Will Godfrey
Director Economics Finance and Markets

Oliver Mulvey, Deputy Director, Rail Strategy,
Department for Transport

Paul Marshall, Group Controller, Network

31 March 2023

Dear Oliver and Paul,

ORR's review of Network Rail's RF11 delivery plan update for the financial year ending 31 March 2023

This letter provides ORR's final views on Network Rail's delivery plan update for its operating, support, maintenance and renewals (OSMR) activities. The plan should be published by May 2023. This is its period 11 re-forecast in year 4 of control period 6 (CP6), known as 'RF11'. The plan sets Network Rail's income and expenditure forecasts for 2023-24 and what it anticipates to deliver in return.

Network Rail updates its OSMR delivery plan for CP6 on an annual basis. We review its updated plan as part of how we hold Network Rail to account against the Periodic Review 2018 (PR18) Final Determination, as well as to provide assurance to funders about Network Rail's delivery. Specifically, we focus on:

- Network Rail's progress against its 2019 Delivery Plan (DP19), which sets out how Network Rail intends to deliver our PR18 Final Determination, and was approved by the Secretary of State (SoS);
- changes since the last annual update to Network Rail's Delivery Plan (the 2022 Delivery Plan, DP22), which we reviewed last year; and
- changes since we reviewed the last iteration of the plan. We documented that review as part of our RF6 note, which was provided to the Department for Transport (DfT) on 16 December 2022. We also shared the note with Transport Scotland.

At RF11, we undertook a targeted review of Network Rail's plan across five areas. We did this because we identified these areas as key risks to Network Rail's CP6 delivery. Our review focused on: (i) Network Rail's management of financial risk; (ii) the impact of very high inflation on Network Rail's income and costs; (iii) renewals profiling; (iv) workforce modernisation; and (v) outputs. We provide commentary on each of these areas (Annex A). We also include in this letter information on the progress made against the full list of issues raised in the RF6 note (Annex B) and a copy of our RF6 note (Annex C). In addition, our review took place in parallel to our assessment of Network Rail's Strategic Business Plan (SBP) for control period 7 (CP7). The output of RF11 informs our view of Network Rail's likely CP6 exit position, so it plays an important role in informing our CP7 determination.

Summary of our findings

We consider that Network Rail's RF11 plans are consistent with DfT's financial limits for 2023-24. They also remain aligned with the current Delivery Plan (DP22) and the SoS approved DP19. Consequently, we do not consider that RF11 requires sign-off from the SoS. This is consistent with our findings at RF6, as communicated to Network Rail and DfT in December 2022.

Table 1: Summary of our findings

Industrial action has cost [redacted] over the course of 2022-23. DfT has provided additional network grants in relation to DfT operators in England & Wales to partly pay for this.	Industrial action has cost [redacted] in 2022-23. DfT has provided [redacted] additional network grants in relation to DfT operators in England & Wales to partly pay for this, and the rest of the required funding has been sourced through the remaining CP6 risk fund and deferrals of renewals. Of the [redacted] that has been paid out to operators, [redacted] has been paid to DfT operators in England & Wales mostly through contractual Schedule 4 or Schedule 8 charges.
Network Rail has now used or allocated all its CP6 risk fund, but some risks remain in its plan. Network Rail is managing these risks through deferral or	Since the last update provided at RF6, Network Rail has been managing the remaining CP6 budget through a process to defer or reprioritise its CP6 renewals. Our view is that the process for making changes to renewals plans should be more transparent and more clearly show the effect of deferrals on safety, asset

reprioritisation of renewals, however we have concerns about the process of making changes to its CP6 renewals plans.	sustainability and efficiency including how Network Rail will mitigate them. Consequently, this has made it difficult for ORR to track the effects of changes to renewals, e.g. because there is a delay between adjusting funding and the impact on the individual renewals projects. This is relevant for the remainder of CP6 and CP7, when Network Rail is planning to largely manage financial risk in this way. We have stressed to Network Rail the importance of having an appropriate process in place to defer or reprioritise renewals and that this must be improved before CP7. We are now regularly meeting with Network Rail on this issue, and we will provide a further update in our draft determination.
The effect of inflation for the final year of CP6 remains uncertain, mainly in relation to contracts with suppliers that are due to end in the final year of CP6.	Uncertainty around the future impact of inflation remains especially because of contracts with suppliers that are due to end in the final year of CP6. This is because Network Rail anticipates that the quotes for new contracts will be affected by the recent increase in inflation. We have requested further information from Network Rail on the impact of inflation on its contract prices and it will provide this in April 2023. Once we have received this information, we will provide it to DfT. Inflation is currently very high, compared to PR18 forecasts and expectations, and difficult to forecast, which Network Rail has highlighted as a key risk in its plan; if inflation is higher than expected then that would increase overall costs in CP6, and Network Rail would need to defer more renewals. Higher overall costs caused by a higher-than-expected inflation impact would lead to further renewals deferrals or reprioritisation to offset the costs. Conversely, lower-than-expected inflation would lead to additional expenditure on renewals, or other priorities.
To manage its risk position Network Rail has had to reduce its total CP6 forecast	Network Rail has reduced its total forecast renewals expenditure for the whole of CP6 by £0.4 billion (circa 2% of total CP6 renewals expenditure). It had done so to partly fund financial risks such as ongoing industrial action

