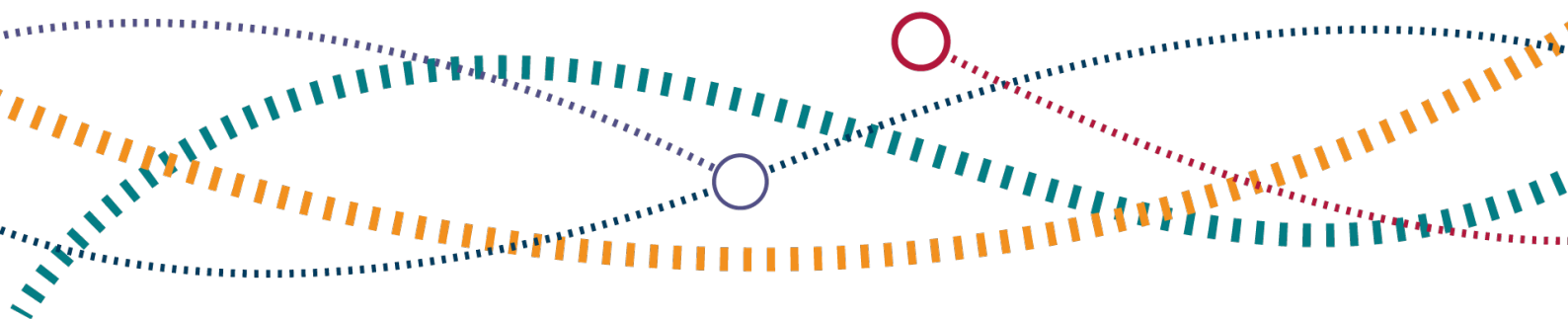




How Network Rail's CP7 funding and outputs are determined

Guidance for funders and stakeholders

30 March 2022



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About this document

The 2023 periodic review (PR23) is an ORR-led statutory process that will establish (amongst other things) Network Rail's funding and outputs for five years, starting from 1 April 2024. We refer to this as control period 7 (CP7). This document seeks to explain how this happens, including the role funders, ORR and Network Rail play.

Network Rail is currently developing its business plans for CP7. Our role is to assess these plans. Our approach is iterative and will focus on two key stages:

- our advice to the Secretary of State and Scottish Ministers (expected early this summer) to help inform their decisions about how much funding they intend to make available to Network Rail in CP7 and what, in return, they want it to deliver; and
- our assessment of the Strategic Business Plans that will form the basis of our overall determination for Network Rail, as well as the underlying settlements for the business units that will set out their funding allocation and specific outputs it must deliver for CP7.

Our assessment will help ensure that Network Rail's CP7 business plans:

- meet Network Rail's legal obligations (noting that Network Rail is responsible for ensuring it is meeting its legal obligations);
- are consistent with funders' priorities as set out in the Statements of Funds Available and the High-Level Output Statements;
- are designed to deliver safety, performance, asset sustainability and efficiency to the benefit of taxpayers and users of the rail network; and
- take appropriate account of the views of passengers, freight users and other stakeholders.

The UK Government's rail reform agenda is progressing alongside PR23. As set out in the Williams-Shapps Plan for Rail, Great British Railways will adopt, and be held to account for, delivering Network Rail's CP7 commitments.

PR23 is taking place under challenging circumstances for the industry. Passenger revenues have fallen due to changed travelling patterns following COVID-19, and it is unclear when they might recover to pre-pandemic levels. This, along with challenging macroeconomic conditions, means governments' decisions on Network Rail's CP7 funding are likely to be difficult. It is important that the industry is able to demonstrate its efficiency

and focus on managing costs, and our assessment will consider how the CP7 business plans account for these challenges and balance the relevant risks and opportunities.

This document is not a formal PR23 consultation. However, if you would like to discuss our approach in this area or share your thoughts, please get in contact with us via our PR23 inbox (PR23@orr.gov.uk).

1. Introduction

Key points

- The UK Government (for England & Wales) and the Scottish Government (for Scotland) set the strategy for and are funders of the railway. As part of PR23, funders will separately decide on the level of funding they will make available to Network Rail and what, in return, they want Network Rail to deliver.
- To help funders with their respective decisions, Network Rail is developing its initial CP7 business plans. We are assessing these plans and using this, amongst other evidence, to inform our advice to Ministers.
- Once funders make their decisions on overall funding and outputs for CP7, Network Rail will develop more detailed business plans for CP7, referred to as the Strategic Business Plans (SBPs). These plans will be based on the level of funding made available and what funders have asked Network Rail to deliver.
- We then assess the SBPs to determine the funding Network Rail needs to deliver its outputs, including for each region and key business unit. This will establish Network Rail's PR23 commitments for CP7.

What is PR23?

- 1.1 A periodic review is a statutory process that the Office for Rail and Road (ORR) leads. A key objective of this process is to establish the level of funding for the mainline GB rail network and the outputs and outcomes it should deliver to rail users and taxpayers over a five-year period. The periodic review process also decides the [framework for the contractual charges and the performance and possessions regime](#) and sets out how we will hold Network Rail to account in CP7. We [formally launched](#) the PR23 programme in June 2021. The rest of this document focuses only on establishing Network Rail's funding and outputs.
- 1.2 PR23 will focus on funding and outputs for Network Rail's infrastructure activities relating to operations, support, maintenance, and renewals (OSMR) activities over CP7. In line with the approach taken for the periodic review 2018 process (or PR18), we expect it will not include rail enhancements (i.e. large-scale projects that deliver new infrastructure capabilities) or how they should be funded, which

the Department for Transport (DfT) and Transport Scotland (TS) will continue to manage separately.

- 1.3 An important element of the periodic review process is governments' decisions about how much funding they will make available for the railway given their other priorities and what, in return, the railway is required to deliver. Making use of Network Rail's developing business plans, we provide advice to Ministers to help inform these decisions. We then set the overall determination on Network Rail that explains what it is required to deliver (i.e. forecast outputs) over CP7.
- 1.4 Setting funding and outputs on a five-year basis is designed to facilitate efficient and longer-term decision-making by providing stability and certainty about what the railway (including the supply chain) needs to deliver. It also helps ensure an enduring focus on the periodic review's core objectives (see Box 1.1).

Box 1.1: The periodic review's four core objectives

The periodic review will focus on the delivery of four key fundamentals (recognising that there may be a trade-off between these depending on the level of funding available):

- **Safety:** the rail network must be maintained in a safe condition for all of its users, workers and the public;
- **Performance:** the railway must be customer focused, making effective use of its capacity to deliver passenger and freight services that are punctual and reliable;
- **Asset sustainability:** assets must be planned and managed to deliver their greatest value over the course of their operational lives; and
- **Efficiency:** Network Rail must be subject to stretching but realistic efficiency targets.

- 1.5 Among other things, the [Williams-Shapps Plan for Rail](#) recommitted the government to five-year funding for rail infrastructure and said that Great British Railways (GBR) will be held accountable for delivery of the commitments made in PR23 when it succeeds Network Rail. Further detail on the interaction between PR23 and rail reform is set out in Box 1.2.

