

Network Rail's response to ORR's Draft Determination: CFO directorate

31 August 2023

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Executive summary

Corporate Services includes areas such as the Chief Financial Officer (CFO) directorate, Group Human Resources (HR), national communications and business transformation programmes.

The Chief Financial Officer's (CFO) directorate brings together key business areas of the corporate core. It provides leadership and strategy, compliance and governance, as well as group wide professional services.

There are eight key functions within the CFO Directorate that deliver a variety of leadership, governance, and service roles:

- Audit and Risk
- Group Finance
- Corporate Finance and Business Development
- Group Property
- Planning and Regulation
- Legal and Corporate Services
- Corporate Commercial
- Rail Investment Centre of Excellence (RiCoE)

Non-controllable costs are also included within the CFO directorate which funds external industry bodies such Railway Safety and Standards Board (RSSB), Office of Rail and Road (ORR) and Railway Heritage Trust (RHT).

Key changes to our CP7 plan since submission of the CP7 strategic business plan in February 2023, include:

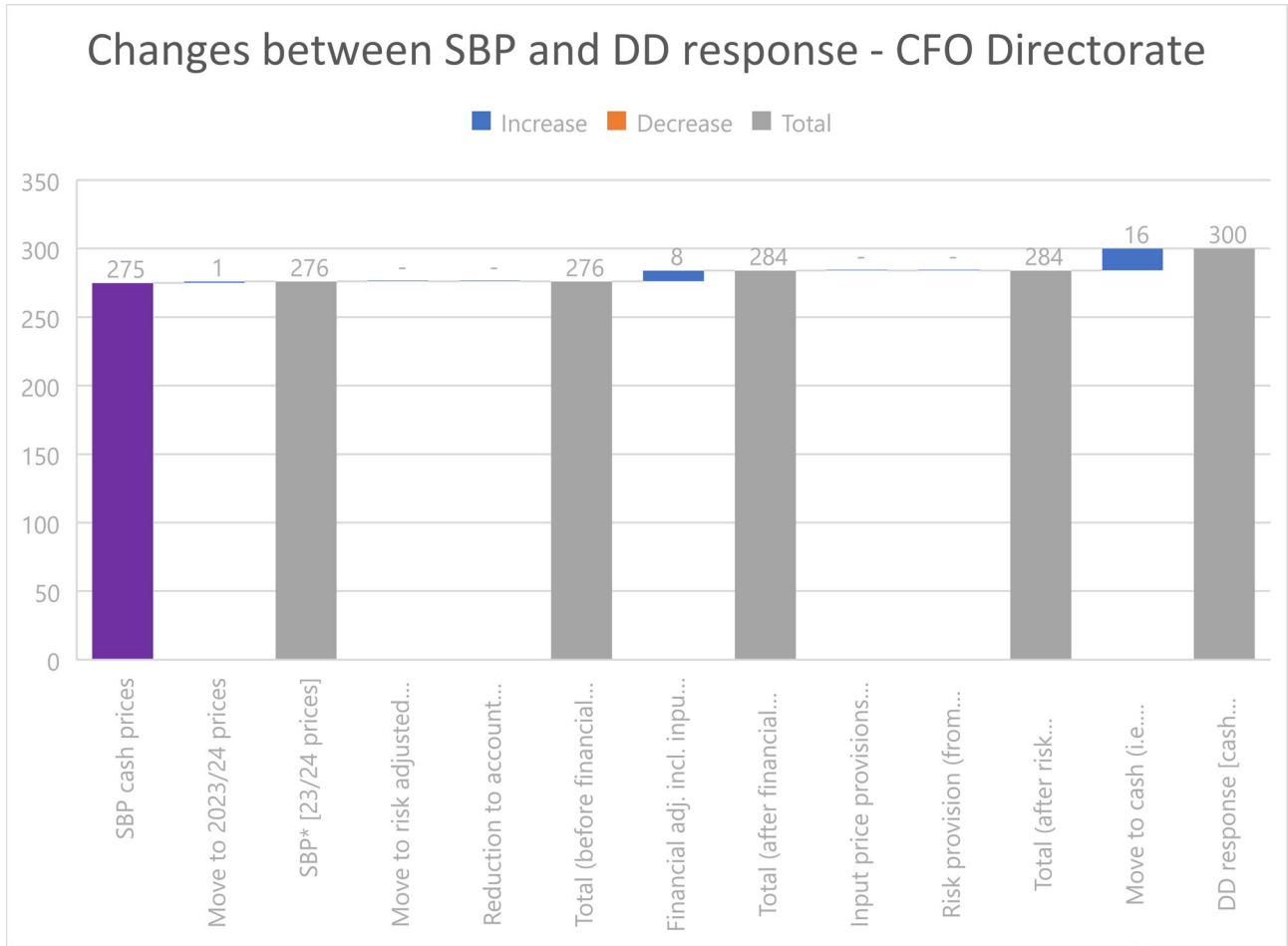
- A 1.2% additional funding stretch on our CP7 plan to respond to the funding pressures faced by Network Rail
- Changes to Industry costs seen in Year 5 of control period 6
- Updates to headwinds and input prices that are consistent (in approach) with other functions and in line with ORR's draft determination findings
- Phasing has been reviewed and updated for all areas of Corporate Services

