

# **Code of Practice**

November 2011

## Code of Practice

### FOREWARD

#### 1. Background

- 1.1 In July 1998 the Government issued a White Paper which referred to and accepted the then Rail Regulator's recommendation that rolling stock leasing companies should be asked to produce Codes of Practice covering their dealings with train operating companies. This Code of Practice (the "Code") has been prepared by Porterbrook Leasing Company Limited ("Porterbrook") in response to that recommendation and sets out our approach to the market and the manner in which our customers can expect to build constructive partnerships with us. The Code explains the basis on which our business practices are founded and indicates our understanding and support of the public interest objective of creating a safe, competitive and efficient rail industry which meets the needs of passengers.
- 1.2 In July 2009 Porterbrook gave undertakings to the Competition Commission that it would remove the non-discrimination obligations from the Code, in accordance with the findings of the Competition Commission in the Final Report from its Rolling Stock Leasing Market Investigation.

#### 2. Our Business Philosophy

- 2.1 We are in business to offer a full range of rolling stock leasing services tailored to meet our customers' particular needs. We have a long term financial interest in the rolling stock that we own and a long term commitment to the industry.
- 2.2 In fulfilling our role, our key business objectives are:
- to provide a safe, reliable and efficient service that customers and passengers regard as good value for money;
  - to build long-term relationships with our customers; and
  - to show professionalism in all that we do.
- 2.3 We will at all times seek to act fairly and to develop constructive relationships with all participants in the rail industry, including existing franchisees, potential new customers, other Rolling Stock Leasing businesses, the Office of Rail Regulation, the Secretary of State for Transport, Scottish Ministers or other relevant authority, as appropriate, and the Department for Transport or Transport Scotland.

#### 3. Our Service Commitment

- 3.1 We aim to offer customers a full range of services covering, depending on customer requirements: the provision of operating leases; the management of new vehicle procurement; and the provision

of maintenance services.

**3.2** We are committed to supporting our customers in their role of providing passengers with a safe, economically efficient and reliable railway service. In doing this we will:

- act fairly and reasonably in all our dealings;
- seek to respond to requests in a timely manner having regard to customer needs;
- strive for continuous improvement in the reliability and quality of our rolling stock in so far as such matters are within our control;
- engage in a regular dialogue with lessees regarding our current service performance and future plans;
- invest in our existing rolling stock to maintain its commercial attractiveness where it is economic to do so;
- accept performance and investment risks where it is appropriate and practical to do so; and
- be a source of advice or guidance to our customers on rolling stock.

#### **4. Safety**

**4.1** We are fundamentally committed to the provision of a safe and secure railway system and this is a key priority in respect of all our customer relationships.

#### **5. Complaints Procedure**

**5.1** Any customer, or potential customer who believes that the terms of this Code have been breached, should in the first instance contact Paul Francis, the Compliance Officer for Porterbrook, at Ivatt House, 7 The Point, Pinnacle Way, Pride Park, Derby DE24 8ZS.

## 1. Introduction

- 1.1** This Code establishes a behavioural framework for the conduct of passenger rolling stock leasing over the national railway network of Great Britain. It is designed to provide appropriate assurances for our customers whilst not unnecessarily restricting commercial activity in a rapidly changing market. We are committed to adhere to the provisions of this Code, under which all customers can expect to receive fair and reasonable treatment from this Rolling Stock Leasing Company (ROSCO). This Code is also designed to ensure that all contracts are entered into between customers and suppliers in a free and competitive environment.
- 1.2** We will apply this Code in a manner which takes into account the interests of the Train Operating Companies (TOCs) and passengers whilst satisfying our requirement to secure a commercial return on investment. The Code establishes a general behavioural framework rather than a set of rigid rules, as the latter would inhibit the proper development of the market and, therefore, would not be in the interest of either passengers or the industry.