renewals expenditure by circa 2%, or £0.4 billion. This reduction will have a knock-on impact on its entry position for CP7.	costs, higher payments to train operators due to poor train performance, and to deal with inflationary pressures. Network Rail has told us that this has mainly impacted projects in the Eastern region, and to a lesser extent the Southern region. Network Rail has told us that these reductions at RF11 compared to DP22 will have a knock-on impact on its regional CP7 plans, both in terms of the volume and funding. However, some of the volume reduction is driven by the slippage of major signalling commissioning in the final weeks of CP6, which will not impact CP7 funding as the slippage does not reflect changes in work. We have asked Network Rail to provide us with details showing to what degree CP7 costs and volumes will be impacted by this change at RF11 across all regions. Network Rail's Technical Authority has told us that ORR should receive an update by 31 March. We will provide further information on this as part of our draft determination.
Network Rail has delivered on its management modernisation programme in CP6. However, there are ongoing delays to its maintenance modernisation programme. These delays could impact its overall CP6 efficiencies target.	Network Rail told us that it has delivered on its management modernisation programme in CP6 through recruitment controls, continued workforce attrition, and its voluntary severance scheme. Network Rail told us that there are ongoing delays to its maintenance modernisation programme and that the financial effect of this was being partly offset by continued attrition and recruitment constraints across its business. It remains confident that its maintenance modernisation programme will be delivered in CP6, with the change continuing to embed in CP7. It has told us there is a small risk to its forecast delivery in the final year of CP6, which could have an impact on its overall CP6 efficiencies target. We have tested the overall efficiency projections from Network Rail, and we still anticipate Network Rail delivering its CP6 efficiencies, and we will continue to monitor and report on this. Network Rail has told us that

	the implementation of its maintenance modernisation programme will be complete by the end of this calendar year.
Network Rail is largely targeting levels of passenger and freight performance that are below the levels it committed to deliver in CP6.	In its scorecard for 2023-24, most of Network Rail's proposed performance targets for CRM-P and FDM-R are lower than its regulatory commitments and below trajectories set in DP22. These targets do not represent an acceptable level of delivery. However, in Annex A we describe why performance will remain challenging in year 5 of CP6. From our review, all targets encourage performance improvement from current levels. The proposed targets should be achievable, though the scale varies. It would be significant in Scotland, notable in Eastern and Southern but limited elsewhere. We consider that the targets should be deliverable; only Network Rail Scotland's target may be notably stretching and potentially not deliverable (as this is the region with most stretch applied compared to current performance). North West and Central's CRM-P target is the least stretching of all targets and it will deliver only a 0.05 percentage point improvement compared to current performance. Network Rail could set more stretching CRM-P targets, while remaining realistic, for all regions except Scotland. However, we also recognise a view that incremental improvement coupled with achievable targets may help to motivate and incentivise staff to deliver improved passenger and freight performance. We know that Network Rail can do more to improve train performance and we are using our regulatory tools to ensure it works with operators to deliver on the improvements it has already committed to. We wrote to Network Rail in November 2022 and January 2023, setting out specific areas it needed to improve on. These included the importance of increasing infrastructure reliability across the regions, focusing on better

	operational response and taking steps to increase timetable resilience. Regardless of the targets set in 2023-24 scorecards, we will continue to hold Network Rail to account for delivery of its CP6 commitments, to ensure it is doing all that it can to deliver passenger and freight performance improvements – and we will take appropriate action if not.

Implications for CP7

Our analysis of Network Rail's SBP has suggested that there are some inconsistencies between its CP6 exit position in the RF11 forecast and its CP7 SBP, which Network Rail will update in the next iteration of its CP7 plan. For example, in the Eastern region work has been deferred to CP7 due to funding shortfalls in CP6. Network Rail highlights its CP6 exit as a key risk in its SBP, and it sets out the potential cost impacts in CP7 as part of its SBP. Our view of the likely CP6 exit position and its implication for CP7 delivery will form a key part of our assessment and draft determination on CP7 funding and outputs.

Next steps

We will continue to review Network Rail's updates to its plan in the final year of CP6 and we are discussing when we do this with DfT. We also intend to keep DfT and Transport Scotland updated on our SBP assessment and our key messages for our draft determination, due to be published in June 2023. Following publication of our final determination in October 2023, we will move to implement it. As part of this, Network Rail will issue its Delivery Plan for CP7 that should be consistent with our final determination. We will then issue our review notice and, subject to Network Rail's acceptance, issue Notices of Agreement and Review Implementation. The Secretary of State, having considered the views of Scottish Ministers, signs off the final version of the Delivery Plan. These will give effect to the decisions made during PR23 in time for CP7 to commence from 1 April 2024 and for Network Rail to develop its plans for delivery.

I am happy to discuss any of the points in this letter with you.

Yours sincerely,

Will Godfrey
Director Economics, Finance and Markets

Annex A: Key findings from ORR's review of Network Rail's RF11 submissions

A.1 Unless we are referring to a specific region or part of Network Rail, the numbers in this annex are for Network Rail as a whole and are presented in cash prices. Where future forecasts are included, this is based on the Office of Budget Responsibility's (OBR) November 2022 inflation forecasts.

How Network Rail is managing its risk position

A.2 Network Rail has now used or allocated all its risk fund, which had a value of £3 billion at the start of CP6. At RF11, the cost of industrial action is forecast to be [redacted] for 2022-23, of which [redacted] was paid to DfT operators under the Schedule 4 and Schedule 8 regimes. DfT has provided [redacted] of additional Network Grant funding to partly fund these payments to DfT operators. The remainder of the industrial action costs have been funded from the CP6 risk fund and deferrals of renewals. No costs of industrial action are forecast for the final year of CP6, and we acknowledge that the pay dispute between the unions and Network Rail has been resolved at the time of writing.

A.3 Network Rail is now managing the tighter budgetary situation through the deferral or reprioritisation of renewals. To a certain extent this way of managing risk in 2023-24 is consistent with how Network Rail has managed financial risk throughout CP6, as no risk money was included within in year budgets, i.e. it is assumed to be spent. However, the main difference is that this is no longer a choice, as there is a tighter financial position, i.e. if there had been unused risk funding, then the renewals expenditure could have been higher. We are discussing this process with Network Rail, as it is important that Network Rail enhances its approach to managing its financial risks to show that it is making the right decisions at the right time, i.e. developing a good understanding of which renewals projects could be more easily 'switched off', if its financial position worsens. One example of how this process works when funding is tight, is that there is a funding gap in Eastern, which Network Rail is working to resolve.

A.4 Our view is that the process for making changes to renewals plans could be more transparent and more clearly show the effect of deferrals on safety, asset sustainability and efficiency and how Network Rail will mitigate them. This process can make it more difficult for ORR to track the effects of changes to renewals, e.g. there is a delay between adjusting funding and the impact on the individual renewals projects. This process for managing risk is relevant for the remainder of CP6 and CP7, when Network Rail is planning to largely manage financial risk in this way, so we will provide a further update in our draft determination.

