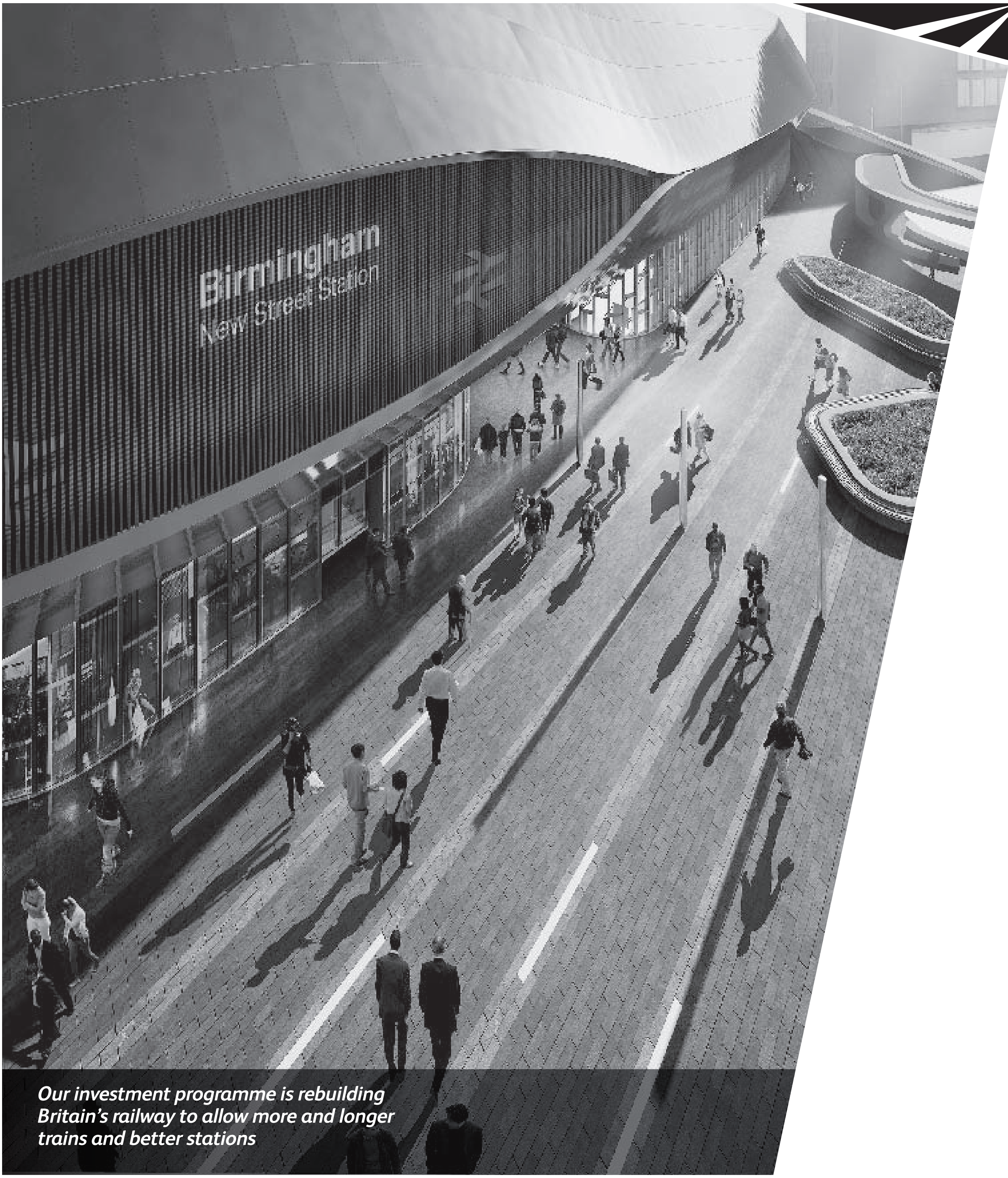
Network Rail Limited
Annual Report and Accounts 2010

Moving ahead
Helping Britain Prosper

NetworkRail



Our investment programme is rebuilding Britain's railway to allow more and longer trains and better stations

Helping Britain Prosper

The £600m investment in redeveloping Birmingham New Street station will help regenerate parts of Birmingham city centre and create thousands of jobs in the area, contributing over £2bn of economic benefits

Contents

Foreword

Rail is one of the most important elements in the UK's transport mix, with over 1.3bn passenger journeys made by rail every year. It is a sector which has grown rapidly since privatisation after years of decline, neglect and lack of investment under state control.

Between 2009 and 2014, the current regulatory period, Network Rail is tasked with relieving passenger overcrowding by getting more and longer trains onto the rail network and improving punctuality and reliability. At the same time the Company is driving out costs from its operations and improving efficiency – to make train travel better value.

To deliver its goals Network Rail is focused on both major projects that eliminate delays and allow more trains to run and smaller projects that reduce the cost of running the railway. Major projects include building and opening the Airdrie-Bathgate line – a new route between Edinburgh and Glasgow designed to improve connectivity and stimulate economic regeneration; more seats and trains for the Bedford-Brighton line that runs through central London; and untangling the railway that runs through Reading and removing a major source of delays.

At the same time Network Rail is implementing hundreds of projects to reduce the cost of running Britain's national rail network. Projects include re-engineering track renewals to drive down unit costs; introducing 'intelligent infrastructure' which allows Network Rail to remotely monitor the busiest parts of the network to predict and prevent faults; and closing user-worked level crossings to improve safety and reduce operating costs.

Rail is a key backbone infrastructure of a thriving, developed economy and an important element of the country's response to climate change. As polluters are increasingly forced to pay for their carbon emissions, the strategic advantages of rail – electrically driven trains fuelled by low carbon power stations combined with dedicated, congestion-free routes directly into our major cities – will come to the fore. Now and in the future, Network Rail is Helping Britain Prosper.

Network Rail is focused on both major projects that eliminate delays and allow more trains to run, and smaller projects that reduce the cost of running the railway.

Our performance

Safety

Maintaining and improving safety is our first priority. Britain's railways are the safest they have ever been and among the safest in the world. Our aim is to make them even safer for passengers, the public and our staff.

11th year

Improved inspection and maintenance once again resulted in fewer broken rails in the year – the 11th successive year of reduction.

14%

There has been a 14 per cent improvement in workforce safety. Sadly, however, there were three workforce fatalities during the year. We will always strive for zero fatalities.

Reliability

Britain has one of the most intensively used railways in the world yet trains are now more punctual than at any time since records began.

91.5%

Punctuality for the year at 91.5 per cent reached a new all-time record, up from 90.6 per cent.

3%

The number of train miles travelled increased 3 per cent last year (9 per cent over the past five years).

£1.6bn

We spent £1.6bn in enhancing the network in the year.

Efficiency

By the end of Control Period 4 in 2014 we will have reduced the cost of operating, maintaining and renewing Britain's rail infrastructure by 42 per cent since 2003.

£3.25bn

£3.25bn is being invested in over 2,000 stations all across the country during CP4.

£2bn+

Network Rail generated over £2bn cash from operations – all of which has been invested straight back in the railway.

↓£265m

We reduced the costs of running the railway by £265m.

↓35%

On average freight costs have fallen by 35 per cent in the year. Charges to passenger train operators were also reduced seven per cent, the equivalent of 22p per passenger train journey.

In Control Period 4 we are committed to get even more trains on the network, more of those trains on time, and to make the railway even safer.

People

We continue to recruit, train and invest in our staff as we build a highly-skilled and motivated workforce. By improving the skill base we can deliver more work in-house, spending less on contractors.

-£21m

We saved £21m on reduced overtime and fewer labour contractors during the year.

20%

Our annual Gallup employee survey shows levels of employee engagement are 20 per cent higher than last year.

3,000

Our new National Centre will bring 3,000 jobs to Milton Keynes.

Future

In Control Period 4 we are committed to get even more trains on the network, more of those trains on time, and to make the railway even safer. We are committed to delivering a £24bn programme of investment, reducing the cost of running the railway by over a fifth. And we are committed to reducing the number of times passengers arrive at a station expecting a train, and find themselves ushered onto a rail replacement bus service.

Over 2009/10 we have made good progress towards meeting our targets and delivering a bigger, better railway for passengers, freight and the whole of Britain.

↓24%

We are aiming to reduce the cost of operating, maintaining and renewing the rail infrastructure by 24 per cent between 2009 and 2014.

92.6%

By the end of CP4 our target is that 92.6 per cent of trains arrive on time.

Financial highlights

For the year ended 31 March 2010	2010 £m	2009 £m
Revenue	**5,668**	6,160
Operating profit	**1,993**	2,556
Profit after tax	**292**	601
Net cash from operating activities	**2,234**	2,811
Net debt	**(23,847)**	(22,319)
Net assets	**5,944**	6,622
Railway network fixed assets	**36,629**	34,925
Investment property	**764**	700
Capital expenditure	**3,920**	4,743

Chairman's statement

Future ambitions demand far greater industry collaboration and require Network Rail to look outward more.

This year is the first year of Control Period 4, the quinquennial regulatory settlement running to 2014 and it has been a solid one for Network Rail

The Company has generally performed ahead of plan financially and operationally, adapting well to some exceptional challenges along the way. Iain Coucher, Chief Executive, and Patrick Butcher, Group Finance Director, provide more detail in this report. It has also been my first year as Chairman, a role I took over from Ian McAllister at the Annual General Meeting in July 2009. Ian did a great job as Network Rail's first chairman, in establishing the Company and leaving a legacy of an accomplished management team. However, my role, inevitably, will have a different emphasis appropriate to the current context.

For the last eight years there has been an uneasy consensus, but nonetheless a consensus that has held. This has been around 'doing the right thing'. Putting right what was wrong. Fixing broken rails. Rebuilding the West Coast. Making trains run on time.

But now we are in a new phase – recovering from a recession and with a climate of public spending cuts – in which rail users' interests and those of the taxpayer are not necessarily aligned. For the rail industry to remain credible with Government and continue to grow, we must be alive to the wider context and be prepared to discuss new approaches, trade-offs and compromises.

My role in this evolution, as the non-executive Chairman of Network Rail, is to lead the Board and motivate the Company's executive to act in the best interest of Network Rail in serving the rail industry as a whole, delivering a highly safe, highly effective and efficient railway. To do this I act as an independent chairman. My role is not to run the Company that is the job of Iain Coucher and his executive. My role is to lead the Non-Executive directors in their task of supporting Iain and his team while holding them to account for Network Rail's performance and approach as well as challenging the Company to question continually its remit and the value it delivers.

To achieve this end, I have had three immediate responsibilities. First to sharpen the primary governance of the Company, recruiting new Non-Executive Directors and improving the scrutiny and assurance approaches. Secondly, to encourage a fresh assessment of the progress of the Company and its future challenges. Thirdly, to act as a champion for the high quality conversations that I regard as crucial to taking the industry forward.

I am pleased to report that that we have made progress in two of the three areas.

The new Board is taking shape. Lawrie Haynes brings great project and leadership experience from Rolls-Royce, the nuclear industry and the Highways Agency. Janis Kong, a former director of BAA plc where she held positions as managing director of Gatwick and chairman of Heathrow, brings both asset management and consumer experience. Graham Eccles brings vast railways experience from several train operators while David Higgins, the current chief executive of the Olympic Delivery Authority, provides us with major programme management experience as well as his property credentials from English Partnerships and Lend Lease.

While the Board is not yet complete it is substantially changed. I would like to express my thanks to those who will no longer serve – Jim Cornell stood down at last year's AGM, Ian Buchan during the year and Yvonne Constance and Chris Green will stand down at the AGM in July.

The primary governance processes have been modified in many ways including the manner in which we seek to be accountable to Members for the quality and effectiveness of this governance.

Meanwhile, the new independent Directors have been making their own assessment of the Company – its past, its present and its future challenges.

Our appreciation for what has been achieved since the creation of Network Rail is unqualified and universal. Difficult decisions were taken in difficult circumstances as a necessarily centralised, 'command and control' approach to recovery paid dividends. The team is to be commended and thanked for what they achieved through their guile, commitment and perseverance.

Future ambitions, however, demand far greater industry collaboration and require Network Rail to look outward more, recognising that it can only succeed it if engages fully with our key delivery partners – our customers, suppliers, rolling stock companies, our regulator and Governments. Meanwhile, as the Company seeks to develop beyond the initial 'command and control' approach that was so crucial to progress in the recovery phase, the goodwill and engagement of our very loyal and talented staff, especially those at the front line, will determine how quickly we can all move forward.

Herein lies our toughest present challenge. We are good at winning the rational battles – as tends to be the strength of engineers and operations management specialists – but we have yet to learn fully how to win the emotional ones. A pervasive improvement of these relationships is our number one priority, key to our own change in culture and, arguably, more broadly.

For only then should we even hope to champion credibly the conversations that can quell the ambient relationship noise in our sector, transcend the challenge of a dwindling public purse and permit us to all fully capitalise on this moment of exceptional aspiration for the railway.

Rick Haythornthwaite
Chairman
3 June 2010

Chief Executive's review

Britain's railway is the busiest it has been since 1946. It is also now the safest and the most punctual since records began. But it could be even better. Iain Coucher reviews a year of good performance and looks forward to the challenges ahead.

This year's annual report is called 'Moving ahead. Helping Britain Prosper', why's that?

I genuinely believe that no company is more vital to Britain's success than Network Rail. Rail is vital to help Britain prosper. It brings economic benefits in the shape of jobs and growth. But also it delivers social inclusion – connecting communities and of course, the sustainable and environmental credentials of rail are clear.

We have just come through an epic election campaign, but for me, what was most satisfying, is that all political parties – despite the straitened financial situation the country faces – recognise the benefits of sustained investment in rail.

All party leaders travelled extensively by train during the campaign. They will all have seen how the rail industry has been transformed in the last decade. We now have the most punctual railway ever recorded, more passengers using it than any time in the last 60 years and the safest railway we have ever had. The public now recognises this and this is reflected in record levels of passenger satisfaction and politicians recognise it too, demonstrated by their new-found strong support for an expanding railway.

Is Network Rail going to get squeezed by spending cuts?

Let's not forget between 1945 and 1995 the railway was in decline – the public and politicians had fallen out of love for it. So, the railway was privatised as a declining asset and no significant expansion or investment was planned. Now, politicians and the public see it differently.

Network Rail is conscious of the fact that Britain's finances are going to be tight in the coming years. However, our financial settlement agreed with the Office of Rail Regulation is secure and in the last year we have been entrusted to deliver around £2bn of additional upgrades to the network. These are projects on top of what was agreed in the periodic review and include schemes such as electrification, the Edinburgh-Glasgow improvement programme, Evergreen 3 and station improvements.

The National Centre will help us build great teams, inspiring better ways of working through an exciting and innovative environment.

In short, in the last eight years Network Rail has gone from rescuing the railway, to fixing the basics, to running a high-performing railway and today being an organisation that Britain trusts to deliver vital infrastructure improvements. This transformation is a testament to the hard work of everyone who works on the railway.

To maintain support for investment in the railway, we have to accept that Network Rail needs to continue to change. In reviewing the last year I cannot omit talking about the current industrial disputes we face. We managed to avoid a damaging national rail strike and we hope the disputes can be resolved by negotiations. If we agree the changes we need the prize for passengers is a more cost-effective railway, with more trains running earlier in the morning, later at night and at weekends and the prize for our people is secure, skilled British jobs.

What are you doing to meet the tough efficiency targets set by the ORR?
As well as running a high-performing and safe service we have a duty at Network Rail to deliver a railway at a price that Britain can afford. This means taking costs out of our business year on year. We achieved a lot in the last control period – cutting overheads by 27 per cent – but in this current control period we have to make further efficiency savings of 24 per cent. We have in place a transformation programme that should allow us to hit these targets.

This is tough. This means we have to look at everything we do and ask ourselves how we can deliver the same or better outputs in a more efficient and smarter way. This means looking at technology, processes and the way we organise our people.

Some examples of how we are achieving more with less include the investment we have made in new technology. For example, we now have a fleet of 26 tilting wagons which can deliver pre-assembled and tested rail, switches and crossings direct to site. The increased use of modular switches and crossings or modular bridges mean we can work much more swiftly to upgrade the railway. This means lower costs and less disruption to passengers with shorter closures of the railway.

How are you addressing the challenges of meeting efficiency targets in track renewals?
This has been a prime focus for us and we appreciate that difficult choices have been faced in our work with our supply chain. However, Network Rail makes no apologies from seeking best value and innovation from its contractors. We cannot sustain companies that cannot deliver this. We are committed to a competitive market in track renewals; this is good for our suppliers and good for the railway.

Achieving efficiencies in this area has been a major challenge for us in recent years. We fell short of the ORR's target of reducing costs by 30 per cent during CP3, only achieving 16 per cent. This means we have to work even harder. We are now working more closely with existing suppliers and increasing competitive tendering to drive down costs. This has resulted in volume reductions in the short-term but we have confidence that the changes we are putting in place will deliver the significant savings we need to achieve throughout CP4.

So, a new strategy for track renewals has been developed, building on a route-based approach. The new plan links the volume of renewal on a route to the impact of asset failure, the existing track construction and the levels of traffic experienced (measured in equivalent million gross tonnes per year); increasing use of component or partial renewal in the track programme; and route teams selecting an appropriate mix of maintenance, renewal and refurbishment on each route to achieve the target outputs.

How is Network Rail changing the way it organises itself to achieve its targets?
The way we organise ourselves as a company is vital to driving down costs too. In the last year we refocused our core activities under five headings: Planning, Network Development, Investment Projects, Asset Management, and Operations and Customer Service.

Allied to this is a thorough-going programme of looking at how and where our people work. Our Company thrives if our people can work in a collaborative and closer way, but too many of our people today are located in dozens of small and unsuitable locations. An exemplar of how we are addressing this is our new National Centre in Milton Keynes for which we have received planning permission to go ahead on 21 January 2010.

The National Centre will help us build great teams, inspiring better ways of working through an exciting and innovative environment. It will be a dedicated centre combining engineering, investment planning and management, logistics, operational planning, information management and national functions. It will enable us to accelerate the pace of cultural and behavioural change by bringing the right people together into a single location. The 400,000 sq ft building will be constructed on the site of the former National Hockey Stadium, bringing up to 3,000 jobs and revitalising an under-used corner of central Milton Keynes. Construction on site is expected to start in late summer, with the building scheduled to open in autumn 2012. The design for the new building includes a host of eco-friendly features including extensive 'living roofs' which will encourage diverse habitats for flora and fauna in the centre of the city and a rainwater harvesting system which will be used to flush toilets and irrigate landscaping.

All over the country we are investing in new facilities that will allow us to work more effectively. These include modern signalling centres at Didcot, Glasgow, Derby and South Wales; and new maintenance facilities such as our super depot in Cowlairs, Scotland. Giving our people great places to work drives up job satisfaction, productivity and culture change. This is good for our people and good for Network Rail.

What were your highlights of the last year?
As well as more trains than ever arriving on time and good safety performance there are a number of other items I would like to mention. This year saw significant work on many big projects; Reading, Birmingham New Street, Airdrie-Bathgate and Thameslink. This a huge step up in the delivery of our enhancement programme from £1.6 billion in 2009/10 to £2.5 billion in 2010/11, before a further increase to £3.3 billion in 2011/12.

But let me focus on some other stand-out activity. From my years at Network Rail I know that our people can always rise to a challenge in adversity. This was demonstrated in the sterling work they have done to keep passengers and trains moving in some brutal weather conditions last winter. I must pay special tribute to the work our people did to reconnect the community at Workington, in Cumbria, when fatal floods cut the town in two.

Train punctuality is what Network Rail is measured upon every day. It is a primary focus; not performance for performance sake, but because we know how crucial it is for passengers that their trains arrive on time.

We knew at Network Rail we had the ability and indeed the duty to do whatever we could for the beleaguered population of Workington so our engineers leapt into action to come up with a plan. We immediately found a site on wasteland just over ½ mile to the north of the existing station. We secured fast approval from the local council and the ORR to build a new, temporary station to reconnect the two halves of the town that have been cut off following flood damage to the footbridges and road bridges in the area.

Our decisive action and the great work of Northern Rail in laying on extra services, shows what we can do when we can cut through bureaucracy. There are lessons here for the rail industry to learn.

What are your immediate priorities?
Passengers now rightly demand a reliable and punctual train service. Mostly, day-in, day-out this is what they are getting. That is our day job, so it should be out of the ordinary when there are occasions that cause passengers' valuable time to be taken up by delays.

So what are we doing? Firstly we are making huge efforts to cut really long train delays and cancellations, as we know that this is greatest cause of frustration to passengers. We are now measured by the ORR in how we tackle this. During this control period we must reduce the cancellations and significant lateness by between 15 and 23 per cent. I can tell you that we have made good progress in the first year in the order of 6.1 per cent.

Performance across the network is good and improving. Yet, there is too much variance between the best performing train operators and others. Our job now is to get all of our customers up to high levels of punctuality and reliability, so that travelling by train is the first choice for passengers.

To do this we need to work ever more collaboratively with our customers to help them deliver for passengers. A good example of this is an initiative, working with the Association of Train Operating Companies and Passenger Focus, to further reduce the need for replacement buses at weekends and bank holidays. We know that passengers do not want their rail journeys interrupted by a bus journey. So, the industry has identified 20 key routes which carry 60 per cent of all weekend passengers. With the operators, we aim to offer a rail journey between key stations on these routes, barring exceptional circumstances. This commitment will be progressively introduced over the next two years and will be monitored by Passenger Focus.

Underpinning all of this is our focus on providing world class asset management. We have made great strides in recent years to improving our infrastructure and the greater use of technology means we can work ever more effectively.

To deliver world class asset management we need a world class safety culture. As ever, this is a continuing priority for Network Rail. In the last year we introduced an 'all orange' policy for our track workers, making them more visible and safer.

How are you planning for the future?
This year Network Rail set the agenda by setting out its plans for the future, beyond CP4. In August last year we published the findings from our new lines study, a study we launched the previous year. We wanted to test the proposition that new, high-speed lines could be the answer to ever-growing demand for passenger services. Our study, we believe one of the most rigorous ever carried out, demonstrated a clear business case for a new high-speed line connecting London with Birmingham and cities in the north west of England and Scotland.

There have been various plans and ideas for high-speed rail that have been discussed recently. This is healthy and shows that there is widespread support from politicians and industry for high-speed rail. Network Rail has never said we have the definitive answers but our authoritative research has helped shape the debate. I firmly believe that high-speed rail is going to happen now and Network Rail has a crucial role to play. When the Government unveiled its preliminary plans for HS2 earlier this year we said high-speed is a vital part of a modern, dynamic economy. By slashing journey times, high-speed rail can drive economic growth and boost jobs. It would also take cars and lorries off the road, cut domestic flights and release capacity on the existing rail network; transforming services even for those communities not served directly by a high-speed line. It is the low-carbon, sustainable transport of the future.

We will need to see how the Government's proposals would expand the network. The railway is a system and we will work with Government to understand how high-speed lines can be developed to make the best use of capacity of the entire network.

Another example of Network Rail planning for the future, beyond the current control period, was our announcement in February of our plans to revolutionise rail in the north of England. We unveiled a £530m investment package to transform rail through better stations and quicker, more frequent services. The Northern Hub study identifies what needs to be done to respond to the significant growth seen in the region and to help drive economic prosperity.

The plans include a 40 per cent increase in trains per day across the region – 700 extra services; capacity for a further 3.5m passengers per year and quicker more frequent services for Newcastle, Liverpool, Manchester, Leeds and Sheffield.

The Northern Hub proposes significant investment in rail over the next 10 years to build on work which is already underway. By removing historic bottlenecks – such as at Manchester – it would allow faster linespeeds, reducing journey times. New track would give greater timetable flexibility – allowing fast trains to overtake and run at speed while still providing space on the network for vital local stopping services and freight.

How is train performance holding up?
Train punctuality is what Network Rail is measured upon every day. It is a primary focus; not performance for performance sake, but because we know how crucial it is for passengers that their trains arrive on time. Everyone's time is valuable and that underpins everything we do.

By the end of CP4 our target is that 92.6 per cent of trains should arrive on time, judged by the public performance measure. Just one year in to the control period punctuality has already reached 91.5 per cent, thanks to the tireless work of both Network Rail and train operators.

This is despite the impact of severe weather last winter. Significant improvements in underlying performance mean that we can go further than the regulated targets. Therefore we have set ourselves even tougher, internal stretch targets. We have done this because punctuality is so important to passengers and this demonstrates our commitment to them.

Yet we are not complacent and realise that there is work still to do on some parts of the network. For example performance on East Coast has disappointed and we are focusing our efforts to improve that, much as we have done successfully before on West Coast.

What about stations?
Travelling by train is just part of the journey experience. That is why we have renewed focus on the quality of facilities at stations. Throughout CP4 £3.25bn will be invested in over 2,000 stations, all over the country.

In a pioneering move, in November, we launched our Action Stations initiative, the first ever nationwide stations research project asking passengers what is important to them at their local station, where they would like to see investment and what are their priorities. The results from this research will inform the work we do as we continue to build a bigger and better railway.

Iain Coucher

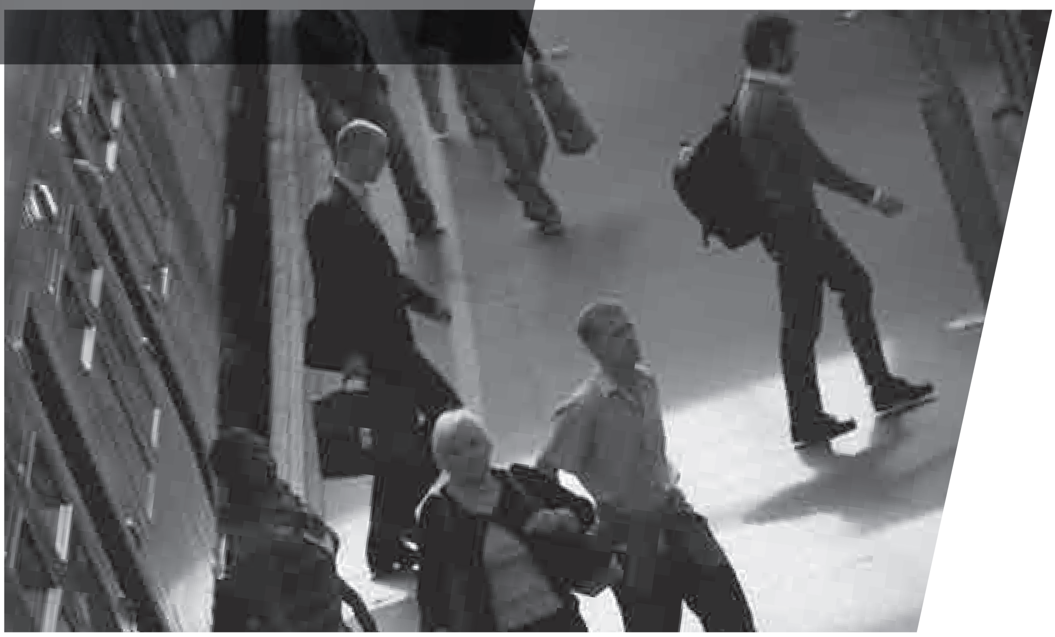
Iain Coucher
Chief Executive
3 June 2010

We now have the most punctual railway ever recorded, more passengers using it than anytime in the last 60 years and the safest railway we have ever had.

91.5%

Just one year into the control period punctuality has already reached 91.5 per cent, thanks to the tireless work of both Network Rail and train operators.

By the end of CP4 our target is that 92.6 per cent of trains should arrive on time, judged by the public performance measure.