Box 1.2: PR23 and rail reform

- As set out in the Williams-Shapps Plan for Rail, the UK and Scottish Governments will continue to provide five-year funding settlements for rail infrastructure during and following the implementation of the reforms. There will be separate funding arrangements for train operations. The UK Government has indicated that GBR will adopt, and will be held to account for, delivering the PR23 commitments that Network Rail enters into.
- Existing devolved administrations and authorities across GB will continue to exercise their current powers and responsibilities.
- At this stage, we are carrying out the PR23 process under the current legal framework. PR23 will continue to focus on Network Rail's infrastructure management activities rather than wider aspects of the rail system. Network Rail is also developing its business plans for CP7 on this basis. However, we would expect the principles contained within this document would apply regardless and, where opportunities present themselves, we will adapt accordingly.
- The UK Government has set up a transition team (GBRTT) to help manage Network Rail's transition to GBR, amongst other things. We will work closely with Network Rail and GBRTT to ensure that the outcomes of PR23 are aligned with funders objectives and the expectations of the future GBR.

Process for establishing CP7 funding and outputs decisions

- 1.6 The periodic review is a cross-industry, collaborative process. Figure 1.1 below illustrates the key stages, as well as the roles and responsibilities of ORR, funders and Network Rail.
- 1.7 As noted above, governments decide the level of funding they will make available to Network Rail and what, in return, they want it to deliver. This is likely to reflect each funder's strategic priorities. For England & Wales, these relate to (amongst other things) the five strategic objectives as outlined in the whole-industry strategic plan (WISP), namely meeting customers' needs; delivering financial sustainability; contributing to long-term economic growth; levelling-up and connectivity; and delivering environmental sustainability. For Scotland, Ministers' priorities include the decarbonisation of rail by 2035; improved resilience and asset management; growing the freight market; and meeting the net cost challenge. This periodic

review is taking place in a challenging macroeconomic environment and funders may have difficult decisions to make for CP7.

1.8 Funders will set out their decisions (separately) through two key documents:

- the **High-Level Output Specification (HLOS) document** that sets out the funder's objectives and what it wants the railway to deliver; and
- the **Statement of Funds Available (SoFA) document** that sets out the level of funding it will make available to deliver the corresponding HLOS.

1.9 To help inform the decisions set out in the HLOS and SoFA documents, we will provide **formal advice** to each funder, which we expect to issue early this summer. This will be based on our assessment of Network Rail's initial CP7 plans (see below), as well as our wider holding-to-account work and other analysis. This is part of wider and on-going engagement with funders about CP7 funding and outputs.

1.10 Once funders have issued their HLOS and SoFA documents, and we have reviewed Network Rail's SBPs, we will issue:

- a **formal determination** that sets out our decisions on Network Rail's overall funding and outputs to be delivered over CP7 (i.e. whether the funding available will deliver the outputs). We will do this separately for England & Wales and for Scotland; and
- **separate settlements** for each region and the System Operator (SO) in Network Rail, which set out our expectations about the funding that will be allocated to them and the outputs that will be delivered by them. Further detail on Network Rail's structure can be found in Annex A.

1.11 As part of its continuous business planning approach, Network Rail will submit its business plans for CP7 at key stages throughout PR23, including:

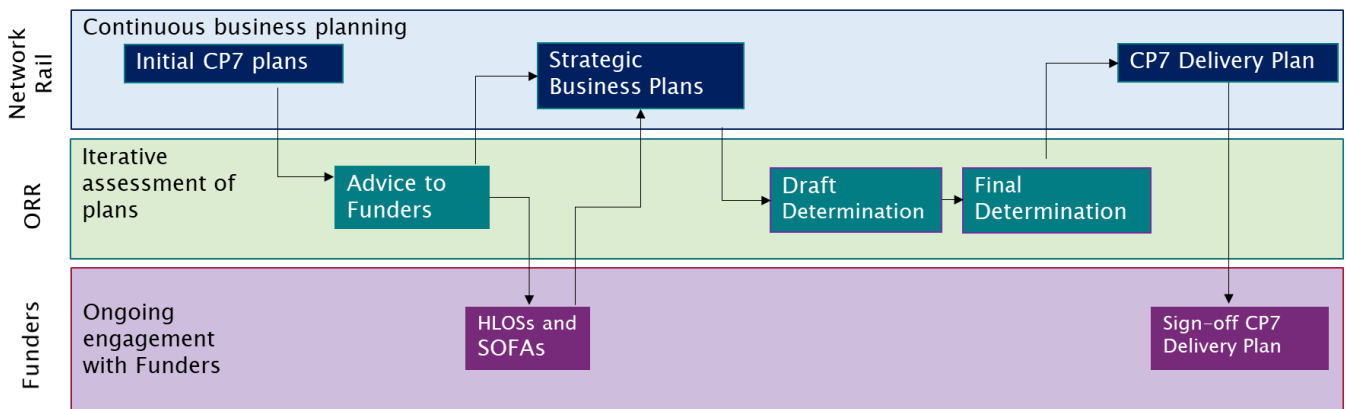
- the **initial CP7 business plans** for England & Wales and for Scotland, which Network Rail is due to submit by the end of March 2022. These plans help inform our advice to funders and, in turn, the HLOSs and SoFAs. Reflecting the fact that the plans are developed at least two years before the start of CP7, they are reasonably high-level (i.e. they are not based on bottom-up assessment of the needs of each asset). Reflecting wider fiscal challenges facing the industry, we understand Network Rail's initial CP7 plans will

include options around different funding levels alongside implications for different outputs (e.g. performance and asset sustainability);

- the **SBPs (or Strategic Business Plans)**, which Network Rail is due to submit in early 2023, that are used to produce our PR23 determination and settlements. These are more developed than the initial CP7 plans and have been informed by (for example) bottom-up business planning by each of the regions/routes (where relevant); and
- the **Delivery Plan for CP7**, which builds on the SBPs to reflect our PR23 determination and settlements (assuming Network Rail accepts this determination). This sets out how Network Rail will deliver what it has been asked to. The Secretary of State (having taken into account the views of the Scottish Ministers) signs off the final version of the plans that Network Rail will use to deliver its OSMR activities in CP7. We expect to use this plan to hold Network Rail to account for delivery of its CP7 commitments.

1.12 We understand that Network Rail is developing its plans in a way that puts greater focus on the whole system context. This is intended to deliver plans that better reflect the needs of passengers and freight users.

Figure 1.1: Roles and responsibilities and key milestones in determining funding and outputs



2. Network Rail's CP7 business plans

Key points

- Network Rail's regions, national functions and the SO each prepare CP7 business plans, including initial CP7 plans, SBPs and the Delivery Plan.
- The CP7 business plans will evolve over time and set out: (1) the expected outputs that Network Rail will aim to deliver, based on the expected income and expenditure in the plans; (2) the expected OSMR expenditure; and (3) the income that Network Rail expects to receive over CP7.

Areas of Network Rail's business plans

- 2.1 For each iteration of its business plans, Network Rail will set out the objectives, outputs and activities it will seek to deliver, as well as forecast expenditure. It will do this for its entire GB-wide activities and separately for England & Wales and for Scotland, as well as for each region and function. The plans should also set out how Network Rail's engagement with funders, customers and other stakeholders have informed the plans. In advance of each iteration of the key business plans, we work closely with Network Rail to set out our expectations of the scope and structure of the submissions. For the purposes of the SBPs, we may provide formal and/or public guidance to Network Rail in this area, as we did for PR18.
- 2.2 Across all plans, Network Rail will cover three key areas of business planning: **outputs**, **expenditure** and **income** forecasts. We address each of these below.

