
ACCESS DISPUTE RESOLUTION COMMITTEE

Determination No. AD13

(Hearing at Kings Cross 20th and 21st October 1997;
determination delivered on 27th October 1997)

1. The Committee was asked by Connex South Central Ltd.(CSC) to rule that the Schedule 8 Performance Regime, as contained within its Fourth Supplemental Agreement with Railtrack, as modified by a further agreement dated 21st March 1996, should be declared void, and that therefore the Benchmarks should be re-negotiated. This submission was made on the grounds that the apparent improvement in Railtrack performance subsequent to the signing of those agreements, and the consequential payments due from CSC to Railtrack, indicated that the Benchmarks were wrongly set, either as a result of a mutual **Mistake** or a **Misrepresentation** by Railtrack to CSC and to the Regulator.
2. The Committee noted the bulk of the two submissions, and in particular that
 - 2.1. despite encouragement and a time extension, the parties had been unable to produce any sort of common statement of their points of agreement, or disagreement, and
 - 2.2. a number of documents submitted in support of CSC's position related to the franchising process, and as such may be informative commentaries, but do not have any direct bearing on the content of the Track Access Agreement between the parties.
3. The Committee noted that it had confirmed (at its meeting on 17th July) that its locus to hear the proceedings was as defined in clause 11.3 of the Track Access Agreement, but that a separate and complementary issue was due to be heard by an imminent meeting of the Network and Vehicle Change Committee.
4. The parties were agreed that a significant improvement in performance, as compared with the documented Benchmarks, had taken place. The parties were not in dispute as to the recording methods that had revealed this.
5. CSC contended that the Benchmarks were intended to be set at a level that reflected the steady state of the network.
 - 5.1. CSC drew attention to a significant and sustained improvement in Railtrack's performance almost immediately after the calibration period (characterised as a "step change") and argued that this improved level of performance represented the true steady state of the network. In CSC's view, both parties had been mistaken at the time of signing the agreement in believing that the steady state was the lower level of performance achieved during the benchmarking period. Because of this mutual mistake, CSC argued, there was no true Agreement between the parties.

- 5.2. Alternatively, CSC argued that, if Railtrack had known that the steady state was at the improved level subsequently achieved, then they had misrepresented the position by failing to disclose this material fact to CSC. In addition, CSC contended that Railtrack had engaged in Misrepresentation by material non-disclosures in the answers dated 15 November 1995 and 9 January 1996 to questions posed by the Regulator. In these answers it was said that no major schemes were planned, whereas in CSC's view Railtrack should have disclosed to ORR and CSC the initiatives to improve performance that were in hand and planned and the effect they would have on the flow of payments between CSC and Railtrack.
- 5.3. In evidence to support their contention that the Benchmarks had been set at the wrong level, CSC drew attention to the fact that in the periods after the calibration period performance had been in the Lower, Central and Upper Bands in the proportions 0%:8%:92% whereas the intention had been that the proportions should be 20%:60%:20%.
6. In answering these points Railtrack argued that:
 - 6.1. the Benchmarks were intended by both parties to reflect past performance during the calibration period and not the potential for future improvements in performance. The term "steady state" was intended to indicate that unusual events during the calibration period (eg strikes) were to be excluded and planned major developments (eg re-signalling or new rolling stock) were to be allowed for;
 - 6.2. using this agreed definition of "steady state" the Benchmarks had been correctly set and there had been no mistake;
 - 6.3. Railtrack had not failed to disclose material matters in the answers to the Regulator's questions since it was correct to say that there were no major schemes. CSC had been made aware of Railtrack's performance improvement initiatives (none of which could be described as major) at a seminar in November 1995 and at regular joint meetings. Moreover, the answers to the Regulator's questions were provided jointly by Railtrack and CSC in the light of this knowledge. There was therefore no Misrepresentation;
 - 6.4. the bands around the Benchmarks were intended to be set so that periods would be expected to fall in the Lower, Central and Upper Bands in the proportions 20%:60%:20%, if underlying performance remained the same. Railtrack's performance had in fact improved significantly (as a result of the management initiatives and good fortune with the weather) and this resulted in the proportions being 0%:8%:92%. The improvement in performance indicated that the incentives provided by Schedule 8 were working and not that the Benchmarks were wrongly set.
7. The Committee reviewed the process by which the Benchmarks had been set, in the context of CSC's contention that both parties had been mutually **Mistaken** as to the intended relationship of the Benchmarks (and performance Thresholds between the bands) to actual performance subsequent to the signing of the Fourth Supplemental Agreement (as amended).