Group Finance Director's review

This annual report marks the end of the first year of Control Period 4 (CP4), our five year regulatory settlement. The Group has made good progress in the year and has delivered a set of financial results that are in line with the business plan (CP4 Delivery Plan) published in March 2009.

Network Rail, in common with most regulated utilities, operates in a complex environment. Each five yearly settlement allows the Office of Rail Regulation (ORR) and Network Rail to take a fresh look at how much money is needed to deliver the required outputs across the control period. As part of this settlement Network Rail has cut its charges to its customers, which has resulted in a reduction of around £500m in revenue. This is possible because of the increasing efficiency and stability of Network Rail which means we need less money to run the railway. This is good news for our customers, passengers and all stakeholders. It is also good news for Network Rail because part of building a sustainable railway is making it more affordable for passengers and freight users.

In this review I will explain a number of different measures and benchmarks to give a broader insight into the performance of the Group. I will compare the performance against the commitments we made in the CP4 Delivery Plan and look at progress towards achieving the required outputs of the control period.

Over the next few pages I will show you:

- why this year was a good start with progress made against the CP4 targets so far
- why the Group's financial position remains strong and sustainable
- the challenges we face in building for future success.

Five key measures

Financial

1. Cost efficiency measure. This measures our progress in reducing the running costs of Network Rail. The Company developed a baseline at 1 April 2009 against which it needs to achieve savings of £1.1bn by the end of CP4. In 2009/10 its operations, maintenance and renewal activities are £265m lower than the baseline.

2. Financial value added. Network Rail's activities this year have been at a net cost that is £101m less than the CP4 Delivery Plan on a like for like basis. This is a good start, but as each year gets tougher, it is too soon to confirm that this will be sustained over the five-year plan.

There has been a significant growth in the number of enhancement projects being delivered in the year.

Asset management
3. Asset stewardship indicator 0.032. This measures the quality of our asset stewardship, based on asset condition, reliability and performance across Network Rail's key assets. The measure finished ahead of the business plan.

Strong and sustainable financial position
4. Interest cover 1.8. The business generated operational cash flows that were 80 per cent greater than required to pay its net financing costs.

5. Gearing ratio (debt to regulatory asset base (RAB)) 63.9 per cent. The debt to RAB ratio measures the value of Network Rail's debt to the value of the RAB. It is important in establishing that the Group debt is at sustainable levels.

A ratio of less than 100 per cent indicates that the RAB is worth more than the debt raised to finance investment expenditure, and that the business has a buffer to absorb unplanned costs.

Good start but a long way to go

Benchmarking performance
Network Rail's performance will be judged against the required outputs for CP4. The financial performance of the business is measured by the extent to which it manages within the five year funding deal.

In March 2009 Network Rail published its CP4 Delivery Plan, which set out how Network Rail plans to deliver the outputs for the five-year regulatory settlement at the appropriate cost.

The CP4 Delivery Plan is a useful benchmark for our financial progress as we move through the control period. To the extent that Network Rail outperforms the financial targets in the CP4 Delivery Plan, it has generated additional funds for investment.

Last year I reported that we exited Control Period 3 behind the ORR efficiency target of 31 per cent at 27 per cent. In setting the CP4 targets the ORR assumed that Network Rail was further ahead on efficiencies than was the case.

The result is that Network Rail will need to save 24 per cent, rather than 21 per cent, across the control period to finish at the same point as the ORR target in 2013/14. The CP4 Delivery Plan Update published in March 2010 set out the path to achieve that target.

Progress to date against the CP4 Delivery Plan
Network Rail is making steady progress in reducing the costs of running the railway, thereby making it more affordable. The business measures its performance against the CP4 Delivery Plan using two key performance indicators (KPI), financial value added and the cost efficiency measure. The financial value added KPI measures the extent that the Company has spent less, in net terms, than the delivery plan on a like for like basis, so deferrals of work are necessarily excluded from this calculation. The cost efficiency measure looks at how much the business has saved in the year against the opening cost base.

The cost efficiency measure indicated that the Group reduced its running costs by around £265m. This represents a good start to our tough, cost efficiency targets and we are ahead of the CP4 Delivery Plan.

By the end of the year the financial value added indicator measured a positive performance of £101m. This means that our activities this year have been at a net cost of £101m less than the delivery plan on a like for like basis. This KPI is the key metric for measuring long-term financial performance in the control period.

The Group performed solidly in the year by having fewer, and less disruptive, possessions, lower financing costs than anticipated and more efficient investment delivery, particularly with regard to track and civils.

Operations
Network Rail generates passenger franchise revenue, revenue grants, freight income, property rental income and open access income from its operations.

Performance
Train performance has a direct effect on the revenue Network Rail receives from its customers. The decline in revenue, from the regulatory settlement, has been partly offset by a strong performance, despite the severe winter weather, in cutting delays to passengers.

The proportion of passenger trains running on time rose to 91.5 per cent, ahead of the required regulatory output of 91.0 per cent and better than last years level of 90.6 per cent. But the unusually harsh weather in January and February meant that punctuality was difficult to deliver during that time, and cost the Group over £40m mainly in performance related compensation payments to customers. The severe winter weather caused 40 per cent of the delay minutes in January.

Network availability
Better planning of investment work, meant that there were reduced payments to train operators for disruption caused by that work.

Net additional income from CP4 performance and availability payments was £42m, £21m better than assumed in the CP4 Delivery Plan.

Revenues
Turnover fell in the year from £6,160m to £5,668m, in line with the CP4 Delivery Plan. In its review of our charges for 2009/14 the ORR agreed that we could afford a lower return on our assets (4.8 per cent compared to 6.5 per cent for the last three years). This has allowed Network Rail to cut its charges to passenger and freight operators. Charges to passenger operators have fallen by seven per cent or 22p per passenger train journey. On average freight costs have fallen by 35 per cent.

It costs 25p less to run a train one mile than it did last year and over £3 less than it did six years ago.

Property
Property rental income, mainly from small and medium sized businesses across the estate and retail tenants at the major stations, held up relatively well in the recession falling by around four per cent in the year. While property sales activity remained low, there were signs of confidence returning to the market as investment properties increased in value by £62m (2008/09 impairment of £208m) in the year.

Reducing operating costs
Network Rail's income is largely fixed by the regulatory regime which means that we place great emphasis on cost efficiency and ensuring marginal costs are exceeded by marginal income.

Staff costs rose in the year to £1,746m (2009/10: £1,656m). Average salaries increased by 2.3 per cent. This absorbed the 3.5 per cent pay rise for non-management grades agreed in December 2008, on the basis of prevailing inflation in Autumn 2008. Additional costs were absorbed by freezing managerial salaries and by replacing leavers with internal promotion.

Reducing maintenance costs
This year saw a good performance in maintenance where costs were reduced by seven per cent or £86m on a like for like basis through a combination of tight cost management, control of headcount, productivity improvements and reductions in waste. Improved management controls and planning led to a reduction in overtime costs and a reduction in the use of labour contractors for core work, saving £21m. We have invested in training over recent years and in 2009/10 we have utilised the increased skills of our employees to carry out tasks previously carried out by contractors. We continue to reduce waste. For example, our fleet management team have achieved a significant reduction in vehicle numbers, by 10 per cent, which will lead to financial savings of over £10m.

Whilst we are committed to driving efficiencies, safety remains our number one priority. As part of our ongoing investment in safety we implemented our 'All Orange Policy' so all our employees and contractors are more visible and safer whilst working. We recognise that communication is key to improved safety so we have improved communication with our frontline workers via our 'Frontline Focus' DVDs which enable managers to get across the key safety messages to our workers.

In the next 12 months we will continue to utilise improved techniques and technology to ensure we can achieve the necessary reductions in costs and continue to improve the safety of the railway for our employees and the general public.

Value for money
The savings highlighted above are a good indication of increased efficiency. An alternative measure is to look at operating costs per train mile and how they have changed over the last six years.

The graph opposite shows that it costs 25 pence less to run a train one mile than it did last year and over £3 less than it did six years ago.

This reflects the fact that the network has become busier year on year with a three per cent rise in the total number of miles travelled by trains on the network last year and a nine per cent rise over the last five years. This has a knock-on effect on the running costs of the railway, for example driving increased maintenance costs. However because Network Rail has managed to absorb these additional costs, by delivering more for less, and spread its overhead costs over a busier network, the average costs per mile travelled have improved significantly.

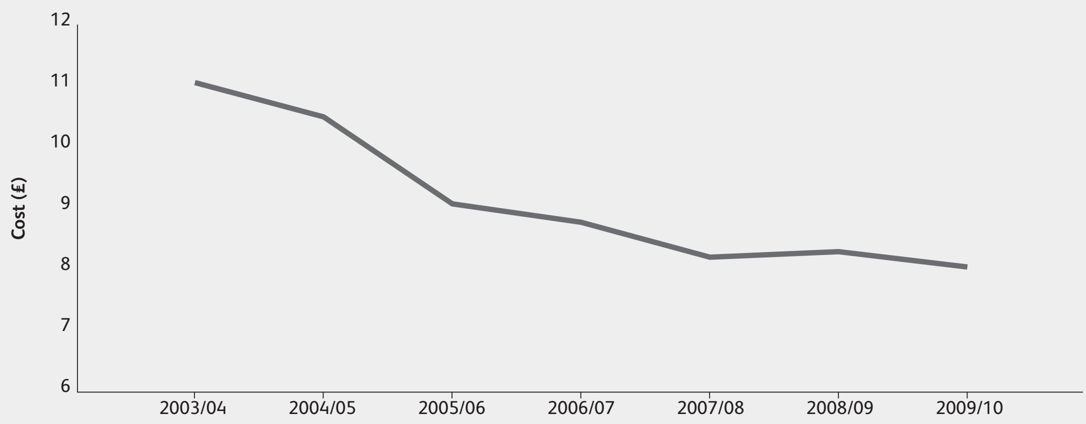
Asset management
Network Rail plans to drive towards world class asset management, and considers the key to success to be the development of asset policies that help reduce whole-life costs while continuing to improve the asset condition.

Network Rail is targeted, by the ORR, to at least maintain the quality of its assets including stations and network capability during this control period, and to do so at an increasing level of efficiency.

In the year, asset condition (as measured by the asset stewardship indicator) improved with solid levels of investment, and it was delivered more efficiently than last year and than the CP4 Delivery Plan.

Asset condition
Network Rail uses the asset stewardship indicator to assess the quality of its assets. It includes over 20 separate measures, which record both the condition and performance of the Group's key infrastructure assets. The measure came in above target for the year but only after remedial action to cope with issues caused by the exceptional weather this winter.

Cost per train mile (£)



This measure consistently showed better than target performance all year until the severe weather events in January and February. The weather affected track geometry because the prolonged freezing conditions caused ground disturbance and ice formation in the soil. This in turn affected train service performance through for example temporary speed restrictions, and contributed to the extra £40m cost in compensation to our customers for January performance.

A recovery plan was put in place immediately to address these problems which restored performance levels and delivered the year end result of 0.032 against a target of 0.019.

High levels of investment and greater efficiency
Network Rail continues to invest at historically high levels in renewing its assets. Network Rail delivered £2.3bn of asset renewals in the last year (2008/09: £2.9bn).

Efficiencies were achieved in track, structures and civils renewals. Track work was delivered in house for less, with volumes brought forward from future years. The amounts delivered included approximately 12 per cent more on plain line track and two per cent more on switches and crossings.

Civils and structures benefited from better external rates as contractors work with us to drive down costs.

Expansion

Enhancements

To take advantage of the growing demand for rail travel Network Rail will deliver enhancements in CP4 to increase the capacity of the network. The Group will deliver a large number of projects during CP4, costing around £8bn in 2009/10 prices as part of the five year funding agreement. This year Network Rail spent £1.6bn in enhancing the network and plans to deliver more next year.

What has been achieved?
There has been a significant growth in the number of enhancement projects being delivered in the year. Several hundred projects are in the development stage with the committed outputs being evaluated to enable efficient and timely delivery and in addition there have been many projects delivered on time, on budget and safely. We are on schedule to deliver our control period commitments both in terms of schedule and cost. Some highlights from the major programmes of work currently under way are:

- Airdrie to Bathgate – a new line being built in Scotland
- the 2012 Programme continues; this includes new lines, new stations, better facilities and new rolling stock on the North London Line and East London Line in addition to works to support and enable the transport links being developed in the Stratford area
- construction has commenced on the Thameslink and Reading projects as part of the transport strategy for London, as well as key development work now underway for Crossrail
- Newport, Gwent station regeneration
- the £600m project to redevelop Birmingham New Street station has attracted over £250m of third party investment.

There are many other smaller scale enhancements projects that were successfully delivered over the past year such as new car parks and line speed improvements.

Development has commenced on Control Period 5 including early commitments to create more electrified lines on the network, Edinburgh-Glasgow route electrification and the launch of the Northern Hub.

Strong and sustainable financial position

This is a company limited by guarantee and funds all its investment by raising debt through its financing vehicles or through re-investing its own profits, sometimes referred to as the railway dividend.

The Group has invested massively in the railway network since taking over from Railtrack, providing a network that will continue to serve the country for years. The cost of this investment to customer and stakeholders is spread over decades and a proportion of the funding required is included by the ORR in calculating track access charges and revenue grants. The remainder of the costs are financed by borrowing.

The Group benefits from the financial indemnity mechanism (FIM) from the Secretary of State for Transport, for which £174m was paid in 2009/10.

How much did the Group need to borrow this year?

	£bn
Cash generated from operations	2.2
Capital grants	0.3
(a) Borrowing to fund investment	1.4
Total investment	**3.9**
(b) Borrowing to refinance	2.4
Bonds issued in the year (a)+(b)	**3.8**

During the year ended 31 March 2010 Network Rail issued £3.8bn of bonds under the Debt Issuance Programme (DIP). These bonds were made up of £3.1bn of long dated inflation linked bonds and a single US dollar nominal bond. Part of this new debt was used to pay back existing loans whilst the remainder was used to invest in the railway infrastructure and to finance activities in 2009/10. As a result net debt rose from £22.3bn to £23.8bn.

Managing interest and foreign exchange risk
Network Rail manages its interest and foreign exchange risk by using derivative financial instruments (hedges). The Company measures its hedges for accounting purposes at their market value as required by International Financial Reporting Standards. A market value is determined by comparing the original value of the hedges against the current market rate.

We do not intend to trade these hedges, but use them to minimise our financial risks. As long as the hedges are economically effective (that they offset changes in the cost of existing and/or future loans), their value at any point in time should not be a key focus when assessing the Group's performance.

By qualifying to use hedge accounting rules we match gains or losses in the market value of hedges to fluctuations in the hedged item (i.e. the loans). These rules are very complex and our hedging of the real rate (i.e. the rate an investor requires to be paid in excess of inflation) on future index linked bond issues does not qualify. This means losses and gains will be taken through the Income statement at each reporting date. To enable appropriate focus to be placed on the underlying business, last year we introduced a third column to the Income statement which separately identifies the impact of the revaluation of debt and hedges on the results.

These losses on debt and derivatives valuations taken through the Income statement were £477m (2008/09: £72m).

Can Network Rail afford this level of debt?
The debt is affordable, because the business generates enough profit to cover the interest expense, and financeable because the value of debt to assets is reasonable. This is set out over the following sections.

Gearing: debt to regulatory asset base (RAB)
The debt to RAB ratio measures the value of Network Rail's debt against the value of the RAB. It is important in establishing that the Group debt is at sustainable levels.

A ratio of less than 100 per cent indicates that without the FIM investors can be sure that the RAB is worth more than the debt raised to finance investment expenditure and that the business has a buffer to absorb unplanned net costs. The debt to RAB ratio for the year was 63.9 per cent which was better than the CP4 Delivery Plan which forecast 64.0 per cent.

The ORR includes regulatory limits on this gearing ratio, because with the FIM in place there are not the same market pressures on borrowing as other utilities face. The gearing ratio is well within the target in the revised licence condition of 70 per cent.

Affordability: interest cover
The Group's adjusted interest cover ratio (AICR) is a measure of the Group's ability to pay interest on its debt after taking into account all running costs including steady state renewals. Network Rail's AICR for the year was 1.8 which is higher than both the business plan and the ORR's determinations. It is lower than last year because Network Rail is operating with lower revenue in CP4 than last year.

This demonstrates that the level of interest payable is affordable because the business generated operational revenue that was 80 per cent greater than the cash required to pay its net financing costs.

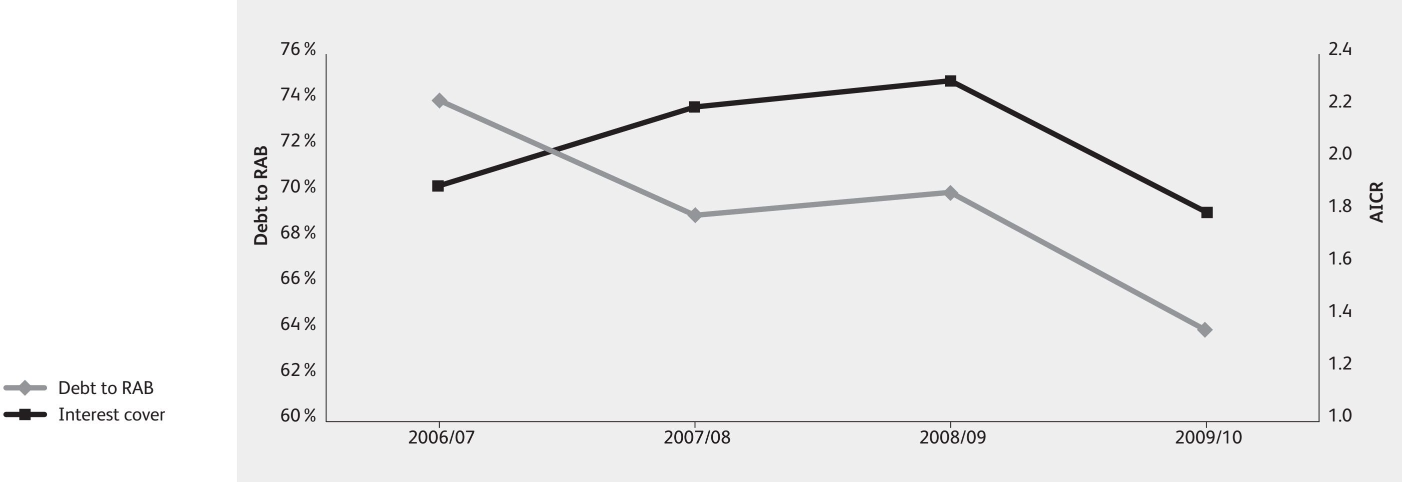
Both indicators show that the Group is financially stable.

Retirement benefits
The status of the defined benefit pension scheme continues to be a matter that is closely reviewed by the Company and the scheme's members.

The Company has taken action to address the provision of retirement benefits and during the previous year introduced a career average revalued earnings pension scheme (CARE) to offer employees a defined benefit pension on a more affordable basis. Changes to the Retirement Pension Scheme have also been made to address the rising costs of the final salary scheme.

These results show that like many other companies, Network Rail's share of the deficit widening, to £985m (2008/09: £664m).

Financial indicators



The increase in deficit has been driven primarily by the way accounting rules measure the present value of future liabilities, rather than by a worsening of the underlying position of the defined benefit scheme. This is despite an increase in the valuation of scheme assets which have risen, by £0.4bn in line with gains in the equity markets in the year.

Accounting rules require that the total projected amounts that the scheme is obliged to pay out in the future are reduced to a present day liability using highly rated (AA) corporate bond indices. It is cheaper to borrow now than it was last year so the amount by which the future pension costs are discounted has fallen, causing the valuation of the liabilities to increase, and the deficit, for accounting purposes, to worsen.

Looking forward

Targets have been achieved, efficiencies have improved and enhancements have delivered this year, but in many ways 2010/11 will be the critical year in the successful delivery of the CP4 plan.

We must deliver a number of key improvements in the next year including the next phase of the re-organisation of maintenance (which will help deliver our ongoing maintenance activities both safely and efficiently) and a stepping up in the delivery of the enhancement programme from £1.6bn to £2.5bn.

Summary

Network Rail has a financial structure that is strong and sustainable and this year represented a good start to the control period. We are slightly ahead on asset condition, performance and efficiency in comparison to our CP4 Delivery Plan. Our enhancements programme is gaining pace, but there is still much to do, and the rate of progress, particularly next year will be the key to our success in this five-year control period.

Patrick Butcher
Group Finance Director
3 June 2010

Directors' report

Whilst not required by law or regulation, Network Rail Limited has undertaken, so far as it is practical having regard to its corporate structure, to comply with the principles of good governance and code of best practice under, or approved for the purposes of, the listing rules of the Financial Reporting Council. As such, it is publishing this Report and Accounts which contains information required to be disclosed by a listed company.

Details of the Group's business activities, key events and changes during the year and likely future developments are contained in the Chairman's statement, the Chief Executive's review and the Group Finance Director's review. This Report should also be read in conjunction with the Corporate governance report, the Directors' remuneration report and the Nominations Committee report set out later in this document. All the information detailed in those sections of the Annual Report which is required for the business review, or otherwise for this Report, is incorporated by reference in (and shall be deemed to form part of) this Report.

Business review and principal activities

Network Rail Limited is the ultimate parent company of the Group which includes Network Rail Infrastructure Limited, its principal operating company.

Network Rail Infrastructure Limited has responsibility for the management of the national rail infrastructure. Its principal activities are the operation, maintenance, renewal and, in co-operation with train operators and funders, the development and enhancement of the national rail network and in particular:

- provision to train operators of railway track access
- management of train timetabling, train planning and signalling
- maintenance, renewal and enhancement of the infrastructure and undertaking major capital programmes.

Results

The profit before tax was £400m (2008/09: profit of £1,512m) and the profit after tax was £292m (2008/09: profit of £601m). Further details of the financial results can be found in the financial statements commencing on page 80.

Share capital

Network Rail Limited has no share capital, being a company limited by guarantee.

Key future issues

The publication in March 2009 by Network Rail Infrastructure Limited of its delivery plan for Control Period 4 (CP4) was a significant moment both for the Network Rail Group and for Britain's railway. It marked a commitment to deliver an even safer, better performing railway that meets the needs of its users and its funders. It committed Network Rail to reducing the cost of operating, maintaining and renewing the rail infrastructure by 24 per cent during CP4, and total savings of 42 per cent since 2003.

The delivery plan also sets out details of its investment programme the like of which the network has not seen since the Victorian era. As well as the key schemes specified by the Department for Transport and Transport Scotland, it contained details of hundreds of other schemes across Britain to deliver a bigger, better railway for passengers and freight users. Passenger numbers have grown substantially in the last decade, to levels not seen for nearly a century. Every indication is that such growth will continue, as the underlying factors driving it remain in place. The delivery plan set out how Network Rail would meet these major opportunities.

By accepting the ORR's final Determinations in February 2009, Network Rail accepted the challenge of raising punctuality to even higher levels, of doubling and then doubling again the levels of investment in the network, and doing both in less time and with less money.

In March this year it published an update to its plans – this was not a wholesale revision of the 2009 Delivery Plan. It provided instead an update on certain areas where more detail is now available or where circumstances have changed over the last year. It also provided an update on the progress that has been made in the first year of CP4.

Last year, there was still a great deal of work to be done on developing its plans in a way consistent with both the sustainable delivery of the necessary outputs and the significant efficiency savings assumed by the ORR. Were it to continue to spend at the levels at the end of Control Period 3 (CP3) in March 2009, it would overspend the funding available for this control period by more than £5 billion. When it accepted the challenge set by the ORR's final Determinations, Network Rail still needed to develop robust plans to achieve the necessary savings.

Good progress has been made so far, but difficult challenges still remain in the implementation of its transformation programme. To overcome them will require a wholesale change in the way Network Rail does business. If it fails to deliver this change, it will not deliver the required outputs with the money available to it or prepare itself for delivery in 2014 and beyond. It is making changes across the whole business so that it can deliver a wide range of outputs and so that failure in one area does not undermine successful delivery of its other targets.

The 2010 Delivery Plan Update provides, therefore, some details on that transformation, and sets out those areas where change will be a priority both in 2010/11 and the remaining years of the control period. It also highlights the development of a set of asset policies that will form the basis of its plans for maintenance and renewals activity. Managing our assets appropriately for the long-term will help reduce their whole-life cost whilst also continuing to improve their condition. This in turn will help Network Rail to deliver the outputs it has committed to deliver. Though there have been changes in some areas, the update showed that the key figures remain broadly the same.

It is crucial that the good progress made so far is maintained, and 2010/11 will be critical in building successful delivery for the whole of CP4. Key improvements which must be delivered in the next year include the next phase of the reorganisation of maintenance (which will help it to deliver its ongoing maintenance activities both safely and efficiently) and a stepping up in the delivery of its enhancement programme from £1.5 billion in 2009/10 to £2.5 billion in 2010/11, before a further increase to £3.3 billion in 2011/12. This includes over £4 billion of enhancements to be delivered during CP4 that are incremental to the schemes funded through the periodic review, including electrification of Great Western main line and the Edinburgh to Glasgow improvement programme.

Further details of Network Rail's plans are contained in the CP4 Delivery Plan published on 31 March 2009 together with the update to these plans which was published on 31 March 2010 both of which are available on Network Rail's website: www.networkrail.co.uk.

The following sections provide a summary of the update to the delivery plans.

Key issues

Safety

Safety will always remain Network Rail's number one priority and decision making focuses on this. The rail industry target for CP4 is to achieve a three per cent reduction over the control period in the risk of death or injury from accidents on the railway for passengers and rail workers.

The risk of death or injury from accidents on the railway for passengers and rail workers is measured using the Rail Safety and Standards Board's Safety Risk Model (SRM), which is updated every 18 months. Network Rail's own safety performance is reported every period in its safety and environment assurance report and annually in its annual safety report.

Building on the substantial improvements in CP3, the SRM reports a continuing and significant reduction in reportable injuries and in passenger safety during 2009/10. Notwithstanding this, it must continue to strive for further improvement, particularly to prevent fatalities on the railway. As can be seen from the table below, good progress is being made towards reducing both industry workforce and passenger safety risk at the start of CP4.

Sadly, however, despite a 14 per cent improvement in workforce safety, three workforce fatalities occurred during the year. Safety must remain, therefore, a key focus.

Key safety indicators

Safety indicators	2009/10	2008/09	2007/08
Workforce fatalities[A]	**3**	3	2
Accident Frequency Rate	**0.159**	0.231	0.226
High risk Category A SPADs[B]	**19**	16	19
Broken rails	**152**	163	181
Collisions with vehicles at level crossings	**14**	21	8
Other potentially high risk train accidents[C]	**30**	23	25
Passenger accidental fatalities[D]	**6**	6	10

A Including contractor fatalities.
B SPAD = signal passed at danger. The measurement is based on a 100 point scale.
C These are derailments, collisions between trains, train collisions with vehicles and buffer stop collisions (resulting in damage or injury) that occur on or directly affect a passenger line.
D None of the passenger fatalities in these years was caused by a train accident.

Key Performance Indicators

Performance indicators	Notes	2009/10	2008/09	2007/08
Safety:				
Passenger Safety Indicator*	1	0.215	0.252	0.276
Performance:				
Train Delay Minutes (million mins.)*	2	8.2	8.9	9.5
Public Performance Measure	3	91.5 %	90.6 %	89.9 %
Asset stewardship:				
Asset Stewardship Indicator	4	0.032	–	–
Value:				
Cost Efficiency measure	5	5.8 %	–	–

* A lower figure represents an improvement.

Notes

1 The Passenger Safety Indicator is the passenger safety risk associated with Network Rail activity, based on the Train Accident Precursor Indicator Model quarterly output, combined with the actual Non-Train Passenger Fatalities and Weighted Injuries at Network Rail managed stations and level crossings normalised per billion passenger kilometres.