Outputs

- 2.3 Network Rail's CP7 business plans will identify the expected outputs that it aims to achieve, based on the expenditure and income forecasts. This will cover its core areas of responsibility, including (but not limited to) health and safety, train performance, asset management and efficiency.
- 2.4 For the initial CP7 plans, we expect Network Rail to set out what it will deliver against funders' priorities (to the extent these are clear) and for its customers and stakeholders, including in the key areas of safety, train performance, asset

sustainability and efficiency. This should also reflect how Network Rail is complying with its legal obligations (relating to, for example, health and safety or environmental). Network Rail will do this for each region and function, though we would not expect the initial CP7 plans to include detailed quantified forecasts for all measures at this stage.

- 2.5 For the SBPs, we would expect Network Rail to articulate in more detail the full range of outputs and outcomes it would expect to deliver, with quantified forecasts where appropriate. This reflects the fact that, once funders have issued their HLOSs and SoFAs, Network Rail has more certainty about the outputs it needs to deliver and the level of funding available to it. The SBPs would need to include, where appropriate, forecasts for each region/function and by year. Network Rail will provide a consolidated SBP for England & Wales and for Scotland, as well as a GB-wide plan.

Expenditure forecasts

- 2.6 The business plans will also set out Network Rail's OSMR forecasts. We describe each expenditure area below:

- **operations expenditure**, which is the cost associated with enabling the operation of train services. This includes, for example, the costs associated with signallers and mobile operations managers;
- **support expenditure**, which refers to activities such as human resources or information technology;
- **maintenance expenditure**, which is the cost of maintaining the rail infrastructure assets. It includes, for example, repairing (but not replacing) infrastructure assets and the cost of asset inspection; and
- **renewal expenditure**, which is the cost associated with renewing (i.e. replacing) parts of the rail infrastructure. It is usually undertaken when it is no longer efficient to maintain the assets and relates to work on tracks, bridges, tunnels, signalling, drainage and earthworks, amongst other assets. Typically, this makes up the single biggest component of Network Rail's OSMR spend. All renewal expenditure is capital expenditure.

- 2.7 Network Rail refers to OSMR as 'controllable' expenditure because it can influence spending levels and the mix of spend. In addition, the business plans also include forecasts for other types of expenditure that Network Rail has less control over

(‘non controllable’ expenditure). These include wider industry costs such as traction power and business rates.

- 2.8 Network Rail’s initial CP7 business plans will include a high-level view for each year of forecast expenditure, including for each element of OSMR and for each asset area, as well as by each region and function. This should be based on realistic assumptions about what it will deliver for the rest of CP6 (reflecting that performance in CP6 will impact delivery in CP7) and give a reasonable indication of the level of overall spend necessary to deliver the outputs included. They will also include options that Network Rail could take forward if enough funding is available.
- 2.9 Network Rail’s SBPs will also provide a view for each year of forecast expenditure for each element of OSMR and for each asset area, as well as by each region and function. However, reflecting that the SBPs will be informed by bottom-up planning, we would expect more detail on the level of forecast spend, as well as the rationale for it.
- 2.10 For PR23, we expect Network Rail’s business plans to exclude expenditure on enhancement-related projects, including large-scale electrification projects. However, reflecting that enhancement projects can influence OSMR expenditure, we would expect the plans to set out baseline assumptions about enhancements to explain their impact on OSMR activities.

Income forecasts

- 2.11 The business plans will also set out the income that Network Rail will expect to receive over CP7.
- 2.12 Network Rail’s key income streams consist of the funding that governments will make available through the SoFAs and the revenue that passenger and freight operators (as users of the network and stations) pay through track access contracts. Network Rail also generates other income for example, revenue from property rental and sales and advertising.

3. General approach to assessment

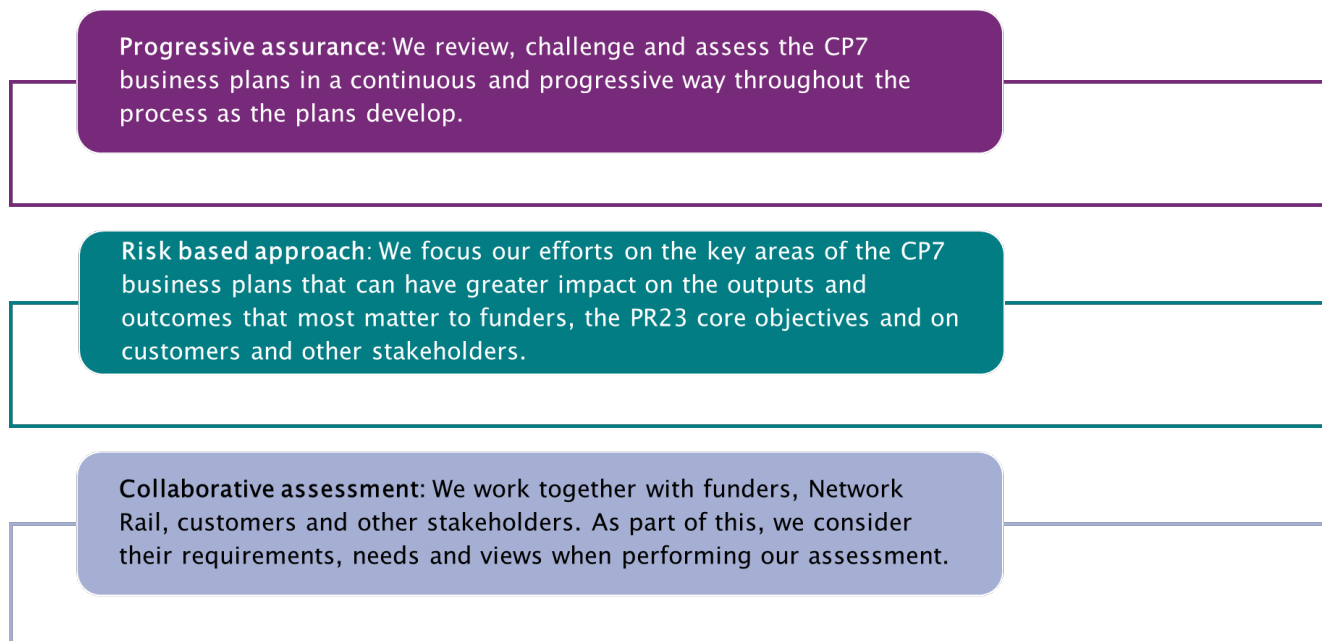
Key points

- Our assessment involves reviewing, challenging and assessing Network Rail's CP7 business plans. The objective is to determine whether the plans are likely to enable Network Rail to meet its legal requirements and that the SBPs and the CP7 Delivery Plan are consistent with funders' HLOSs and SoFAs and our PR23 core objectives. We will also consider how customers and other stakeholders' views have been taken into account.
- We use a risk-based, progressive-assurance and collaborative approach to assess Network Rail's plans. Our team is multi-disciplinary and will consider a wide range of sources of information.
- Our **expenditure and output assessment** considers whether the forecast outputs in the business plans (individually and when considered as a whole) and the associated expenditure are consistent with funders' priorities and PR23 objectives.
- Our **income assessment** reviews Network Rail's forecasts for areas such as property income from sale and rental, and revenue from Network Rail's access charges.
- Once a funder has issued its SoFA and HLOS, we also undertake an affordability assessment that brings together our assessments relating to expenditure, outputs and income to determine whether there are sufficient funds in each SoFA to meet the associated HLOS. We do this separately for England & Wales and Scotland.