8. The Committee concluded, in the light of all evidence presented, that the parties had carried out properly the instructions laid down for arriving at a Schedule 8 Performance Regime conforming with the agreed template;
 - 8.1. the calibration had been carried out in accordance with the procedures as laid down in the calibration guide produced by Rail Operational Research (ROR), and the parties had agreed the data and periods to be used to assess the Benchmarks and Thresholds in accordance with those same laid down procedures;
 - 8.2. Benchmarks had been calculated for all five service groups; the Committee noted that, for two groups, more demanding Benchmarks, derived from Passenger's Charter standards, had been set in accordance with instructions;
 - 8.3. Both parties had been given the benefit of every opportunity provided for in the laid down process for the Benchmarks to be adjusted, and this had occurred; and
 - 8.4. the parties had submitted the resulting Schedule to the Regulator for approval, in a joint submission, and had submitted joint responses to the Regulator's follow up questions.
9. The Committee gave especial consideration to the question of what should have been understood by the term "steady state" in relation to the calibration process and concluded that, within the protocols to be observed in carrying out the procedures prescribed in the Calibration Guide,
 - 9.1. references to a "steady state" related to the picture of the level, and variability, of performance that could be derived from a backward look over the representative periods chosen by the parties to support the calibration, with corrections only for "one-off" factors;
 - 9.2. performance over a period should tend to fall into the proportions 20%:60%:20% as between the Lower, Central, and Upper Bands, only "if underlying performance remains at the same level as over the benchmarking period" (ROR Schedule 8 Calibration Guide 15th June 1995, para 8.1); and,
 - 9.3. there is **no** implication that, where subsequent performance differs widely from the Benchmark, or does not correspond with a 20%:60%:20% split as between the bands, Benchmarks and performance Thresholds should be reviewed or amended.
10. The Committee therefore rejected CSC's contentions
 - 10.1. as to the scope of the definition of "steady state", in favour of a definition that only related to the description of performance within the calibration periods, and
 - 10.2. that the Parties had been Mistaken.

11. The Committee reviewed the submission from CSC that, because, in their joint responses to the Regulator, the parties had not specifically answered the question regarding possible projected cash flows over the next two years, and Railtrack had concealed the range of initiatives it had both planned and in hand, there had been **Misrepresentation** by Railtrack
12. The Committee was initially faced with different views from the parties as to the scale of the performance improvement, the impact of the initiatives undertaken by Railtrack, the timing of those initiatives, and the extent to which they had been the subject of consultation with CSC. The Committee was able to resolve these differences by questioning the parties, and by reference to additional documents presented by the parties at its request. In consequence the Committee felt it unnecessary to adopt a suggestion from CSC that the parties should jointly commission an independent study of the cause and effect relationship of initiatives undertaken, and performance improvements achieved, both during and since the period of calibration.
13. The Committee, in considering whether or not there had been Misrepresentation, took the following factors into account:
 - 13.1. in the joint reply to the Regulator (9th January 1996), -“There are no major schemes over the next two years which may be likely to affect the overall balance of performance”- the phrase “major schemes” was one, at the time, generally understood to relate to significant expenditure on major engineering works, and not to local, relatively low cost initiatives, of the type described by Railtrack;
 - 13.2. this reply was not inaccurate, and could not be understood as implying that there would be no performance improvements;
 - 13.3. there was a documented record of discussions between Railtrack and CSC, which had been in operation throughout the period that the details of the Benchmarks had been in calculation, and which demonstrated that, through those discussions, CSC had been informed of all significant initiatives proposed by Railtrack to improve performance.
 - 13.4. it would not have been reasonable to predict, in the light of experience at the time, which, if any, specific initiative would have what, if any, specific impact upon performance, and therefore upon performance payments; on the other hand
 - 13.5. it would have been a matter of arithmetic to determine, in advance, the financial impact upon performance payments of reducing delay by a stated (postulated) amount.
14. The Committee concluded that they had not found any evidence of **Misrepresentation.**

15. In summary, the Committee concluded that,
 - 15.1. notwithstanding the level of out-payments faced by CSC as a consequence of the relationship between the Benchmarks and recent actual performance, those Benchmarks had been calculated, and incorporated into a formal agreement, in accordance with all the procedures laid down for Railtrack and Train Operators;
 - 15.2. there had been no Mistake nor any Misrepresentation to affect the form of the Performance Regime; and that, therefore,
 - 15.3. there were no grounds for the Committee to declare the agreement null and void.
16. The Committee therefore **determined** that
 - 16.1. it would not declare the Fourth Supplemental Agreement (and the Agreement of 21st March 1996) void;
 - 16.2. it would not direct the parties to re-negotiate the Benchmarks;
 - 16.3. it would not direct Railtrack to pay any form of compensation to CSC.
17. As a consequence the Committee **directed** that
 - 17.1. CSC resume all payments due under the terms of the contract, including the release, with immediate effect, to Railtrack of any moneys previously paid into escrow; and,
 - 17.2. each party should bear its own costs in relation to the bringing of the reference, given that the matters in question were of significant import, and were submitted in a proper way.

**Bryan Driver,
Chairman,
Access Dispute Resolution Committee**