2 Train Delay Minutes are the number of minutes of train delays attributable to Network Rail (rather than the train operating companies) as defined in the contractual performance regime with operators. Delays attributed to Network Rail also include externally caused events such as trespass, vandalism, weather related incidents and similar types of disruption.

3 Public Performance Measure is the overall rail industry key performance indicator measuring punctuality and reliability of train performance. It shows the percentage of trains that arrive 'on time' at their final destination compared to the number of trains planned to run on a given day. 'On time' means arrival within 10 minutes of the scheduled arrival at destination time for long distance services and within five minutes for London south east or regional services.

4 Asset Stewardship Indicator is an indicator of the quality of Network Rail's asset stewardship, based on asset condition, reliability and performance across Network Rail's key assets. This is the first year that it has been in operation. Comparison with previous years' indicator is not appropriate. The individual stewardship indicators are: track (40 per cent), signalling (25 per cent), electrification and plant (10 per cent), telecoms (five per cent), operational property (10 per cent) and structures (10 per cent).

5 Cost Efficiency measure is a KPI that assesses reductions in the running costs of Network Rail. This is the first year that the measure has been in operation.

Performance

Network Rail's performance is measured through a variety of indicators including a detailed corporate metrics of measures which are reviewed at executive and Board level.

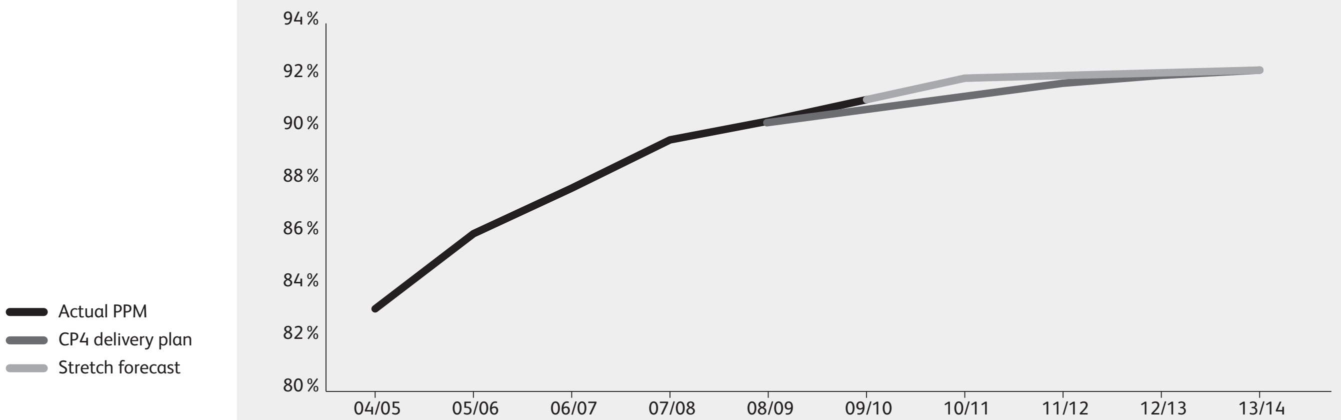
The key measures and comparative performance against each are set out in the table above.

Punctuality continues to improve achieving new highs against recorded history. The average punctuality over the past year was 91.5 per cent.

Thus overall punctuality was better than forecast in 2009/10 despite the severe weather conditions during the winter. Before the impact of the exceptional weather, and even taking that into account, significant improvements have been achieved in underlying performance. There has been some local performance which has not met all of these improvements and are subject to combined Network Rail and train operators' focus to bring in line with national improvements.

As a result, and recognising the importance of punctuality to passengers, it has set itself tough internal targets to outperform those set by the ORR. These stretch targets,

CP3 and CP4 punctuality (PPM%)



which are summarised in the graph on page 18, would achieve performance improvements earlier in CP4 than had originally been planned. The graph also shows the overall improvement it has made since the start of CP3.

Network availability
Network Rail's focus is on delivering maintenance, renewal and enhancement of the network while minimising disruption to passengers and freight users wherever possible. It has been measuring network availability using the new possession disruption indices which were developed by the ORR for CP4.

During 2009/10, it has consistently outperformed the regulatory output trajectories, and remains committed both to meeting the output requirements for the remainder of CP4, but also to making the railway available when its users want and need it to be. These indices are new, and it is still developing, therefore, its understanding of how the measure responds to the level of engineering access as the metrics are highly sensitive to the location, number and duration of possessions. Given the uncertainty in understanding these metrics at a network level, it is not yet publishing stretch targets or disaggregated operator targets at this stage. However, the new metric is promoting the right behaviours within Network Rail, with an increased focus on understanding and reducing the level of engineering access that it uses.

Its plans to improve availability and meet the output targets are set out in the Network Availability Implementation Plan, which is published on Network Rail's website. This describes the activities and investments it is undertaking, and their contribution to the delivery of network availability outputs.

Capability
Network Rail's obligation is to maintain network capability at the level as at 1 April 2009, in terms of track characteristics such as mileage and layout, line speed, gauge, route availability, and electrification type and mileage. Network capability is primarily defined by data contained within the National Electronic Sectional Appendix (NESA) and associated systems. Last year it provided the ORR with a statement of the capability of the network as at 1 April 2009 for the above characteristics and baseline data is also published on the Network Rail website. The NESA now provides details of its capability for all routes. Where the actual capability differs from that published in the baseline, a statement of discrepancies is also published alongside the NESA. The resolution of discrepancies is being addressed within existing CP4 funding. In some cases this will involve full physical restoration. However, if it is identified that there is no demand for that capability and therefore its restoration would not be the most effective use of resources, it will propose changing the published capability through the industry Network Change procedure.

The ORR has written confirming it is satisfied with Network Rail's strategy for maintaining and improving gauging data and a key focus for it now is to apply the same approach to information on the power supply capacity of the network.

Capacity
Network Rail committed to deliver the projects specified in the High Level Output Specifications (HLOSs) for England and Wales, and Scotland, as well as other projects.

During 2009/10, it has continued to develop enhancement projects to deliver increased capacity and other improvements during CP4. Over the last six months, there have been a small number of changes to the baseline, which have been agreed through the formal change control process. Some further changes are expected as it continues to develop detailed remits for delivery of these schemes. The most significant change it expects to make will be the re-profiling of the Thameslink project as the requirements of the next key stage (key output 2) become better defined. Other material changes will be the inclusion of the new electrification works on the network and an expansion of detail on its commitments for the Edinburgh to Glasgow improvements programme.

Beyond the changes that are currently in development, there are likely to be further areas where it will need to make changes to Network Rail's plan. It is also likely that it will seek to rollover some funding for at least one project to take account of the overall funding arrangements for the programme. Further details are contained in the CP4 Delivery Plan Update 2010.

The DfT announced earlier this year that it is reviewing its Intercity Express Programme. Network Rail's plans include a programme of enabling works so that the network is ready to accept the operation of new trains. Until the outcome of DfT's review is clear, it will continue developing its programme of enabling works. One major project may need, therefore, to undergo change control to reflect the latest client requirements in its scope, outputs and milestones.

A significant number of enhancement projects are being developed that were not funded through the periodic review. These may be promoted by Government, Network Rail's customers and other stakeholders, or they may be schemes it is promoting to deliver benefits for the railway beyond 2014. Over the last year, there have been an increasing number of projects being promoted by Government that will be financed through use of Network Rail's regulatory asset base.

Stations and depots
Over the past year, there has been an increased focus across the industry on stations, including the publication of the Better Rail Stations report which was commissioned by DfT. Network Rail recognises that stations are an integral part of the overall journey experience for passengers. Collaborating with train operators it will continue to find ways of making progress in this area both faster and easier.

Stations are categorised between A and F and Network Rail is required to maintain average condition scores within each station category, both in England and Wales and in Scotland. The categories reflect the different sizes and passenger throughput of each station. Network Rail believes that its plan supports delivery of the station condition targets.

Income
Network Rail's income forecasts are broadly consistent with the delivery plan after taking into account revised inflation assumptions. There are two areas where it believes that there will be a shortfall against the assumptions in the delivery plan: freight and property income. During 2008/09, freight income was lower than it had projected and this continued as expected into 2009/10. However, it assumed that freight income would recover during 2010/11. This now appears unlikely so it has reduced its freight income forecasts by around £10 million per year for the remainder of CP4.

Network Rail also assumed that it would receive income in 2013/14 of £65 million from developments at Euston and Victoria stations. It is now clear these projects will not be completed within CP4 so it has removed these from its plan. In its final Determinations, the ORR stated that Network Rail will be compensated in CP5 for any income shortfall on these schemes arising from market conditions.

In other areas, income is marginally ahead of the delivery plan in 2009/10. Network Rail is forecasting that these improvements will continue for the remainder of CP4.

Overview of expenditure plans
In overall terms, Network Rail's expenditure plans remain broadly consistent with the delivery plan, which is illustrated in the graph below. In the first year of CP4, it has made progress towards implementing many of the initiatives and activities described in its delivery plan aimed at delivering significant efficiency savings. This continues the substantial progress made in CP3. During CP4, it plans to achieve efficiency savings of 24 per cent.

Operating and maintaining the network
Network Rail has developed detailed budgets for each part of the business for 2010/11 which have been rigorously challenged and agreed by the Board so it continues to deliver cost savings. For maintenance, this will be through a programme of restructuring, advances in processes and the increased use of technology. The next phase of the reorganisation of its maintenance activities will help it to deliver its ongoing maintenance both safely and efficiently. Together, this will result in total savings of around 24 per cent by the end of CP4.

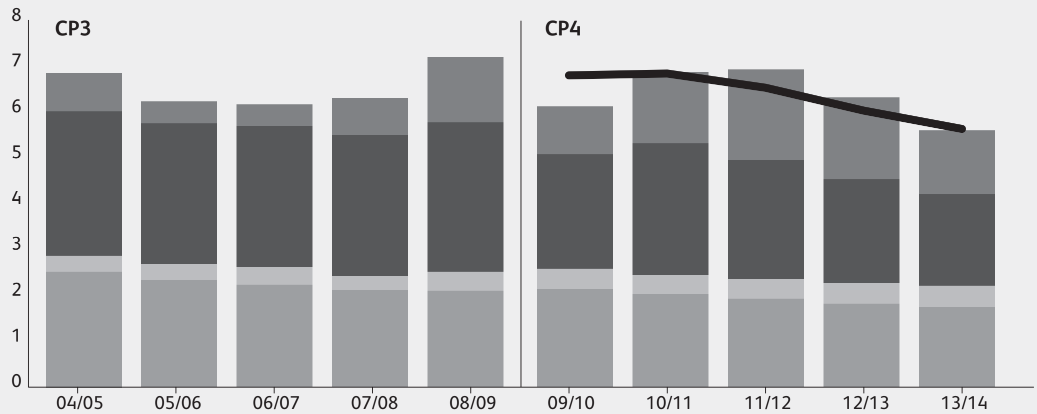
Operating costs are slightly higher than those in the delivery plan. The level of savings that can be achieved in this area is limited as operational costs are largely fixed or semi-fixed in the short-term. It still plans to achieve savings, through a range of operational efficiency initiatives, totalling around 14 per cent by the end of CP4. While it has not yet developed detailed plans beyond 2011/12 for delivering savings in Network Rail support processes, a key enabler will be the move to its new National Centre in Milton Keynes during 2012. It has assumed therefore that it will continue to deliver annual savings in its support costs of around five per cent for the rest of the control period.

For non-controllable operating costs, the increase reflects the revised level for cumulo rates, which was finalised during 2009, and the costs of British Transport Police which, despite huge pressure, have not reduced as expected in the ORR's assumptions.

Projections for the rest of the control period are set out in the CP4 Delivery Plan Update 2010.

Renewing the network
Network Rail has an extensive network renewals plan as detailed in the delivery plan. Its overall renewals expenditure is currently consistent with the delivery plan where it stated that it would achieve efficiency savings through unit cost and scope efficiencies. As part of its transformation programme it has carried out analysis that supports the sustainable reduction in scope of asset management (i.e. with no impact on longer-term funding and outputs). The ORR is currently assessing whether it accepts that these changes are sustainable.

CP3 and CP4 expenditure trend (£bn, 2010/11 prices)



CP4 delivery plan
Enhancements
Renewals
Non-controllable opex
O&M

Enhancing the network
While it needs to increase significantly the level of enhancement activity over the next two years, Network Rail believes the progress made in 2009/10 provides a solid platform for delivery of its commitments over the rest of CP4.

When Network Rail published the delivery plan, it explained that the forecast aggregate cost of the enhancement portfolio was significantly in excess of the funding provided. During 2009/10, it has made good progress in driving down the cost of many of its enhancement programmes. In particular, it has reduced the expected cost of the programme to support train lengthening in London and the south east. However, it still faces a number of major challenges to manage the cost of enhancement programmes within the funding available and to achieve the project milestones. The programmes with the most significant gap are the power supply upgrade and East Coast main line improvements, where there is considerable focus on delivering the required outputs within the funding available. While some projects will cost more than has been included in the final determinations, Network Rail will be able to deliver others for less. At this stage, it is forecasting that most programmes will be broadly in line with the ORR's Determinations. However, it is only one year into the control period and there is a significant risk in this area which is being managed proactively, learning from past experience.

Financing
Network Rail continues to finance its business by raising debt supported by the Government indemnity. Its financing requirements for the remaining four years of CP4 are projected to comprise new debt issuance of approximately £9 billion to finance net capital investment, and the refinancing of at least £6 billion of bonds which mature during CP4. It continues to raise all debt through its debt issuance programme. During 2010/11, it will need to raise approximately £4 billion of further debt, which includes £2 billion of debt to be refinanced. It also expects to maintain sufficient short-term facilities and/or investments to cover at least the next 12 months' funding requirements (excluding refinancings). Some of the debt is issued in foreign currencies. It expects to continue the existing policy of hedging all exposure to exchange rate changes on any debt denominated in foreign currency, and at least 80 per cent of forecast interest rate exposure over CP4. It continues to believe it is right that it seeks to move away from relying on debt supported by indemnities from Government. It will keep this under review as market conditions and other factors change over the next few years.

Improving business performance
In its delivery plan, Network Rail described its commitment to continue to change its organisation and drive better delivery throughout the Company. It has an extensive transformation programme that has already made significant progress. The changes it has identified should generate substantial savings by 2014. While further savings of around £800 million still need to be found over the control period, the financial projections in its delivery plan assume it is able to find ways of closing this gap. Alongside these changes, significant improvements to the financial efficiency and customer focus of the business will enable Network Rail to deliver both sustainably and within the funding it has available.

In 2009/10, it has already made good progress in making significant changes, and early improvements are delivering efficiency savings. During 2010/11, it will continue to deliver improvements to enable further savings. By 2012/13, the majority of changes should be in place and being consolidated. The new process-led organisation will be fully embedded, and the National Centre will increase its organisational effectiveness. Efficiency in planning and delivery will have increased substantially, and it will be delivering an improved service to all of its customers as the effects of the earlier years begin to influence beliefs.

Further plan updates and change control
Network Rail will publish further annual updates of its plan throughout CP4, identifying any major changes to its plan, as well as updates of its enhancement programme on a quarterly basis, reflecting changes agreed through the formal change control process.

Comparison to CP4 delivery plan
In the delivery plan, it provided a comparison of the plan itself against the ORR's final Determinations for England and Wales, and Scotland, which showed these were broadly consistent. A key measure of Network Rail's success is its performance compared to the delivery plan, which measures using its financial value added key performance indicator.

It has then made a number of adjustments to the delivery plan to reflect project or operational changes. After taking into account these adjustments, the differences between the delivery plan update and the updated delivery plan are not significant.

In 2009/10, Network Rail has made good progress in driving costs down and is currently achieving greater savings than it assumed in the delivery plan. However, it needs to manage successfully a number of significant challenges over the remaining years of CP4 in order to deliver the required outputs. As a result it is assuming that its plan update is consistent with the delivery plan.

It will continue to assess the extent to which savings can be sustained to the end of the control period and whether it is achieving overall out-performance of the delivery plan. If it is confident it will be achieved over the control period as a whole, it will assess the level to be shared with train operators through the efficiency benefits sharing mechanism.

Beyond Control Period 4
By March 2014, at the end of this control period, the railway will have seen ten years of record levels of investment. The improvements this will have delivered for those who use the railway can then become the foundations for further success for the rail industry and Network Rail in CP5 and beyond.

Delivering Network Rail's commitments will create a railway better able to exploit the opportunities for further improvement. The railway will be more reliable, safer and capable of carrying more passengers. At the same time it is one of the most carbon friendly forms of transport.

As well as delivering these improvements over the next four years, Network Rail must look, therefore, well beyond 2014. Over the next few decades, the demand for passenger and rail freight services is set to rise. A return to economic growth, increasingly congested roads and skies, and a commitment that the UK cuts its carbon emissions by 80 per cent by 2050 all point to a doubling in rail demand over the next 30 years, and possibly a tripling beyond that. The industry cannot plan solely in five year periods, and Network Rail is developing a long-term framework that allows the industry itself as well as key funders to plan effectively.

It is important to recognise that delivering sustained improvements in the railway industry means taking a longer-term view than the time horizons that this plan covers. As a result, it has been working with its colleagues across the industry to develop a longer-term vision for rail. Creating consensus on this vision will allow the industry to work towards a set of common goals and to be clearer on the priorities for the next control period (2014/19).

Network Rail published the first in a series of documents in June 2009 in which it and the passenger and freight operators set out the vision for the railway and its planning and development of a 21st century railway that will benefit passengers, freight users and Britain as a whole. Network Rail intends to publish its next document in June 2010 which will set out its progress on the development of a long-term planning framework and the emerging priorities and strategic issues for the next control period. This will form an important step in developing plans for CP5, particularly in setting out a starting point for engagement with funders and other stakeholders.

The rail industry can play a key role in a long-term strategy for sustainable economic growth. However, it has to make the case that by building on rail's core strengths it can drive economic development, improve the connectivity and productivity of cities and, by delivering a more attractive service, support a lower carbon economy by attracting passengers and freight traffic from road and air transport.

Attracting more customers to rail will improve the productivity and efficiency of the railway, making more use of the assets it has. Overcoming the challenges, and delivering the CP4 commitments, will provide the most solid of foundations for the railway to build on in the decades to come.

Health and safety
The health and safety of its employees and contractor employees and of the public travelling on the rail network are of great importance to Network Rail. Its policies and procedures relating to health and safety at work recognise the requirements of current legislation and are kept under constant review with the aim of providing a safe working environment for all employees. Significant resource is committed to safety, health and environmental matters and Network Rail aspires to continuing improvement of its performance in these areas.

Previous incidents and recent regulatory penalties
The derailment which took place at Potters Bar in May 2002 is the subject of continuing ORR investigations; the outcome is unknown at present. The derailment in Cumbria in February 2007 has also been the subject of investigation by the British Transport Police which has recently announced that it has completed this investigation and has now passed the matter to the ORR for it to investigate; the outcome of its investigations is unknown at present.

No regulatory penalties were imposed by the ORR during 2009/10 for breach by Network Rail of its network licence.

Corporate responsibility and sustainability
Network Rail is committed to carrying out its activities in a responsible manner in respect of customers, rail users, employees and local communities and other stakeholders. As part of its objective of operating in a transparent and accountable manner, a corporate responsibility report on these aspects within its business is published annually. This report also contains details of Network Rail's sustainability policy. The next report will be published in the summer of 2010. This report will be available on Network Rail's website: www.networkrail.co.uk.

Details on corporate responsibility are set out on pages 76 and 77.

Network Rail's corporate responsibility performance has been independently rated against the Business in the Community (BitC) Corporate Responsibility Index in the last three years. In the latest rating in 2009 its performance rating improved with it being awarded a gold rating (2008: silver). This increase reflects Network Rail's improving management of its impacts across the areas of workplace, community, marketplace and the environment. Network Rail's Community Safety and Talent programmes retained their Big Tick status in BitC's 2010 Awards for Excellence. Network Rail was able to demonstrate that these programmes continued to have a significant positive community and workplace impact, resulting in this re-accreditation.

Environmental sustainability

Network Rail's approach is to focus on the key environmental issues facing it as operator of the rail infrastructure and also the issues facing society as a whole – including climate change, waste, bio-diversity and land management. Network Rail remains committed to its three environmental sustainability goals:

- to acheive sustainable consumption and production
- to improve energy efficiency and reduce the reliance on fossil fuels in running the railway
- to protect natural resources.

Network Rail's response to the challenge of managing environmental risk includes improving the line-side environment with policies that manage the balances between a responsibility to provide a safe and reliable railway whilst acknowledging the benefits of minimising the impact on the natural habitat. Waste management is also important with schemes in place to improve responsible waste handling and recycling both by the Company and by its contractors.

Climate change is an ongoing focus with participation in research programmes organised by various specialist bodies. Likewise energy and water usage are subjects of ongoing reduction programmes.

Environmental, societal and economic impacts are considered with a view to continuing to develop rail as a sustainable form of transport. Key performance indicators have been developed.

Code of Business Ethics

Network Rail has issued its Code of Business Ethics which replaced its existing business conduct policy. The code applies to all of its activities and sets out the minimum standards which the Board of Network Rail expects from all employees and Directors in their dealings with colleagues, customers, stakeholders and third parties. Consultants, contractors and business partners are also expected to act in accordance with the principles contained within the code.

Research and development

During the year the Group charged £1m to the Income statement (2008/09: £1m) on research and development. Other costs relating to significant development work have been capitalised in property, plant and equipment.

Most of the Group's development activities are applied as capital projects within the investment programme. The remainder is charged against the Income statement.

Directors

The table on page 24 identifies Directors who have served during 2009/10 and who are also Directors of Network Rail Limited. The dates of their appointment are also detailed.

Under the provisions of the Articles of Association of Network Rail Limited all Directors, except the Special Director (if appointed – there being no Special Director at the time of publication of this report), must retire by rotation, and may stand (together with any new Director appointed since the last general meeting) for re-election or election (as applicable) by the Members of that Company at least every three years. Save as shown in the table on page 24, there were no other changes to the Board during the year.

At the forthcoming Annual General Meeting of Network Rail Limited Yvonne Constance and Christopher Green, both Non-Executive Directors, will step down from the Board. New Non-Executive Directors Janis Kong, Lawrie Haynes, Graham Eccles and David Higgins will offer themselves up for election by the Members being the first such meeting after their appointments. Peter Henderson, Executive Director, and Mike Firth, Non-Executive Director, will retire and, being eligible, will offer themselves for re-election on the rotational basis.

Moreover, whilst not required under the terms of the Articles of Association, Rick Haythornthwaite as Chairman of the Board will also voluntarily offer himself up for re-election on an annual basis commencing at the meeting this year. This accords with his responsibilities in this role and reflects leading best practice.

David Bailey is now 70 years old. There is no legal requirement for a Director over the age of 70 to seek re-election annually. As a matter of good practice, however, in Network Rail a Director reaching this age offers themselves up voluntarily. In line with this, David Bailey will also be seeking re-election at Network Rail Limited's AGM in July 2010.

Details of the Executive Directors' contracts of employment (service agreements) and remuneration are contained in the Directors' remuneration report.

The biographical details of the Directors can be found on pages 28 and 29.

Serving Directors during 2009/10

Current Directors	Position	Date of first appointment	Next due date for election/re-election
Rick Haythornthwaite*	Chairman	23 March 2009	July 2010
Executive Directors			
Iain Coucher	Chief Executive	3 October 2002	July 2012
Patrick Butcher	Group Finance Director	20 April 2009	July 2012
Robin Gisby	Director, Operations & Customer Services	1 October 2008	July 2012
Peter Henderson	Director, Asset Management	3 October 2002	July 2010
Simon Kirby	Director, Investment Projects	1 October 2008	July 2012
Paul Plummer	Director, Planning & Development	1 October 2008	July 2012
Non-Executive Directors			
David Bailey*	Non-Executive Director	3 October 2002	July 2010
Yvonne Constance**	Non-Executive Director	1 May 2005	n/a
Graham Eccles	Non-Executive Director	7 February 2010	July 2010
Michael Firth	Non-Executive Director	4 December 2004	July 2010
Christopher Green**	Non-Executive Director	26 June 2005	n/a
Lawrie Haynes	Non-Executive Director	26 January 2010	July 2010
David Higgins	Non-Executive Director	1 April 2010	July 2010
Janis Kong	Non-Executive Director	13 January 2010	July 2010
Steve Russell	Non-Executive Director	19 September 2007	July 2011
Past Directors who stepped down during 2009/10			
Ian Buchan	Non-Executive Director		Stepped down on 31 March 2010
Jim Cornell	Non-Executive Director		Stepped down on 22 July 2009
Ron Henderson	Executive Director		Retired on 18 April 2009
Ian McAllister	Non-Executive Director		Stepped down on 22 July 2009

* Will be seeking voluntary re-election in July 2010.
** Will be stepping down at the Annual General Meeting in July 2010.

Directors' interests

At no time during the year did any Director hold a material or any other interest in any contract with the Company or any of its subsidiaries other than service agreements between Executive Directors and the Company and letters of appointment between Non-Executive Directors and the Company.

Insurance

Network Rail has purchased and maintained throughout the year directors' and officers' liability insurance.

Employees and business performance

Details of the number of employees and related costs are set out in Note 6 to the financial statements on page 91.

Network Rail believes that business performance improvement is influenced significantly by the skills, behaviour and attitude of its employees. Substantial investment is being dedicated by the Company to deliver high quality, accredited training and development programmes as a primary means of stimulating cultural change and management competence. Development programmes from apprenticeship schemes through to leadership skills are used.

Effective communication in raising the level of employee engagement is also important. To do this a wide range of communications media is being used, encompassing local information cascades and briefings, videos, the Company's internal magazine, email news bulletins, electronic data links, Chief Executive's blog and briefings by the Directors to reach all employees.

During the annual Business Briefings conducted in April 2010 approximately 8,000 employees were able to attend the geographically spread briefings at which the Company's safety and operational performance was discussed. Employees had the opportunity to question the Executive Directors on any aspect of the business that they chose to raise.

Employees also have the opportunity to voice their opinions and ask questions through Network Rail's intranet site. Face to face briefings and team meetings are actively encouraged and are held in all functions across the Company.

There is a direct link between business performance and engaged employees – who are safer, less likely to leave and more likely to enjoy what they do. To monitor progress in developing employee engagement Network Rail conducts an annual independently-run survey of its employees specifically on this topic. Each question in the survey is designed by Gallup and is proven to be an accurate measure of the level of employee engagement in an organisation. Every team in the Company is expected to set their own action plan to improve their performance and their next set of scores. This survey is conducted each year, the most recent being in November 2009.

Significant progress has been made with improving the levels of engagement within Network Rail since 2002 when the first of these surveys was conducted. In that time engagement index levels have risen from 3.16 to 3.8 in 2009. Our target is 4.15. The speed of improvement in engagement has slowed recently, however, and plans continue to target key areas of the business where the levels of engagement do not meet the upper quartile of performance measured elsewhere in Network Rail. The next survey is scheduled to be conducted in November 2010 with further surveys planned for subsequent years.

During the year, Network Rail also launched its Promise and its Management Principles. The Promise is Network Rail's statement of intent so all employees can work together towards a common purpose. The Management Principles are the ways by which this is to be achieved. Briefings to about 4,000 employees have been conducted to embed these in work practices.

The Board strongly believes in the importance of consultation on issues affecting the workforce. Frequent consultation and information sharing is conducted, therefore, at regular intervals through both national and local procedures with representatives from Network Rail and trades unions. During 2009/10 this has included continuation of discussion with the trade unions on the modernisation of terms and conditions of employees engaged in the Infrastructure Maintenance function. Consultation has also taken place on the Company's pension schemes.