Principles of our approach

- 3.1 We base our assessment of Network Rail's business plans around three key principles, as set out in Figure 3.1 below.

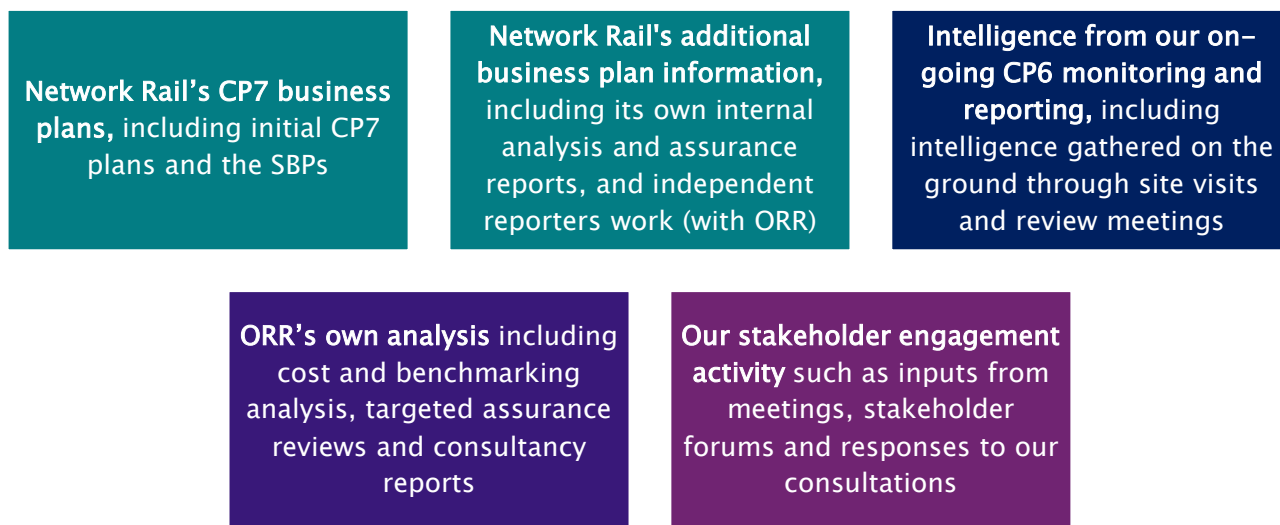
Figure 3.1: Principles of our assessment approach



Our assessment 'toolkit'

- 3.2 Our assessment is a cross-office exercise that draws on our expertise in economic regulation, railway engineering and operations, regulatory finance, cost management and health and safety. We use a multidisciplinary approach and multiple sources of information to do our assessment.
- 3.3 While Network Rail's CP7 business plans are the starting point of our PR23 assessment, we also use a range of additional evidence to assess the CP7 business plans. This is illustrated in Figure 3.2.

Figure 3.2 Key sources of evidence to assess the CP7 business plans



Network Rail's complementary business plan information

- 3.4 We make use of a wide range of additional, supporting information to inform our assessment.
- 3.5 The nature of the information differs depending on whether it is provided as part of the initial CP7 plans or the SBPs though, as a minimum, is likely to include Network Rail's deliverability assurance report and financial risk and efficiency analysis.
- 3.6 We also review evidence from Network Rail's stakeholder engagement to understand how it has engaged with its stakeholders and taken account of their views. For our assessment of the SBPs, we will consider (for example) the extent to which Network Rail has engaged with its passenger and freight operator customers to agree train performance forecasts.

Intelligence from our CP6 monitoring and reporting

- 3.7 We monitor and report on Network Rail's activities across its activity areas. This provides useful information and evidence to help inform our assessment of Network Rail's CP7 business plans.
- 3.8 Our monitoring activities include intelligence gathered on the ground from site visits, safety inspections and from our review meetings with Network Rail's regions

and national functions, as well as our ongoing analysis of Network Rail's performance. Our reporting activities are similarly wide-ranging and include, for example, our [annual review on the progress](#) that Network Rail is making on delivering the current CP6 plans, as well as our [annual financial and efficiency assessments](#).

Our own wider analysis

3.9 We also rely on evidence produced from our own internal analysis, including:

- **our knowledge and experience, along with the results of our 'challenge sessions' with Network Rail:** This includes applying our knowledge to the assessment of Network Rail's plans and using challenge sessions to probe the reasons for Network Rail's income and expenditure assumptions and whether they are appropriately justified;
- **our internal analysis on specific areas:** This includes, for example, our analysis of the historical links between output performance and related expenditure levels, [targeted assurance reviews](#) (TARs, which we undertake to gain a more in-depth understanding of an issue), cost analysis and comparisons among regions' business plans, analysis of the forecasts included in the business plans and of the underlying business planning assumptions;
- **our cost benchmarking statistical analysis:** This is a top-down statistical analysis technique. We use this analysis to complement our understanding of the relationship between Network Rail's key cost drivers and its efficiency; and
- **input from external independent parties.** This includes, for example, our [independent reporter](#) reviews that we use to enhance our knowledge in particular areas where we have a gap, or to target areas where we have concerns over Network Rail's performance. We also commission stand-alone consultancy studies to address specific issues (e.g. we are currently procuring specialist consultants to review Network Rail's early forecasts relating to property rental and sales income).

Our stakeholder engagement activity

3.10 As discussed in Chapter 2, we expect Network Rail to engage with funders and stakeholders throughout the development of its business plans. It should also

explain how this engagement has informed or changed its plans and make clear if there are issues where it has not been possible to address concerns.

- 3.11 ORR regularly engages with funders as well as industry groups (e.g. Rail Delivery Group, Railway Industry Association). We also continue to meet with individual stakeholders to discuss specific issues. This engagement will help inform our advice to Ministers and our determination.
- 3.12 Ahead of our Final Determination, we will consult formally on the proposed allocation of funding and outputs to each region and function and by activity area. Stakeholders will have an opportunity to engage with us on this, including by providing a formal response.

Structure and content of our assessment

- 3.13 Our assessment focuses on Network Rail's forecasts with respect to its expenditure and outputs and its income. We also consider whether there are sufficient funds in each SoFA to meet the associated HLOS (our affordability assessment); see Box 3.1 for further details.
- 3.14 It is important that our assessment takes into account the prevailing circumstances. This will include:
- Network Rail's plans and assumptions for recovery from COVID-19;
 - changes to passenger behaviour in recent years;
 - the interactions with rail reform; and
 - the wider fiscal challenges.
- 3.15 Our assessment will put particular focus on ensuring Network Rail is being as efficient as is realistically possible and can deliver the HLOSs for the funding set out in the SoFAs. Network Rail's CP7 business plans should draw out any areas where there could be long-term implications on health and safety, asset condition and performance of the network. As part of this, we will assess how Network Rail is planning to manage any emerging risks.
- 3.16 We explain each area of our assessment below.

