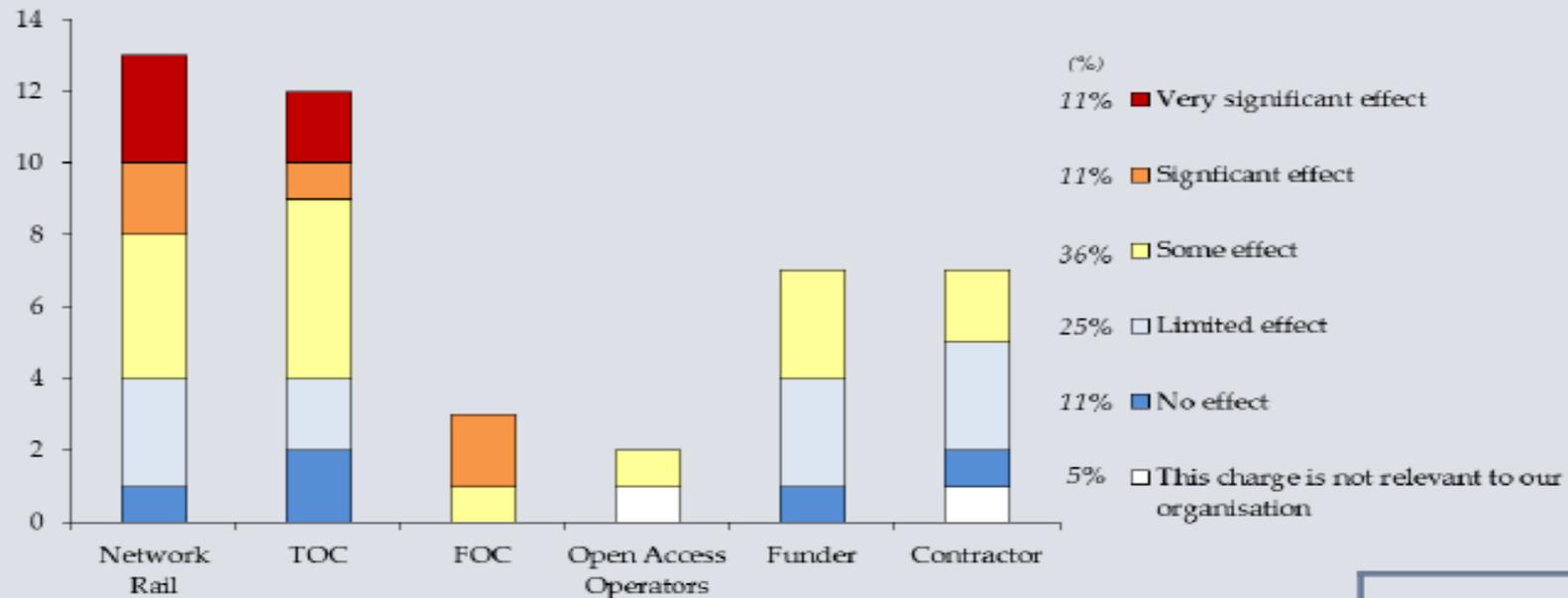


Schedule 4: ORR Review

ORR review of charges and incentives – Schedule 4

How far Schedule 4 impacted behaviours in Control Period 4 (2009-13)

Summary of responses



Number of respondents

Network Rail: 13 FOC: 3 Funder: 7
TOC: 12 Open Access: 2 Contractor: 7

Positive responses (%) : 62%

Schedule 4 had significant impact on Network Rail, TOC and FOC behaviours but discussions with these industry parties revealed that schedule 4 was rarely the key driver of behaviours but rather one factor of many considered. The importance of Schedule 4 therefore depended on its relative materiality.

Schedule 4 regime - Summary

- RU/ Schedule 4 regime is strongly supported by GB rail industry
- RU compensation scheme can reduce the costs and impacts of service disruption on operators due to RU:
 - Reduces disruption by incentivising Network Rail to plan RUs efficiently and minimises disruption to operators
 - Informs Network Rail's decisions in trading-off the cost of restricting access to operators against minimising engineering costs in respect of length and number of RU
 - Aligns incentives between Network Rail and operators
 - Reduces disputes and transaction costs
- But is one part of the decision making process in planning and managing RU
 - Materiality of RU compensation in respect of overall engineering budget
 - RU compensation impact higher where budgets held locally - route management
 - Collaboration between infrastructure managers and operators also important and the impact of collaboration greater where RU management is at route level