Employee practice

Network Rail is committed to offering all of its employees a fulfilling and challenging career in an environment free from discrimination, harassment, victimisation and bullying irrespective of their gender, sexual orientation, marital status, race, nationality, ethic origin, disability, age, religion or union membership status. Its policies and procedures in recruitment and selection, training, career development, working arrangements, promotion and performance appraisal support this commitment. Moreover Network Rail continues to work with trades unions in the area of equality of opportunity and development of policy to promote best practice within the business.

The equal opportunities policy is communicated to employees. Its Code on Business Ethics also highlights the importance of equality and diversity issues.

Employee review processes are in place to allow every individual manager to discuss key performance issues in a structured, fair and consistent way and to identify training and development needs. Emphasis is placed on performance against the Company's corporate values and personal development opportunities.

Charitable donations and community support

Network Rail continues to support community initiatives and charitable causes. During the year £762,893 was donated to charitable organisations (2008/09: £785,000).

Network Rail's charitable giving objectives came into effect on 1 April 2006. To focus efforts and align Network Rail's charitable giving with its corporate activities, it supports charities which:

- preserve Britain's railway heritage
- promote engineering to young people
- protect or restore our natural environment
- prevent or tackle the consequences of incidents on the railway
- provide help to the homeless in our local communities
- provide emotional support to the railway community or the public
- put otherwise unused assets and waste products to use for local communities.

As part of this ambition, Network Rail encourages employees to support charities through its charitable giving schemes. The Company offers employees up to five days' paid volunteer leave with a supported charity; matches employees' fundraising contributions (up to £100,000 per year in total) and encourages employees to give to charity through their payroll using its Give As You Earn scheme.

In addition Network Rail supports a charity of choice, chosen by employees. Between 2008 and 2010 the charity of choice was the National Society for the Prevention of Cruelty to Children. In March 2010 over 40 per cent of employees participated in voting for a new charity for Network Rail to support, and chose Cancer Research UK as the Company's next charity of choice.

In 2009/10 the Company welcomed 30 regional charity partners, each delivering services that align to Network Rail's charitable giving objectives. A donation was made to each charity and employee volunteering opportunities are being developed to build and maintain long-term and mutually beneficial relationships.

Network Rail's support for the community also extends to engagement relating to railway crime and misuse. This includes railway and level crossing users as well as within local communities which experience high levels of railway crime.

Network Rail's Community Safety aim is to improve safety, raise awareness, reduce incidents of crime as well as reducing costs to the business and society. This is achieved by applying a variety of interventions working within the rail industry itself as well as with organisations from the public, private and voluntary sector.

Regional Community Safety Managers develop and implement Network Rail's community safety strategy and, in addition are responsible for the delivery of Network Rail's award winning No Messin'! and Don't Run the Risk campaigns.

The team works in communities nationwide, primarily engaging in 'hotspot' areas which represent the greatest risk to railway users and to the infrastructure. As part of developing the No Messin'! campaign, Network Rail is working on a number of innovative projects with the aim of providing a sustainable diversion and positive alternative to participating in railway crime and misuse, whist providing an educational message.

The team, with its partners, regularly attend high profile level crossings, offering advice and information and asking level crossing users 'Would it Kill you to Wait?'. In 2009/10 the team held over 100 level crossing safety awareness events across the UK. In addition, Network Rail has committed £10m to its national level crossing closure programme. The purpose of the programme is to close level crossings that are operated by the user. So far it has agreements in place to around 400 crossings, which will remove the risk of incidents at these locations.

Sadly, suicides continue to occur across the network with over 200 incidents in the past year. In January 2010 Network Rail announced a groundbreaking five-year partnership with the Samaritans to develop a national programme of work which aims to reduce both the business impact and frequency of suicide incidents on the railway as well as supporting staff and customers who experience an incident of suicide. The aim of this partnership is to reduce incidents of suicide on the railway by 20 per cent over the next five years.

Political donations

In line with the Company's policy, no donations to political parties were made in the year.

The Companies Act 1985 required companies to obtain shareholders' authority for donations to registered political parties and other political organisations totalling more than £5,000 in any 12 month period, and for any political expenditure, subject to limited exceptions. The definition of donation in this context was very wide and extended to bodies concerned with policy review, law reform and the representation of the business community. It could also have included special interest groups, such as those involved with the environment, which the Company and its subsidiaries might wish to support, even though these activities are not designed to support or influence support for a particular party.

The relevant provisions of the 1985 Act have been replaced by similar provisions in Part 14 of the Companies Act 2006 (CA 2006) with effect from 1 October 2006. The meaning and implications of this legislation, whilst improved by the CA 2006, still remain somewhat uncertain as to its application. It continues to be extremely wide in scope and could extend to routine activities undertaken by Network Rail as part of its normal day-to-day contacts, such as its active and important policy of providing regular briefings for MPs.

Network Rail needs to work closely with all types of community representatives. As part of this, the Company has a significant amount of contact with a wide range of elected representatives (Members of Parliament, Members of the Scottish Parliament, London Assembly, Welsh Assembly and others) as well as non-governmental organisations, pressure groups and campaigning organisations. This includes meetings to discuss issues facing the Company and those using the railways, both passengers and freight traffic nationally and regionally. Opportunity is also taken each year to explain to elected representatives our business plans, the Company's performance and significant developments within the business. This is sometimes best achieved through the Company organising briefings and similar functions at which presentations are given.

Whilst it remains Network Rail's policy not to make political donations to any political parties, given the uncertainty of the precise meaning of the legislation it considers it prudent to obtain approval from Members of Network Rail Limited to avoid inadvertently breaching the CA 2006.

Accordingly, since it remains vital that Network Rail communicates frequently with the full spectrum of political organisations, the Board annually seeks Members' approval at the AGM of Network Rail Limited for Network Rail Infrastructure Limited, as the principal subsidiary company running the railway infrastructure, to incur 'political expenditure' and to make 'political donations' to political parties or independent candidates and political organisations (as widely defined in this law).

Creditors payment policy

It is our policy, with respect to payment of our suppliers, to settle the terms of payment when agreeing the terms of each transaction where standard terms are not used, to make suppliers aware of the terms of payment and to abide by the terms of payment.

At 31 March 2010 the Company's creditor days compared with the value of suppliers' invoices received in the year was 48 days (2008/09: 47 days).

Recognising the current economic climate and the importance of its suppliers and contractors for delivery of its business objectives, Network Rail has reviewed its payment policy. As reported in 2009, where possible, having regard to prudent business management, Network Rail continues to seek to make payments that are due more speedily than its standard terms of payment. Action has also been taken in specific cases to seek alternative methods of alleviating financial constraints on key suppliers and contractors identified on a case by case basis.

Auditors

At the next Annual General Meeting of Network Rail Limited on 21 July 2010, a resolution will be proposed to appoint PricewaterhouseCoopers LLP as the Group's auditors and to authorise the Directors to fix their remuneration. Details of tender process adopted to select PricewaterhouseCoopers LLP are set out in the Corporate governance report. Details of the fees earned by Deloitte LLP during the period, for both audit and non-audit work, are set out in Note 5 on page 91.

Details of the process for review of the external auditors are set out in the Corporate governance report on page 68.

Directors' responsibilities

The statement of Directors' responsibilities in relation to the financial statements is set out on page 77. The statement by the external auditors on corporate governance matters is contained in their report on pages 78 and 79.

Pursuant to the Companies Act 2006 Section 418(2), each of the Directors in office at the date of this report confirms that, so far as he or she is aware, there is no relevant audit information of which the Company's auditors are unaware and that he or she has taken all reasonable steps in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Going concern

The Directors are satisfied that the Network Rail Group has adequate resources to continue to operate for the foreseeable future. For this reason they continue to adopt the going concern basis in preparing the accounts. See Note 2 of the Accounts on pages 84 to 90 and page 77 of the Corporate governance report.

Annual General Meeting

The 2010 Annual General Meeting of Network Rail Limited will be held on 21 July 2010 in Manchester. A separate document accompanying the Annual Report and Accounts contains the Notice convening the meeting and a description of the business to be conducted at that meeting.

Significant events subsequent to 31 March 2010

The new Government has agreed with Network Rail that it will reduce spend by £100m over the rest of CP4 on enhancements that offer relatively low value for money. This will include the programme of station enhancements announced in November 2009 and other elements for Network Rail to determine.

There have been no significant balance sheet events subsequent to 31 March 2010 to the date of this report.

By order of the Board

Hazel Walker
Company Secretary
3 June 2010

Board of Directors


Rick Haythornthwaite


Yvonne Constance

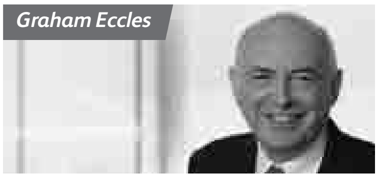

Mike Firth


David Bailey


Iain Coucher


Robin Gisby


Patrick Butcher


Graham Eccles


Chris Green

Rick Haythornthwaite
Chairman
Rick Haythornthwaite, 53, has been the Company's Non-Executive Chairman since July 2009. He was Chief Executive of Invensys plc, from 2001 to 2005. He was also previously Group Chief Executive of Blue Circle Industries and spent 18 years with BP in various senior roles. He is currently non-executive chairman of MasterCard Inc, a senior advisor to STAR Capital Partners and President of PetroSaudi International (UK) Ltd. His previous non-executive roles included Board membership of ICI, Land Securities and Lafarge. In the voluntary sector, he is also chairman of the Southbank Centre.

David Bailey OBE
Non-Executive Director
David Bailey, 70, joined the Board in 2002. David has a procurement and logistics management background. He was formerly Commercial Director for London Transport, having previously held various director-level roles within London Underground. David is Chairman of the charity, Home-Start North East Hampshire.

Patrick Butcher
Group Finance Director
Patrick Butcher, 42, joined the Board in 2009 having previously held the position of finance director at English Welsh and Scottish Railway (now DB Schenker) between 2004 and 2008. Before this he was finance director at Mapeley Ltd, London Underground and King's College Hospital. His early career was at Deloitte & Touche as a management consultant and auditor. Patrick is a Member of the Institute of Chartered Accountants (South Africa).

Yvonne Constance OBE, JP
Non-Executive Director
Yvonne Constance, 67, joined the Board in 2005 having previously been Chairman of the National Electricity Consumers' Council between 1995 and 1999, a Non-Executive Director of Innogy plc from 2000 to 2002 and a Non-Executive Director of St Mary's Hospital NHS Trust. Until its cessation in 2005 she was also a member of the Greater London Magistrates' Courts' Authority, as well as being a Justice of the Peace since 1976 and, in the 1980s, practised as a barrister. Yvonne will retire from the Board in July 2010.

Iain Coucher
Chief Executive
Iain Coucher, 48, took over as Chief Executive in 2007. Prior to this, from October 2002 when Network Rail acquired Railtrack plc, he was Deputy Chief Executive. Before that he was Chief Executive of Tube Lines, which followed working for EDS for 16 years. His career has included experience in the transportation sector, particularly with London Underground. He was seconded to the TranSys consortium between 1996 and 1998 as its Chief Executive and led the development of the Underground's smartcard ticketing system. Iain is an engineering graduate from Imperial College, London and also has an MBA.

Graham Eccles
Non-Executive Director
Graham Eccles, 63, joined the Board in February 2010 following a long career in the railways. Graham's former positions include Deputy Chairman of London Midland, Chairman of the South East Strategic Health Authority, Board Member of Stagecoach Group plc, Chairman and Managing Director of South West Trains and Co-Chairman of Virgin Rail Group Ltd.

Mike Firth
Non-Executive Director
Michael Firth, 67, joined the Board in 2004 having previously been Head of Corporate Banking at HSBC Bank plc until his retirement in September 2002. He is also a Non-Executive Director of Communisis plc and Gartmore European Investment Trust plc. He was previously a Non-Executive Director of Somerfield plc and First Technology PLC. Michael is an Associate of the Chartered Institute of Bankers and a Fellow of the ifs School of Finance.

Robin Gisby
Director, Operations & Customer Service
Robin Gisby, 53, joined the Board in 2008, having been employed by Network Rail and its predecessor since 1998 and was appointed Director, Operations and Customer Services for Network Rail in May 2004. Previous roles in the Company include two regional director positions and, prior to these, within Railtrack, Director, Network Development and Director, Freight. Before joining Railtrack he had engineering and operational roles in both the UK and overseas mainly with GKN plc. He has a first degree in Engineering Science and an MBA, and is a Chartered Engineer and a Fellow of the Chartered Institute of Transport.

Chris Green
Non-Executive Director
Christopher Green, 66, joined the Board in 2005 following his retirement as Chairman of Virgin Rail Group. Chris has over 45 years of railway experience, having joined British Rail upon leaving university. He held various management positions including Managing Director of Network SouthEast and Intercity. He was Chief Executive of Virgin Trains from 1999 to 2004. Chris was also Chief Executive of English Heritage, a non-executive director of Eurotunnel and past Chairman of the Railway Forum. He is a Fellow of the Institute of Logistics and Transport. Chris will retire from the Board in July 2010.

Lawrie Haynes
Non-Executive Director
Lawrie Haynes, 57, joined the Board in January 2010. Lawrie is President – Nuclear at Rolls-Royce Plc. He was previously Chief Executive at White Young Green plc. Prior to that, he was Chief Executive of British Nuclear Group and a main board director of BNFL plc. He was also Chief Executive of the Highways Agency. Lawrie has a degree in Business Law (Heriot Watt) and is on the Board of Trustees of the Royal Air Force Benevolent Fund and is Chairman of its pension fund.

Peter Henderson
Director, Asset Management
Peter Henderson, 56, has responsibility for Engineering, Asset Management, Maintenance and National Logistics. Joining the Board in 2002, he has over 25 years' rail experience. Starting with the construction of the Tyne and Wear Metro, he then spent 16 years with the Hong Kong Mass Transit Railway Corporation as Head of Major Projects. He returned to the UK in 2000 to work for Bechtel where he was Projects and Engineering Director for Rail. He has an MSC in Engineering Business Management.

David Higgins
Non-Executive Director
David Higgins, 55, joined the Board in April 2010. David is the Chief Executive of the Olympic Delivery Authority (ODA) and has held this role since March 2006. Prior to this, he was the Chief Executive Designate at the ODA from December 2005. Prior to December 2005, he was Chief Executive of English Partnerships for three years. His early career was at Lend Lease Group, where he was appointed Managing Director and Group Chief Executive in 1995. David graduated in Civil Engineering from the University of Sydney and holds a Diploma from the Securities Institute of Australia.

Simon Kirby
Director, Investment Projects
Simon Kirby, 44, joined the Board in 2008, having been with the Company since 2003. He is responsible for delivery of all large enhancement and renewal infrastructure projects. He has held positions in the Defence industry and has been involved in a number of Land and Naval Weapons System projects including the Trident Nuclear Submarine Programme. In 2000 he was appointed Managing Director of three BAE Systems shipyards before, in 2002, becoming Managing Director of the BAE Systems Type 45 Prime Contract Organisation. Simon has an MSc in Engineering Business Management from Warwick University and is also on the board of the Major Projects Association.

Janis Kong
Non-Executive Director
Janis Kong, 58, joined the Board in January 2010. She is a Non-Executive Director of Kingfisher plc, Portmeirion Group PLC and VisitBritain, and Chairman of the Board of Trustees of Forum for the Future. During her 33-year career with BAA, Janis held a number of operational roles and until her retirement in March 2006, was a director of BAA plc and Chairman of Heathrow Airport Ltd as well as being Chairman of Heathrow Express. Prior to that, she was Managing Director of Gatwick Airport. She was previously a Non-Executive Director of The Royal Bank of Scotland Group Plc.

Paul Plummer
Director, Planning & Development
Paul Plummer, 44, joined the Board in 2008, having been with the Company since 2002. He is responsible for the network planning and enhancement sponsorship, regulation and contract services. Previously he was Chief Economist and Director of Economics and Finance at the Office of Rail Regulation from 1999 to 2001. He has also worked at National Economic Research Associates (NERA), NM Rothschild and Accenture advising companies, governments and regulators on utility regulation, restructuring, privatisation, strategy, finance and M&A in the UK and overseas. He has a degree and MSc in Economics.

Steve Russell
Senior Independent Director
Steve Russell, 65, joined the Board in 2007. Previously he was Chief Executive of Boots Group PLC between 2000 and 2003, working there since he started his first job at the company in 1967. He was previously a Non-Executive Director of Barclays PLC – where he was a member of the audit committee (previously having been chairman of this committee), the board risk committee, nomination committee, governance committee and he is Chairman of Business Control Solutions. He is also a trustee of St John's Ambulance and Tommy's, the baby charity. He was appointed the Senior Independent Director of Network Rail in July 2009.

Directors' remuneration report

Highlights

With the support of the Executive Directors, the Remuneration Committee (the Committee) froze the basic salaries of the Executive Directors and other senior executives in 2009 and in 2010.

During 2009 and 2010, significant consultation was undertaken by the Committee with a range of stakeholders, and in particular the Company's Members, on the basis of remuneration and incentivisation. The views expressed were then taken into account by the Committee in determining both the awards for 2009/10 and the terms of the incentive plan for 2010/11.

The Committee conducted an extensive review in 2009/10 of the principles for and the terms of remuneration of the senior management of the Company and in particular the Management Incentive Plan (MIP).

The review outcome was that the Committee remains firmly of the opinion that the performance-related elements of the Executive Directors' remuneration continues to be stretching and is designed to align their interests with the risks to the Company and the interests of its stakeholders and to promote the long-term success of the Company.

In considering whether to exercise its discretion to reduce payable awards under the MIP 2009/10, the Committee conducted an extensive and thorough review of all key aspects of the Company's performance in the year, including its impact on meeting the targets for Control Period 4 (CP4).

Report contents

Un-audited information

Compliance

The following report has been prepared in accordance with the Directors' Remuneration Report Regulations 2002 (the Regulations) and the Financial Reporting Council's current Combined Code. The report also meets statutory requirements, in particular the Companies Act 2006 Schedules 5 and 8.

In addition to and in line with its aim for maximum transparency and corporate governance best practice compliance, the Committee continues to aim to reflect best practice guidelines provided by other sources including guidance published by the Institutional Voting Information Service (IVIS) of the Association of British Insurers (ABI), the National Association of Pension Funds (NAPF) and Pensions & Investors Reporting Consultants (PIRC) where appropriate.

The role of the Remuneration Committee

In contrast to most listed companies (if not all) the Remuneration Committee of Network Rail (the Committee) is empowered under the Articles of Association of Network Rail Limited to determine remuneration for Directors as opposed to making recommendations to the Board in respect of this. This responsibility reflects the aim of Network Rail to provide independence of the decision making process as appropriate for the highest levels of corporate governance and reflects the importance of remuneration and incentive schemes in supporting the delivery of the Company's responsibilities.

The Committee's composition

The Committee comprises Non-Executive Directors including the Chairman of Network Rail. The following table details who has served on the Committee during 2009/10:

Current members	From
Steve Russell (Chairman of Committee from July 2009)	September 2007
David Bailey	October 2002
Yvonne Constance*	May 2005
Michael Firth	December 2004
Christopher Green*	June 2005
Rick Haythornthwaite	March 2009

Previous members	From	To
Ian McAllister	October 2002	July 2009
Ian Buchan	February 2006	March 2010
Jim Cornell	October 2002	July 2009

* Stepping down from the Board in July 2010.

The Group Company Secretary is the secretary to the Committee.

The Human Resources Director attends the meetings by invitation to assist the Committee in its considerations of market practice and the alignment of incentive arrangements to business strategy. The Human Resources Director is responsible for employees within Network Rail and is not a Board Director nor is he appointed by the Committee. The Chief Executive is also invited to attend certain parts of some Committee meetings (other than when his own remuneration is being discussed or decided) to assist the Committee in its consideration of the Company's performance and key operational objectives.

Remuneration Committee's activities during 2009/10

The Committee is required under its terms of reference to meet at least once a year and during the year 2009/10 it met six times. The Committee's activities during that period have been summarised in the table shown below.

The Committee commissioned Hewitt New Bridge Street Consultants LLP, Towers Watson and Deloitte to provide independent expert advice on remuneration generally and management incentive schemes. Hewitt New Bridge Street provided no other services to Network Rail. Deloitte supplied audit services to Network Rail during the year, together with and subject to the approval of the Audit Committee other limited non-audit services.

The Remuneration Committee's activities in 2009/10

Meeting	Agenda items
May 2009	• Decision on Executive Directors' awards under the annual and long-term elements of the MIP 2008/09 • Setting of targets for the MIP 2009/10 • Approving the content of the MIP 2009/10 statement to be published • Review of the then current debates on corporate governance relating to remuneration and in particular the latest guidelines on best practice recently published by certain bodies • Review of the contents and wording of the Directors' remuneration report for the 2009 Annual Report.
September 2009	• The annual review of the Executive Directors' remuneration • The annual review of the senior executives' remuneration • Review of the structure of the MIP beginning April 2010.
November 2009	• Review of the Incentive Policy and principles for remuneration within Network Rail • Consideration of the structure of the MIP 2010/11 • Review of a report by Towers Perrin on incentive scheme options and market trends • Consideration of the nature of the performance measures to be used in the MIPs during CP4 from April 2009 • Discussion on engagement with stakeholders and in particular Members in relation to the Committee's work.
5 January 2010	• Consideration of the structure of the MIP for Control Period 4 • Review of Members' views on remuneration generally and the MIP expressed at the Members' meeting in December 2009 and subsequently • Discussion on pension changes announced in the Government's pre budget report and considering current market practice in relation to pension provision for senior executives.
19 January 2010	• Further discussion in relation to the structure of the MIP 2010/11, the process for determining 2009/10 MIP's incentive awards and in particular the manner for and processes facilitating the exercise of discretion.
February 2010	• Further consideration of the principles of remuneration and in particular incentivisation of senior executives and the structure of the MIP for CP4 • The annual review of the terms of reference of the Committee, the general effectiveness of the Committee and its composition.

During 2009/10 Towers Watson Limited advised Network Rail in respect of pension related matters included in the remuneration policies.

In December 2009 the Chairman of the Remuneration Committee, Steve Russell conducted a Members' discussion session at which the basis for and the principles relating to remuneration and in particular incentivisation were discussed. The output of the discussions was shared with all Members who were invited to contribute further. Steve Russell also wrote to Members on a regular basis updating them on the deliberations of the Committee and the emerging views of it and the resulting shape of the MIP for 2010/11. The Committee then took views of Members into account in structuring the process and key considerations for exercising its discretion in relation the MIP awards for 2009/10 and for finalising the terms of the 2010/11 MIP.

The Committee's objectives

The Committee is a committee of the Board of Network Rail. Its terms of reference are available from the Group Company Secretary and can be found on the Company's website: www.networkrail.co.uk.

In summary the Committee is responsible for determining all matters concerning incentives and remuneration of the Executive Directors of the Company. This includes:

- making decisions in respect of the framework of the Executive Directors' remuneration and its cost
- determining, on behalf of the Board, specific remuneration packages for each of the Executive Directors
- deciding the remuneration package for the Chairman without the Chairman being present
- deciding upon the form and content of the Executive Directors' MIP for each financial year (within the terms of the Incentive Policy)
- determining the framework of certain senior executive employees' remuneration as well as the form and content of their MIP.

Remuneration principles

In order for Network Rail to achieve its responsibility for serving and collaborating with its customers – the train and freight operating companies – in the joint pursuit of the best possible current experience for the public and freight users; future prospects for the railway in Great Britain; and value for money in the eyes of both users and tax-payers, it must attract and retain the best people to lead its delivery recognising that it competes in an environment determined by competitors (broadly defined), governments and regulators.

The Committee believes that senior executives should be rewarded (on a market competitive basis) for the delivery of stretching targets beyond those targets set by the ORR. To achieve this alignment Network Rail's remuneration approach is leveraged, with a high percentage of pay 'at risk' against the achievement of those stretching targets. For 2009/10 the use of long-term incentive terms is closely tied to the long-term value of executive remuneration to the delivery of financial value added requirements.

The Committee has identified the key remuneration principles by which it must conduct its responsibilities as being:

1. **Targets and goals are linked with customer and stakeholder interests:** the Company's remuneration policies are designed, as far as possible, to align the interests of our senior management with those of our customers and other diverse stakeholders in delivery of the Company's business plans
2. **Remuneration is competitive to attract and retain necessary talent:** each year the Remuneration Committee assesses the competitiveness of total remuneration levels for senior executives to enable the Company successfully to attract and retain executive talent from the private as well as public sector
3. **Remuneration is proportionately balanced between short and long-term performance objectives:** the Remuneration Committee provides a total remuneration package consisting of fixed and variable pay, recognising the long-term nature of investments in the railway industry, whereby emphasis is on variable pay to reward short-term out-performance and significantly on long-term out-performance measured against pre-established targets and objectives
4. **Remuneration is aligned to effective risk management:** the remuneration structure is designed to be aligned to encourage innovation by senior executives whilst discouraging excessive risk-taking
5. **Incentive awards paid fairly reflect all relevant factors** – notwithstanding achievement against incentive scheme targets, the Remuneration Committee will always assess overall business performance particularly safety (and such other relevant factors as it considers appropriate) in deciding the level of incentives to be awarded.

In applying these principles the Committee also recognises the criticality of alignment between the delivery plans for each control period (and beyond) and the remuneration policy and practice of Network Rail's senior executives.

The principles and objectives are then structured within a total remuneration approach, defined as the sum of basic salary, incentives and benefits. The use of variable pay through the availability of incentives to form a significant part of total remuneration is intended to ensure that each individual's reward is clearly linked to the successful delivery of Company objectives.

Regulatory requirements

In addition Network Rail Infrastructure Limited has a network licence condition requirement to have a MIP for its Executive Directors and senior executives and for that plan to be cascaded throughout that company whereby incentive awards are available to all employees upon targets being met.

Under this condition Network Rail is required, when formulating its MIP, to have particular regard to:

- securing the safe operation and maintenance, renewal and replacement, improvement, enhancement and development of the network especially operational performance, asset serviceability and condition, efficiency and economy
- infringement by Network Rail of any access contracts and safety factors
- achievement of the licence requirement of dealing with dependent persons with due efficiency and economy and in a timely manner and compliance with Network Rail's Code of Practice for dealings with dependent persons
- the extent to which Network Rail is subject to orders and to statements by the ORR on non-compliance with the licence.

These objectives are supported by a remuneration policy which can be modified only with the consent of the ORR. Under this policy the objectives and principles are to:

- provide strong incentives to deliver the actions and objectives specified in the business plan
- identify specific accountability for the achievement of the actions and objectives laid out in the business plan
- enable Network Rail to recruit, retain and motivate individuals with the right skills, knowledge, experience and competencies
- draw on best practice for listed companies in the UK where appropriate given the unique mission and structure of Network Rail
- recognise that Network Rail is accountable for the public interest as a monopoly owner and operator of an asset of considerable public importance
- recognise that Network Rail Limited is a company limited by guarantee founded on a 'not-for-dividend' principle
- reflect the fact that the Company is unable to offer the traditional benefits of UK listed companies including stock options and other profit-share mechanisms.

The ORR may also specify other objectives in connection with the MIP.

Regulatory MIP statement

As required under the network licence of Network Rail Infrastructure Limited, a statement is published each year detailing the contents of the current year's Executive Directors' MIP.

Application of principles and policy

Total remuneration for Executive Directors

Total remuneration package levels are informed by relevant pay data from the private sector although not necessarily the rail sector (European or worldwide), and in particular broadly the median range of the FTSE 100. These reference points are chosen to reflect Network Rail's equivalent to market capitalisation and /or comparable companies within regulated and non-regulated with synergies of business type and business drivers and the positioning that is appropriate to Network Rail in those different comparator groups. This data, in particular incentives, is then moderated, to reflect emerging circumstances, nationally (and internationally), within the relevant industry sector, Network Rail's unique corporate environment and the performance of the Company itself.