Expenditure and output assessment

- 3.17 Our expenditure and output assessment is wide-ranging. Generally, we assess whether the forecast outputs in the business plans (individually and when considered as a whole) and the associated expenditure:
- enable Network Rail to meet its legal obligations (noting that it is not our role to tell Network Rail how to do this);
 - are consistent with funders' priorities;
 - are aligned with the PR23 four core objectives around safety, asset sustainability, train performance and efficiency;
 - consider customer and other stakeholder views, such as freight operators and the supply chain; and
 - are realistic but stretching to provide the right incentives for Network Rail to deliver.
- 3.18 For the purposes of our advice to Ministers, we review the initial CP7 plans to consider whether the plans have made reasonable assumptions based on the guidance provided by the funders.
- 3.19 We do a more detailed assessment of the SBPs to determine the funding needed to deliver the HLOSs and the allocation of funding across regions, the SO and national functions, as well as the output to be delivered in CP7.
- 3.20 For PR23, we have also identified a set of key focus areas (set out in Chapter 4) against which to assess the business plans. This approach should enable us to ensure that the business plans are delivering against funders' priorities, the PR23 core objectives and customer and other stakeholder needs. Chapter 4 of this document sets out our approach in more detail.

Income assessment

- 3.21 It is important that Network Rail's other income forecasts (i.e. income from sources other than the network grant or network charges) are appropriate as, all other things being equal, this income reduces the amount of funding it requires. The focus of our review will be Network Rail's CP7 forecast for each source of other income. We will consider whether there are any gaps and further opportunities Network Rail should be exploiting or whether its market assumptions are realistic.

To do this, where practical, we will compare Network Rail’s forecasts to those of comparable businesses.

3.22 For the purposes of our advice to Ministers, we review the initial CP7 plans to consider the extent to which the plans make appropriate assumptions about income streams that are clearly explained and consistent with the wider plans.

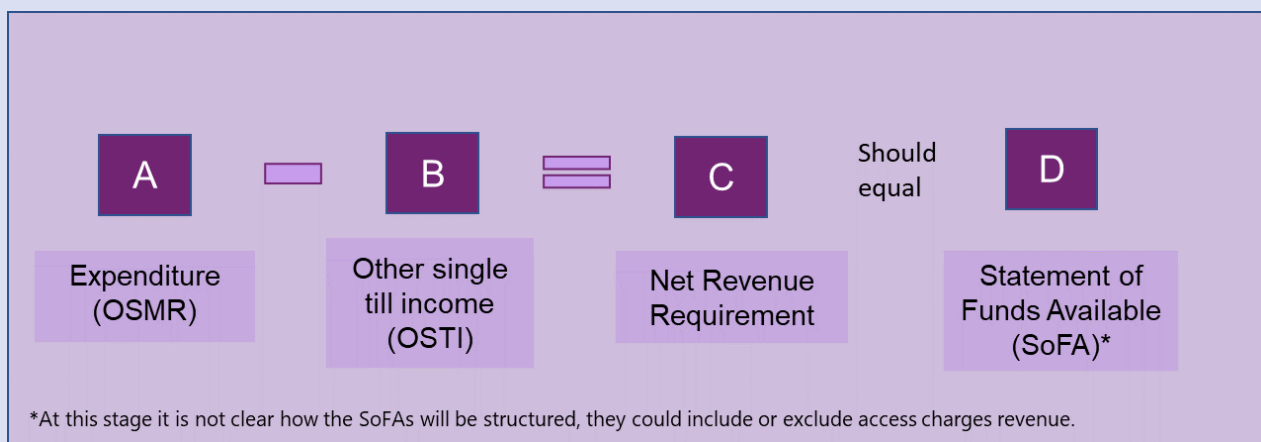
3.23 We will place particular focus on Network Rail’s assumptions for property income from sales and rentals. We will review the Group Property Unit’s business plan as well as the regions’ plans for property within their control. We have a particular interest in understanding the long-term impact of COVID-19 and potential for recovery. This reflects that our most recent annual efficiency and finance assessment shows Network Rail’s property income has significantly reduced because of the pandemic.

3.24 We will also review Network Rail’s forecast of income received from access charges, to ensure this reflects the latest assumptions about traffic volumes and the CP7 charging framework.

Box 3.1: Our affordability assessment

- Once a funder has issued its HLOS and SoFA, we will assess whether there are sufficient funds available in the SoFA to deliver the associated outputs in the HLOSs. We complete our assessments separately for England & Wales and Scotland. We will do this by comparing Network Rail’s forecasts with the assumptions in the funder’s HLOS and SoFA. Figure 3.3 below explains the steps involved in our mismatch assessments:

Figure 3.3: ORR’s affordability assessment



- Network Rail must do everything reasonably practicable to deliver the outcomes within the funding available. However, if we consider that there are insufficient funds to meet the associated outputs, we are required to notify the relevant government, which may then revise its HLOS and/or SoFA.

4. Areas of our assessment

Key points

- Our assessment of the regional business plans will focus on the following issues: health and safety, asset management, deliverability, cost efficiency and allocation, train performance, financial risk management, innovation and technology adaptation, environment, and accessibility. We will also consider how these aspects of the plans relate to each other and what they may mean for Network Rail's overall delivery.
- Our assessment of the SO's business plan will consider each of its key accountabilities, including its role in capacity allocation, timetabling, strategic planning, and delivery to freight and national operators.
- Our assessment of the business plans will evolve as the plans become more detailed.

Health and safety

- 4.1 Our assessment considers the extent to which Network Rail's plans – if implemented – are likely to enable Network Rail to continue to operate its network safely and in line with its legal requirements. It is not our role to tell Network Rail how it should meet its legal obligations. Our assessment of health and safety is undertaken alongside our review of the plans' asset management, cost and efficiency assessments (which we discuss below).
- 4.2 We expect to pay particular attention to, for example:
- weather resilience, including the extent to which Network Rail is addressing the risk of derailments;
 - industry-wide changes to fatigue management (including their impact on rostering and resourcing) and local commitment to the continued implementation of health improvement initiatives;
 - other specific areas of concern (including those highlighted through our inspections) such as metallic structures (bridges), ash-die back and harmful polychlorinated biphenyls (PCBs) in location cabinets; and

- the impacts and mitigation measures relating to any proposed deferrals of renewals and changes to the frequency of inspections and maintenance of the network.

4.3 For the **purpose of our advice to Ministers**, our review considers the extent to which the initial plans are broadly appropriate in enabling Network Rail to deliver health and safety outcomes. As part of this, we consider, for example, whether the initial plans:

- have a clear health and safety strategy;
- address existing health and safety concerns, where applicable;
- have identified relevant health and safety issues for further, more in-depth review (in advance of the SBPs); and
- have identified any potential trade-offs in the delivery of key strategic health and safety outcomes that Network Rail may need to make.

4.4 For the **purposes of our determination**, we consider in more detail whether the SBPs have sufficiently demonstrated that Network Rail can continue to operate its network safely and in line with its legal requirements. As part of this, we also consider whether the SBPs demonstrate a suitable health and safety strategy.

Asset management

4.5 Our assessment considers the extent to which Network Rail's CP7 business plans support the delivery of what funders want and enable Network Rail to maintain and renew the infrastructure network in an appropriate manner. Our assessment of asset management is closely linked to a number of other areas including cost assessment and innovation (which we discuss below).

