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Dear Rob

Schedule 8 Network Rail benchmarks in CP5 – Network Rail conclusions

On 20 August 2013, Network Rail consulted on the assumptions and detailed methodology employed to develop Network Rail Schedule 8 benchmarks for CP5. We also presented a set of Network Rail benchmarks for each TOC which were consistent with the regulatory performance trajectory in ORR's PR13 Draft Determination. This consultation followed:

- a 'principles level' consultation on Schedule 8 benchmarks in May 2013;
- ORR's email confirming the principles which Network Rail should follow when calculating the Schedule 8 benchmarks for CP5, sent on 14 August 2013;
- discussions between Network Rail routes and TOCs around the appropriate CP5 PPM / CaSL trajectories for each TOC that could underpin Schedule 8 benchmarks; and
- discussions between TOCs, Network Rail's Regulatory Economics team and Network Rail routes around the appropriate approach for 'translating' PPM / CaSL trajectories into Schedule 8 benchmarks.

This letter provides our conclusions in relation to Network Rail Schedule 8 benchmarks for CP5. ORR recently shared its expected Final Determination regulatory performance trajectory in order for the Schedule 8 benchmarks work to be completed (see below for more detail). In developing the benchmarks, we have taken account of ORR's expected final regulatory performance trajectory for CP5, the representations made by TOCs and other parties as part of this process, and the final set of Schedule 8 benchmarks principles that ORR shared with the industry in August 2013, which built on Network Rail's earlier proposed principles.

This letter also sets out our views on a number of high-level issues that relate to some or all TOCs. This letter will be published on our website. We have also prepared conclusions specific to each TOC, which address particular issues raised. We are sharing these TOC-specific conclusions – along with the relevant benchmarks – with you and the relevant TOC separately (see below). We understand that this TOC-specific information is considered confidential and should not be published on our website.

We would like to take this opportunity to thank TOC colleagues for their engagement in this process. We have taken on board a large number of suggestions and believe that this has helped improve the analytical work in particular, and ultimately resulted in a more robust set of benchmarks for CP5. Where we have not changed our view, we have explained our reasons why in the appendices to this letter (see below). We would also like to thank ORR for its support in this process, which we consider has struck the right balance between providing high-level scrutiny whilst allowing the industry to work together with the aim of establishing suitable Schedule 8 benchmarks for the next control period.

The regulatory performance trajectory in CP5

In Network Rail's August 2013 consultation, we set out benchmarks under two scenarios:

- The first was based on 'bottom-up' PPM / CaSL trajectories developed by Network Rail routes in discussion with TOCs. The resulting trajectories came short of 'adding up' to the national PPM trajectory set out in ORR's Draft Determination in the early years of CP5, reflecting industry-wide nervousness around achieving such a level of performance so soon.
- The second set of benchmarks was consistent with the national performance trajectory set out in ORR's Draft Determination.

Our consultation emphasised that we did not believe that the performance trajectory set out in ORR's Draft Determination was the most realistic assessment of likely CP5 performance, particularly in the opening years of the control period. We reiterated this point in our response to ORR's Draft Determination, and proposed an alternative CP5 performance trajectory.

As noted above, ORR has confirmed the performance trajectory for CP5 which it expects to provide in its Final Determination. Compared to the Draft Determination trajectory, the trajectory that ORR expects to set out in its Final Determination trajectory has a lower CP5-entry level of PPM but a 'steeper' profile within the control period¹. The various trajectories are set out in Table 1, below.

¹ The final determination performance requirements were shared by ORR with Network Rail in an email dated 3 October 2013. This was shared with operators by ORR by email on 9 October.