The Committee recognises the need to guard against upward ratcheting of remuneration and as such it views the data with great care and scrutiny.

Incentive awards – Committee discretion to reduce

Under the incentive schemes the Committee has the ability to reduce (but not increase) awards payable in the year.

One of the key roles of the Committee, therefore, is the annual consideration of the incentive awards which are payable and whether the Committee should exercise its discretion under the terms of the MIP, to reduce the overall annual and long-term incentive payments actually awarded to the Executive Directors.

The general principles against which the Committee exercises its use of this power of discretion are set out in this section. Details of its decision for 2009/10 incentive awards are set out on pages 40 to 42.

The Committee is very aware of the need to recognise the incentive scheme as an important variable element of the Executive Directors' (and senior managers') remuneration to be used appropriately and proportionately. The design of the MIP needs careful consideration and the actual awards made need to be effective and based on clear, visible and demonstrable measures. The overriding discretion held by the Committee must be used, therefore, on a consistent and proportionate basis and the use of the discretion must not undermine the confidence of the Executive Directors in the achievability of incentive awards. It recognises the importance of applying its discretion justly, fairly and proportionately whilst also being mindful of public scrutiny.

As part of the process of achieving this, at the end of each financial year the Committee has regard to a variety of overriding considerations above and beyond the achievement of targets and triggers within the mechanism of the MIP. These discretionary considerations have been carefully designed to balance the competing aspects of delivering a successful rail infrastructure performance and include:

- safety performance (passenger and workforce)
- the extent to which the key objectives of the Delivery Plan over the performance period have been achieved
- financial performance
- reputational issues
- compliance with the obligations set out within the network licence
- compliance with the conditions as set out in the Access Agreements with our customers
- any breaches of contract or other significant issues; and
- any other objectives that ORR may specify from time to time.

Additionally the views of stakeholders, including the ORR, are taken into consideration in the deliberations.

Previous exercises of Committee's discretion

2002/03 awards	The Committee exercised its discretion having determined that it would be inappropriate to make awards under the MIP for 2002/03 to any of the Executive Directors due to the relatively poor train performance even though other targets within the MIP were achieved. No annual incentive awards under the Network Rail scheme were made for that year.
2003/04 awards	The total potential award for 2003/04 was 32 per cent of basic salary. This included the impact of the non-use of a £50m contingency sum within the budget on the performance achievement level. The Remuneration Committee chose to use its discretion by adjusting the Financial Efficiency Index (FEI) performance to include the £50m contingency thereby reducing the level of achievement. As a consequence the overall incentive award for the Executive Directors reduced to 24 per cent of their basic salary.
2006/07 awards	The total potential award for 2006/07 was 20 per cent of basic salary. The Remuneration Committee exercised its discretion taking into account the overall performance of the Company during that year. The Committee was mindful that the failure to meet the FEI target was due to the impact of the Cumbrian incident. In addition it took into account the many areas of performance, including safety, where there had continued to be significant improvement in the last year. In order to underline the importance of the Company's commitment to continuing focus on operational excellence, however, the Committee decided to exercise its right to reduce the award for 2006/07 by 15 per cent.
2007/08 awards	The Committee recognised the disruption caused to Network Rail customers and passengers as a result of the Christmas 2007 overruns. It concluded in relation to the awards for that financial year that the inconvenience and disruption were already reflected in the outturn of the reliability performance measure of the MIP. The FEI measure was also adversely affected by the ORR's fine levied. In combination the awards payable under these two measures (which comprise two thirds of the incentive measures) were automatically impacted by the overruns reducing them by a significant percentage. This reduction also represented an important validation of the robustness of the MIP performance measurement structure as having relevant and effective mechanisms reflecting the significance of performance failures to train operators, passengers and freight customers. Notwithstanding this, the Committee believed that the adverse reputational impact to the Company of the overruns had been significant. Consistent with the Company's commitment to continuous focus on operational excellence, therefore, the Committee concluded that in addition to the resulting automatic reductions in incentive awards it would exercise its discretion to reduce the awards further. The awards in total were reduced by the Committee, therefore, by a further 10 per cent over and above the initial reduction under the terms of the MIP.
2008/09 awards	Of the specific performance indicators within the MIP, the financial efficiency target for 2008/09 was achieved. Notwithstanding this, the Committee decided to remove from the calculation of the FEI performance an amount of £20m contained within the 2008/09 budget relating to the cost of standardisation of terms and conditions of employment within the Infrastructure Maintenance function which was not utilised since negotiations with the trade unions on this had not yet concluded. Also in relation to the Edinburgh Waverley project Network Rail earned a contractual bonus for early completion of the project supplementing the FEI by £5m. Both items were excluded from the calculation of FEI performance for the purpose of the MIP awards The level of achievement of this measure was halved by these exclusions.

The constituent parts of remuneration

Set out below is a summary of the key considerations used when setting basic salary and incentive awards. These constituent parts of remuneration packages are considered by the Committee, together with pension and other benefits, as a whole for Executive Directors. It seeks to create the right balance between each of these elements so that short-term success, delivery of the objectives of the delivery plan and long-term sustainable improvement are recognised.

Basic salary

Payment	This is a fixed cash sum payable over 13 periods during the financial year.	
Review	The Committee reviews salaries annually as part of the total reward package recognising market levels and personal contribution. Current salaries are shown on page 40, following the most recent salary review movement effective from 1 July 2008. A nil increase was made in July 2009 and there will again be a nil increase in 2010.	
Benchmarking	This is benchmarked as for total remuneration but with positioning and progression taking into account of individual career development and current performance. The following have been used during 2009/10 as comparator companies for benchmarking purposes, with a discount applied reflecting Network Rail's unique market position:	
	AMEC plc	Northumbrian Water Group plc
	Arriva plc	Pennon plc
	Atkins plc	Royal Mail
	Balfour Beatty plc	Scottish and Southern Energy plc
	Carillion plc	Serco plc
	FirstGroup plc	Severn Trent plc
	Go-ahead plc	Stagecoach plc
	National Express Group plc	United Utilities plc
	National Grid plc	VT Group plc
Market discount	The Committee recognises that on the financial front it is appropriate to make distinction between the environment for Network Rail with that of some other companies. The Committee has applied a discount within the MIP, therefore, to compensate for the predictability of the financial market within which Network Rail operates which acts as a 'cushion' against more conventional market conditions. Most of its profits and losses and its balance sheet is not influenced so directly by market conditions. That said, the Committee considers it is still important to recognise that Network Rail is not immune to the economic climate.	
Best practice	Recognition is also made of guidelines from bodies such as IVIS and NAPF on specific issues relating to basic salaries.	
Workforce comparison	Reviews of basic salaries are also compared against those for the general work force. In 2009/10 the workforce basic salary increased on average by 0.8 per cent. The Executive Directors' salaries had a nil increase in 2009/10.	

Incentive arrangements

Alignment with risk	The MIP is designed to discourage management behaviours which expose the Company to excessive risk. Instead the measures under the scheme complement and mirror appropriate risk management. The structure of the MIP is designed around six measures with three focused principally around the key risk areas for Network Rail – operational performance, asset stewardship and financial performance. The measures for each of these are equally balanced and are designed to counteract each other preventing distorted focus on any one aspect of business performance to the detriment of the overall performance delivery objectives since each are inter-dependent on each other for success. For example high train performance could be achieved through deferring maintenance but this would then reduce the asset stewardship measures. Equally asset stewardship could exceed targets at the expense of financial efficiency in which case the financial measures would not be met.

continued overleaf

Incentive arrangements continued

Governance best practice	The Committee is committed to meeting so far as possible the principles contained within guidelines published by leading bodies in this field such as the ABI and NAPF. In 2008 PIRC reviewed the Company's corporate governance against its published guidelines for best practice. In relation to the MIP 2008/09, PIRC concluded that: • the inclusion of the Public Performance Measure (PPM), being a non-financial measure, to be best practice • the targets for each set of performance measures to be laid out clearly and discussed in the Strategic Business Plan 2007 and Update 2008 • the total potential awards under all the incentive schemes were not excessive. Consequentially PIRC awarded to the MIP for 2008/09 a status of compliance of 'BBB' which the Committee understands to be a high rating given infrequently by PIRC.
Stakeholder focus	The incentive opportunities available to the Executive Directors and other senior executives must have strong exposure and focus on achievement of the performance delivery levels expected by stakeholders.
Stakeholder engagement	Being mindful of the wide range of stakeholders affected by the performance of Network Rail, the Company continues to seek transparency in relation to remuneration through the following means: • publication each year a statement detailing the contents of the year's MIP • explaining to and encouraging Members to discuss the Committee's thinking on remuneration, and in particular the principles adopted by the Committee in the design of the MIP and the proposals for the terms of the MIP, which the Committee takes into consideration when determining the final terms of the MIP • publishing in detail the reasoning for any awards made under the MIP including the points considered in deciding whether and to what extent it exercised its discretion in making any awards.
Stakeholder support	Notwithstanding that there is no legal or regulatory requirement for Network Rail to seek formal approval by its Members of its long-term element of the MIP (L-TIP), each new L-TIP or revised L-TIP involving a significant change is the subject of formal approval at the relevant Annual General Meeting of Network Rail Limited. The latest form of the L-TIP received approval from its Members by a resolution at the Annual General Meeting in July 2009.
Short and long-term incentives	The MIP provides for annual and long-term awards being available on targets being met:
Annual	This element of the MIP represents incentive award as a function of the degree of achievement of the corporate performance targets set out in the relevant year's MIP with cash awards given.
Long-term (L-TIP)	The structure of this element of the MIP is limited by the lack of availability of share option mechanisms for Network Rail. Seeking to introduce an alternative measure aligned with the objective of achieving greater efficiency a financial value added measure was introduced in 2009. Details are set out on page 42. Award under this element of the MIP represents a deferred cash payment, based upon achievement of corporate performance targets set out in the relevant year's MIP. The long-term element of the MIP is only realised if the stretching targets are met.
Targets and triggers	The targets under the MIP are carefully set to provide true incentive and, secondly, are set at appropriate levels to promote challenge and stretch to performance delivery. The alignment of these within the incentive measures is closely reviewed each year by the Remuneration Committee through rigorous practices and processes both in terms of the appropriateness of the measures and also the target levels set. Targets set by the ORR are reviewed as the starting point but the Remuneration Committee often imposes more stringent targets. Outstanding performance must always be demanded with achievement duly rewarded. The identification and delivery of stretching targets (in the case of Network Rail above and beyond those set by the ORR) must be central to this.

continued opposite

Incentive arrangements continued	
Discretion to reduce	The MIP also contains an overriding ability for the Committee to reduce (but not increase) awards payable in any year. All awards are subject to the discretionary sanction. In considering the exercise of its discretion the Committee undertakes a detailed review of the process especially in those vital areas of safety. It has adopted a thorough, robust and transparent process drawing on both internal data and reports from the Audit Committee and Safety, Health and Environment Committee in relation to the management of risk. In past years the discretion has been exercised in five of the eight years of awards. Further details of the exercise of discretion are set out on pages 34 and 40 to 42.
Safety	Safety is and will remain Network Rail's primary focus. No death is acceptable. The Committee believes safety focus within the MIP is best served through the application of its overriding discretion in such a way that sends the right signal to the executive management, and gives confidence to Members and other stakeholders that the safety improvement is truly the top priority for Network Rail. In its consideration of safety related performance within the Company the Committee seeks to balance the prioritisation of safety with the need to encourage the delivery of business improvement. The objective is to penalise severely in the event of real, systemic Network Rail attributable safety failures, whilst exercising appropriate judgement elsewhere.

Pension	
Railway Pension Scheme (RPS)	Participation is in the RPS (after qualifying period of five years' service if joined Network Rail after 31 March 2004); benefit is normally payable from age sixty to sixty-five and accrues at a rate of one-sixtieth of final year's pensionable pay (less 1.5x single person's basic state pension), capped at £123,600 in 2009/10 for each year of membership; contribution to the RPS at the same rate as other members of the Network Rail section. A deferred cash sum is payable on retirement payable in the form of lump sum/4-weekly payments.
Network Rail Defined Contribution Pension Scheme (DCPS)	This is available to all employees joining from April 2004, providing Company contributions of up to seven per cent of pensionable pay, capped at £123,600 in 2009/10.
Network Rail Career Average Revalued Earnings Pension Scheme (CARE)	This was introduced as an alternative for all employees to the RPS and DCPS in November 2008. It provides a pension from age sixty-five of one-sixtieth of capped pensionable pay in each year of membership; contributions to CARE are at the same rate as for other members of the scheme.
Other pension benefits	Some Directors are also entitled to additional pension benefits that are provided through the DCPS.

Other benefits

Certain benefits are provided on an affordability basis
- cash car allowance
- private medical insurance
- discounted rail travel
- life assurance.

MIP 2009/10

Annual incentive

As detailed in last year's Annual Report, participants under the MIP 2009/10 were eligible to receive incentives based again on demanding business performance measures and targets. The annual incentive for 2009/10 took account of the particular requirements for Control Period 4, revisions to the Network Licence and a wider review introducing new key performance indicators (KPIs).

The business and individual performance measures related directly to the objectives set out by the ORR in Condition 16 of the Network Licence of Network Rail Infrastructure Limited, compliance with other licence conditions and with conditions of access agreements.

Business performance measures

The amount payable to Executive Directors was calculated by reference to performance against two key groups of measures:

a) **Mechanistic measures** – There are four key 'mechanistic' measures being objective measures reflecting network performance:
- Public Performance Target (combined freight/passenger train performance)
- Asset Stewardship Indicator
- Cost Efficiency
- Passenger Satisfaction.

The first three of these measures were similar in purpose to the three measures used in previous years' MIPs; the fourth was a new measure reflecting the importance of passenger satisfaction.

These four measures were equally weighted.

b) **Judgemental elements** – There are two judgemental elements where no single formal index exists:
- Customer Satisfaction
- Progress on delivering major enhancement and renewal schemes.

These two elements were also equally weighted.

The sum of the mechanistic elements and the judgemental elements made up the total 'derived' bonus payment. However, the Remuneration Committee continued to have discretion to determine whether the amounts payable might be reduced.

The total potential incentive award payable was the sum of the outcomes of each measure. Each of the performance measures below stood alone and was calculated independently.

Details of the mechanistic measures:

Measures	Weighting	Description
Public Performance Target (PPT)	20 per cent	This incorporated the Public Performance Measure for passenger journeys and an equivalent measure for freight journeys, with weightings which reflected the relative traffic flows of passenger and freight.
Asset Stewardship Indicator	20 per cent	This measured the quality of Network Rail's asset stewardship, based on asset condition, reliability and performance across Network Rail's key asset categories. This was calculated by measuring relevant asset stewardship measures across the key asset categories using the weightings detailed in the table on page 39.
Cost Efficiency	20 per cent	This was defined as the annual cost of Network Rail, normalised by the capacity provided and adjusted by renewals activity. This was then compared to a baseline. This measure reflects, therefore, the savings made by Network Rail through unit cost and scope efficiencies. The Cost Efficiency Measure tracked the efficiency savings for operating, maintenance and renewals costs. The measure was expressed as a percentage and reflected expenditure compared with the ORR pre-efficiency assumptions. The measure covers all operations, maintenance and renewals activities and measures total expenditure adjusted by the network capacity provided, as measured by vehicle miles and freight gross tonne miles. Each year, the Cost Efficiency Measure will measure cumulative efficiency across the whole of CP4 and the efficiency compared to the previous year. The targets for this MIP are expressed on an annual basis.
Passenger Satisfaction	20 per cent	This was measured through the National Passenger Survey (NPS) commissioned by Passenger Focus which provided a network-wide picture of customers' satisfaction with rail travel. The target used in this MIP was based on the 'overall satisfaction' rating in that survey. The NPS measures satisfaction twice a year, and the ratings used as 'actuals' for the purpose of the MIP were the average of the two ratings in Spring and Autumn 2009.

Details of the Asset Stewardship Indicator:

Asset categories included in the Asset Stewardship Indicator

Asset categories	Factors included in this asset category	Weighting
Track	Good track geometry; poor track geometry; rail breaks; intervention and immediate action faults	40 per cent
Signalling	Condition assessment; signalling failures causing over 10 minutes delay to trains	25 per cent
Electrification and plant	Substation and contact system condition; power supply incidents causing train delays	10 per cent
Telecoms	Telecoms condition	5 per cent
Operational property	Station stewardship; depot stewardship	10 per cent
Structures	Assets subject to special investigation or inspection; temporary speed restrictions	10 per cent

Taper

The structure of the MIP for 2009/10 incorporated a taper principle in respect of the four mechanistic measures. This allowed significant performance to be recognised against a background of continued year on year stretch performance changes. The specific targets and taper trigger points were decided by the Committee, taking into account regulatory targets.

Trigger

Payments under each of the four measures can only be made if performance met or exceeded the trigger performance as determined by the Committee in accordance with the taper principle. If target levels were achieved, payments would be calculated for above-target performance on a 'straight line' basis up to 'maximum' target level; the maximum incentive could be earned by achieving a level of performance at least equal to delivering one year early the 2010/11 performance on each measure as contained in the 2009 CP4 Delivery Plan.

Mechanistic incentive measures out-turn 2009/10

Performance measure	Taper Target	Target	Maximum Target	Actual
Public Performance	88.8	89.0	89.6	89.7
Cost Efficiency Index	1.4	2.9	5.8	5.8
Asset Stewardship Indicator	0.013	0.019	0.025	0.032
Passenger Satisfaction	82.4	83.4	85.4	82.3

Personal performance measures

There are no individual performance measures set for the Executive Directors. The Committee believes that collective accountability of the Directors necessitates a focus on collective performance incentives without individual performance measures. Other senior executives do have individual performance measures in addition to the business performance measures.

Committee discretion

The Committee may exercise its discretion and reduce the amounts payable if, over the year, the overall business performance of Network Rail, including the level of safety performance and net debt, is deemed by the Committee to be unsatisfactory. See pages 40 to 42 for details.

Details of the judgemental measures:

Measure	Weighting	Description
Customer Satisfaction	10 per cent	This was an assessment of how well Network Rail engages with its key customers (principally train and freight operating companies). The assessment of payments under this measure was made by the Committee, taking account of the ORR's quarterly performance reports and principally the results of the Customer Satisfaction Survey carried out by a third party. An improving result would produce a potential payment, the size of which would be determined by the Committee, taking account of this and any other relevant information that may be available.
Progress on Delivering Major Enhancement and Renewal Schemes	10 per cent	An annual report on the degree of achievement against progress on delivering major enhancement and renewal schemes was produced by Network Rail. In determining the extent to which a payment was to be made under this measure, the Committee made an overall judgement after reviewing the annual report. No payment was to be made under this measure if a number of milestones were not achieved or authorised project costs overspent.

Remuneration policy in practice

Basic salary

Annual basic salary as at 31 March 2010

Executive Directors	£
Iain Coucher	613,000
Patrick Butcher*	350,000
Robin Gisby	330,000
Peter Henderson	440,000
Simon Kirby	330,000
Paul Plummer	310,000

* Appointed to the Board of Directors on 20 April 2009.

2009/10 incentive awards – considerations by the Committee

As stated on page 33, each year, and notwithstanding that targets and triggers having been met and thus awards are payable, the Committee has the ability to exercise discretion to reduce the awards in respect of both the potential annual incentive awards and also any maturing L-TIP award.

Process adopted

In preparing for this aspect of this element of its role in relation to potential awards for 2009/10, the Committee gave considerable thought and discussion to the content of the process. Gathering a wide range of data, information and informed opinion was identified as a crucial tool in achieving the balanced decision needed.

Reports from the Board Committees responsible for reviewing key risk aspects of Network Rail's business – the Safety, Health & Environment Committee and the Audit Committee – were prepared by those committees at the request of the Remuneration Committee with the objective of providing more detailed conclusion and observation on the key risk performance statistics and, importantly, the overall appetite and responsiveness of the executive team to risk and the effectiveness of its management of these.

As part of this process, in the same spirit of collaboration as was adopted in consulting Members on the structure of the MIP, in April this year the Committee took the opportunity of seeking the views of Members. The Chairman of the Committee wrote to all Members inviting them to comment on application of the discretion.

The Committee also benefited from being able to consider the views of the ORR as expressed in a letter from the ORR to the Chairman of the Committee in which the ORR set out its general assessment of Network Rail's achievements in the year, together with a subsequent meeting. This formed a major contributor to the Committee's thinking given the role of the ORR and the benefit it has in expertise and resource to analyse Network Rail's performance generally and especially against the challenges of CP4.

In their non-executive capacities Committee members also made their own observations and assessment of performance of Network Rail over the year. The Committee members drew, therefore, on their own views on performance and opinions voiced to them.

In April and May 2010 the Committee then met on a number of occasions to consider the potential awards payable which matured for 2009/10. With the benefit of the weight, depth and breadth of all the data and opinion to hand, the Committee debated at length the overall performance of the Company, the degree of success in implementing performance improvements, the areas where progress has been less than expected or required and the implications of both in delivering the outputs for CP4 and facilitating the success of the rail industry in CP5.

Key considerations for 2009/10

In this report the Committee wishes to highlight its assessment on the following key focus areas of performance:

Safety

Safety is one of the key discretionary items for assessment for the Committee, when it comes to consideration of payments under the incentive plan. Rightly so, it commanded particular scrutiny again this year.

The Committee reviewed safety performance during the year against a range of safety indicators under various headings including passenger fatalities, workforce fatalities, accident frequency rate (AFR) and RIDDOR incidents. Against these the Committee identified that good progress towards the regulatory outputs for safety is being made. Overall risks to passengers have declined significantly. The British rail system is, by independent assessment, one of the safest in Europe. Workforce safety has benefited from a 30 per cent reduction in the AFR, making railways one of the safest places to work, when compared to industries delivering in similar environments. Measurements in the RSSB's Precursor Indicator Model support the view that indicators are moving in the right direction. The implementation of the major organisational changes in November 2009 was noted by the Committee including its application of safety assurance tests.

Regrettably, however, there were three fatalities amongst those people working on the infrastructure: one Network Rail employee and two working for its contractors. Investigations are on-going on each of these but to date no evidence of fundamental failure or systemic failure of safety systems has been established. Moreover areas for improvement against the RSSB's Precursor Indicator Model have also been identified in several areas.

The Committee then applied a judgement as to how effective the executive leadership team had been in providing appropriate safety leadership to promote and drive safety excellence through the Company and into its supply chain throughout the year. It also considered what message the Committee believed should be sent to all in Network Rail since a safety culture must pervade the full spectrum of activities in the business and represents a collective responsibility of all those who work within or for it.

The Committee concluded that, without seeking to detract from the improvements made, there was still more to be achieved, that continued focus on delivery of this was needed and further step changes in the development of the Company's safety culture needed to be undertaken. For this reason the Committee exercised its discretion and reduced awards in 2009/10 to reinforce the importance of this.

Operational performance
Punctuality and delay minutes performance during the bulk of the year was ahead of the regulatory target and against individual plans for most train and freight operating companies. The impact of the exceptionally cold and snowy weather on the performance of the railway, however, was profound during several months of 2009/10.The Committee recognised Network Rail's performance prior to this as a significant achievement and so too was the delivery of services in very challenging environments during the bad weather.

The Committee noted, however, that not all industry performance targets were met – in Scotland and the south east for example. On the east coast, performance issues also arose. Whilst analysis indicates that there was a variety of reasons for this, not all being within Network Rail's control – such as extreme weather, suicide or increasing levels of cable theft and the performance of rolling stock – areas for improvement by Network Rail have been identified and are being implemented. The impact of these events on the MIP performance measures reflected these issues. As such the additional application of the Committee's discretion in this area was not considered appropriate.

A vital enhancement to maximising capacity on the network and handling the increasing complexity of operations has needed the introduction of new timetabling technology. The new integrated train planning system (ITPS) will bring great benefits to passengers, freight users, customers and Network Rail. Preparations for its introduction in May 2010 experienced, however, some teething problems. Whilst appreciating that the introduction of any complicated software technology is likely to experience some issues at the initial stages, the Committee considered it important to acknowledge the significance of the role of ITPS in facilitating future improvements. Accordingly it was not considered appropriate to reduce the level of award against this measure specifically because of any technology issues experienced in this area during 2009/10, but its impact was influencial in the general considerations for the application of the overriding discretion.

Cost efficiency
There is a fundamental variance of approach to the measurement of efficiency between that of the ORR and that of the executive team. Both agree about the need to drive through efficiency. The executive team has plans to deliver the outputs for CP4 through its published Delivery Plan. This is designed to provide flexibility to scheduled work and priorities between years within the control period. The ORR measures efficiencies in line with the profiles contained in the Determinations.

Both recognise the challenge in the remainder of CP4 but the executive team believes that its plans combined with the evidence of ability to deliver in the first year of the control period provide support of the sustainability and likelihood of success in achieving the outputs for the full five years.

The Committee has to assure itself that the incentive regime for 2009/10 on efficiency and the outturns for the year have been met and consider whether there is any evidence as to whether these have been achieved in a way that can meet the outputs of the CP4 Determinations in 2013. At this point in time it has concluded that it is satisfied with the methodology of the performance outturn. There is, in its view, therefore, no basis for penalising the team through the MIP on this measure.

Asset stewardship
The Committee considered the overall achievements to date and also the plans for sustaining on-going improvements in asset management. Note was made of the assurance from a best practice review undertaken by AMCL (consultants working for the ORR) which was largely positive when comparing Network Rail against an asset management excellence model and how it had progressed since the previous review in 2006. The Committee also considered that there was evidence of the continuing focus of the executive team on further improvement with asset management.

Some areas of management, however, need particular focus going forward such as power supply. On sustainability policies for structures, work is being undertaken in collaboration with the ORR. Notwithstanding this, the Committee viewed the progress made to be significant with evidence of on-going commitment and planning. Accordingly no reduction on this measure was made at this time.

Customer and passenger satisfaction
The Committee noted that the latest satisfaction surveys showed much improved levels of passenger satisfaction as well as some progress in freight user and stakeholder measures and that these improvements received positive comments from the ORR. All, including the executive team, acknowledge, however, that there is still more to be achieved to improve these key indicators and that these should remain a major focus going forward. The Committee concluded that this needed recognition in the exercise of its discretion in these areas.

Investment programme
Good progress has been made in delivery of investment in the rail network. An example is the challenging environment of the Thameslink project where milestones have been met despite the demands of a programme of enormous complexity and scale. The increased activity in enhancements has also been supported by improvements in enhancement management which has be acknowledged by the ORR. Major improvements have been made to the way in which major investment schemes are delivered resulting in reduced level of passenger disruption during investment activity and no major overruns in improvement works. There have been some areas, however, where management has as yet been unable to achieve the efficiencies targeted. Also, and as acknowledged by the Executive team, there have been some weaknesses in some enhancement areas.

Minimising the impact of disruption to passenger and freight users from planned engineering work has been a major focus of the executive team in 2009/10. The CP4 target for this new measure was achieved demonstrating the result of this effort in planning works and methods of delivery.

Consequentially, in the view of the Committee, the successful delivery of significant engineering activity in the year needed to be acknowledged but the discretion should be applied in part to this MIP measure.