### Fair and reasonable terms

- 1.3** We will always seek to offer terms that are fair and reasonable and in accordance with this Code and under no circumstances will we abuse or seek to abuse any significant market power we may have as a result of the particular market conditions prevailing from time to time.
- 1.4** In addition, we also accept the importance of behaving in a fair and reasonable manner at the time of franchise renewal and, to that end, we will not abuse any significant market power that we might enjoy at that time. We will offer quotes to potential franchise operators supported by the Secretary of State for Transport, Scottish Ministers or other relevant authority, as appropriate, on a fair basis. Our dealings with potential franchise operators will be on a fair and reasonable basis.

### Non-preferential Treatment for Vertically Integrated Companies

- 1.5** Where a customer is owned in whole or in part or controlled by this company or is directly or indirectly owned in whole or in part or controlled by a company which also owns or controls this company we will not give any preference to that customer, except on the basis of the factors outlined in this Code in paragraph 2.21, although in exceptional circumstances additional factors may be taken into account.

### Enforceability and compliance

- 1.6** The Code must be seen in the context of the legal and contractual relationship which exists between this company and its customers. It is important to appreciate that the Code does not constitute a contract and does not constitute an agreement or intention to vary, waive, amend, replace or add to any existing contractual terms.
- 1.7** We will seek to comply with the provisions of this Code. Principal responsibility for compliance with the Code shall lie with the Compliance Officer identified in the Foreword.

## 2. Areas of Application

### Lease Terms

## Introduction

- 2.1** We will continue to adopt a flexible and customer-driven approach to all aspects of lease terms and seek, so far as is possible, to meet the individual needs of specific customers. We will offer prices and other terms which reflect the value of the services provided and risks assumed.
- 2.2** In considering customer requests in relation to proposed or existing lease terms (including requests relating to the period of the lease; sub-leases; handbacks and cancellations; cascades; mixing of stock and modifications) we will normally take into account some or all of the criteria listed in paragraphs 2.3 to 2.20 and 2.22 below, as applicable, although, in exceptional circumstances, we may take into account additional criteria. Additional criteria applicable to individual leases will, whenever it is reasonably possible to do so and subject to confidentiality requirements, be identified to customers during negotiation of a lease, including during the negotiation of any variations of a lease.

## Lease terms for new trains

- 2.3** We will seek to ensure that any acceptance regime we negotiate in respect of new trains, to be procured by us from a manufacturer and leased to a customer, does not unfairly oblige the customer to accept trains which are not fit to enter revenue-earning service.

## Flexible periods

- 2.4** We will seek to accommodate customers' requirements for particular lease periods. The length of the proposed lease period is one of the factors influencing the lease charge (as listed in paragraph 2.21). In particular, lease charges will typically reflect the impact of different length leases on the expected value of the rolling stock over its entire lifetime, with lower charges tending to apply where uncertainty about releasing is reduced. The impact of specific lease periods on the lease charge will typically depend on:

- the contracted proportion of the future anticipated life of the rolling stock;
- the likely demand for the particular stock at the end of the proposed lease period;
- the extent to which the payments during the term of the lease facilitate raising finance for the relevant rolling stock;
- the reduced residual value risk when rolling stock is leased for longer periods of time;
- the reduced marketing costs associated with leases which are re-let on fewer occasions; and
- whether the lease and the franchise are coterminous.

## Sub-leasing

- 2.5** Customer requests to sub-lease rolling stock will usually be considered favourably and our consent given provided that we know the identity of the person using the rolling stock, where the rolling stock is to be located and are satisfied that the terms and conditions imposed on the sub-lessee are no less favourable than those in the original lease. In order for us to consent to the sub-lease of particular rolling stock, we will typically seek confirmation that:
- the sub-lessee will be able to operate and maintain the rolling stock to the required safety

standards;

- any Government undertakings or any security interests in the rolling stock are maintained;
- the sub-lessee has a satisfactory operational record and creditworthiness such that it will not affect the primary lessee's obligations;
- there will be no reduction in the anticipated quality and reliability of the rolling stock concerned, taking into account the proposed use of the rolling stock;
- there will be no restriction placed on our security of interest in the rolling stock to be sub-leased; and
- there will be no reduction in capital allowances in respect of the rolling stock.