Impact of very high inflation, compared to PR18 forecasts and expectations, on Network Rail's income and costs

A.5 Uncertainty around the future impact of inflation remains, especially regarding contracts with suppliers that are due to end in the final year of CP6. This is because the quotes for any new contracts will be affected by the recent increase in inflation. Network Rail has said that this could lead to a proportionally larger impact on costs where existing contracts locked prices in and protected certain business areas from the full impact of higher inflation rates. We have requested further information from Network Rail on the impact of inflation on its contract prices and it will provide this in April 2023. Once we have received this information, we will provide it to DfT.

A.6 Network Rail has told us that its assumptions for the overall impact of inflation in the final year of CP6 have decreased compared to its previous forecasts. However, higher overall costs caused by a higher-than-expected inflation would lead to further renewals deferrals or reprioritisation to offset the costs, or more expenditure on renewals, or other priorities, if inflation is lower than expected.

Renewals

A.7 Since DP22 Network Rail has reduced its total forecast renewals expenditure for the total of CP6 by £0.4 billion (circa 2% of total CP6 renewals expenditure). It had done so to partly fund financial risks such as ongoing industrial action costs, higher payments to train operators due to poor train performance, and to deal with inflationary pressures. Network Rail has told us that this has mainly impacted projects in the Eastern region, and to a lesser extent the Southern region.

A.8 The Eastern region has reported an 11% reduction in renewals costs and a 54% reduction in effective volumes (i.e. how much additional life Network Rail's renewals activities add to its assets, providing a view on asset sustainability) for the final year of CP6 since RF9. The disproportionate fall in volumes compared to costs is because Network Rail only recognises that a volume has been delivered when the renewed assets are brought into operation. This is particularly a problem for signalling projects that take a few years to deliver, e.g. Selby re-signalling – where most of the costs will be incurred in CP6 but volumes will now be declared in early CP7. Also, the inconsistency between changes in volume and costs could arise because there is a delay between adjusting funding and the impact on the individual renewals projects.

A.9 The reduction in effective volumes in the Eastern region includes several key deferrals from CP6 to CP7, for example Liverpool Street Station Renewals works and Kentish Town Road structures renewals. These deferrals could result in delivery inefficiencies and potential supply chain issues. Network Rail has said that these supply chain impacts should be minimal.

A.10 In the Southern region, Network Rail has re-allocated funds between asset types to accommodate an increased spend in signalling and telecoms and an acceleration of CP7 earthworks schemes. These increases have been offset by delayed works for track because of industrial action, machine productivity issues and access constraints, and a decrease in structures work due to issues relating to access, price, and scope changes.

A.11 Network Rail has told us that because of these reductions at RF11 compared to DP22 there will be a knock-on impact on CP7 plans, both in terms of the volume and funding. We have asked Network Rail to provide us with details showing to what degree CP7 cost and volumes will be impacted by this change at RF11 across all regions. Network Rail's Technical Authority has said that ORR should receive an update by 31 March 2023. We will provide further information on this as part of our draft determination.

A.12 We also set out in our last review of Network Rail's plan that there are deliverability risks in CP6 associated with backend loading across certain asset types e.g. signalling, structures and telecoms. These deliverability risks are not related to affordability. These are technical or operational issues with some areas of renewals spend. This position remains largely unchanged at RF11. There are also additional risks that could occur in the final year of CP6, which we have discussed with Network Rail. For example, no risk funding remains and so if further extreme weather impacts are experienced in the final year of CP6, then Network Rail may need to further re-assess its planned renewals (e.g. in earthworks or elsewhere) to fund any major earthwork failures. However, milder than anticipated weather could provide more capacity to increase renewals volume.

A.13 As part of its CP7 deliverability work, Network Rail planned to incorporate any associated change in volume caused by CP6 deferrals. Our analysis of

Network Rail's SBP has suggested that there are some inconsistencies between its CP6 exit position in the RF11 forecast and its CP7 SBP, which Network Rail will update in the next iteration of its CP7 plan. Our view is that this means that its delivery of planned renewals in CP6 remains uncertain. For example, in the Eastern region work has been deferred to CP7 due to funding shortfalls in CP6. Network Rail highlights its CP6 exit as a key risk in its SBP, and it sets out the potential cost impacts in CP7 as part of its SBP. We are monitoring Network Rail's planned delivery of its CP6 renewals closely through regular engagement with Network Rail and we will provide further information on this as part of our assessment and draft determination on CP7 funding and outputs.

Network Rail's workforce modernisation plans

A.14 We are monitoring Network Rail's workforce modernisation plans to ensure that it is not compromising on efficient and safe delivery, and that it is on track to deliver its workforce reform programme during CP6. This reflects that delivery of these reforms is a key element of Network Rail's overall CP6 efficiencies, as well as its assumed starting position for CP7, which has a significant effect on its CP7 expenditure forecast.

A.15 At RF11, we met with Network Rail to discuss progress against its workforce modernisation plans. Network Rail told us that it has outperformed on its management modernisation programme in CP6 through recruitment controls, continued workforce attrition, and its voluntary severance scheme. With regards to its maintenance modernisation programme and its pay offer, at RF11 Network Rail told us that:

- Maintenance modernisation programme: industrial action has delayed the implementation of its maintenance reforms, which is resulting in risks to delivering its overall workforce reform programme in CP6. Previously Network Rail told us that the implementation of its maintenance modernisation programme was forecasting a delay of three months and would now be delivered by July 2023 instead of April 2023, meaning that the start of the savings from the programme were delayed from the end of 2022-23 into 2023-24. At RF11, Network Rail told us that the go live date has been re-phased and will vary across Network Rail's regions depending on their own local consultation timelines. The expectation is that some regions will go live in July 2023, but others may be later than that, for example, Southern region has told us that its implementation date will be September 2023.