Table 1 – England & Wales PPM trajectories for CP5 (per cent)

	2014-15	2015-16	2016-17	2017-18	2018-19
Network Rail 'bottom-up' trajectory	92.0	92.1	92.3	92.4	92.5
Draft Determination trajectory	92.2	92.3	92.4	92.4	92.5
Network Rail Draft Determination response trajectory	91.7	92.0	92.2	92.4	92.5
ORR expected Final Determination trajectory	91.9	92.1	92.3	92.4	92.5

ORR expects that for the majority of TOCs, the minimum PPM for the final year of CP5 will remain the same as the Draft Determination, at 90 per cent. For East Coast and Virgin, ORR expects the minimum PPM for the final year of CP5 will be 88 per cent with a 2018-19 CaSL target of 4.2 per cent for East Coast and 2.9 per cent for Virgin. ORR has stated that this is a level of CaSL equivalent to 90 per cent PPM.

As part of these conclusions, we have set benchmarks on the basis of the trajectories and other requirements that ORR expects to set in its Final Determination, including in respect of CaSL for East Coast and Virgin. However, we remain concerned that CaSL trajectories for East Coast and Virgin are not realistic and discussions around this important issue are continuing. Should the Final Determination set a different set of requirements, it will be necessary to modify the final Schedule 8 benchmarks.

TOC-specific performance trajectories in CP5

Over recent weeks, Network Rail's Performance Team and routes have worked to establish TOC-specific PPM / CaSL trajectories that are consistent with ORR's expected Final Determination overall. Where changes have been made from earlier arrangements, routes have discussed these with TOCs. In constructing these trajectories, we have sought to ensure that the regional makeup of the national performance trajectory is realistic, fair and cost-effective to our funders. We believe that the final trajectories set out as part of these conclusions achieve this.

In their response to our consultation, some TOCs expressed concern that the PPM and/or CaSL trajectories upon which we consulted in August 2013 were not sufficiently ambitious, and requested that Network Rail Schedule 8 benchmarks be set on the basis of a higher level of performance than that proposed.

The benchmarks accompanying this conclusions letter are based on the expected **overall requirements of the Final Determination**. This means that benchmarks are consistent with the national expected Final Determination PPM and CaSL trajectories. We have constructed the expected Final Determination consistent trajectories by taking the 'bottom-up' trajectories (the 'sum' of which is contained in Table 1, above), and making adjustments by exception².

² It should be noted that the CaSL trajectories developed as part of this 'bottom-up' process did not 'add up' to the 2014-15 level that ORR expects to set out in its Final Determination. Therefore, a number of adjustments have been made to 2014-15 CaSL to ensure that the figures submitted as part

In general, we understand that some operators desire a level of performance beyond the level that has been proposed by Network Rail routes. In light of TOCs' responses, routes and our central Performance Team have revisited the modelling and assumptions underpinning the performance trajectories and made adjustments, where appropriate.

In some instances, it has not been possible to make the changes to PPM / CaSL trajectories requested by TOCs. This is because the planning and analysis undertaken by routes has indicated that the desired level of performance is less likely to be deliverable given the financial, operational and planning constraints that will be faced by the relevant routes in CP5. The reasons why the desired performance of certain TOCs are particularly challenging vary locally, and are provided in the appendices to this letter. Since the PPM / CaSL trajectories underpinning these conclusions 'add up' to the ORR's expected Final Determination trajectory, as required by the ORR benchmarking principles, any increase in performance for one set of passengers (or in relation to a particular TOC) will reduce performance for others. As emphasised above, we believe that the PPM / CaSL trajectories underlying our conclusions provide the most fair and efficient 'allocation' of performance, and have the best chance of being achieved, in practice.

It is true that Network Rail is funded to deliver the outputs defined in the Final Determination and the company will face significant tradeoffs at the national level in CP5, not least in relation to performance. Against a backdrop of traffic and enhancement levels which are unprecedented in the modern era, achieving the national level performance trajectory in the Final Determination and the HLOSs in CP5 will be very challenging.

However, we believe that Schedule 8 benchmarks and their underlying PPM / CaSL trajectories do not – and are not intended to – place limits on the industry's aspirations for further improvements. We are committed to working with operators and funders to find ways of delivering even better performance, beyond that implied by Schedule 8 benchmarks and the performance trajectories, where possible.