Committee's decision

Taking all of these views and others into consideration, the Committee formed the decision that Network Rail's performance achievements need to be assessed in the context of delivering against a demanding and stretching set of outputs for CP4. It believed that there is a significant amount still to be achieved in order to deliver a world class railway. This requires further changes to both what Network Rail does and how it does it, whilst simultaneously making further efficiencies in every area of the business on top of the 27 per cent cost reduction delivered in the previous five year control period. Measurement of performance should be against the Delivery Plan as this was approved by the Board of Network Rail as being what and by when Network Rail would deliver its objectives. It detailed the priorities and expectations of the Board for the year, as well as laying out how Network Rail would achieve the outputs for CP4, for the available funding levels, and meet other commitments and the Company's aspirations for the future.

In reviewing its overall responsibility to consider a discretionary overlay on the annual award the Committee reached, therefore, the following conclusion. It had regard to its overall assessment of a year of real progress towards long term objectives. But beyond those decisions reached against the mechanistic targets and judgemental measures the Committee felt that it was appropriate to apply a downward discretion of 20 per cent on the award. The major part of this applies to the issue of safety. The Committee noted the real progress made on a number of key measures of safety as outlined in this report but felt that it also needed to be recognised that there is still much to do and that there have been a number of very regrettable workforce incidents, including the fatality of one Network Rail employee and two contractors. Moreover, both the Committee and management share the view that Network Rail needs in the future to build even further on progress to date on its path to world class standards. The Committee determined that in the absence of clear further improvements to the safety record next year there will be further, and potentially more severe, downward discretion applied to future awards.

In addition to the safety issue, the Committee took due recognition of other concerns including those of the ORR relating to external relationships and the cost efficiency measure.

Annual awards 2009/10	Award maximum salary weighting	Discount or discretion applied
Mechanistic measures		
Public Performance	20%	0%
Cost Efficiency Index	20%	0%
Asset Stewardship Indicator	20%	0%
Passenger Satisfaction	20%	100%
Judgemental measures		
Customer satisfaction	10%	70%
Investment programme	10%	20%
Reduction against measures		29% of maximum payable
Discretionary overlay		20%
Total annual award reduction		43.2% of maximum payable

L-TIP awards 2009/10	Discretionary reduction applied
PPT	0%
Operations, maintenance and renewals targets	0%
Total L-TIP award reduction	8% of maximum achievable

Details of the monetary incentive awards approved by the Committee as a result of these discretionary reductions are set out on page 43.

Future developments of the MIP and the application of the Committee's discretion

The intense review undertaken by the Committee in 2009 reinforced the Committee's appreciation of the scale of challenge in finding the right balance of encouragement and that of penalty for the executive team. In particular, in the light of current economic circumstances, upon request by the Board, the Committee has agreed that for the Executive Directors and members of the Executive Committee the future MIP 2010/11 will be suspended pending a review to assess its suitability for the new environment in which Network Rail operates. Upon conclusion of the review process the Committee will publish its plans for the MIP 2010/11.

As the nature of the demands on Network Rail and its performance delivery develop, so too must the means by which the Committee exercises its overall discretionary powers as well as its responsibility for shaping the mechanism of the MIP each year and setting the targets and triggers within these.

The Committee will continue to consider the options available for the optimum incentive regime appropriate for Network Rail's unique position in its industry and the constraints upon the adoption of conventional and universal incentive methodologies. Short and long-term aims of the MIP will focus on providing assurance to stakeholders of the effectiveness of its structure in incentivising delivery of the wide responsibilities that Network Rail's management has, including in relation to safety, service delivery and the Company's corporate responsibilities. The Committee will also continue to focus on what alternative structure for the long-term incentives can be adopted which create a symbiotic relationship between reward for long-term objectives (such as out-delivery of a control period's targets and even longer-term objectives for the rail industry) and the sharing of the risks in achieving these.

2009/10 incentive awards – outturn

Audited Name	Annual incentive £	L-TIP for three years to 31 March 2010 – amount earned* £
Current Directors		
Iain Coucher	348,184	293,165
Patrick Butcher**	198,800	nil
Robin Gisby	187,440	121,434
Peter Henderson	249,920	210,444
Simon Kirby	187,440	143,918
Paul Plummer	176,080	137,380
Past Director		
Ron Henderson***	11,085	90,849

* Indicative only as amount only earned if stretching targets met and may be reduced by the Committee exercising its discretion.
** Appointed to the Board of Directors on 20 April 2009.
*** Retired from the Board of Directors on 19 April 2009.

Long-Term Incentive Performance measure

Following approval at the Network Rail Limited's AGM in July 2009 of the three-year period running from 2009/10 to 2011/12, a new single measure for the long-term incentive has been introduced; this is Financial Value Added (FVA). This single measure is defined as the value added in the relevant three-year period, over and above the amount determined by the ORR for the relevant period.

The formula for FVA is the differences between the ORR's income and expenditure determinations and Network Rail's actual income and expenditure.

FVA is expressed in £m. Thus, if Network Rail outperforms the ORR determinations by £100 million over the relevant three-year period, the FVA Index is expressed as +£100m.

L-TIP for three-year period – 1 April 2007 to 31 March 2010

Public Performance

Maximum target	Minimum target	Actual
89.6 %	88.8 %	89.7 %

ORR cost reduction targets

Maximum target	Minimum target	Actual
(12,687)	(13,363)	(12,795)

Potential L-TIP awards

Director	Performance period: 1 April 2007 to 31 March 2010 £	1 April 2008 to 31 March 2011 £ 2008/09	2009/10	2010/11	1 April 2009 to 31 March 2012 £ 2011/12	1 April 2010 to 31 March 2013* £ 2012/13
Iain Coucher	293,165	302,209	348,184	2011 MIP Value	613,000	
Patrick Butcher**	Nil	Nil	Nil	Nil	350,000	
Robin Gisby***	121,434	130,185	187,440	2011 MIP Value	330,000	
Peter Henderson	210,444	216,920	249,920	2011 MIP Value	440,000	
Simon Kirby***	143,918	160,215	187,440	2011 MIP Value	330,000	
Paul Plummer***	137,380	149,575	176,080	2011 MIP Value	310,000	
Total	**906,341**	**959,104**	**1,149,064**		**2,373,000**	

* Subject to review – see page 42.
** Appointed to the Board of Directors on 20 April 2009.
*** Appointed to the Board of Directors on 1 October 2008 – includes potential award amounts relating to previous position within the Company before appointment to the Board of Directors.

Notes
1 For performance period 1 April 2008 to 31 March 2011 the L-TIP will be calculated on an average of three annual award payments subject to performance conditions.
2 2008/11: The maximum L-TIP payment for the performance period 1 April 2008 to 31 March 2011 is equal to the average of the annual payments received for the years 2008/09, 2009/10 and 2010/11. For example, for Iain Coucher the calculation to set the maximum award will be: L-TIP maximum = (£302,209 + (£348,184+2011 MIP value)/3.
3 2009/12: The maximum L-TIP payment for the performance period 1 April 2009 to 31 March 2012 is equal to the maximum value the Director is eligible to receive under the relevant MIP award. For example the calculation for Iain Coucher will be: L-TIP maximum = 100 per cent of basic salary as at 1 April 2009 (£613,000).

These maximum sums will only be paid if the performance measures outlined on page 38 are met in full.

Pensions

Executive Directors are entitled to a pension provided from one of the three Company pension schemes on the same terms as for other employees. In addition, a pension supplement is paid either into the Defined Contribution Pension Scheme or as a cash alternative. Details are set out on pages 48 and 49.

Executive Directors' contractual terms

The Executive Directors of the Company are also the Executive Directors of Network Rail Infrastructure Limited and their employment contracts (service agreements) are with that company. No other contractual provisions or remuneration arrangements exist in relation to their directorships of the Company or any other company within the Network Rail Group.

At the time of drawing up each service agreement the Committee takes into consideration the UK Listing Authority's corporate governance code and the recommendations published at that time by certain bodies, for example statements of the ABI and the NAPF on best practice on executive contracts and severance. These are applied as far as practicable and appropriate having regard to the nature of the business, the corporate structure of the Company and current practice of the time.

All the Executive Directors' service agreements provide for notice periods of no greater than one year, to reflect current corporate governance best practice. Executive Directors are required to give not less than six months' notice if they wish to leave.

The Chief Executive's service agreement (and the letter of appointment of the Chairman) also contains provisions for termination of his appointment without compensation upon the occurrence of certain significant financial failures of the Network Rail Group unless a majority of the Board of the Company and the DfT (in its role as provider of credit facilities) decide that these appointments should not be terminated.

Taking the principles contained within current corporate governance best practice relating to compensation in the event of early termination of a director's service agreement, each such agreement contains an express provision requiring the departing director to exercise their duty to mitigate their loss. Network Rail will have regard to that duty and contractual requirement on a case by case basis when assessing the appropriate level of compensation which may be payable, including using phased payments.

Current service agreements:

Executive Directors	Effective date of contract
Iain Coucher*	1 August 2007
Patrick Butcher	20 April 2009
Robin Gisby**	1 October 2008
Peter Henderson	3 October 2002
Simon Kirby**	1 October 2008
Paul Plummer**	1 October 2008

* Previously held the position of Deputy Chief Executive under an earlier employment contract (service agreement) effective from 3 October 2002.

** Previously held other senior executive position under an earlier employment contract.

Policy on Executive Directors' external appointments

It is recognised that Executive Directors may be invited to become non-executive directors of other companies or hold positions in other organisations or bodies and that such appointments can broaden their knowledge and experience to the benefit of the Company. An individual Executive Director will normally be required to account to Network Rail for all fees received in respect of such directorships unless otherwise approved by the Committee.

None of the Executive Directors currently holds any such positions other than those associated with the performance of their duties within Network Rail. No fees are received by them for any such positions.

None of the Executive Directors is a non-executive director on the board of any listed company.

Non-Executive Directors

Non- Executive Directors' contractual terms

Non-Executive Directors are appointed by the Board on the recommendation of the Nominations Committee. Their appointment is for an initial term of three years, subject to election by the Members of Network Rail at the first AGM following their appointment. They do not have employment contracts. Instead the terms of their engagement are set out in a letter of appointment and their appointments may be terminated at any time on six months' notice without compensation. Further, as mentioned above, the letter of appointment of the Chairman also contains provisions for termination of his appointment without compensation upon the occurrence of certain significant financial failures of the Network Rail Group unless a majority of the Board of the Company and the DfT (in its role as provider of credit facilities) decide that these appointments should not be terminated.

Current letters of appointment:

Current Non-Executive Directors	Effective date of original letter of appointment
David Bailey*	3 October 2002
Yvonne Constance	1 May 2005
Graham Eccles	7 February 2010
Michael Firth	4 December 2004
Christopher Green	26 June 2005
Lawrie Haynes	26 January 2010
Rick Haythornthwaite	23 March 2009
David Higgins	1 April 2010
Janis Kong	13 January 2010
Steve Russell	19 September 2007

* David Bailey's appointment in 2002 was as Special Director; upon conversion of his appointment a new letter of appointment was issued in 2005. He then sought election by the Members at the Network Rail Limited AGM in July 2005.

Non-Executive Directors' remuneration

As stated above, the Non-Executive Directors of the Company are also the Non-Executive Directors of Network Rail Infrastructure Limited but their letters of appointment are with that company covering both positions.

No other contractual provisions or remuneration arrangements exist in relation to their directorships (if any) of any other company within the Network Rail Group. For the purpose of this Directors' remuneration report and the Directors' remuneration report for Network Rail Infrastructure Limited, therefore, the following provisions of this report also appear in the Annual Report of that company. The letters of appointment are available for inspection at the Company's registered office.

Fees are reviewed bi-annually and, with the exception of the fee for the Chairman (which is determined by the Remuneration Committee), are set by the Executive Directors to attract individuals with the appropriate range of skills and experience. In determining the level of fees their duties and responsibilities are considered, together with the level of time commitment required in preparing for and attending meetings. Benchmarking is also undertaken against comparable companies, both regulated and under-regulated with synergies of business type and business drivers. The strategy for Non-Executive Directors' fees is broadly to reflect the relevant market median. The fees were last reviewed with effect from February 2010 and no increase in base fees was awarded. Additional fees for the chair of certain committees are paid.

Current annual fees (audited) for the Non-Executive Directors (£)

				Committee chairmanship**				
	Board membership	Senior independent director	Safety Health and Environment	Remuneration	Policy and Performance	Audit	Treasury	Nominations
David Bailey	50,000		10,000					
Yvonne Constance	50,000							
Graham Eccles	50,000							
Michael Firth	50,000					10,000	6,000	
Christopher Green	50,000							
Lawrie Haynes	50,000							
Rick Haythornthwaite	250,000*				Nil***			Nil***
David Higgins	50,000							
Janis Kong	50,000							
Steve Russell	50,000			10,000				

* On appointment as Chairman on 22 July 2009 fee increased from £50,000.

** In view of the additional responsibilities and time commitment placed upon the chairmen of Board committees, and in line with the recommendations of the Higgs Report and good corporate governance practice, additional fees have been paid to a Non-Executive Director who chairs certain of the Board committees.

*** Fee introduced in 2010 but Rick Haythornthwaite, as current chairman of this Committee, has waived payment of this fee.

Non-Executive Directors' contractual terms of appointment

Provision	Policy
Period	Three year term which can be extended by mutual consent
Termination	By the Director or the Company giving the other six months' written notice without compensation
Fees	As described on page 45
Expenses	Reimbursement of expenses reasonably and properly incurred in attending meetings of the Board or otherwise in the performance and discharge of their duties and responsibilities
Time commitment	Varying dependent on Board and Board committee duties but in general terms estimated to comprise as a minimum per annum*: • Eight Board meetings (three of which will be off-site in 2010/11)** • Typically six or more Board Committee meetings (depends on committee membership)** • Three Stakeholder relationship events • Two board strategy days** • One AGM** • One Half Year Members' meeting • Two Members' workshops/meetings** • Three Non-Executive Directors only meetings. * excluding induction phase. ** each of these are anticipated to require preparation time of up to one day per meeting.
Additional directorships	Consent from the Chairman of the Board of Network Rail is required in relation to taking up other positions outside Network Rail
Special terms	None

Non-Executive Directors – Pensions

Non-Executive Directors do not receive any benefits from the Company or from the Network Rail Group nor participate in any incentive scheme or pension arrangements. Christopher Green and Graham Eccles receive pensions from other sections of the industry-wide Railway Pensions Scheme (RPS) that are not associated with Network Rail as a result of their previous employment within the rail industry.

Policy on Non-Executive Directors' external appointments

Prior to appointment of the Board of Network Rail the existing other appointments of candidates for Non-Executive Director positions are reviewed by the Nominations Committee and assessed as to their time demands. Appointees are also required to confirm within their appointment terms that they have adequate time to meet their responsibilities as a Non-Executive Director of Network Rail. Furthermore each is required to seek approval from the Chairman of the Board before taking up any additional positions.

Disclosure of Directors' remuneration for 2009/10

Audited

This section of the report sets out the remuneration paid or payable to the Directors in respect of the financial year to 31 March 2010.

Directors' remuneration comparison 2009/10 against 2008/09 (£000s)

	Basic salary/fees†		Bonuses		Benefits		Supplementary Company pension contributions/AVC payments by the Company		Total	
	2009/10	2008/09	2009/10	2008/09	2009/10	2008/09	2009/10	2008/09	2009/10	2008/09
Executive Directors										
Iain Coucher[A]	613	605	641	150+	15	15	178	177	1,447	947
Patrick Butcher[B]	350	–	199	–	15	–	105	–	669	–
Robin Gisby	330	150	309	139	96	72	–	–	735	361
Peter Henderson[C]	440	434	460	329	15	15	126	125	1,041	903
Simon Kirby	330	150	331	137	15	7	93	74	769	368
Paul Plummer	310	141	313	142	92	68	5	2	720	353
Non-Executive Directors										
David Bailey	56	47	–	–	–	–	–	–	56	47
Ian Buchan	50	47	–	–	–	–	–	–	50	47
Yvonne Constance	50	47	–	–	–	–	–	–	50	47
Jim Cornell[D]	20	68	–	–	–	–	–	–	20	68
Graham Eccles[E]	7	–	–	–	–	–	–	–	7	–
Michael Firth	65	62	–	–	–	–	–	–	65	62
Christopher Green	50	47	–	–	–	–	–	–	50	47
Lawrie Haynes[F]	9	–	–	–	–	–	–	–	9	–
Rick Haythornthwaite	188	1	–	–	–	–	–	–	188	1
David Higgins	–	–	–	–	–	–	–	–	–	–
Janis Kong[G]	11	–	–	–	–	–	–	–	11	–
Ian McAllister[H]	85	265	–	–	–	–	–	–	85	265
Steve Russell	55	47	–	–	–	–	–	–	55	47
Past Executive Director										
Ron Henderson[I]	20	413	102	319	6	118	–	–	128	850
Total emoluments of Directors	**3,039**	**2,524**	**2,355**	**1,216**	**254**	**295**	**507**	**378**	**6,155**	**4,413**

A Value of basic salary/fees for 2008/09 based on three months at £585k per annum and nine months at £613k per annum reflecting salary review in July 2008.
B Joined the Company on 2 March 2009 and was appointed to the Board of Directors on 20 April 2009. Basic salary includes salary payment made in the financial year prior to his Board appointment (1 April 2009 to 19 April 2009).
C Value of basic salary/fees for 2008/09 based on three months at £420k per annum and nine months at £440k per annum reflecting salary review in July 2008.
D Stepped down from the Board 22 July 2009.
E Joined Board of Directors 07 February 2010.
F Joined Board of Directors 26 January 2010.
G Joined Board of Directors 13 January 2010.
H Stepped down from the Board 22 July 2009.
I Retired from the Board of Directors 19 April 2009.
† Executive Directors receive salaries and Non-Executive Directors receive fees.
\+ In 2009, given his overall leadership position, Iain Coucher and the Remuneration Committee mutually agreed that he would not be considered for any annual bonus for 2008/09. Value of £150k represents L-TIP payment only.

Notes

1. 'Benefits' – all Executive Directors received life assurance benefits during such part of the year as they were employed by the Company that relate to the cost incurred by the Company of insuring the Directors' life assurance and spouses' benefits which, had they died during the year, could not have been wholly paid by the relevant pension scheme and would therefore have been met by the Company's insurer. The disclosure also includes the cost of private medical insurance, car benefits and any additional pension allowance that was selected as an alternative to an additional contribution in DCPS. All the numbers disclosed include the tax charged on the benefits. No Director received an expense allowance during the year.
2. No compensation payment for loss of office was made to any Director or past Director during the year.
3. For the purpose of disclosure required by Schedule 5 of the Companies Act 2006 the total aggregate emoluments of the Directors in respect of 2009/10 was £6.2m (2008/09: £4.4m).
4. The supplementary Company pension contributions/AVC payment by the Company reflect values for the full year.

Directors' emoluments

The following sections headed Directors' emoluments and Executive Directors' pensions along with their associated footnotes have been subject to external audit.

The fees, which are neither performance related nor pensionable, are benchmarked and periodically reviewed against, and are in line with those paid by other comparable companies taking into account time commitment and competition for similar positions in other companies.

The total amount of Directors' emoluments for services provided solely to the Company during the year was £6,155,000 (2008/09: £4,413,000). This figure includes emoluments for additional Director appointments made during the year.

Executive Directors' pensions

The table below and on page 49 shows the pension entitlement from the respective Network Rail pension scheme for each Executive Director of the Company during the year ended 31 March 2010, together with the increases in those benefits during the year, calculated using the accrued benefit basis.

The increases in pension benefits during the year represent the amount of the extra annual pension entitlement earned resulting from additional length of service and/or changes in salary.

The increase in accrued approved benefit during the year is shown in the table below. Values are normally shown before (column A) and after (column B) the exclusion of the effect of inflation. However as inflation was negative in the year to 30 September 2009 no inflation adjustment was required. All benefit values shown exclude the effect of any additional voluntary contributions made by the Director.

Executive Directors participate in either the RPS or the CARE Scheme and benefit accrues at a rate of one-sixtieth of capped final pensionable pay (RPS) or capped average pensionable pay (CARE) for each year of membership. They contribute at the same rate as other members of the respective scheme. In addition, some Directors are entitled to either additional pension benefits that are provided through the Network Rail Defined Contribution Pension Scheme (DCPS) or an additional cash allowance.

Executive Directors are members of one of Network Rail's three occupational pension schemes. In normal circumstances the earliest age at which they are entitled to receive their defined benefit pension without actuarial reduction is age 60 in the RPS or age 65 in the CARE Scheme. However, the Directors can retire early on the same terms and conditions that apply to other members of the respective scheme from the age of 50 in the RPS or 55 in the CARE Scheme. The minimum retirement age in the RPS increased to age 55 from 6 April 2010 for members joining after 5 April 2006. The actuarial reduction factors that apply under the RPS are a two per cent per annum reduction between the ages of 60 and 55 and a three per cent per annum reduction for ages below 55, although for RPS members not covered by

Core pension benefits – audited

	Gross increase in accrued occupational pension £ (A)	Increase in accrued occupational pension net of inflation† £ (B)	Total accrued occupational pension at 31 March 2010 £ (C)	Transfer value of accrued occupational pension at 31 March 2009 £ (D)	Transfer value of accrued occupational pension at 31 March 2010 £ (E)	Total change in transfer value during period £ (F)	Value of net increase in accrual over period £ (G)
Current Directors							
Iain Coucher	2,708	2,708	15,413	139,097	171,537	19,857	17,557
Patrick Butcher*	2,038	2,038	2,130	527	15,497	6,756	6,618
Robin Gisby**	3,283	3,283	27,260	329,147	393,537	51,807	34,817
Peter Henderson	2,708	2,708	15,413	193,532	250,043	43,929	31,352
Simon Kirby**	2,635	2,635	13,912	104,025	129,638	13,030	11,975
Paul Plummer**	2,934	2,934	20,064	156,202	184,791	16,006	14,440
Past Director							
Ron Henderson***	761	761	13.805	229,218	238,285	8,836	12,912

† As in prior years inflation adjusted values reflect the year to prior 30 September. The RPI to 30 September 2009 was negative (-1.4%) and a collar of 0 has therefore been applied in accordance with actuarial advice and market practice.

* Joined the Board of Directors on 20 April 2009 and having joined Network Rail on 2 March 2009 a member of the CARE Scheme from that date.

** Joined the Board of Directors on 1 October 2008. Being employed by Network Rail prior to that date the figures shown include pension benefits relating to prior service as required under the Companies Act 2006.

*** Retired from the Board of Directors on 19 April 2009.

Notes

1 Pension accruals shown are the amounts which would be paid annually on retirement (or earlier leaving) based on service to the end of the year.

2 Transfer values as at 31 March 2009 (D) and 31 March 2010 (E) have been calculated in accordance with version 8.1 of guidance note GN11 issued by the actuarial profession.

3 The change in the transfer value (F) includes the effects of fluctuations in the transfer value due to factors beyond the control of the Company and Directors, such as stock market movements. It is calculated after deducting the Director's contribution.

4 The value of net increase (G) represents the incremental value to the Director of their service during the year, calculated on the assumption that service terminated at the year end. It is based on the accrued pension increase (B) after deducting the Director's contribution.

Additional pensions benefits – audited

	Company contributions to additional pension provision or optional salary supplement whilst a Director during the year £	Company contributions to additional pension provision or optional salary supplement whilst a Director during prior year £	Matching Company additional voluntary contributions whilst a Director during the year £
Iain Coucher[A]	178,405	176,611	–
Patrick Butcher[B]	105,264	–	–
Robin Gisby[A,C]	81,251	63,956	–
Peter Henderson[A]	126,305	125,111	–
Simon Kirby[A]	93,178	74,126	–
Paul Plummer[A,C]	75,999	59,913	4,844
Ron Henderson[D]	5,212	103,648	–

A These Directors were Directors for the whole year.
B This Director was appointed on 20 April 2009.
C This Director elected to receive an equivalent additional allowance in 2008/09 in lieu of additional pension contributions. This payment is included in the benefit figure reported on page 48.
D This Director retired on 19 April 2009.

Notes
1 None of the Non-Executive Directors are members of any Network Rail pension arrangement nor do they have other pension entitlements save that Chris Green and Graham Eccles each receive a pension from the Railway Pension Scheme relating to their previous employment – see page 60 for details.
2 Where a Director is entitled to additional pension benefits they can choose the payment as salary supplement, less a deduction for national insurance or a pension contribution to the DCPS.

the Protection Order under the Railways Act 1993 cost neutral early retirement terms apply for pension benefits accrued from July 2009. In keeping with other members of the RPS scheme, the right to take early retirement benefits from the RPS is at the option of the individual, subject only to having left the Company's employment. In the CARE Scheme, the employer's consent is required and the pension is then subject to cost neutral early retirement terms

In addition to members' benefits, dependants' pensions are payable after the death of the member, in line with those payable to all members of the RPS and CARE Scheme. These are at the rate of half the pension the member would have received at normal retirement age on death in service or half the member's basic pension on death in retirement or after leaving service. Basic pension is pension before commutation for cash and excluding any benefits arising from Additional Voluntary Contributions. In addition, under both schemes pensions are payable to surviving children based on a proportion of the dependants' pension. The RPS provides guaranteed increases to all pensions in payment and deferment in line with the retail prices index. In the CARE Scheme the same terms apply subject to a maximum annual increase of five per cent.

Additional pension benefits

As described above, some Directors are entitled to additional pension benefits in which case the Director could choose the extent to which the gross payment was made to the pension arrangement, or taken as cash. Future contributions are at a pre-determined level, and the amount has been notified to each Director.

The contributions made during the year together, where appropriate, with contributions in respect of benefits accrued prior to the year under review are shown above.

The RPS also operates a matching additional voluntary contribution facility, whereby voluntary contributions paid by scheme members are matched by equivalent payments from the Company, up to certain limits. These matching arrangements were frozen for all scheme members of the Network Rail section of the RPS at the levels applicable on 6 November 2003, and this limit was applied to Directors as to other scheme members.

Performance graph

As the Company has no listed shares total shareholder return cannot be illustrated.

Directors' interests

As the Company has no listed shares Directors have no interests in shares of the Company.

On behalf of the Remuneration Committee

S.B. Russell.

Steve Russell

Chairman, Remuneration Committee
3 June 2010

Nominations Committee report

Highlights

Review of the composition of the Non-Executive Directors' skills and experience against the demands of Control Period 4.

Development and publication to Members of role profiles for Non-Executive Directors with invitation to Members to comment on these.

Extensive recruitment searches undertaken to identify four new Non-Executive Directors appointed between January and April 2010.

Extensive transparency of process with Members and other stakeholders.

Report contents

This report includes:

- the Committee's objectives and principles
- the Committee's composition and main activities in 2009/10.

Governance

The Committee is a committee of the Board of Network Rail. Its terms of reference are available from the Group Company Secretary and can be found on the Company's website: www.networkrail.co.uk.

The Nominations Committee was in place throughout 2009 comprising:

Current members	From	
Rick Haythornthwaite (Chairman of Committee from July 2009)	March 2009	
David Bailey	October 2002	
Steve Russell	November 2008	
Previous members	**From**	**To**
Ian McAllister (Chairman until July 2009)	October 2002	July 2009
Jim Cornell	October 2002	July 2009

Rick Haythornthwaite holds the chairman position of this Committee on a temporary basis pending the finalising of the current Non-Executive Director recruitments at which time the Board plans to identify another Non-Executive Director to hold this position. In the meantime, whilst the Committee is chaired by the Chairman of the Board (and thus not deemed independent for the purpose of this Committee), the other two members of the Committee are independent Non-Executive Directors in accordance with provision A.3.1 of the Combined Code. When dealing with any matters concerning his membership of the Board the Chairman will absent himself from the meeting of the Committee as required and meetings will be chaired by Steve Russell, the Board's Senior Independent Director.

The Committee asks the Chief Executive and Group HR Director to attend certain of its meetings.