4.6 For the **purposes of our advice to Ministers**, our review considers whether Network Rail's initial CP7 plans demonstrate a reasonable approach to understanding its asset base and to allocating the resources available in a way that reflects funders' strategic objectives. We also highlight any areas of concern we think need to be addressed in the SBPs. As part of our review we consider, for example, whether the initial plans:

- take due account of safety, long-term asset needs and performance;
- take account of funders' priorities (where these are clear) and identify the choices funders have available to them;

- are based on clear, appropriate asset management policies;
- include appropriate justification for the volumes of proposed work, including by year, asset type and region (this will also consider likely actual renewal volumes given the absence of any separately allocated risk funding in the initial CP7 plans); and
- identify the implications for asset sustainability and management (including at an England & Wales and Scotland level).

4.7 To support this work, we have already completed several [TARs](#) that will form part of our assessment of the initial CP7 plans. This includes reviews into Network Rail's asset management, procurement of on-track machines, structures examination, drainage maintenance, earthworks weather resilience, and the hot weather resilience of overhead line equipment.

4.8 For the purposes of our determination, we consider in more detail whether the SBPs have sufficiently demonstrated Network Rail's ability to maintain and renew the infrastructure network in line with funders' requirements (set out in the HLOSs) for the funding available (set out in the SOFAs). We expect to pay particular attention to whether the SBPs:

- are consistent with the requirements funders have set out in their HLOSs;
- are based on whole-life cycle cost considerations such that Network Rail is not creating cost or deliverability risks for the longer term (e.g. by delaying renewals). If the funding is not sufficient to deliver a minimum whole-life cycle cost, we will assess whether Network Rail has made appropriate trade-offs (e.g. whether it has appropriate mitigations in place if a renewal is being delayed);
- address specific areas of concern, such as metallic structures (e.g. bridges), earthworks, ageing of the infrastructure and complexity of the system;
- address the challenge of weather resilience and climate change adaptation in CP7 and beyond;
- reflect an appropriate allocation of funds between the regions, the SO and other functions; and
- whether the plans address any concerns we (e.g. through our TARs) or other parties have raised.

Deliverability

- 4.9 Our assessment considers the extent to which Network Rail and its supply chain can deliver its plans. As part of this, we expect to consider changing rail demand and the scope to optimise track access in delivering works, as well as the impact of other, competing infrastructure (e.g. HS2) on the capability of the supply chain to deliver work. We also consider how Network Rail should be required to report on its delivery (e.g. through particular measures) to provide transparency and confidence to funders and stakeholders.
- 4.10 For the **purposes of our advice to Ministers**, we consider whether the planned volumes of renewals work as set out in the initial CP7 plans are realistic based on our knowledge about the capacity and capability of Network Rail and its supply chain. We will also specifically consider whether the initial plans:
- give appropriate consideration to the likely CP6 exit point;
 - reflect appropriate input from key stakeholder groups, including the supply chain; and
 - reflect the findings of Network Rail's own internal assurance.
- 4.11 For the **purposes of our determination**, we consider deliverability in more detail, including the extent to which the SBPs:
- show a level and profile of expenditure across the control period (and across the regions and national functions, the SO and central functions) that is likely to be deliverable with the resources available;
 - are based on a programme of work that appropriately considers and plans for available access to the network in England & Wales and Scotland to undertake engineering works;
 - reflect input from the appropriate range of stakeholders required to help deliver the plans;
 - consider the potential disruption of renewals on customers; and
 - identify and support a smooth transition from CP6 to CP7 and from CP7 to CP8.

Cost efficiency and allocation

- 4.12 Our cost and efficiency assessment considers whether Network Rail's CP7 plans include an appropriate level of efficiency improvements for CP7 (i.e. one that strikes a balance between being challenging and achievable). Further information on how we assess efficiency is set out in Annex B.
- 4.13 For the **purposes of our advice to Ministers**, we consider whether the initial CP7 plans:
- include appropriately challenging and stretching efficiency assumptions in the forecasts;
 - have appropriate proposals for delivering efficiency savings (noting that the detail in the initial plans is reasonably high-level at this stage); and
 - have a sufficiently robust allocation of costs between England & Wales and Scotland to inform funders' decisions.
- 4.14 For the **purposes of our determination**, we will assess whether the SBPs include:
- a realistic and efficient level and mix of OSMR expenditure, including a level of efficiency improvements that are sufficiently challenging and achievable; and
 - an appropriate allocation of the national functions' business plans costs to the regions and the SO.

Train performance

- 4.15 Train performance refers to the punctuality and reliability to passenger and freight services. Our assessment considers whether Network Rail has included appropriate train performance forecasts in its CP7 plans. We also review how the regions and the SO have considered and plan to manage potential risks to train performance.
- 4.16 As part of this, we expect to pay particular attention to key drivers of performance, including the impact of Network Rail's plans and its assumptions about how the railway transitions to a post-pandemic environment.
- 4.17 For the **purposes of our advice to Ministers**, we consider whether the initial CP7 plans:

- have considered the CP6 exit point in terms of performance and the rate of post-pandemic recovery;
- explain the key drivers of future performance, including how the plans could drive improvements or effectively manage a situation where services are reduced;
- use reasonable assumptions to underpin the analysis;
- use measures that we understand, have been discussed with stakeholders and are aligned with what is known about funder objectives and priorities;
- propose measures that cover the full range of operators (including freight); and
- forecast the level of train performance to be delivered in CP7, including by region and key user group (e.g. freight).

4.18 For the **purposes of our determination**, our assessment focuses on whether the SBPs set appropriate performance trajectories for CP7 that:

- are consistent with each funder's HLOS;
- take account of customer and stakeholder priorities;
- are deliverable in light of CP6 exit position; and
- are appropriately stretching and realistic in light of the HLOSs.

4.19 We will also consider whether the SBPs identify potential risks to delivering train performance and have in place appropriate plans to manage this.

Financial risk management

4.20 Our financial risk management assessment considers whether the CP7 business plans have sufficiently identified and quantified the financial risks that Network Rail faces and how Network Rail will manage them. This includes looking at financial risks emerging from inflation pressures, cost shocks or adverse weather events. Our assessment will be carried out at both an England & Wales and Scotland level.

4.21 For the **purposes of our advice to Ministers**, we consider whether the initial plans:

- identify the range of risks Network Rail may face and sets out an appropriate risk management approach;
- identify, at a high level, the level of risk funding that might be needed and where that will come from (e.g. from changes to renewals plans);
- clearly show underlying expenditure that is consistent with a P50 approach and whether this is clearly set out. P50 represents the project cost with sufficient funding to provide a 50% level of confidence in the outcome (i.e. there is a 50% likelihood that the final project cost will not exceed the funding provided); and
- allocates risks and risk funding between England & Wales and Scotland on a clear and appropriate basis.

4.22 We also consider whether the explanation of the level of risk is consistent with current performance and risks, and we will flag to funders any gaps we identify.

4.23 For the **purposes of our determination**, our assessment of the SBPs will consider in more detail whether Network Rail has set out a robust risk management plan. We will consider, for example, whether there is sufficient risk funding in place that reflects the scale of the risks, including whether risk funding has been appropriately allocated to regions, the SO and national functions. We will also consider whether appropriate governance procedures are in place to manage risk during CP7.

Innovation and efficient technology adoption

4.24 Our assessment considers whether the proposed Research and Development (R&D) related activities:

- support delivery of PR23 objectives and funder priorities, as well as reflecting whole-system challenges and opportunities;
- reflect engagement with local stakeholders and operational staff in a way that identifies the needs and opportunities for innovation; and
- appropriately allocates the costs and benefits between England & Wales and Scotland.