Engagement around TOC-level PPM trajectories

Over the summer of 2013, Network Rail routes developed 'bottom-up' PPM and CaSL trajectories at the TOC-level in order to underpin Schedule 8 benchmarks. Routes engaged with TOCs as part of this process. The level of engagement has varied nationally, with some routes and TOCs achieving a great deal of agreement around performance assumptions, whereas others have not.

Following Network Rail devolution, it is appropriate that Network Rail routes and TOCs conduct their relationships in a way which best suits local circumstances, developing PPM performance trajectories for Schedule 8 benchmarks being just one example. This flexibility is already delivering improved outcomes in a number of areas, and we believe that increased engagement at the local level, for purposes of

of the current exercise are consistent with the CaSL trajectory that ORR expects to set in its Final Determination.

developing TOC-level PPM trajectories for Schedule 8 benchmarking, has improved the robustness of the benchmarking work overall.

At the same time, we recognise that devolution can bring with it differences in approaches. Some customers may prefer a more unified and consistent approach. Following completion of the benchmarking work, we plan to examine how the engagement process for developing TOC-level PPM trajectories went, and what lessons can be learned for similar exercises in future. We would, of course, welcome stakeholders' views in this regard and operators are invited to contact us using the details above if they would like to suggest how improvements could be made. This input could be particularly useful to feed into the long-term review of charges led by the Rail Delivery Group (RDG) that is scheduled to commence in early 2014.

Converting PPM and CaSL trajectories into Schedule 8 benchmarks

A core activity has been to convert TOC-level PPM/CaSL trajectories into Schedule 8 benchmarks (defined in terms of 'average' and 'deemed' minutes lateness). We have engaged with TOCs about our approach to this over recent months. Operators have helped shape the approach to a substantial extent. The models have been reviewed by consultants Steer Davies Gleave – with oversight from Network Rail and ORR – in order to ensure that they are fit for purpose and computationally correct.

Feedback from stakeholders received in response to our consultation was favourable with regard to our modelling approach to this task. We are encouraged by the positive industry engagement regarding this. We believe that this builds on recent work by the RDG and helps illustrate the good results that can be achieved through closer industry working.

Appendices

Alongside this letter, we are sharing a series of supporting appendices which relate to each TOC individually. These are:

- Appendix 1, TOC-specific assumptions – this sets out important assumptions such as baseline performance minutes provided by Halcrow (including adjustments for berthing offsets made by Halcrow where applicable) and CP5 TOC-specific PPM/CaSL trajectories;
- Appendix 2, Network Rail's final proposal for Network Rail Schedule 8 benchmarks – this sets out the final benchmarks being proposed by Network Rail for each TOC for CP5; and
- Appendix 3, TOC-specific conclusions – this sets out our conclusions in relation to each TOC, including our response to specific issues raised by operators.

These appendices are being shared with each TOC individually. In addition, we are sharing the final models for each TOC with you and the relevant operator.



Conclusion

The benchmarks and TOC-specific conclusions being submitted to ORR alongside this letter have been set taking account of TOCs' responses to our consultation, and are consistent with ORR's expected Final Determination on performance outputs for CP5. However, we remain concerned that CaSL trajectories for East Coast and Virgin are not realistic and discussions around this important issue are continuing. Should the Final Determination set a different set of requirements, it will be necessary to modify the final Schedule 8 benchmarks.

We will continue to support ORR around Schedule 8 benchmarks over the coming weeks. Network Rail routes will also continue to work on the CP5 Delivery Plan and the associated annual performance plans.

We understand that you will make the final decision on the CP5 Schedule 8 benchmarks and will circulate these, along with the CP5 payment rates, to Network Rail and train operators by 8 November 2013.

We hope that you find our conclusions helpful. Please do not hesitate to contact me to discuss any aspect of this letter.

Yours sincerely

Joel Strange
Senior Regulatory Economist