Activities in 2009/10 During the year ended 31 March 2010, this Committee met eight times and its main focus was on managing the search for new Non-Executive Directors for which purpose it retained the services of Egon Zehnder and Korn Ferry Whitehead Mann. The search resulted in Janis Kong, Lawrie Haynes, Graham Eccles and David Higgins being nominated and duly appointed to the Board. These individuals broaden the business-to-business customer service, generalist, transport related business and project management experience available to the Board respectively.

Details of the key activities

The principal activities undertaken by the Committee in the period under review are set out opposite.

The Nominations Committee's activities in 2009/10

Meeting	Agenda item
April 2009	• Review of the status of the search for new Non-Executive Directors • Considering the process previously adopted for review of the performance of the Chief Executive and what options were available for alternative or additional approaches to such review.
August 2009	• Considering the selection criteria for new Non-Executive Directors, review of the skill base of the existing Non-Executive Directors and a revised selection criteria for future Non-Executive positions.
October 2009	• Receiving an update on the status of the search for new Non-Executive Directors • Considering a paper reviewing the terms of reference of the Committee and the allocation of responsibility between Board committees for review of succession plans for senior executive manager positions in the Company.
November 2009 (two meetings)	• Receiving updates on the status of the search for new Non-Executive Directors • Receiving an update on the status of search for advisers to the Board committees.
December 2009	• Considering the retirement of existing Non-Executive Directors • Reviewing the composition of the Board committees and agreeing the recommendation for changes to the composition • Agreeing the recommendation for the appointment of Non-Executive Directors.
January 2010	• Reviewing status of the search for other new Non-Executive Directors positions.
February 2010	• Reviewing status of the search for other new Non-Executive Directors positions • Considering the composition of a sub-committee of the Nominations Committee to review succession plans for executive positions.

Non-Executive Director recruitment

Following the recruitment of Rick Haythornthwaite early in 2009 as successor to Ian McAllister as Chairman of the Board, the Committee has been active in reviewing the composition and skills sets of the Non-Executive Directors. It formed the view that further evolution of composition would be timely – reviewing the skills needed for the future, adding different experiences and enhancing knowledge of Non-Executive Directors where appropriate.

The Committee also reviewed the long-term succession plans for Non-Executive Directors looking at the balance of skills and experience available to the Board as well as the vitally important success of the chemistry and competence of the Board as a whole. In addition, this analysis was applied to the Board committees.

With the decisions of several Non-Executive Directors to step down from the Board during 2010 analysis was undertaken by the Committee on the background, experience and skills required. Two firms of external search consultants, Egon Zehnder and Korn Ferry Whitehead Mann , were engaged to draw-up a diverse long list of possible candidates for the various role identified. Following further review, short-listed candidates met with Committee members and candidates for nomination to the Board were identified. At the end of this process, the following were appointed to the Board to serve as Non-Executive Directors:

Graham Eccles David Higgins

Lawrie Haynes Janis Kong

The terms of their appointments are detailed in the Remuneration report.

During the year, Ian Buchan retired from the Board on 31 March 2010. Further, Yvonne Constance and Christopher Green advised the Committee that they did not wish to serve for a further term but agreed to remain on the Board until the Annual General Meeting of Network Rail Limited on 21 July 2010.

Members' and stakeholders' engagement

In order to establish transparency of the process of recruitment of the new Non-Executive Directors and effective engagement in this important governance matter, the Chairman of Committee reported periodically to Members and other key stakeholders through the year on the views of the Committee and progress of the search.

In a series of letters to Members of Network Rail, also circulated to key stakeholders, the competencies profile of each of the Non-Executive Director positions identified by the Committee as being appropriate were provided. This accompanied the personal attributes expected for a Non-Executive Director position and explanation of the details of the recruitment process being adopted. Members (and other stakeholders) were invited to comment on these.

Upon selection by the Board, the Chairman has also given Members written explanation and rationale to the individual's appointment. Moreover in the case of the selection of one Non-Executive Director, on-line discussion has been encouraged seeking to provide a further opportunity for dialogue and assurance.

Election and re-election at annual general meeting
At the forthcoming Annual General Meeting resolutions on the election of each of the newly appointed Non-Executive Directors will be presented together with those Directors who are due for re-election. Accompanying the notice of that meeting will be detailed biographies and explanation of the reasoning for appointment for each Director seeking election or re-election.

Moreover, as part of Network Rail's general policy of adoption of corporate governance best practice, the Chairman of the Board, Rick Haythornthwaite, will also be seeking from this year annual re-election notwithstanding his election last year or the terms of the Articles of Association of Network Rail Limited.

Board committee membership
The Committee is responsible for nominating appropriate individuals for membership of the Board's committees. A number of changes were made to committees during the year to reflect changes to the composition of the Board and in order that the committees comprised individuals with the appropriate skills, knowledge and experience, and also that they comply with the requirements of the Articles of Association of Network Rail Limited and Network Licence requirements of Network Rail Infrastructure Limited.

Executive management succession planning
The Committee is responsible for reviewing the plans and processes aimed at ensuring that the Company has a senior executive resource with the necessary skills and experience to meet the Group's future needs. On an annual basis the Committee receives a detailed report on the Group's senior executive planning and development processes. This covers the succession plans for key operational and functional positions (including existing Executive Director appointments) and development priorities and plans for individuals.

For 2010 a special sub-committee of the Committee has been set up to consider succession planning for senior executive levels within the Company in greater depth as part of the overall programme for equiping Network Rail with the skilled and experienced management to take the company through into CP5.

Evaluation of board performance
The Nominations Committee is charged by the Board to review annually the performance of the Board, its principal committees and individual Directors. The policy adopted by the Nominations Committee is for external assistance to be provided in conducting the review on a bi-annual basis. In the interim year the review is to be conducted internally by the Group Company Secretary.

Board evaluation process
In line with this policy, consultants, Egon Zehnder International, were engaged to assist with the process for 2008/09. This review was conducted in January 2009. The review was achieved through a formal process whereby guidelines to areas of focus had been drawn up with the assistance of the external consultants. These guidelines formed the basis for the evaluation process.

Each review focused on Company strategy, performance, delegation and accountability, corporate responsibility, succession, relationships with stakeholders, Board and committee composition, Board communication and the contribution and effectiveness of individual Directors. The consultants interviewed each of the Directors who were also required to complete a questionnaire based upon the guidelines. The findings of the review and the consultants' conclusions and recommendations were considered and discussed by both the Nominations Committee and then the Board. The review of individual Directors was also considered by the Chairman of the Board. Each Director received personal feedback given by the consultants.

The performance of the Chairman was included in this review process and took into account the views of Executive and Non-Executive Directors. Feedback to the Chairman was provided by the consultants.

Timing of board evaluation
The next evaluation was due to be undertaken in January 2010. Due to the ongoing changes to the composition of the Board and its Committees, however, including the appointment of a new Non-Executive Chairman and Group Finance Director in 2009, the in depth review of roles on the Board undertaken in the summer of 2009, the retirement of three Non-Executive Directors in 2010 and the appointment of four new Non-Executive Directors, the Nominations Committee considered a formal evaluation not appropriate.

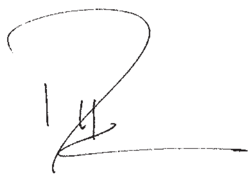
Formal performance evaluation will re-commence, however, in early 2011 following the appointment of the new members of the Board and a period of time having elapsed enabling the Board to settle into its new composition and format. In the interim the Nominations Committee will support the Chairman in continuing to monitor the performance of the Board, its committees and each Director and in particular to assess the skills and experience required for each role. Where necessary, steps will be taken as may be appropriate to provide continuous enhancement of performance.

Evaluation of Director performance
The Nominations Committee has also concluded that each Director is continuing to contribute to the overall effectiveness and success of Network Rail and that each of the Directors who is proposed for election or re-election at the AGM of Network Rail Limited in July 2010 demonstrates the necessary commitment to Network Rail and to be a fully effective member of the Board.

Board committee review
In addition to the overall evaluation, and in accordance with the terms of reference of the Board Committees, each Committee reviews its performance against its responsibilities under its terms of reference each year.

In January 2010, and notwithstanding the decision not to conduct the formal overall evaluation, the Committees each undertook their own assessment. This included considering the terms of reference as to their continuing appropriateness and effectiveness, the composition of the Committee, the number of meetings scheduled and the contents of the meetings. For 2009/10 each Committee concluded that it was satisfied with its performance and composition including the current level of resourcing available to perform its responsibilities under the terms of reference.

On behalf of the Nominations Committee



Rick Haythornthwaite
Nominations Committee Chairman
3 June 2010

Corporate governance report

Highlights

Significant enhancement of top level governance of Network Rail.

Drawing up of Network Rail Governance Principles.

Appointment of four new Non-Executive Directors.

Exclusive Non-Executive Director composition of Board committees.

Enhancement of role of Board committees.

Creation of new Board committee – Policy and Performance Committee.

Extensive engagement with Members and other key stakeholders on governance matters.

Launch of a quarterly Members' governance letter written by the Chairman.

Enhancement of the independence of the Members' selection process by the removal of the requirement for Non-Executive to be a member of the Membership Selection Panel.

Focus meetings held with Members to probe members of the Board on matters of governance as well as have the opportunity to get briefings on major topics.

Twice a year Members' meetings with the Chief Executive following announcement of half year and year end results to discuss with Members the key aspects of operational and financial performance.

Compliance with the provisions of the Combined Code on Corporate Governance

The Board considers that good corporate governance is central to achieving the Company's objectives and to the principle of safeguarding stakeholders' interests in the rail infrastructure. The Company is committed to high standards of business behaviour and has an established governance framework which comprises an organisational structure, internal control systems and business conduct policies. These form the framework for effective decision-making and delivery of the quality rail infrastructure this country needs.

It is also a condition of the network licence of Network Rail Infrastructure Limited that, from 3 October 2002, it complies with the governance principles contained in the Combined Code on Corporate Governance (the Code). The Code sets out guidance in the form of principles and provisions on how companies should be directed and controlled to follow good corporate governance. The Financial Services Authority requires companies listed in the UK to disclose how they have applied the main principles of the Code and whether they have complied with its provisions throughout the accounting year. Where the provisions have not been complied with, companies must provide an explanation for this. The Code was amended on 1 June 2008 taking effect from 29 June 2008.

Having reviewed the requirements of the current Code, the Directors consider that Network Rail has complied throughout the financial year ended 31 March 2010 with the provisions of the Code. This Corporate governance report, coupled with the Directors' remuneration report, explains how the Company has applied the governance principles set out in the Code. Details of the Company's internal controls are set out on pages 66 to 68.

Network Rail's governance principles

Network Rail Limited, being the ultimate parent company of Network Rail Infrastructure Limited has Members instead of shareholders to which its Board of Directors is accountable. Further details relating to Members is set out on pages 72 to 75.

To assist Members of Network Rail in performing their role, a set of ten governance principles has been drawn up which describes the basis of the role of Members and the measurement by which the Board of Network Rail can be judged in relation to how it runs the Company and against which the Board should be held to account.

The principles are conceptually based on the principles adopted by Hermes in relation to its institutional investor role with companies in which it invests.

The ten principles are set out in the table on page 55.

The Network Rail governance principles

Overriding requirement:

Network Rail must serve and collaborate with its customers – the train and freight operating companies – in the joint pursuit of the best possible current experience for the public and freight users; future prospects for the railway in Great Britain; and value for money in the eyes of both users and tax-payers.

Principle 1: Safety
The Company should regard the safety of all those working and travelling on the railways as its paramount duty, using the principle of ALARP (As Low As Reasonably Practicable) to support this.[1]

Principle 2: Leadership
The Company should drive for extraordinary performance in the short-term as well as look to the future, providing clear leadership in the rail sector in both its facilitation of a widely shared vision and its approach to stakeholder relationships, reputation and societal impact.

Principle 3: Setting targets
The Company should benchmark itself against the best in the world in all activities (including estate management), setting targets that aspire to be or continue to be the best. It should actively seek ways to calibrate its benchmark position and offer clear justification wherever ambitions fall below stakeholder expectations. The targets should always be positioned to motivate a delivery of performance that exceeds expectations and encourage thoughtful questioning of fundamental and potentially constraining business assumptions.

Principle 4: Delivery and risk management
The Company should have the appropriate structures, processes and systems in place to be assured of delivering its primary governance responsibilities and ambitions, including the demands of its Licence and other legal, regulatory and contractual requirements and commitments. These systems should include an explicit framework of plans and accountabilities, a comprehensive risk management approach and an effective network of internal communication and information flows.

Principle 5: Decision-making
The Company should seek that all investment and operational decisions will achieve an appropriate balance of improved safety, reliability, capacity, availability, respect for the environment and value for money, both separately and collectively. It should carefully and proactively manage situations where short-term disruptions to customer service are considered necessary to deliver long-term benefit.

Principle 6: Performance and incentives
The Company should have cost-effective performance evaluation and incentive systems in place to attract and retain high calibre managers as well as incentivise those managers to deliver beyond the demands of the current Control Period and with the best long-term interests of the public, freight users and tax-payers in mind.

Principle 7: Employees and the organisation
The Company should, in all its decisions and actions, have respect for its employees and their health and well-being, while also continuously seeking to adapt the organisational shape, processes and culture in a planned and measured fashion to meet its evolving ambitions and challenges.

Principle 8: Financial flexibility
The Company should, as a matter of prudence, consider its expected capital availability as being subject to change, always seeking to generate surplus cash flow beyond target levels, diversify capital-raising options and adapt activity as required without, if possible, compromising on future delivery or commitments to other funders, including tax-payers.

Principle 9: Licence to operate
The Company should seek continuously to develop and demonstrate to all stakeholders the relative advantages of a regulated private company undertaking a public service role over other governance models. In other words, it should never take its licence to operate for granted.

Principle 10: Communication
The Company should maintain an honest and open dialogue with Members and other key stakeholders, always seeking a pragmatic balance between transparency and best practice and the constraints of regulatory and legal requirements, commercial sensitivity, information transmission and executive resource. It should communicate clearly and in a timely manner the plans it is pursuing and the intended performance consequences of those plans. It should consult widely on matters that are of significant strategic or reputational importance, including senior executive remuneration. It should be prepared to argue the logic behind its judgements and decisions and, to the greatest possible extent, communicate on a ‘no surprises’ basis.

1 ALARP is an established Health & Safety principle by which Health & Safety Executive/ORR and other UK safety bodies assess risk associated with the design and development of safety systems. Under ALARP, the residual risk should be as low as reasonably practicable and it should be possible to demonstrate that the cost involved in reducing the risk further would be grossly disproportionate to the benefit gained. This captures the notion that in combination the risk to individuals, society, and the environment should be as low as reasonably practicable. ALARP is best common practice of judgement of the balance of risk and societal benefit rather than a quantitative measure of benefit against detriment.

Board of Directors

The Board is responsible to Members and other stakeholders for the appropriate overall management of Network Rail. In particular the Board governs the strategic direction of the business, supervises its operational management and provides leadership within a governance framework which it oversees. It is, first and foremost, collectively responsible for driving the success of the Company, providing entrepreneurial leadership within a framework of the HLOS outputs sought by Government and establishing prudent, effective controls which enable risk (both operational and financial) to be assessed and managed. This responsibility extends to taking overall responsibility for financial performance, internal controls and risk management of the Company. Secondly, it sets Network Rail's values and standards required to meet its obligations to its Members and other key stakeholders.

The Board comprises a mix of Executive Directors who (along with other senior executives) run the Company, and Non-Executive Directors. In general, it is the Executive Directors who take the entrepreneurial role and the Non Executive Directors who provide independence, bringing their experience to bear where necessary. This independence is critical to providing assurance that the executive team is exercising good judgement in key areas of delivery strategy and to sound decision-making in areas where there are possible conflicts of interest, such as on remuneration policy, Executive Director appointments and senior executive team succession. The Non-Executive Directors are required to scrutinise the performance of management against agreed goals and objectives, monitor the reporting of performance, satisfy themselves that financial information is accurate, and determine that financial controls and systems of risk management are robust and defensible.

The Board aims to carry out its role by focusing on seven key issues:

- **the purpose of the organisation** why it exists and what it wants to be
- **its strategy** how it proposes to achieve success and manage risk
- **performance measurement** implementation and monitoring of the Company's financial and non-financial indicators, and assessing the Board's own performance and that of the executive team
- **accountability and communication** the processes of dialogue and reporting by which it informs its shareholders, and wider stakeholders, and takes account of, and learns from, the feedback received
- **added value** generated by constructively questioning and challenging the thinking of the executive management team and ensuring that appropriate controls are in place and operate effectively
- **the Company's values** what it stands for and will not stand for
- **its key relationships** who and what it depends on for success, the delivery of its values and the development and/or protection of its corporate reputation.

The information on pages 28 and 29 shows that at the date of this report the Company is led and controlled by a Board currently comprising a Non-Executive Chairman, six Executive Directors and nine Non-Executive Directors. It is expected, however, that the size of the Board will reduce over the coming months. The Board believes its composition possesses wide experience as well as the necessary range of qualities, skills and experience to lead the Company effectively.

Directors

Directors are appointed by the Board and are also the Directors of Network Rail Infrastructure Limited. Under the provisions of the Articles of Association of the Company the Directors are not subject to retirement by rotation due to it being a wholly-owned subsidiary of Network Rail Limited. Under the provisions of the Articles of Association of Network Rail Limited, however, all Directors (other than the Special Director – see page 59) must retire by rotation, and may stand (together with any new Director appointed since the last general meeting) for re-election or election (as the case may be) by the Members of the Company at least once every three years.

In the autumn of 2009 a review was conducted of the composition of the Non-Executive Directors. Given the change in the challenges facing Network Rail in its delivery of the objectives of Control Period 4 (CP4) and beyond, four new Non-Executive Directors have been appointed recently – Janis Kong and Lawrie Haynes who both joined the Board in January 2010, Graham Eccles who joined in February 2010 and David Higgins who joined in April 2010. Ian Buchan retired from the Board on 31 March 2010. Yvonne Constance and Christopher Green have also both announced that they will be stepping down from the Board in July 2010.

These new appointments are intended to pave the way towards establishing a balance of experience and skill sets of those Non-Executives Directors both within and outside the rail industry. Graham Eccles brings his lengthy rail experience to join that of David Bailey (his tenure with Network Rail combined with his related experience from London Underground) providing significant and relevant rail knowledge. Janis Kong, David Higgins and Lawrie Haynes complement this focus with their own respective experience gained in other industries.

The names of the Directors due to stand for election or re-election at Network Rail Limited's AGM in July 2010 are set out on page 23 of the Directors' Report. This includes Rick Haythornthwaite, Chairman, who has chosen to be subject to voluntary annual election by Members. Further information on each Director seeking election or re-election will be given in the documents accompanying the Notice of the AGM to be sent to Members of Network Rail Limited.

In January of each year an evaluation of the effectiveness of the Board and its Committees is conducted. Due to the recent review of the composition of the Non-Executive Directors referred to above and the ongoing changes to that composition, the Nominations Committee, which has responsibility for the conduct of the evaluations, chose not to conduct a review in January 2010. The next evaluation will be undertaken in January 2011. Further details of the evaluation process are set out in the Nomination Committee report on pages 52 to 53. Biographical details of all of the Directors are set out on pages 28 and 29.

None of the Directors has served on the Board for nine years or more. There is no legal requirement for a Director over the age of 70 to seek re-election annually. As a matter of good practice, however, in Network Rail a Director reaching this age offers themselves up voluntarily for re-election. David Bailey turned 70 years during the financial year. In line with this practice in Network Rail, therefore, he has agreed to be put forward for re-election at Network Rail Limited's AGM in July 2010. The Board of Directors supports his re-election in recognition of the continuing valuable contribution he makes to the activities and responsibilities of the Board. Also the Board considers continuity of Board membership to be important in the coming year given the various changes to its composition during recent months.

The Board's responsibilities

Certain matters are formally reserved for decision by the Board and its duly authorised committees. These include approval of

- the Group's overall strategy and annual operating budget
- the interim and year-end financial statements of the Company
- the business plan
- material changes to the network licence
- key pension matters
- appointments to the Board
- adequacy of internal control systems
- major capital investments and expenditure
- review of the performance of the Board and its committees.

Matters delegated to the Executive Committee or below are also subject to financial and other risk limits above which Board approval is required. Further details on the Board committee structure are set out on page 62.

Separation of the Roles of Chairman and Chief Executive

The roles of the Chairman and the Chief Executive are distinct and separate and their responsibilities are clearly established being set out in writing and having been agreed by the Board.

The responsibilities of the non-executive Chairman include leading the Board and ensuring its effectiveness. Working closely with the Group Company Secretary, he sets the agenda for the meetings of the Board and arranges for a timely, accurate and clear information flow to the Board members both at board meetings and also through updates on issues arising between meetings. Supporting papers for scheduled meetings are distributed the week before each meeting. Access to documents is also available through the Group Company Secretary.

The Chairman's contractual commitment to the Group is two days per week although, since his appointment as Chairman in July 2009, his actual level of activity relating to Network Rail has exceeded this. The Chairman has recently confirmed that the performance of his outside responsibilities continue to be achieved without detriment to his duties to Network Rail and he anticipates this will remain so going forward. His main interests outside the Company are set out in his biographical details on page 28.

The Chief Executive is responsible for leading and managing the business on a day-to-day basis within the authorities delegated by the Board and is accountable to the Board for the financial and operational performance of the Group.

Statements of Responsibility for both the Chairman and Chief Executive are published on Network Rail's website and are summarised below:

Role of Chairman	**Role of Chief Executive**
General	**General**
Providing leadership of the Board. Being the pivotal role in creating the conditions for overall Board effectiveness. Setting the Board's agenda for approving the Company's safety, operational and financial strategies. Promoting high standards of corporate governance and seeking compliance with the provision of the Code to the extent that it applies to the Company. Seeking to uphold the highest standards of integrity and probity of the Board as a collective body.	Creating, maintaining and regularly reviewing the organisational structure for the business of the Company. Leading and managing the Executive Directors and senior executives in the day-to-day running of the Company. Leading the development, delivery and regular review of the Company's safety, operational and financial strategies and actions. Developing an effective senior management team including establishing and maintaining effective succession planning for the senior executives of the Company. Managing the effective implementation of the principles of corporate governance within the Company. Leading the communications programme with stakeholders including, in conjunction with the Chairman, representing the Company. Creating the conditions for overall Executive Director effectiveness, both inside and outside the Boardroom.
Board	**Board**
Chairing Board and general meetings of the Company. Promoting effective decision-making and constructive debate within the Board with a focus on strategic matters and forward looking agendas. Managing the process by which the Board receives information to enable the Board to promote the success of the Company. Managing the Board agendas to allow sufficient time for discussion of key issues. Actively encouraging Board members to contribute fully in addressing and agreeing on all major strategic issues. Addressing the development needs of the Board as a whole.	Being accountable to the Board for managing the creation and maintenance of proper financial and operational stewardship of the assets of the Company including internal controls, the implementation of the Board's decisions and the effectiveness with which the organisation works in accordance with the strategic objectives of the Company. Running the executive function of the Board. Developing and maintaining a close and effective working relationship with the Chairman, consulting regularly with him/her and keeping the Chairman advised of key issues relating to the Company. Addressing the development needs of each of the Executive Directors with a view to achieving and maintaining their effectiveness as a member of the management team. Maintaining the integrity of the Company by requiring that the Board's executive committees are properly structured and run and that all corporate governance matters are properly addressed.

Role of Chairman	Role of Chief Executive
Directors	**Directors**
Establishing a close and effective working relationship with the Chief Executive and other Directors. Encouraging active engagement by each of the members of the Board and effective relationships and open communication between Directors. Facilitating the effective contribution of Non-Executive Directors to the responsibilities of the Board. Taking the lead in the design, implementation and monitoring effectiveness of the induction and ongoing development of the individual Directors.	Leading and managing the executive function of the Board including seeking effective performance of each of the Executive Directors. Establishing and managing an effective relationship with each of the Non-Executive Directors. Providing support and advice to each Executive Director while respecting executive responsibility.
Stakeholders	**Stakeholders**
Promoting the provision of effective communication with Members and other stakeholders. Maintaining sufficient contact with Members and other key stakeholders to understand their issues and concerns, in particular relating to governance and strategy. Managing the process by which the Board has an understanding of the views of stakeholders.	Developing and maintaining regular and effective communication and relationships with the Company's stakeholders including Network Rail Members and employees. Establishing and managing effective and consistent delivery of the communication policy, strategies and statements of the Company as agreed by the Board to the stakeholders including Network Rail Members and employees.

Senior Independent Director

The Code states that the Board should appoint one of the Non-Executive Directors to act as Senior Independent Director (SID). Within Network Rail the main responsibility of the SID is to be available to Members and other stakeholders should they have concerns that they are unable to resolve through normal channels of the Chairman or Chief Executive or other Executive Directors, or where these channels are inappropriate. The SID provides a sounding board for the chairman. The SID is also expected to work closely with the Chairman in providing an independent source of counsel as well as serving as an intermediary for the other Directors when necessary.

Annually the SID leads evaluation by the other Board members involving a discussion without the Chairman present on his performance. The SID's role also extends to providing leadership in relation to the appointment of a new chairman when required.

To maximise accessibility by Members to the SID, he attends a variety of meetings with Members and also has a personal email address which is publicised to all Members enabling them to make contact with him easily and quickly.

A Statement of Responsibility of the Senior Independent Director is published on Network Rail's website.

The current Senior Independent Director is Steve Russell. He was appointed to the role following Jim Cornell's retirement in July 2009, and his biographical details are set out on page 29.

Non-Executive Directors and their independence

The Non-Executive Directors combine broad business and commercial experience (both from the rail industry and from other industry sectors) to enable them to challenge and contribute constructively to the development of the strategy of the Group. They also scrutinise the performance of management in meeting agreed goals and objectives and monitor operational performance of the business. Careful consideration has been given to the composition of the Non-Executive Directors with an aim to maximising the breadth of skills and experience as well as the mix of individuals holding executive positions and those who have retired from full-time employment in other companies (recognising the respective time commitment opportunities of both).

The Board considers that each of the Non-Executive Directors is independent of the Company. With regard to the guidelines on the meaning of 'independence' as set out in the Code, however, it is appropriate to disclose that:

1 **David Bailey** – previously the Special Director appointed to the Board of Network Rail Limited by the Strategic Rail Authority (SRA) pursuant to its then rights under the Articles of Association of that company. Following the changes under the Railways Act 2005 with the responsibilities of the SRA passing principally to the Department for Transport (DfT), the DfT has not exercised its right to appoint a Special Director. The Board considered that David Bailey makes a valuable contribution to the Company in his Non-Executive Director role. His wide ranging commercial experience has enabled him to provide additional perspective on issues and the Company wished to retain him as it moved into its new roles. At the AGM of Network Rail Limited in 2005, his appointment as a Non-Executive Director was approved by the Members of Network Rail. In 2009 his re-election was also approved.

2 **Christopher Green** – currently receives a pension from the Railway Pension Scheme. This pension scheme was created at privatisation of the rail industry and is a scheme in which over 100 companies from this industry participate. The scheme is run by independent trust managers with trustees drawn from across the membership of the scheme (including from other companies within the scheme). The Board considers, however, that as a Non-Executive Director of Network Rail, Christopher Green is independent as he has not been an employee or Executive Director of Railtrack PLC. Moreover, Network Rail's membership of the Railway Pension Scheme is not considered to compromise his independence given the structure of the scheme of which Network Rail is only one of many contributing companies. Furthermore the corporate structures of this Company and of Network Rail Limited, being a not-for-dividend company, eliminate any potential or perceived conflicts between his being a Non-Executive Director of the Company and receiving a pension from the Network Rail section of the scheme. The Board considers, therefore, that, as a Non-Executive Director of Network Rail Christopher Green is independent. Christopher Green retires from the Board in July 2010.