Network Rail has told us that the implementation of its maintenance modernisation programme will be complete by the end of this calendar year.

At RF11, Network Rail told us that the voluntary redundancy scheme for maintenance employees has started and exits are expected to occur in the first quarter of 2023-24. It also told us that the delays to its maintenance modernisation programme were being partly offset by continued workforce attrition and recruitment constraints across its business. Because of this it has been able to bring forward maintenance efficiencies into 2022-23 offsetting the delay to the programme benefits in 2023-24.

Network Rail remains confident that its maintenance modernisation programme will be delivered in CP6, with the change continuing to embed in CP7. It has told us there is a small risk to this in the final year of CP6, which could have an impact on its overall CP6 efficiencies target. Network Rail has told us as part of its CP7 SBP that if the workforce reform objective is not met in CP6 then this would have an adverse impact on delivery, efficiencies and industrial relations of up to circa [redacted] to [redacted] a year in CP7. We have tested the overall efficiency projections from Network Rail, and we still anticipate Network Rail delivering its CP6 efficiencies. We will continue to monitor and report on this.

- Pay offer: Network Rail has told us that a CP6 pay offer of 5.5% then 4%, over 2022-23 and 2023-24 respectively, was accepted in March 2023. Network Rail has told us that that this pay award will be funded in CP6 through additional savings from its modernising management programme and performance related pay. We have asked Network Rail to provide further information on the impact of its pay offer, now it has been agreed, on its CP7 plan.

At RF11, Network Rail told us that the current plan is for some staff to move to different maintenance contracts from October 2023. This is expected to cost Network Rail circa £8 million for 2024-25 and then circa [redacted] per annum for the remainder of CP7. Network Rail has told us that the [redacted] per annum figure is not in its SBP due to RF11 being produced later than its SBP. Network Rail is working on solutions to fund this gap, including the potential benefits that could arise from the new rostering arrangements because of its maintenance modernisation programme. Network Rail will provide an update on how it intends to fund this gap by the end of March 2023.

A.16 As outlined above we are also monitoring Network Rail's workforce modernisation programme to ensure that it is not compromising on safe delivery. Previously Network Rail told us that it had formed a Safety Validation Panel for its maintenance modernisation programme. The role of the panel is to independently review the safety validation submissions produced by the programme team, which include details of the proposed organisational changes, and to confirm that the requirements of the common safety method for risk evaluation and assessment have been applied by the programme team. We are an observer on this panel to ensure that the panel applies rigour to its work, and to have visibility of the way in which the changes are being considered. At RF11, Network Rail told us that the national programme team had produced outputs in the form of hazard logs and implementation safety assurance, which have been passed to its regions. These outputs will be used by the routes and regions to help finalise their implementation plans and, in doing so, assess the safety risks and devise appropriate risk mitigations.

A.17 In February 2023, we informed Network Rail of our concerns with this approach. Specifically, that it puts the onus of risk control on the routes with the potential for routes to focus on cutting costs during CP6 at the expense of delivering the changes safely, meaning risks may not be properly controlled. We recognise that Network Rail has a change management framework that allows for central oversight of how the changes are managed. However, risk management will depend on the rigour of the routes in setting out their risk control strategies, and the robustness of central oversight. We will carry out inspections of this process to obtain our own view of how well these processes work and will provide a further update when Network Rail next updates its CP6 plan.

Outputs

A.18 Network Rail discussed its governance processes for the setting of 2023-2024 scorecard targets. It described work it had done over the past 12 months. Improvements to its process include, for example, a more robust change control process, earlier engagement with Network Rail's Chief Executive, alignment with CP7 and teach ins with Network Rail Board and its Executive. These improvements provide us with assurance Network Rail has appropriate governance in place.

A.19 The most substantive metric change is to TARR (train accident risk reduction). We have reviewed the new elements of this measure and support the changes.

A.20 We have reviewed the CRM-P and FDM-R targets. We have also reviewed the customer agreement templates. From the customer agreement templates, while Network Rail was able to demonstrate engagement with its customers, most regions had not yet set specific local targets. Many operators wanted to wait until the annual business planning process with funders had completed. Our focus was therefore on the regional CRM-P and FDM-R targets.

A.21 From our review, all CRM-P targets encourage performance improvement from current levels and, in most cases, the proposed targets should be achievable:

- Southern is the only region to set its CRM-P target at a level that is better than its regulatory trajectory for year 5 of CP6;
- Eastern, North West & Central and Scotland regions have set CRM-P targets at a level that is below the regulatory trajectory (for Network Rail Scotland, below the equivalent CRM-P level to meet the trajectory for PPM which is its regulated measure); and
- Wales and Western has set its CRM-P target below both its original CP6 trajectory and its regulatory floor, but consistent with the recovery plan it is currently working to. As set out in our mid-year letter on performance, we have reviewed the region's recovery plan and consider that it demonstrates sufficient focus and represents a credible approach to the delivery of improvements.

A.22 The improvement would be significant in Scotland, notable in Eastern and Southern but limited elsewhere. Only Network Rail Scotland's may be notably ambitious (as this is the region with most stretch applied compared to current performance); North West & Central's appears to be the least ambitious (only 0.05 percentage point improvement compared to current performance).

A.23 On freight (FDM-R), the Network Rail national scorecard will be set at 92%. From our review we consider that all targets imply a level of performance improvement compared to today. A greater level of stretch has been applied to FDM-R targets:

- Eastern and North West & Central regions have set FDM-R targets at a level that is below (worse than) the regulatory trajectory;
- Southern's target is better than the regulatory trajectory;

- Wales and Western are targeting to be both below the regulatory trajectory and its regulatory floor; and
- Network Rail Scotland's regional scorecard will be set at 94.5% to align with the CP6 High Level Output Specification (HLOS).

A.24 Network Rail's Scotland's and Wales and Western's FDM-R targets are likely to be a significant challenge.

A.25 In most cases these levels do not represent good performance as would have been expected for the end of CP6.