ORR's draft determination findings deemed that "...Corporate Services expenditure in the SBP lacks detail on increases in expenditure". The increase in industry costs from the SBP submission is detailed below.

ORR suggest Group Property income forecasts are conservative. The response to this will be covered in the Other Income response template.

The CFO directorate is continuing to engage with regions and wider stakeholders and has the right governance arrangements in place to ensure there is delivery against stakeholders' priorities, and for both the UK and Scottish Governments' HLOS priorities.

Figure 1: Waterfall of changes between SBP and DD response – CFO Directorate



CFO directorates response to ORR's PR23 draft determination settlement document

1. Introduction

This document is our response to ORR's PR23 draft determination findings on CFO directorate. We also provide an update on any key changes to our CP7 plan since submission of the CP7 strategic business plan in February 2023.

We cover GB-wide activities. We have considered how our updated plans and response to ORR's draft determination impacts delivery of both the UK and Scottish Governments' priorities within available funds, as set out in their respective High Level Output Specifications (HLOSs) and Statements of Funds Available (SoFAs).

Following the publication of ORR's draft determination, we have reviewed and considered ORR's draft proposals, decisions and actions, in relation to our activities. This document sets out our response on these areas. To inform this response, we have undertaken a targeted review of our CP7 strategic business plan (SBP), as part of our iterative CP7 plan development process. This update has also been reviewed and assured by subject matter experts where relevant. Recognising the limited time available to update, assure and consolidate CP7 plans, our approach has been necessarily targeted and high-level.

As we have moved through the rounds of CP7 planning, our CP7 planning assumptions have evolved as funding and government requirements have become clearer, as business requirements have matured, and as new information has emerged about the level of inflation we expect to face in CP7.

The key changes we have made since submission of our SBP to ORR in February 2023 can be summarised as follows:

- **Funding / guiderails:** Whilst overall the cash funding for CP7 has not changed since the SBP submission (it is fixed by the England & Wales and Scotland SoFAs), inflation forecasts are higher and so an additional stretch of 1.2% has been applied to CFO directorate to reflect the funding pressures Network Rail face and ORR's draft determination proposals. For CFO directorate, this stretch amounts to £3.4 million.
- **Inflation:** ORR's draft determination suggests considering "*reflecting the revised cost of inflation assumption in its CP7 forecast*". The Round 7, Part B submission has been updated to reflect the latest May 2023 Bank of England CPI inflation forecasts which is higher than the November 2023 OBR forecast used in Round 6, and higher than the March 2023 OBR forecast used in Round 7, Part A.
- **Input prices:** ORR's draft determination suggests considering "*reflecting the revised input price inflation assumptions in its CP7 forecast*". As a result, input price assumptions have also been updated to reflect the latest inflation forecasts. Our latest submission increases by £7.6 million to reflect input price inflation for E&W and Scotland.

- **Headwinds:** ORR's draft determination suggests considering "*reflecting the revised headwinds assumption in its CP7 forecast*". The latest submission is now reflective of the lower level of headwinds that we identified in the SBP as an overlay to region and functions' strategic plans. Our latest submission reduces by £2.6 million to reflect headwinds for E&W and Scotland.
- Changes to property income will be covered within the Other Income response template.
- **Efficiencies:** The changes above have a resulting impact on efficiencies, as such the efficiencies generated by the CFO Directorate have reduced by £0.4 million.
- **Phasing** has been reviewed and updated for all areas of Corporate Services to reflect existing spend patterns and a ramp up in activity towards the final year of the control period. Efficiencies phasing has also been updated to be evenly distributed across the control period. No changes have been made to phasing for Group Property.
- These changes align with ORR's proposed financial adjustments (to input prices, inflation, headwinds, property income) in the draft determination findings and we will continue our collaborative approach in discussing the latest inflation forecasts and assumptions with ORR.

