Will Godfrey
Director Economics, Finance and Markets
Office of Rail & Road
25 Cabot Square
London E14 4QZ

Paul Marshall
Group Finance Director
Network Rail
The Quadrant:MK
Elder Gate
Milton Keynes MK9 1EN

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By email only

Dear Will,

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

I write in response to your letter of 31 March 2023 which set out ORR's views on Network Rail's period 11 re-forecast ('RF11') delivery plan update.

I welcome ORR's confirmation that Network Rail's RF11 plans are consistent with DfT's financial limits for 2023-24. We appreciate ORR's positive engagement and constructive challenge during this review process. The purpose of this letter is to acknowledge your findings and to provide additional clarity on some of the key themes raised.

Management of financial risk

Our risk funds have enabled us to efficiently respond to significant issues during CP6, such as Covid-19, high inflation, extreme weather events and industrial action. The risk funds, by their design, were not intended to be used to cover risks within a current year. We have processes to manage our risks and make sure that there is a plan ahead of each year to spend any unused risk funding on additional asset management activities. Therefore, as planned, all risk funds have been allocated within the 2023-24 plan. We will continue to monitor and manage risks during 2023-24. Should any of those risks materialise, we will make informed, balanced asset management decisions to reprioritise or defer activities based on safety, performance and value for money.

We have policies, processes and governance at route, region, function and national level to challenge and assure ourselves that risks are acceptably managed when we make changes to our plans. For example, we have:

- a clear process for the deferral of asset renewals where we risk assess the change, increase maintenance and use other controls such as speed restrictions, as required.
- a safety validation process for organisational change, which is overseen by ORR.
- enterprise risk management, business assurance committees and a national audit and risk committee to check that risks are adequately controlled.

There has been recent dialogue between ORR and our chief health, safety and well-being officer to aid understanding of these processes and provide ORR with further information where needed.

Looking towards 2024-2029, our CP7 Strategic Business Plan sets out our planned approach to managing financial risk and uncertainty in CP7. It notes that we will not have sufficient funding to separate out and hold risk provisions in that plan at the same level as we have in CP6.

Impact of very high inflation on NR's income and costs

Inflation has been extremely high during 2022-23 and inflation risk will continue to be volatile during 2023-24. We use the latest inflation rates issued by the Office of Budget Responsibility when reforecasting our plans. However, it is challenging to predict how contractor behaviour may impact changes to the costs of existing contracts, through variation orders, or increases to new contracts over the next year. We will continue to monitor the risks and impacts of inflation throughout 2023-24.

Renewals profiling

Our total CP6 renewals expenditure is 2% lower than previously forecast. This is because funding has been diverted to mitigate the impact of inflation, train performance and industrial action. As previously mentioned, we will continue to monitor and manage risks during 2023-24 and reprioritise or defer renewals activities if necessary.

We understand that you are interested in the impact that changes to our CP6 plans may have on our CP7 plans. We will continue to update both plans over the next year and our business planning process will focus on making sure the forecasted CP6 exit position and transition into CP7 are aligned.

Outputs

I appreciate that you recognise many of the positive steps we have taken this year in improving our annual scorecard including the governance around 2023-24 target setting, earlier engagement with our chief executive and positive changes to our train accident risk reduction metric.

Although our 2023-24 performance targets for CRM-P (consistent region measure – performance) and FDM-R (freight delivery metric – region) are in many instances lower than our regulatory baselines, we are targeting an improvement from our current performance. These targets stretch us to achieve better performance whilst also being realistic and acknowledging the current challenges that are impacting train performance across the industry. You will note in our recent letter exchange on train performance that all regions and System Operator have developed improvement action plans. We will continue to update ORR on progress against those plans through our regular engagement meetings.

In addition, the joint performance strategies between Network Rail and the operators for 2023-24 set out the priorities and interventions that we are all committing to deliver to improve performance outcomes for passengers and freight users. These documents are shared with the ORR as part of our annual planning process.

Implications for CP7

We reforecast our CP6 plans at four intervals during a year and use the latest available CP6 exit forecast to inform the evolving CP7 plans. We stated as a key assumption that our CP7 Strategic Business Plan used "a forecast CP6 exit position for expenditure and outcomes, as at period 9 of financial year 2022/23" (RF9). ORR's review of our CP6 plans were conducted on the RF6 and RF11 forecasts in 2022-23. Both CP6 and CP7 plans will continue to be updated, and inform each other, over the next year.

Next steps

We will continue to engage with ORR as we update our plans during 2023/24. Should you have any questions in the meantime, please don't hesitate to contact me.

Yours sincerely,

Paul Marshall

Group Finance Director