A.26 Network Rail could set more stretching targets, but we recognise the broader context and the realism of prevailing circumstances that has been applied. For example, the following issues are likely to have an impact on achievement of CRM-P and FDM-R targets in the final year of CP6:

- the residual impact from industrial action by Network Rail staff, such as immediate performance impacts from postponed activities (for example some of those planned during the Christmas 2022 strike action);
- transitional effects of the Modernising Maintenance programme while changes to working practices are embedded;
- impact of Train Operating Companies' industrial relations issues – including transition away from rest day working - which could impact on ability to recover service following Network Rail delays (which will affect CRM-P);
- impact from safety-driven changes to working practices that have not yet been optimised – specifically relating to track access and weather management; and
- longstanding timetable weaknesses (including the impact of late notice changes) being highlighted by greater passenger volumes.

A.27 Further, we note that Network Rail may consider it appropriate to set achievable improvement targets to help engage staff following recent organisational challenges.

A.28 Regardless of the targets set, we know Network Rail can do more to improve passenger and freight train performance and we are pressing it to deliver on the performance improvements it has committed to. We are also continuing to challenge Network Rail on other important areas – for example improving its operational response to incidents and ensuring greater timetable resilience. We wrote to Network Rail in November 2022 setting out specific areas it needed to focus on, including the importance of increasing infrastructure reliability to improve performance across the regions (most notably Wales and Western). Network Rail has subsequently responded; all regions are in the process of providing detailed recovery plans, beyond the normal performance strategies. We will continue to hold each of the regions to account to delivery of these plans and ensure trajectories set within those plans are at least consistent with the scorecard targets.

Annex B: Network Rail's progress against the issues raised at RF11 (March 2022), RF3 (September 2022) and RF6 (December 2022)

Table B.1 Open issues

Issue	Progress made at RF11	Next steps
If the pay offer (which is consistent with its latest negotiating position) is approved then Network Rail intends to fund this in CP6 via an increase in CP6 efficiencies, however it does not have a firm plan in place to deliver these increased efficiencies.	Please refer to Annex A.	Please refer to Annex A.

Issue	Progress made at RF11	Next steps
Network Rail did not provide us with assurance of its ability to deliver its planned renewals.	Network Rail to use its re-forecasts to update delivery information and assess confidence on deliverability. Deferrals of planned CP6 renewals will be risk assessed as per the standard Network Rail processes and any impacts to CP7 planning will be factored into the regional SBP submissions. The CP7 deliverability assurance work will incorporate any associated change in volume caused by CP6 deferrals as part of that workstream.	The CP7 Deliverability report was shared with ORR as part of the suite of SBP documents. Further to this, an update will continue to be provided for future RF notes on volume delivered and forecast to be delivered. These will be covered in reports and Asset bilateral meetings.

Table B.2 Closed issues

Issue	Reason for closure
It is still unclear if Network Rail has appropriate governance arrangements in place to ensure that risk funding is distributed at the right time and is used in the most efficient manner in the regions.	Network Rail has produced a tracker, which will allow it to track how and where the remaining risk funding will be spent. This will be shared with ORR on an ongoing basis.
Network Rail should provide better transparency over costs and benefits incurred in its track worker safety arrangements in the regions.	Meetings were held with Network Rail to discuss this issue further and Network Rail has provided further transparency on both the costs and benefits in CP6.
Assurance around the longer-term impacts of being behind on its effective volumes in the areas of plain line, switches & crossing and structures.	It was agreed that this assurance work would be provided as part of future reforecasts.
'Shadow' reporting of Network Rail's maintenance numbers. Network Rail's regions provided us with its new maintenance indicator as part of its RF11 plan. We expect the accuracy of the data to improve over the next quarter.	To be taken forward as part of the regular engagement between ORR and Network Rail asset management teams. It was agreed that maintenance volume KPIs were to be included in Network Rail's executive packs going forward.
Network Rail has not fully explained how it will monitor the impact of its workforce modernisation plans on its wider commitments to asset management, safety, and train performance.	A meeting was held between ORR and Network Rail on Monday 17th October 2022 where additional information was provided by Network Rail. It was agreed that this issue could be closed and that we would continue regular engagement with Network Rail's executive on its workforce modernisation programme.

Issue	Reason for closure
Network Rail needs to better explain in its plan why it considers £323 millions of risk funding to be adequate, as well as the key risk mitigation strategies it is considering. This should include Network Rail clearly explaining how, if necessary, instead of drawing down risk funding it could manage financial risks in other ways.	Network Rail has no CP6 risk funding remaining at RF11. Network Rail will now manage risk through deferring renewals. A meeting was held on the 17 November 2022, where Network Rail's asset management team explained the current work on its risk management strategy to ORR. We will work with Network Rail to identify a way that it can show that its process is robust and how we can monitor and report on it.
Network Rail Scotland's financial risk position and how this is managed.	Network Rail Scotland has improved transparency around its risk fund.
Network Rail's regions did provide us with some information on the implementation of the Lord Mair/Dame Slingo recommendations however we require additional information so that we can understand how they are implementing the recommendations.	ORR has been provided with greater detail on regional action plans. Network Rail has provided justification for the Lord Mair recommendations that have not been progressed. ORR is continuing further work with Network Rail in this area as part of the Weather Risk Task Force.
Network Rail Scotland will fall below the regulatory floor at the end of Year 3 of CP6. (This means that Network Rail Scotland is not delivering sufficient renewals to achieve the levels of asset sustainability it agreed to in the Final Determination). A reduction in asset sustainability in the long term is likely to cause a deterioration of network assets through ageing and wear-out. This will have implications for areas such as train and freight service performance.	It has been agreed that any further involvement on this issue should be taken forwards in business as usual forums such as the NRAA.