4.25 We also consider the methodology used to estimate likely return on investment (ROI) of R&D projects and how this accounts for different success rates of projects

at different levels of maturity. We will also assess the benefits the CP6 programme has delivered.

- 4.26 As part of this, we review the scope of proposed R&D activities, the governance framework, the level of funding included and the benefits that will be delivered, as well as their timing.
- 4.27 For the **purposes of our advice to Ministers**, we consider whether the initial CP7 plans:
- identify appropriate opportunities for R&D during CP7;
 - appropriately consider a whole-system approach to R&D; and
 - reflect the benefits of previous R&D and innovation (e.g. whether they demonstrate how Network Rail will embed the benefits of R&D). We recently conducted a TAR into Network Rail's performance in adopting technology into its business-as-usual activities.
- 4.28 For the **purposes of our determination**, we will consider in more detail whether the SBPs' proposed R&D-related expenditure levels and activities are appropriately targeted to support PR23 core objectives, funder priorities and customer/stakeholder needs. We will also consider the methodology used to estimate likely benefits of R&D-related projects.

Environment

- 4.29 It is increasingly important that Network Rail considers both the impact climate change has on its infrastructure and activities and the wider environmental sustainability of its plans. This is relevant to all areas of Network Rail's activities, in particular its asset management plans and proposed approach to (for example) decarbonisation, air quality, biodiversity, and weather and resilience adaptation.
- 4.30 Our assessment focuses on the extent to which Network Rail's proposed expenditure, activities and outputs are in line with funders' objectives, as well as wider legislative requirements and industry standards. We will also take into account the fact that there is different legislation in England & Wales and Scotland in relation to environmental targets. For example, [The Climate Change Act 2019](#) commits Scotland to net-zero emissions by 2045, whereas England & Wales will have until 2050.

- 4.31 For the **purposes of our advice to Ministers**, we consider whether the initial CP7 plans:
- identify appropriate activities to deliver environmental outcomes; and
 - consider funders' expectations around environmental issues (e.g. carbon reduction).
- 4.32 We will also identify any other areas we consider Network Rail should focus on when refining its plans.
- 4.33 For the **purposes of our determination**, we will consider whether the SBPs:
- are consistent with each funder's expectations as set out in the relevant HLOS;
 - appropriately prioritise issues such as resilience to climate change; and
 - provide sufficient detail in the SBPs for ORR to appropriately hold Network Rail to account.

Accessibility

- 4.34 Accessibility is about ensuring that all customers, including disabled or aged customers, can access railway services easily. It is Network Rail's responsibility to ensure its business plans meet the required accessibility performance thresholds in relation to Network Rail's passenger-facing activities at their managed stations.
- 4.35 Much of Network Rail's funding to make rail services more accessible falls outside of the periodic review process. However, OSMR expenditure can support accessibility. For example, renewals expenditure may be used to improve how a station platform is configured to support on/off boarding of trains. Furthermore, expenditure on support costs is used to provide information and passenger assistance at Network Rail-managed stations (e.g. staff training, station guides, information on passenger assistance).
- 4.36 For the **purposes of our advice**, our review considers whether the plans have taken into account the accessibility needs of customers, to the extent possible and appropriate.
- 4.37 For the **purposes of our determination**, we consider in more detail whether the SBP has sufficiently demonstrated that Network Rail has taken due account of accessibility. Specifically, we will consider whether the SBPs have reflected any

HLOS requirements and are aligned with relevant public policies (including DfT's 2018 Inclusive Transport Strategy and Transport Scotland's Accessible Transport Framework as set out in the 2020 National Transport Strategy).

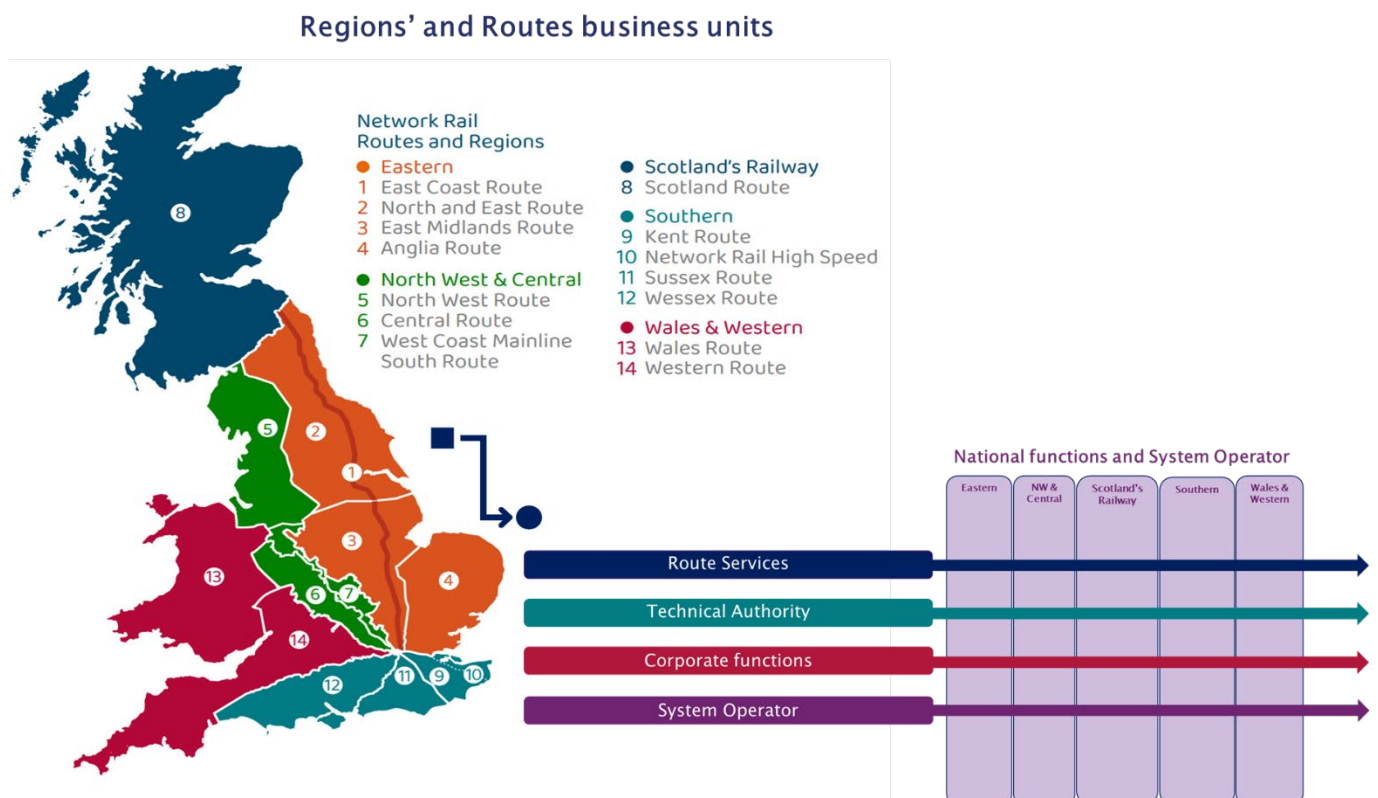
System Operator

- 4.38 The SO is a business unit within Network Rail that is responsible for certain system operation activities, including strategic planning, managing changes to what the network delivers, producing the timetable and selling access to the network.
- 4.39 Our work reviewing and challenging the SO's plan is an important aspect of our overall assessment of Network Rail's plans, reflecting the key role it plays in providing services to operators and wider customers. Our assessment considers each of the SO's key accountabilities. We expect to pay particular attention to, for example, the SO's plans for delivering (and reforming, where appropriate) industry timetabling processes and strategic planning (including in the context of the forthcoming WISP and in a way that supports funders' requirements).
- 4.40 For the **purposes of our advice to Ministers**, our review focuses on whether the initial CP7 plans:
- provide appropriate funding for the SO to carry out its functions; and
 - gives sufficient consideration of delivery for freight customers, including the extent to which the SO has ensured freight's requirements are integrated across its activities (e.g. capacity allocation).
- 4.41 For the **purposes of our determination**, we will consider in more detail the SO's proposed outputs and expenditure, as well the governance arrangements, and underlying strategies. We will consider whether the SBPs have sufficiently demonstrated how the SO will deliver its capacity, access and timetabling function as well as how it supports the strategic planning of the network and network integration.