2. Our response to ORR's draft determination findings on CFO directorate

Network Rail has followed a reasonable approach to aligning its National Functions' plans to available funding, including regional engagement and prioritisation.

ORR's draft determination finds "*... Corporate Services expenditure in the SBP lacks detail on increases in expenditure, noting the headcount reduction already made in CP6. We are asking Network Rail to provide further clarification, but this area may present an opportunity to contribute to further cost reduction in the final delivery plan*".

Industry costs accounted for within non-controllable costs such as ORR and RDG costs have seen an increase of £7m across Control Period 7, this is reflective of the CP6 cost base. There are no changes to Property Cumulo rate assumptions.

The determination also goes on to state "*In the light of headcount reductions in the National Functions that have taken place in the latter half of CP6, we concluded that there would be limited potential for further operational expenditure cost reductions from levels proposed in the SBP.*"

Whilst we are in agreement with this statement, since the submission of the CP7 strategic business plan in February 2023, an additional 1.2% funding stretch has been applied to CFO directorate to respond to the funding pressures faced by Network Rail.

The CFO directorate (excl. Property) has responded to this challenge by proposing to amend the Business Development strategy for CP7. Group Property is proposing to increase the stretch on efficiencies via workplace accommodation strategy to meet the 1.2% funding stretch. Reducing any further Network Rail discretionary activity such as Business Development will have a direct impact on staff satisfaction levels, particularly on resourcing and equipping staff to work effectively with the tools provided, - a statement which scores low on the Your Voice survey

‘Network Rail provides me with the tools and resources I need to be productive in my work’. This statement also from the Your Voice Survey has a direct impact on our ability to deliver against the ‘Safety and Security’ element of the HLOS requirements.

We have already taken steps in CP6 to deliver efficiencies through the MM programme and identify further efficiencies in CP7. As we look to address the 1.2% additional saving, we will explore additional efficiency opportunities in our plan although we note that this will be challenging.

3. Governance and stakeholder engagement

The CFO Directorate continue to assess and deliver the needs of regions and wider stakeholders by engaging with regions and ensuring the right governance arrangements are in place so that there is delivery against stakeholders’ priorities. Our approach is broken down in Figure 1 below.

Figure 2: ORR set of expectations in CP7 in relation to the National Functions

Expectation	Comment	CFO directorate approach
Clear governance arrangements which facilitate customer engagement and internal holding to account	Lines of engagement between the National Functions and the regions should be transparent and structured. The regions should have means by which they can challenge the National Functions and ensure their views are taken into account in decision making.	Engagement is led separately within each functional area through Regional Directors (e.g. Regional Property Directors, Regional Business Development Directors, and Regional Finance Directors) and through account lead relationships with key internal customers (e.g. Corp Commercial team in the CFO Directorate supporting Regional assurance).
Transparency around their activities and how they are assessing and delivering against the needs of stakeholders	We expect to be provided with clarity on, for example, the business plans, priorities, and challenges for the National Functions. As stakeholder engagement has supported the development of their SBPs, we expect this engagement (and delivery against the outcomes from this) to be a continued focus for them across CP7.	Broadly speaking, our customers in the regions and national functions have told us that they want a ‘warm welcome’, meaning we should be clear on the why and the value, know ourselves better, and seek to build relationships. They also want us to ‘listen to understand’ so that we better understand our customers, think about their needs and challenges, as well as engaging and empathising with their local challenges. Finally, they want us to ‘own it and make things happen’

		through being proactive, collaborative, and setting clear expectations of the service offering.
Timely and efficient delivery of core programmes on behalf of the regions	In CP7 the National Functions have responsibility for some organisation-wide programmes. Timely and efficient delivery of these is key for the benefits (e.g., performance, safety, asset management) of these to be realised. Clear measurement and reporting of the benefits delivered by the programmes.	The CFO Directorate leads national efficiencies and supports the regions and national functions on a number of key projects e.g. Project Reach, Carbon Reduction. There is strong governance in place across all our major programmes involving all major regional and functional stakeholders in the challenge and ongoing review.
Clarity over how they are responding to concerns raised by Network Rail's regions and System Operator, ORR or wider stakeholders	We expect to be provided with assurance that these concerns are being prioritised and addressed in a timely fashion. Our approach here will be in accordance with our Holding to Account policy.	Concerns raised about the CFO Directorate will initially be dealt with through functional engagement forums e.g NBACs, FRGC, FCGC, RIDAB. As well as ELT (as required), or through the Holding to Account policy as applicable.

Annex A: Sign-off

Job Title	Name	Signature	Date
Managing Director	Paul Marshall		