Issue	Reason for closure
There have been changes to the DfT-funded enhancements portfolio. We are seeking assurances that comprehensive mitigation measures are in place and are aligned at the regional and national level; and that any residual impacts, including abortive costs, are considered when planning for CP7.	Network Rail provided assurance that issues or abortive costs are being mitigated effectively. The Southern region also identified additional renewals costs. ORR will continue to monitor in business as usual forums.
Network Rail has now used or allocated nearly all its risk funding and at RF6 it has £5 million remaining unallocated (this is just for Network Rail Scotland). Network Rail will need to manage financial risk differently in the remainder of CP6 to its approach so far.	A meeting was held between Network Rail and ORR, which included representatives from both Asset Management and Finance from both organisations. Network Rail demonstrated how risk was being managed and the impact on funding now there is no remaining risk funding. The meeting also covered mechanisms for how risk and funding will be managed in CP7, broadly in line with current methods. It was agreed that ORR Finance would attend Asset Management Bi-Lateral Meetings (between ORR and Network Rail), at RF, in order to observe combined reporting and how asset management and finance are being managed, including the impact, management and mitigation of risk and opportunity. This issue will also be included as a standing item for the Business Planning Progressive Assurance meeting.
Network Rail Scotland has undertaken further deferrals of renewals from year 4 to year 5 of CP6 in its latest update of its CP6 plan (June 2022), which has increased our concerns that it will not deliver these projects in CP6. The largest movement in renewals volumes has been in Scotland where Network Rail Scotland has reported that it is forecasting to under deliver on its year 4 effective volumes budget across all asset types by between 9% and 16%. The original budget set for year 4 was incorrect, which has caused part of this variance.	Network Rail Scotland has demonstrated a significant improvement in its governance around changes to its renewal plans, including improved links between finance, asset management and capital delivery teams. We have seen more stability in the reporting of renewals volumes, which provides more confidence that the reported volumes are being reviewed and amended when required. We will continue to monitor renewals reporting closely through our regular engagement with Network Rail, i.e. the NRAA.
Network Rail has not provided commentary on the safety implications of changes to its regional plans.	We wrote to Network Rail on this issue and we have received a reply. Further discussions will take place on this issue as part of our regular engagement with Network Rail.

Annex C: RF6 note

Please see RF6 note attached.

This publication is available at orr.gov.uk

Any enquiries regarding this publication should be sent to us at orr.gov.uk/contact-us

Carl Hetherington
Deputy Director, RME

Becky Lumlock
Group Director Transformation, Network Rail
cc DfT, Transport Scotland and Welsh Government
Sent by email

19 June 2019

Dear Becky

Following on from ORR's Opinion on Network Rail's "Putting Passengers First" programme, which we issued on 24 May 2019 (our Opinion)[1], this letter provides further information on our arrangements for regulating Network Rail at a regional level in control period 6 (CP6) and in particular during 2019-20, including specifying what baselines we will be using to hold Network Rail to account.

As Network Rail confirms further details of its new operating model, we will consider whether it is appropriate to further adapt our approach to regulation. We expect Network Rail to proactively notify us of all planned changes at the earliest opportunity, and to take full responsibility for ensuring compliance with its licence, discussing with ORR well in advance if it considers any changes to the licence may be needed. As we stated in our Opinion, if any new information materially affects the programme or its expected impact, we may update our Opinion.

Since we issued our Opinion in May 2019, we have been notified of some changes to the programme in relation to the System Operator (SO)[2]. We expect Network Rail to continue to engage with us on these changes, and are not yet in a position to address the SO proposals in this letter.

1. Stakeholder engagement

When we published our Opinion, we asked stakeholders for feedback on how well Network Rail engaged with them on this programme.

The level and quality of engagement reported by stakeholders appears to be mixed, with some reporting a lack of engagement or that the consultation appeared to be a 'tick box exercise'. Other stakeholders provided positive feedback on the level of engagement, adding that they were clear on Network Rail's aims and understood the forthcoming changes.

It is important that Network Rail engages well with its stakeholders, e.g. in relation to the changes to Network Rail's scorecards, where we need to know how Network Rail will assure itself that the interests of its customers are being met across the organisation. We will continue to monitor Network Rail's engagement with its

[1] https://orr.gov.uk/__data/assets/pdf_file/0016/41146/managing-change-policy-letter-2019-05-24.pdf
[2] As highlighted in our Opinion, Network Rail has not yet provided us with a full description of its programme and the programme has continued to evolve. Also, its initial information on the SO changes was not clear.

stakeholders throughout CP6, including in its implementation of the “Putting Passengers First” programme.

2. Ongoing issues

We highlighted a number of issues in our Opinion that need further consideration as discussed below.

Delivery of the 2018 periodic review (PR18) requirements while implementing the change

It is essential that Network Rail ensures the changes being implemented do not have an adverse effect on its ability to deliver, particularly during the implementation period between June 2019 and April 2020, when programme risk is higher.

Network Rail has submitted further high-level information on its governance process. But it has not yet fully addressed our concerns about the change potentially being a distraction from delivery – a concern shared by some stakeholders.

Network Rail has agreed to send us by 12 July 2019, more detailed information on the measures it is putting in place (in addition to the normal monitoring measures) to enable it to monitor its progress delivering the PR18 requirements during this period and ensure clear lines of accountability.

Safety

It is essential that Network Rail fully assesses the health and safety impact of the proposed changes and puts in place effective measures to ensure that risks continue to be managed. Network Rail should also ensure it manages the changes in accordance with good change management principles.

We acknowledge Network Rail’s response to our Opinion and will continue to engage with Network Rail on these matters to obtain assurance that risks are controlled and change is managed safely. This will include our role in the safety validation process.

Network Licence

Network Rail’s licence was revised earlier this year, reflecting its business structure at that time, and includes many requirements (for example around business structure, governance and stakeholder engagement) that we consider are essential to ensuring effective accountability.

At present, the network licence has not been modified as a result of the “Putting Passengers First” programme. We will consider whether this is needed, once we have greater clarity on certain issues and Network Rail’s position on how these changes align with the current licence conditions.

Scorecards

In the PR18 final determination, our policy on scorecards was centred around alignment between Network Rail's objectives and targets, to those of its customers. This remains unchanged and we will place reliance on how comfortable Network Rail's customers are with its new approach to scorecards and Network Rail's wider governance.

We decided to use Network Rail's scorecards in our regulatory approach for CP6 in order to support two high-level aims of PR18. These were to:

- support route comparison and competition; and
- focus Network Rail's geographic areas on customer requirements, benefitting end-users in turn.