#### Handbacks and early termination

- 2.6** A lease may contain provision for the handback of rolling stock or for the early termination of the lease, or both. There is a relationship between the inclusion of one or both of these provisions and the price at which the rolling stock is leased. For example, in the case of a lease containing an early termination provision, the value to the customer of the early termination provision will be reflected in the lease terms.
- 2.7** Where a lease provides for the handback of rolling stock and the sharing between ourselves and the original lessee of any subsequent rental payments, we will use our best endeavours to find alternative uses for the rolling stock in the U.K.
- 2.8** If a lease does not contain any provisions relating to the handback of rolling stock or the early termination of the lease, we will consider proposals for alternative arrangements for the use of the rolling stock in question. If alternative uses for the rolling stock can be arranged, we will explore with the original lessee the implications of such alternative use, including some release of the lessee's obligations under its existing lease.

#### Facilitating cascades between customers

- 2.9** A special case of handback occurs when stock is cascaded, enabling TOCs to take advantage of newer stock which becomes available for leasing. Such transactions usually require the approval of the Secretary of State for Transport, Scottish Ministers or other relevant authority, as appropriate, and involve rolling stock transferring between several TOCs, at present mainly through sub-leasing arrangements.
- 2.10** We will consider all reasonable requests for cascades and will (subject to the wishes of the existing lessee) bring opportunities for cascades to the attention of present and potential customers who we may reasonably believe may be interested in such rolling stock. It is to be noted that, depending on the nature of the rolling stock, the costs of performing any particular cascade, any material difference in the creditworthiness of the different TOCs involved, any government undertakings or security interests which may need to be transferred and the requirements of the underlying financing, some changes to lease charges may be required.

#### Mixing of stock within train sets

- 2.11** Where we lease individual vehicles, we do not expect to place any restriction on a customer combining these vehicles with other vehicles built to compatible standards and leased from another lessor, within the same train formation, provided that such arrangement is consistent with the required safety standards and does not adversely affect our existing contractual or financing arrangements.
- 2.12** Where we lease multiple-units, a customer can combine such stocks with compatible multiple-units leased from other lessors to form a train where the units in question have compatible standards and safe operational characteristics (such as maximum speed).
- 2.13** Where we lease a fixed formation train, a customer may not normally vary the formation of that train unless this is specifically provided for in the lease terms. However, we will consider reasonable proposals to vary fixed formation rolling stock and will assess the implications of such proposals on applicable lease charges. In doing so, we will take account of the impact of the proposed variation on:
- the loading on power units (if applicable);
  - maintenance programmes, standards and safety requirements;
  - the technical performance of the rolling stock (in terms of reliability, working life and maintenance requirements);
  - the future commercial value of the rolling stock (including the nature of the offer that could be made on releasing the rolling stock); and
  - the consent of third parties, if required.
- 2.14** Where both we and another supplier own spare vehicles which, in combination, could allow a complete train or multiple-unit to be created, then we will negotiate in good faith with that supplier either a pooling arrangement or a purchase/sale price. We reserve the right to satisfy ourselves that the condition of the other supplier's rolling stock to be mixed or sold in this way is satisfactory and, in respect of pooling arrangements, that our rolling stock will remain commercially attractive to re-let at the end of the applicable lease period. In such circumstances we will negotiate in good faith and under the auspices of the Secretary of State for Transport, Scottish Ministers or other relevant authority, as appropriate.

#### Maintenance

- 2.15** We will seek to develop and promote maintenance arrangements which have regard to the interests of passengers. Such arrangements will include a maintenance regime (that is the periodic overhaul of the rolling stock) which achieves required safety levels, sustains operating efficiency and preserves the working life of the train.
- 2.16** We recognise that each customer will have specific requirements in relation to maintenance and we are willing to consider a range of possibilities including: the customer undertaking maintenance; our arranging maintenance or the sharing of such undertakings and arranging in a specified manner. Whichever option is adopted, it is of course essential that the required standards of safety and maintenance are observed and that there is proper opportunity for monitoring, inspection and

enforcement.

Where we have contractual responsibility for maintenance we will process claims arising from this responsibility in a timely manner following the receipt of all relevant information from the customer.