Annex A – Network Rail’s current business structure

1. Network Rail’s structure reflects the infrastructure and system operation activities it performs, plus all the required business support activities. Figure A.1 below depicts Network Rail’s current structure.
2. For PR18, we made route settlements along with a separate settlement for the SO (as well as the Freight & National Passenger Operator (FNPO) business unit, whose responsibilities now broadly sit with the SO following a Network Rail reorganisation). Early in CP6, Network Rail restructured itself meaning these routes now sit within 5 regions. We expect to adopt a similar approach to the regions and the SO for PR23. We will be consulting on our wider regulatory framework for CP7 in more detail in our consultation in Summer 2022.

Figure A.1 Network Rail’s current structure



Source: Network Rail

3. Reflecting Network Rail’s devolved structure, there are five regions responsible for the OSMR activities of the regional rail network infrastructure. The regions are made up of

14 routes. Routes are responsible for the day-to-day delivery of train performance and the relationships with their local train and freight operating companies and other regional stakeholders. Routes are accountable to regions.

4. The SO is responsible for system operation and co-ordinating activities across the regions, including timetabling, capacity allocation, network integration and strategic planning. The role of the SO has evolved since PR18. Since early 2021, the Network Strategy Operations and Freight, National Passenger & Customer experience teams from the Network Services directorate all moved into the SO.
5. In addition, Network Rail also has other business units that perform important business support activities, which are referred to as national functions. These include:
 - **Route Services**, which supplies Network Rail's routes with services that the national team is best placed to provide (e.g. supply chain operations, some procurement and IT). These services are brought together into a single, service delivery directorate. This approach allows national co-ordination where appropriate, and for Network Rail to benefit from economies of scale and greater efficiency from specialised delivery;
 - **Technical Authority**, which provides technical leadership in areas including health and safety, sustainability and managing quality and information, providing support and delivering assurance for the safe, reliable and effective functioning of infrastructure assets; and
 - **Corporate functions**, which are business units that include areas such as Chief Financial Officer (CFO) unit, human resources, communications and business transformation programmes. The CFO includes corporate finance, legal, property unit, and risk and assurance. The property unit provides advice on retail and rental strategy to each of the regions, which ultimately have accountability for their own property portfolios.

Annex B – Network Rail’s ‘post-efficient’ cost plans

1. Network Rail produces its ‘post-efficient’ cost plans as follows:

- Prepare CP7 plans based on a set of ‘pre-efficient’ cost assumptions: Network Rail prepares OSMR expenditure plans for CP7 based on a set of initial ‘bottom-line’ costs. Network Rail calculates these initial bottom-line costs assuming it is no more efficient than at the end of CP6. It refers to the resulting bottom-line costs as ‘pre-efficient’ costs. Network Rail uses these business plans as a baseline to quantify the cost efficiencies it is forecasting for CP7;
- Analyse the impact of general inflation and other cost pressures that it considers to be largely outside of its control (referred to as ‘headwinds’ and ‘tailwinds’): Network Rail forecasts the impact on the bottom-line ‘pre-efficient’ costs from general inflation (based on the consumer price index (CPI)), as well as headwinds and tailwinds. For example, this could include the financial impact from a change in input prices or taxation;
- Analyse the impact of efficiency improvements: Network Rail forecasts the efficiencies it will aim to deliver over CP7. Network Rail does the quantification with reference to the bottom-line ‘pre-efficient’ costs. Network Rail is expected to use a mix of bottom-up and top-down approaches to assess the level of efficiencies it can deliver in CP7; and
- Finalise CP7 plans based on a set of ‘post-efficient’ cost assumptions: As explained in Figure B.1 below, Network Rail calculates the post-efficient OSMR expenditure by starting with the ‘pre-efficient’ costs and adding the quantified impacts from headwinds and tailwinds and efficiency improvements. Network Rail refers to these plans as the ‘post-efficient’ cost plans.

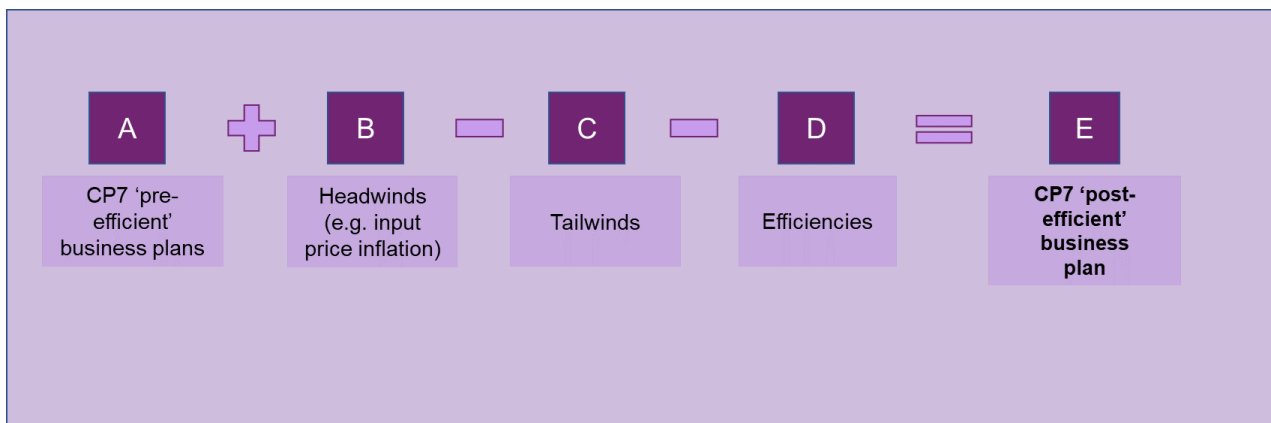
2. To support the ‘post-efficient’ cost plan calculations, Network Rail’s CP7 business plans and supporting information will include details about:

- the evidence it has to show that its efficiency and headwind forecasts are appropriately challenging. This will include the use of ‘top-down’ benchmarking and ‘bottom-up’ analysis of required work activities. This

should be supported by the use of independent consultancy studies as appropriate;

- how it will deliver the efficiency improvements in CP7, minimise headwinds and maximise tailwinds; and
- the challenges that it anticipates in delivering these forecasts and how it will seek to mitigate them.

Figure B.1: Calculation of the 'post-efficient' cost plans





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