Network Rail's letter of 31 May 2019 (in response to our Opinion) informed us of some additional changes in the content and structure of Network Rail's regional scorecards.

During PR18, we said that we would make greater use of scorecards in our monitoring and reporting, if they met our requirements – and if they did not we would adjust our approach accordingly. Network Rail's letter informed us that regions are taking different approaches to the train performance and local customer measure sections of their scorecards. Some regions have included a summary scorecard line per customer, and other regions have included summary lines per route. While all regions have included a regional CSI (Composite Sustainability Index) score, two regions have not included regional CRM-P (Consistent Route Measure – Passenger performance) or regional FDM-R (Freight Delivery Metric – Route level) on their scorecards.

In the last quarter of 2019-20, we will review the effectiveness of these changes and adjust the way we hold Network Rail to account if necessary. In terms of using Network Rail's scorecards during CP6, we intend to place reliance in our monitoring and public reporting[3] on:

- the new region-level CP6 baseline trajectories and regulatory minimum floors identified in the annex to this letter;
- the regional comparison scorecard, with individual region scorecards considered alongside these; and
- supporting management information provided to us through the data protocol.

We are reviewing how we use the scorecard information to help hold Network Rail to account. In some cases, we will need to consider information at a route level.

We note that Network Rail is considering reviewing a number of related areas in the context of its transformation programme, such as the role of Railway Boards in relation to scorecards and the nature of the relationship with performance related pay. We intend to keep the effect of these proposals on Network Rail's scorecards in CP6 under review.

[3] This will include publishing the CRM-P and regional FDM-R measures for the two regions that have not included them on their scorecards.

Regarding presentation of scorecards more generally, we made a number of points regarding transparency and ease of use of scorecards in our PR18 final determination and subsequently in response to Network Rail's December 2018 interim business performance report. We continue to expect Network Rail to make significant improvements in this area.

Freight and national passenger operators (FNPO)

A key feature of Network Rail's licence is the principle that Network Rail must ensure its structure and governance arrangements duly take into account the interests of both freight operators and passenger services crossing geographic boundaries (there are also a number of other important protections for freight).

We expressed some concerns in our Opinion about whether Network Rail's passenger and freight operator customers and other stakeholders would have sufficient transparency and influence under the new approach. These concerns were echoed in some of the responses from stakeholders.

Network Rail's letter of 31 May 2019 responded to these concerns and set out the oversight and governance arrangements for the FNPO, recognising the need for Network Rail to provide clear and strong representation for its customers and funders. We welcome this approach, which is important as Network Rail's proposals to place FNPO within a new Network Services Directorate, should neither diminish the role of the FNPO nor make it more difficult for Network Rail's stakeholders to engage with Network Rail. We will be monitoring Network Rail's delivery of these commitments closely to ensure that it is meeting the needs of its FNPO customers and is addressing the concerns they recently raised with us.

We note that there is currently no timeline set out for embedding in place the FNPO structural changes as described in your letter, post the initial change on 24 June 2019. It is important that Network Rail's commitments to improve the accountability and transparency of the FNPO, and its visibility within Network Rail's structure, are set up as soon as possible and communicated to Network Rail's stakeholders. As we said in our Opinion, and Network Rail accepts, we also expect Network Rail to meet the commitments set out in the FNPO route settlement.

Please could you therefore provide us with an update on progress by 30 September 2019. We will work closely with the FNPO and Nick King, Network Rail's Group Director, Network Services, to monitor and report on the effectiveness of the FNPO's engagement with geographic regions/routes and delivery of the route settlement. We will report publically, for example in our Monitor, on areas for improvement and areas that are working well. We will continue to discuss this further with Network Rail in our regular meetings regarding the FNPO.

3. Regional regulation and our approach for 2019-20

As set out in our Opinion, we will be regulating Network Rail at a regional level (supported by information at the new route level where appropriate) from 24 June 2019. To enable this, we asked Network Rail to 're-cut' its baselines and scorecards on a regional basis. Subject to the clarifications below we intend to use that information to hold Network Rail to account during CP6.

Baselines

Financial baselines

Network Rail will update its financial baselines as each stage of the programme goes live. Network Rail has today published its regional financial baselines on its website for each year of CP6[4], reflecting the changes from the first tranche of the programme.

The programme does not change Network Rail's overall financial and operational commitments and is effectively, from a financial point of view, a 're-cut' of the existing plans. We have agreed the methodology Network Rail has used to 're-cut' the route baselines from its latest delivery plan for the tranche 1 changes and are content that the baselines are consistent with the PR18 final determination. We will use these baselines for 2019-20 as the basis for our reporting and comparisons in 2019-20.

Baseline trajectories for regional consistent measures

In addition, as part of PR18, to enable us to compare between routes we set eight route level CP6 baseline trajectories (and eight regulatory minimum floors) for three consistent route level measures. These were for route level passenger train performance (CRM-P), freight performance (FDM-R) and network sustainability (CSI). Network Rail updated these trajectories in its March 2019 delivery plan, in a manner which reflected the PR18 final determination.

We have worked with Network Rail to create regional trajectories from these delivery plan route trajectories. These are set out in Annex A to this letter, together with some detailed points regarding our approach.

Regulatory Minimum Floors

We have produced regional regulatory minimum floors from the floors set in the PR18 final determination (see Annex A). As per our PR18 final determination, a regulatory minimum floor is the point below which we will be highly likely to consider a formal investigation into whether or not Network Rail has breached its licence, i.e. whether Network Rail is doing everything reasonably practicable to deliver the reasonable requirements of its customers and funders, having regard to all relevant circumstances, including the ability of Network Rail to fund its licensed activities. The floor is set at a level below which we consider performance to be unacceptable.

We have based the regional floors on the figures included in our PR18 final determination (and not those updated in Network Rail's delivery plan[5]), using the same methodology in each case.

[4] They are available at: https://www.networkrail.co.uk/who-we-are/publications-resources/cp6deliveryplans/
[5] We were clear in our PR18 final determination that the floors would remain consistent and would not change simply because targets were updated.