**2.17** We will:

- be receptive to ideas from customers and suppliers as regards methods of improving rolling stock maintenance, including methods of improving the supply of spare parts;
- proactively seek ways of improving maintenance arrangements;
- ensure that arrangements are in place that promote an effective supply of 'scarce spares'; and
- offer, whenever practical, a performance regime commensurate with our ability to manage the associated risks.

**2.18** The basis for determining maintenance charges is that they should reflect the whole life cost of maintaining the asset. Where changes are made to the contracted maintenance arrangements, we will aim to agree an equitable allocation of any incremental costs or savings. The criteria that will be taken into account in allocating costs and savings will usually include one or more of the following, although in exceptional circumstances additional criteria may be taken into account:

- the period over which the costs or savings will arise;
- the impact of the change on the estimated residual value;
- the impact on the customer's operating costs; and
- the risks associated with the proposed changes.

Modifications

**2.19** We will consider all reasonable requests for rolling stock modifications subject to the existing conditions of the relevant lease. When considering such requests we will have regard to such factors as:

- whether the modification is compatible with the objectives of improving safety and reliability;
- whether the modification is likely to increase (or decrease) the value of the stock to subsequent lessees and, therefore, the residual value at the end of the current lease term;
- whether the modification will have an appreciable effect on the overall value of the broader portfolio of rolling stock; and
- the requirements of any relevant existing financing arrangements.
- We will agree to share with the customer the cost of agreed modifications where we reasonably believe that the modifications will have a value to us after the expiry of the existing lease and if the required funds are available.

Where we are responsible for implementing mandatory safety modifications we will, subject to the terms of the lease and provided that the relevant customer co-operates, use reasonable endeavours to agree a suitable, compliant programme for fitment that minimises, where practicable and subject to relevant legal requirements, the time that vehicles are unavailable for revenue-earning service.

## Pricing Issues

Avoidance of excessive or predatory prices

**2.20** We will seek to agree prices which are reasonable having regard to the economics of the rolling stock, the specific terms of the proposed contract and broader market conditions.

Principal factors for determining and agreeing prices

**2.21** We will negotiate prices in good faith. The factors we take into account in agreeing a lease price will usually include some or all of the following although additional factors may be taken into account:

- the terms of the contract;
- the financing, acquisition and development costs of the rolling stock;
- maintenance arrangements and costs in respect of the rolling stock;
- the type and characteristics of the rolling stock;
- the physical condition and proposed use of the rolling stock;
- the estimated residual value of the rolling stock (see paragraph 2.22 below);
- the length of the contracted period;
- expected rental and performance characteristics of the rolling stock that could compete with the stock concerned;
- any customer specific factors (such as credit worthiness, operational record);
- current and anticipated levels of taxation, inflation and interest rates; and
- treatment of changes in applicable law.

Residual Value

**2.22** The residual value of the rolling stock is the forecast value of the future income beyond the proposed contracted period of the lease, and constitutes a commercial risk accepted by ourselves. Our estimate of residual value will be determined mainly by the following factors:

- the projected level of lease rentals for the rolling stock;

- the projected working life of the rolling stock;
- the expected degree of utilisation of the stock over its remaining working life. This depends on both the expected balance between supply and demand in the rolling stock leasing market (or the relevant market segment) and also the nature of the stock (for example, the extent to which it can be used on different parts of the network);
- the economic, legal and regulatory environment (including safety and other matters);
- contract-specific factors, such as the proposed use of the train; and
- the discount rate(s) or cash flow implications applied to the particular lease.

### **3. Stock available for lease and disposal of stock**

#### Advertising of available stock

- 3.1** From time to time, we will make available to all operators and to the Office of Rail Regulation a list of stock which is available for lease, indicating the type, age and condition of the stock. We will respond promptly to bona fide enquiries from potential customers regarding the lease of such stock.

#### Refurbishment and disposal

- 3.2** The list of rolling stock available for lease will also indicate where we propose to dispose of a vehicle (i.e. withdraw for scrapping or sale outside of Great Britain). No rolling stock shall be disposed of until this statement of intention has appeared on a published list for at least three months, and the condition of the Secretary of State for Transport, Scottish Ministers or other relevant authority, as appropriate, relating to the disposal of vehicles has been complied with.
- 3.3** We will explore with potential customers, upon reasonable request, the scope for refurbishing stock which is available for lease, in order to enhance its attractiveness, subject to the commercial considerations set out in paragraphs 2.19 and 2.21.
- 3.4** "Stock available for lease" excludes rolling stock which is reserved by us for use as donor vehicles whose parts can be used as spares for other rolling stock; or as rolling stock available to be substituted for rolling stock currently on-lease and either the terms of the lease make specific provision for stock to be reserved or; because of the nature of the contract (in particular the payment or performance regime) it is reasonable for rolling stock to be reserved for substitution.
- 3.5** A separate list of stock withheld as donor vehicles will be supplied to the Office of Rail Regulation on those occasions when a list is provided under the terms of paragraph 3.1. We will minimise the number of donor vehicles and retain no more than the number of vehicles required to maintain a supply of spares at a prudent level. The criteria we would have regard to in deciding whether particular rolling stock should be reserved as a donor vehicle will normally include some or all of the following:
- our existing supply of equivalent spares;
  - the anticipated requirement for such spares;

- the availability of alternative supplies; and
- any existing contractual obligations and safety requirements

#### **4. Re-leasing and future franchising rounds**

Information to bidders and Secretary of State for Transport, Scottish Ministers or other relevant authority, as appropriate

- 4.1** We are committed to assisting the Secretary of State for Transport, Scottish Ministers or other relevant authority, as appropriate, or any successor, during the re-franchising process. We will offer lease and maintenance (when appropriate) terms to all qualified bidders during the re-franchising process in a timely manner. Having been selected as preferred supplier we will endeavour to enter into a contract in respect of a lease and (where appropriate) maintenance agreements with the selected bidder for the franchise, such that new leases will be in place in good time before the new franchise period is due to commence.

#### **5. Confidentiality**

- 5.1** We will not disclose any confidential information to third parties in relation to our customers save where:

- the information is already in the public domain;
- there is a legal duty on us to disclose such confidential information;
- we are required to provide the information by the Office of Rail Regulation, the Secretary of State for Transport, Scottish Ministers or other relevant authority, as appropriate, or any successor, the Office of Fair Trading or by any court or other competent authority;
- disclosure is made at the request of the customer; or
- disclosure is to our parent or affiliate provided that any such disclosure is made in accordance with any applicable undertakings to the Secretary of State relating to the disclosure of such information.

- 5.2** We will respect our customer's entitlement to require, prevent or restrict the disclosure of confidential information. However, in keeping with the commitments of fairness which we have given in this Code, customers should be aware that we will not withhold information nor disclose information (including information which the customer has requested to be disclosed) with the intention of restricting or distorting competition in the rolling stock market or in circumstances in which the disclosure may have the effect of so restricting or distorting competition.

- 5.3** We expect our customers to observe similar standards in relation to confidential information provided to them.

#### **6. Complaints and contracts**

- 6.1** One of our key objectives is to maintain constructive relations with our customers and avoid the need for our customers to invoke any complaints procedure. Where a customer considers that it does have cause to complain, we will always acknowledge the fact that a complaint has been made (in writing) and will take the complaint forward in a timely and efficient manner. Complaints should, in the first instance, be addressed to the contact identified in the Foreword.

**7. Liability and insurance**

- 7.1** We will continue to make rolling stock property insurance available to our customers and charge on the basis of passing the cost of arranging such insurance through to customers. We will give proper consideration to any suggested alternatives in relation to insurance, subject to ensuring that our interests in the rolling stock are adequately protected.

**8. Arrangements for promoting, reviewing and changing the Code**

- 8.1** We will make copies of this Code available to all existing customers and on request to all prospective customers, and will take reasonable steps to make customers and prospective customers aware of the existence of the Code.
- 8.2** The Code will be reviewed, and where appropriate amended, at periodic intervals. Prior to amending the Code we will consult with and take account the views of the Office of Rail Regulation in respect of such proposed amendments.



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