We have reviewed whether the level of the floors remains appropriate now that the data is at a regional level. At this stage we have not revised the overall level of the floors, so the challenge on Network Rail remains unchanged. But we will keep this under review during the early years of CP6, particularly in relation to the Southern region.

4. Next Steps

We will continue to work closely with Network Rail regarding the points above. We will address the SO issue referred to earlier in this letter separately in the coming weeks.

Yours sincerely

Carl Hetherington

Carl Hetherington

Annex A

Agreed operator baselines

In our PR18 final determination, we highlighted that five operators had agreed trajectories with their respective routes for the control period (c2c, Arriva Rail London, Great Western Railway, Merseyrail and Caledonian Sleeper). Where trajectories were agreed we said we would place weight on this agreement in our monitoring, noting that these may be updated or revised through annual scorecards during CP6. These trajectories are set out in our PR18 final determination.

Where annual targets are agreed between a route and an operator, we will place weight on this in our monitoring and reporting. We note nearly all operators agreed targets for year 1 of CP6, including updated targets for those five operators who agreed CP6 trajectories.

Consistent Route Measure for Passenger Performance (CRM-P)

In reviewing Network Rail's Delivery Plan (which forms the basis of the new regional trajectories) we have identified that Network Rail's routes have taken an inconsistent approach to creating trajectories for CRM-P, in particular for the Anglia route. Anglia's approach was also different from the approach Network Rail took for PR18.

Given the low materiality of this issue, we have decided to accept the trajectories that Network Rail has put forward. CRM-P is a consistent measure designed to enable comparison between different geographical areas managed by Network Rail. As such, a consistent approach is important. In future in CP6, we expect Network Rail to either:

- create CRM-P trajectories in a manner consistent with the approach Network Rail took in PR18 (i.e. using its central model); or
- set out for us an alternative consistent approach in good time for us to ask our independent reporters to assess this in advance of making any changes.

In the event that we consider any regulatory action in relation to the CRM-P, we will take account of this inconsistency in reaching any decisions.

The regional CRM-P baseline trajectories, which we will compare Network Rail's performance and targets to during CP6 are:

Region	2019-20	2020-21	2021-22	2022-23	2023-24
Eastern	1.50	1.36	1.31	1.28	1.27
North West & Central	1.71	1.62	1.58	1.55	1.52
Southern	2.90	2.88	2.82	2.74	2.70
Western & Wales	1.88	1.84	1.68	1.64	1.64
Scotland	1.06	0.96	0.89	0.89	0.88

The regional CRM-P floors are as follows:

Region	2019-20	2020-21	2021-22	2022-23	2023-24
Eastern	1.70	1.63	1.57	1.55	1.54
North West & Central	2.02	1.94	1.90	1.88	1.85
Southern	3.49	3.44	3.38	3.30	3.26
Western & Wales	2.23	2.19	2.10	2.02	1.99
Scotland	1.25	1.15	1.08	1.08	1.07

Freight Delivery Metric

In our PR18 final determination, we accepted the FNPO's proposed trajectory for the Freight Delivery Metric (FDM), which was 94% for each year of CP6. This is unchanged as a result of the structural changes at Network Rail.

In creating the regional FDM-R baseline trajectories we identified a small number of detailed methodological issues regarding how Network Rail is producing targets and trajectories for FDM-R. We are continuing to close out these issues with Network Rail and if there are any material points to be resolved we expect Network Rail to agree the approach to resolve them with us, and include the revised trajectories in its business plan for year 2 and the remainder of CP6.

Subject to this, the regional FDM-R baseline trajectories, which we will compare Network Rail's performance and targets to during CP6 are:

Region	2019-20	2020-21	2021-22	2022-23	2023-24
Eastern	94.0%	94.0%	94.0%	94.0%	94.0%
North West & Central	94.6%	94.6%	94.6%	94.6%	94.6%
Southern	92.8%	92.8%	92.8%	92.8%	92.8%
Western & Wales	93.4%	93.4%	93.4%	93.4%	93.4%
Scotland[6]	93.0%	Staged improvements[7]			94.5%

The regional FDM-R floors are:

Region	2019-20	2020-21	2021-22	2022-23	2023-24
Eastern	92.5%	92.5%	92.5%	92.5%	92.5%
North West & Central	93.5%	93.5%	93.5%	93.5%	93.5%
Southern	90.0%	90.0%	90.0%	90.0%	90.0%
Western & Wales	91.9%	91.9%	91.9%	91.9%	91.9%
Scotland[8]	92.5%	92.5%	92.5%	92.5%	92.5%

[6] This is consistent with our PR18 final determination for Scotland here.
[7] As set out in our PR18 determination.
[8] As above.

Composite Sustainability Index (CSI)

We have worked with Network Rail to create regional CP6 baselines. Network Rail has provided us with updated figures as envisaged in our PR18 final determination, to reflect the CP5 exit position. We are aware that they need to be assured internally within Network Rail. In the event that Network Rail's assurance process results in any material changes, we will decide whether to make any changes. More generally in this area we note that there were more variations in route level outturns than Network Rail anticipated (with a minimum impact at the national level) and we will work with Network Rail to understand why this occurred and how it can be improved in future.

Subject to the outcome of the assurance of the CP5 exit position, the regional CSI trajectories, which we will compare Network Rail's performance and targets to during CP6 are set out below. Note that this is a single end-CP6 figure in each case.

Region	2019-20	2020-21	2021-22	2022-23	2023-24
Eastern	-	-	-	-	-1.7%
North West & Central	-	-	-	-	-3.3%
Southern	-	-	-	-	-4.1%
Western & Wales	-	-	-	-	0.2%
Scotland	-	-	-	-	2.9%

The regional CSI floors are:

Region	2019-20	2020-21	2021-22	2022-23	2023-24
Eastern	-	-	-	-	-2.2%
North West & Central	-	-	-	-	-3.5%
Southern	-	-	-	-	-4.9%
Western & Wales	-	-	-	-	-0.4%
Scotland	-	-	-	-	2.4%