3 **Graham Eccles** – likewise currently receives a pension from the Railway Pension Scheme. The Board considers, however, that, for the reasons set out above in relation to Christopher Green, as a Non-Executive Director of Network Rail Graham Eccles is independent. Moreover he was never an employee of Railtrack PLC.

None of the Non-Executive Directors are members of more than three committees of the Board except David Bailey and Steve Russell. David Bailey is a member of the Nominations, Remuneration, Audit and Safety, Health and Environment Committees (originally at the request of the Strategic Rail Authority). Upon the conversion of his appointment in June 2005 to Non-Executive Director, he has continued to be a member of these committees due to the valuable contribution he is able to make to each of these. He is also a member of the Policy & Performance Committee. Steve Russell is a member of the Audit, Nominations, Remuneration, Treasury and Policy & Performance committees.

A Statement of Responsibility of the Non-Executive Directors is published on Network Rail's website.

Board and Committee meetings

Board meetings

The Board has adopted a timetable of eight scheduled Board meetings each year and it met formally eight times in 2009/10. Facility is also made for special Board meetings should the need arise. The format for each meeting is designed to enable focus on and opportunity to debate future strategic issues facing the rail industry in addition to reviewing current performance of the business. A key strategic item of business is also allocated to each meeting's agenda for particular review and discussion. The Directors review corporate strategy regularly together with the operations and results of the business units within the Group and to discharge their other duties. Each meeting also includes reports on the safety, health and environmental performance of the Group as well as on operational and financial performance against the business plan and targets.

There is a schedule of items to be brought to the Board throughout the year including those listed on page 57.

Risk management is central to the structure of governance within the Company. A range of non-executive and senior executive committees and panels has been set up to oversee and review how the wide range of risks relating to the business are mitigated. At Board level there are also periodical corporate risk management reviews of the key strategic risks to the Group and the Board receives regular presentations from senior management on both current issues as well as future plans. Further details are set out on page 62.

The Chairman holds regular scheduled meetings with the Non-Executive Directors without the Executive Directors present to discuss the performance of the Company under the executive leadership. In 2009/10 the Non-Executive Directors met separately from the Executive Directors on three occasions. In addition, periodically a meeting of the Non-Executive Directors chaired by the Senior Independent Director is held without the Chairman present at which the Chairman's leadership of the Board is discussed.

Attendance by individual directors at meetings of the Board and its Committees between 1 April 2009 and 31 March 2010 is shown in the table on page 61.

Meeting attendance

Total number of scheduled meetings held during the year ended 31 March 2010 and the number of meetings attended of the maximum number that each Director was entitled to attend

	Board	Safety, Health & Environment*	Nominations	Remuneration	Audit	Executive	Treasury*	Policy & Performance
Number of meetings held	8	7	8	6	4	12	2	2
Attendance								
Patrick Butcher[A]	7/7	–	–	–	–	11/12	1/1^ 1/1~	–
David Bailey	7/8	7/7	8/8	6/6	4/4	–	–	2/2
Ian Buchan[B]	8/8	7/7	–	6/6	–	–	–	–
Yvonne Constance	7/8	–	–	6/6	4/4	–	–	–
Jim Cornell[C]	3/3	2/2	1/1	1/1	–	–	–	–
Iain Coucher	8/8	2/3^ 3/4~	–	–	–	12/12	1/1^ 1/1~	–
Graham Eccles[D]	1/1	–	–	–	–	–	1/1	
Michael Firth	8/8	–	–	6/6	4/4	–	2/2	–
Robin Gisby	8/8	–	–	–	–	11/12	–	–
Christopher Green	6/8	6/7	–	6/6	–	–	–	–
Lawrie Haynes[E]	1/1	0/1	–	–	–	–	–	1/2
Rick Haythornthwaite	8/8	–	7/7	3/6	–	–	–	2/2
Peter Henderson	8/8	5/7~	–	–	–	12/12	–	–
Ron Henderson[F]	1/1	–	–	–	–	–	–	–
Simon Kirby	8/8	–	–	–	–	12/12	–	–
Janis Kong[G]	2/2	1/1	–	–	0/1	–	–	–
Ian McAllister[C]	3/3	–	1/1	1/1	–	–	–	–
Paul Plummer	8/8	–	–	–	–	12/12	–	–
Steve Russell	7/8	–	7/8	6/6	3/4	–	2/2	2/2

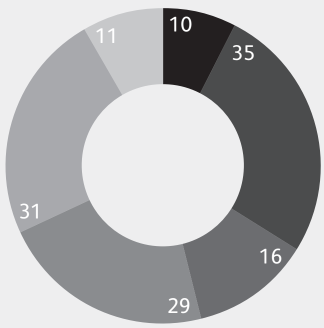
A Joined the Board on 20 April 2009.
B Stepped down from the Board on 31 March 2010.
C Stepped down from the Board on 21 July 2009.
D Joined the Board on 26 January 2010.
E Joined the Board on 7 February 2010.
F Stepped down from the Board on 20 April 2009.
G Joined the Board on 13 January 2010.

– Indicates not a member of that Committee.
* In November 2009 the composition of this Committee was revised. with it comprising only Non-Executive Directors.
^ As Committee member.
~ As attendee.

Notes
1 During 2009/10 there were a number of occasions where circumstances prevented a Director from attending a meeting in person. These occasions were a result of illness, adverse weather conditions and existing conflicting diary commitments, especially in respect of Directors newly appointed during the year. For future years plans are in place aimed at minimising such diary conflicts.
2 Where a Director is unable to attend, it is usual practice for the Director concerned to review the papers and convey any views to the Chairman of the meeting in advance.

Allocation of agenda items in Board meetings during 2009/10

- Safety
- Governance and risk management
- Strategy
- Finance and investment
- Operational
- Regulatory



Board committees

The Board has established an organisational structure which is designed to allow for effective and efficient decision-making across the business. The Board has delegated authority on specific matters to the Committees described on the following pages. These authorities are reviewed regularly.

The role of the Board Committees is to challenge and scrutinise business targets, initiatives and executive judgements. To enhance this role, during 2009 it was decided that all such committees would comprise only Non-Executive Directors with the aim of maximising the range of skills and experience of Board members without placing undue reliance on any one individual.

Opportunity was also taken in 2009 to review succession plans for Non-Executive Director positions on the Board. This review considered the mix, experience and stature of the Board with an aim to establish the future composition to be of a level commensurate with the scale, challenge and complexity of the company as it progresses through CP4 and the challenging outputs sought. This resulted in the Nominations Committee undertaking recruitment searches of a number of new Board members.

Under this new structure and composition the activities of the Board is focused through the non-executive committees and in particular, in relation to review of risk management, through: Safety, Health and Environment Committee, Audit Committee and Treasury Committee. The Nominations Committee and Remuneration Committee continue as independent committees charged with succession and recruitment issues and compensations issues respectively. The unitary Board then receives reports from each Committee and reviews assurance issues as guided by the Committees; bring collective insight and experience to policy and strategic initiatives; and provide supportive assistance to the Executive Directors.

To support and enhance this approach a new committee – the Policy and Performance Committee – was created a the end of 2009. The main responsibilities of this Committee are to monitor the quality, scope and integrity of the long and short-term planning, to champion a systems approach to resource and risk management, and to provide assurance that performance metrics are appropriate, fully considered and lead to timely, effective responses. The Committee also monitors stakeholder goodwill and the Company's approach to stakeholder relationships, with particular emphasis on customers and their customers. Its terms of reference are also available on Network Rail's website.

Each Committee may request any information from the executive management necessary to discharge its functions and may, if it considers necessary, seek independent advice and counsel.

There are now, therefore, six standing Board Committees with defined terms of reference and scheduled meetings throughout each year. These terms of reference are published on Network Rail's website. Minutes of all Committee meetings are made available to all Directors.

Control environment

Risk management comprises the interaction of various key components of assurance.

Executive management has the overall accountability for managing all risks relevant to the business – financial, non-financial and operational. It is responsible for designing, implementing and monitoring the operation of the system of internal control and for providing assurance to the Executive Committee, the Safety, Health and Environment Committee, the Audit Committee and the Treasury Committee, as relevant, that it has done so. The various risk and compliance functions within the Company are accountable for providing objective guidance to and challenge and oversight of the business' management of risk through systems of internal control. The Internal Audit function is accountable for providing reliable independent assurance to the Audit and Treasury Committees, Board members and the Executive Committee on the adequacy and effectiveness of the system of internal control.

The internal controls within the business are summarised on pages 66 to 68.

Risk management structure

Whilst the Board is ultimately responsible for risk management and periodically reviews this during the course of the year, it delegates the more detailed oversight of risk management and internal control principally to the following committees:

- Safety, Health and Environment Committee
- Audit Committee
- Treasury Committee

The Safety, Health and Environment Committee assists the Board in the integrity of the methods of discharge of the safety, health and environmental responsibilities of the Company and satisfies itself as to the adequacy and effectiveness of the safety, health and environment policies and strategies within the Company. The Audit Committee is responsible for assisting the Board in discharging its responsibilities for the integrity of the Company's financial statements and the effectiveness of the system of internal financial control and monitoring the effectiveness, performance and objectivity of the internal and external auditors. The Treasury Committee is responsible for monitoring the effectiveness of treasury controls and the appropriateness of proposed treasury transactions.

This structure is able, therefore, to provide focus on the breadth of risks involved in the business of Network Rail including key risk areas relating to the current economic climate such as funding and investment-related risks and pension-related risks. Balanced with this is the emphasis required by the Company to adopt innovation as part of its delivery plans for CP4. The Transformation Programme designed to deliver the targets for CP4 is, therefore, another key focus for scrutiny in relation to associated risks.

Further details on the responsibilities of these Committees and their discharge of these are set out on pages 63 to 69.

Committee details

The Safety, Health and Environment Committee

Members

Current members		From
David Bailey (Chairman from July 2009)		February 2003
Graham Eccles		February 2010
Christopher Green*		June 2005
Lawrie Haynes		January 2010
Janis Kong		January 2010
Previous members	From	To
Ian Buchan	February 2006	March 2010
Jim Cornell (Chairman until July 2009)	October 2002	July 2009
Iain Coucher**	August 2007	November 2009

* Stepping down from Board on 21 July 2010.
** In line with general policy adopted in November 2009 executive directors stepped down from all Board Committees.

The Chief Executive, Director, Asset Management and Director, Safety & Compliance attend the meetings by invitation.

Role The Committee's role is to monitor the integrity of the methods of discharge of the safety, health and environmental responsibilities of the Company and to satisfy itself as to the adequacy and effectiveness of the safety, health and environment policies and strategies within the Company. It also reviews the principles, policies and practices adopted in complying with all statutory, sub-statutory, standards and regulatory requirements in respect of safety, health and environmental matters affecting the activities of the Group.

Its work in fulfilling its responsibilities includes:

- monitoring of the Group's safety, health and environment policies and strategies
- considering the areas of significant corporate and individual safety, health and environment risk and whether management is managing these effectively
- reviewing the structure, adequacy and effectiveness of safety, health and environment managerial committees within the Company including review of any terms of reference for the same
- reviewing the scope and results of any safety, health and environment audit on the effectiveness of the Company's safety, health and environment audit policies and strategies and such audit's cost effectiveness and the independence and the objectivity of the audit body
- considering the major findings of internal and external investigations and management's response thereto and, where necessary, with a view to the making of recommendations to the Board in respect of the same.

Process The Committee conducts its responsibilities through a series of scheduled meetings with forward agendas set each year to meet the responsibilities of the Committee. The Committee chairman reports on the Committee's activities to the Board meeting immediately following a Committee meeting.

The Committee members are notified of any serious safety, health or environmental issues arising between meetings and they also receive safety reports between the scheduled meetings.

In addition to this Committee, and reflecting the recommendations in the Cullen Report, two executive committees consider strategic and tactical safety matters. The Board receives a report on safety, health and environment matters at each of its scheduled meetings.

Activities in 2009/10 During the year ended 31 March 2010, this Committee met seven times and set out below are its principal activities.

The Safety, Health and Environment Committee's activities in 2009/10

Meeting	Agenda item
May 2009	• Review of the safety, health and environment performance of Network Rail during the preceding period • Receiving an update on the implementation of the on-track plant safety project • Receiving an update on where the current principal safety risks lie within the Operations & Customer Services function and how the risks are being mitigated and managed.
June 2009	• Receiving a briefing on the current position and approach of the Office of Rail Regulation (ORR) on safety • Review of the safety, health and environment performance of Network Rail during the preceding period • Receiving an update on where the principal safety risks lie within the Engineering function and how the risks are being mitigated and managed • Considering a report on progress with implementation of the Railways & Other Guided Transport Systems (Safety) Regulations 2006 • Considering an update on the processes for handling safety-related issues in the context of the Transformation Programme • Receiving a further update on the progress against each of the recommendations from the Grayrigg Formal Investigation report (Part 1) and an update on RAIB's investigation into Grayrigg (Part 2) • Considering the actions taken within the delivery functions to achieve a better understanding of the actions necessary to improve Network Rail's system safety.

continued overleaf

The Safety, Health and Environment Committee's activities in 2009/10 continued

Meeting	Agenda item
September 2009	• Considering a proposal for revision of the terms of reference of the SHE Committee together with proposals for development of the role of the Committee • Review of the safety, health and environment performance of Network Rail during the preceding periods • Receiving a report on the recent activities of the Strategic Safety Group (SSG) and Tactical Safety Group (TSG)* • Receiving an update on recent initiatives reviewed at TSG in respect of safety culture and behaviours • Considering the key Infrastructure Maintenance strategic risks • Considering the effects of the Transformation Programme on strategic safety risk profile • Considering progress of Network Rail's safety assurance activities, recommendations arising from Rail Accident Investigation Branch reports, trends emerging from whistle blowing and CIRAS reports and analysis of Enforcement Notices and prosecutions • Receiving an update on the Network Rail Safety Assurance Map.
November 2009 (two meetings)	• Receiving a paper setting out the context for the improvement target of three per cent reduction in risk consistent with the HLOS safety metric, a safety risk measure for passengers and workforce • Review of the safety, health and environment performance of Network Rail during the preceding periods • Considering the outcome of a review by TSG of irregular workings incidents and actions for reducing associated risks • Review of an update on actions taken following an incident on the rail network • Considering the key Infrastructure Investment strategic risks • Considering the effects of the Transformation Programme on strategic safety risk profile • Considering fire safety responsibilities and management of fire risks on the Network Rail controlled infrastructure • Considering the key points from the recently published annual reports of the Rail Safety & Standards Board, the ORR and the Rail Accident Investigation Branch • Considering the basis for and the processes for implementing the re-organisation of the Maintenance function and the safety risk management associated with the re-organisation.
January 2010	• Review of the safety, health and environment performance of Network Rail during the preceding periods • Receiving the recent activities of the SSG and TSG* • Review of the current status of an investigation into an incident and the resultant recommendations made • Considering an update on Network Rail's approach to competency and training throughout the business • Considering priorities for 2010 in relation to the Supplier Assurance Framework • Receiving an update on the implementation of the on-track plant safety project • Considering progress made on actions to improve the understanding and management of Network Rail's system safety • Receiving an update on the Network Rail Safety Assurance Map • Considering an update on the effects of the Transformation Programme on strategic safety risk.

The Safety, Health and Environment Committee's activities in 2009/10 continued

Meeting	Agenda item
February 2010	• Review of the safety, health and environment performance of Network Rail during the preceding periods • Review of a report into an incident at a station including the background to the incident, the investigation underway, process for managing similar incidents • Considering an update on the actions being undertaken to manage level crossing risk and to improve level crossing safety during Control Period 4 • Considering an update on the work of the Safety & Compliance function • Receiving the high level processes used for safety risk management and describing how these relate to the Strategic Risk management process • Considering an update on progress of Network Rail's safety assurance activities, recommendations arising from Rail Accident Investigation Branch reports, trends emerging from whistle blowing and CIRAS** reports and analysis of Enforcement Notices and prosecutions • Considering how the Committee would provide input to the Remuneration Committee on its deliberations on safety performance in 2009/10 • Undertaking the annual review of the terms of reference of the Committee, the general effectiveness of the Committee and its composition • Reviewing the management of workforce health and safety risks associated with the Transformation Programme and the change control arrangements in place to manage these risks.

* The Strategic Safety Group and Tactical Safety Group are two Network Rail senior executive management committees, reflecting the recommendations in the Cullen Report, considering strategic and tactical safety matters.

** CIRAS (Confidential Incident Reporting & Analysis System) is an independent body to which workers in the UK rail industry can report safety concerns which is in addition to each rail industry company's own safety channels.

The Audit Committee
Members

Current members	From
Mike Firth (Chairman since January 2006)	December 2004
David Bailey	October 2002
Yvonne Constance*	September 2005
David Higgins	April 2010
Janis Kong	January 2010
Steve Russell	September 2009

* Stepping down from Board on 21 July 2010.

The Chairman of this Committee has a strong and lengthy financial background and has experience of chairing a listed company's audit committee. Mike Firth is also a Fellow of the ifs School of Finance and an Associate of the Chartered Institute of Bankers.

The Chief Executive, the Group Finance Director, the Head of Internal Audit and Head of Insurance and Risk attend meetings of the Committee by invitation. Two partners from the external auditors also attend each of the meetings and periodically meet with the Committee without executive management present.

The Board continues to be satisfied that the composition of the Committee fulfils the Code's requirement that at least one member of the Committee has recent and relevant financial experience. It also considers that it complies with the Smith Guidance on Audit Committees in all material respects.

Role The main responsibilities of this Committee are to monitor the integrity of the financial reporting and the audit process and to monitor that an effective management and internal control system is maintained. The Committee has a structured programme of activities including receipt of regular detailed reports on relevant aspects of management, focused to coincide with key events of the annual financial reporting cycle.

Its work in fulfilling its responsibilities includes

- reviewing the internal control framework and the register of financial and non-financial risks (so far as these are not reviewed by other Board committees such as the Safety, Health and Environment Committee)
- monitoring financial reporting policies and practices and compliance with accounting standards
- reviewing significant accounting estimates and judgements
- reviewing interim and annual financial statements before publication
- considering and making recommendations to the Board in relation to the appointment, re-appointment and removal of the external auditors following its assessment of their independence and objectivity (including the safeguards that are in place to maintain such independence) and their terms of engagement and remuneration
- reviewing the internal and external audit process including the scope of the planned audits and the audit findings
- reviewing the policy and procedure whereby employees can raise, in confidence, concerns about possible improprieties.

Process The Committee conducts its responsibilities through use of a series of scheduled meetings with a forward agenda and a defined set of items of business for each meeting. The Committee chairman reports on the Committee's activities to the Board meeting immediately following a Committee meeting. Between meetings, the Committee chairman reviews emerging issues as appropriate with the Group Finance Director and other senior managers.

Internal control

The Board is responsible for the Network Rail Group's system of internal control and for reviewing its effectiveness. Such a system is designed to manage, rather than eliminate, the risk of failure to achieve business objectives. It can only provide reasonable, (rather than absolute), assurance against material misstatement or loss.

The Audit Committee's activities in 2009/10

Meeting	Agenda item
May 2009	• Review of the key issues and areas of judgement relating to the financial statement of Network Rail Limited and Network Rail Infrastructure Limited for the year ended 31 March 2009 • Receiving a report from Network Rail's external auditors on the 2008/09 audit including the key audit matters identified • Considering a report by the Head of Internal Audit on the basis and rationale to support the internal control section of the Network Rail corporate governance statement for inclusion in the Annual Report and Accounts for the year ended 31 March 2009 • Review of drafts of sections of the Annual Report and Accounts for 2009 applicable to the Audit Committee • Review of the current status of risk management across Network Rail • Receiving a report on the output from the Internal Audit function's recent programme of work • (In the absence of the executive management from the meeting) seeking the views of the external auditors as to whether there were any other issues arising from the audit for 2008/09 or relating to the management of the Company that they wished to raise with the Committee.
September 2009	• Considering the external auditors' interim review plan for the period ending 30 September 2009 • Review of risk management of Network Rail including the risks identified to be high and the status of their mitigation and the strategic risk map 9 and in particular the Transformation Programme, which is concerned with the failure to deliver the benefits of the change programme • Receiving a report on the output from the Internal Audit function's recent programme of work, progress on the delivery of the internal audit plan • Considering the proposed approach and timeline for the re-tendering of the audit services for Network Rail.
November 2009	• Review of the key issues and areas of judgement relating to the interim financial statements of Network Rail Limited and Network Rail Infrastructure Limited for the six months ended 30 September 2009 • Considering the external auditors' report on the 2009/10 interim review • Considering risk management including the current risk profile, a summary of the findings from the recent review of the Company's strategic risk map 10 and progress with aligning the corporate risk matrix with the emerging corporate objectives and balanced scorecard • Receiving a report on the output from the Internal Audit function's recent programme of work • Considering proposing methodology for measuring internal audit findings.
February 2010	• Review of the proposed timetable for production of the 2009/10 statutory accounts • Considering the external auditors' year end audit plan, the proposed fees and the scope of the audit (including the key business risks which will be the focus of the audit) and the management letter • Receiving a report on the output from the Internal Audit function's recent programme of work • Considering the findings from the recent review of certain key risks and an overview of the current status of risk management across the Company including a periodical update on key risks relating to the Transformation Programme • Considering the key risks relating to the Western Corridor projects and the management of these risks • Considering how the Committee would provide input to the Remuneration Committee on its deliberations on risk management and other audit matters in 2009/10 • The annual review of the terms of reference of the Committee, the general effectiveness of the Committee and its composition • Receiving a paper requesting approval for the provision of non-audit services by a company acquired by the external auditors • Receiving an oral update on progress with the re-tendering of the external audit services.

The Board considers the management of risk and internal control to be fundamental to achievement of the Company's objectives and has formally established a risk management standard for identification, evaluation and on-going review of the significant risks faced by the Group which accords with the Turnbull Guidance. During the year the Executive Directors have formally reviewed the key risks faced by the Group. Moreover, the Directors keep the effectiveness of the system of internal control under review and have done so throughout 2009/10.

The risk management process is now well established and forms an integral part of the Network Rail planning and review activity. Risk types actively managed include safety, reputation, performance and financial risks. Risk management processes incorporate the following:

- the identification of risks to the achievement of business objectives by all business units and major projects together with the likelihood/impact analysis and the development of mitigation actions to manage risks at the desired levels
- a Company Standard for risk management to provide consistency of approach across business units
- a self certification process which requires function heads to confirm that risk management processes are being complied with and that their risk data is accurate and complete
- the capture and recording of risks, risk scoring and action plans in a company wide risk management system
- the regular reporting and review of business unit and major project risks by the Executive Directors at monthly business reviews
- the peer review of causal risk maps which provide an overview of strategic risk interaction across functions and support regular review of the risk profile by the Audit Committee and the Board
- the inclusion of risk assessment into investment planning processes using the corporate risk matrix scoring system
- the risks associated with the Company's Transformation Programme which have been identified and are regularly reported and reviewed by the Transformation Programme Steering Group and the Board.

There are established internal control procedures for managing the risks faced by the Group. The key elements are:

- a business conduct policy, supported by Human Resources procedures, that sets out Network Rail's ethical framework and defines expected standards of behaviour
- regular structured reviews of all business units and major projects by the Executive Directors assessing progress against objectives with action being taken as required
- a framework of delegated authority and accountability based on a templated organisation structure
- Board approval of business strategies and objectives, together with plans, annual budgets and targets
- the periodic reporting of financial results, safety and other operational performance indicators, including an Executive Key Performance Indicator Dashboard
- procedures for planning, approving and managing all investment expenditure including the use of the Guide to Railway Investment Projects (GRIP) specifying the requirement and timings for approvals sought by the Investment Panel and, where above it's delegated financial level, by the Executive Committee and the Board
- Financial Regulations governing the accounting and stewardship of all financial transactions
- centralised treasury operations acting within defined limits and overseen by the Treasury Committee
- monthly accounting reviews to scrutinise financial data and increase confidence in the integrity of the accounts
- a sourcing and supplier governance framework which sets out standards for contracting and procurement
- continuous monitoring by the Legal Services function within the Company, of claims and litigation issues affecting the Group as well as the identification of changes in the law or regulations which impact on the Company's activities
- governance of all business change initiatives through the Executive Transformation Steering Group
- commitment to continuous improvement in levels of competence via leadership, competency and training programmes and a performance appraisal system linked to objectives and Network Rail values
- insurance assessment and appropriate cover for residual risks
- business continuity and disaster recovery plans for key operational assets, corporate offices and IT applications
- policies and practices for detecting, reporting and preventing fraud and serious breaches of business conduct.

Internal Audit

The Company has an independent Internal Audit team that is affiliated to the Institute of Internal Auditors. Its primary role is to provide objective and independent assurance regarding the adequacy of the Group's internal control framework and compliance with policies, laws and regulations. Internal Audit is also responsible for reviewing the effective operation of the Company-wide risk management system as well as improving processes, providing advice and proliferating best practice.

The work of internal audit is focused on the areas of priority as identified by risk and materiality analysis and is in accordance with an annual audit plan which is approved by the Audit Committee. The Audit Committee receives regular reports on audit findings from the Head of Internal Audit, who has direct access to the Chairman of the Audit Committee. Recommendations to improve the internal control framework are reported to the Audit Committee through this process.

Internal Audit works closely with the external auditors and other assurance providers to encourage co-ordination of audit plans and optimisation of audit resources. The Head of Internal Audit and the external audit partner meet on a regular basis.

The Company also has an established process by which staff may, in confidence, raise concerns about possible improprieties. Matters arising from the investigation of fraud are reported to the Audit Committee by the Head of Internal Audit. There is an ongoing programme undertaken by Internal Audit to raise awareness of fraud issues with management.

During the course of its review of the system of internal control, the Board has not identified nor been advised of any failings or weaknesses which it has determined to be significant. Nevertheless, the Board recognises that there is still an ongoing need to build on the above framework and uses the opportunity to review internal control processes against incidents when they arise in order to promote continual improvement of the internal control system.

External auditors

Independence and objectivity of the external auditors is of great importance and the Committee has put in place safeguards to protect auditor objectivity and independence. It has established therefore a policy to assist this whereby employment of the external auditors on work for Network Rail is prohibited, other than audit services or tax consulting services, without prior approval by the Audit Committee. The Committee oversees compliance with the policy and considers the infrequent requests to use the auditor for non-audit work.

Furthermore, to enhance independence and in line with established auditing standards, a new lead partner of the external auditors is appointed every five years, with other key audit principals within that firm rotated every seven years.

The Committee has responsibility for advising the Board on the appointment, re-appointment and the remuneration of the external auditors. Deloitte LLP (Deloitte) have been the Company's external auditors since 2002 (and prior to that to Railtrack plc since 1996).

Each year the Audit Committee conducts an assessment of the effectiveness of Deloitte, the firm's independence and objectivity and assesses the work of the audit team. In addition periodically it conducts a more detailed review. In 2008 the Committee again conducted this more detailed review, having previously done so in 2005. A lengthy questionnaire was completed by the external auditors detailing their procedures, training and audit processes as well as more detail of how independence and objectivity is maintained. Consultation within the Company as to the performance of the external auditors was also carried out.

Being mindful of the length of engagement of this firm as the Company's external auditors, however, in September 2008 the Committee considered whether this service should be tendered in 2009. It concluded that, with the combination of the commencement of Control Period 4 and the retirement of the existing Group Finance Director scheduled for April 2009 and his replacement joining the Company at that time, it was not in the Company's best interest to conduct a tender at that time. As a result of the assessment, the Audit Committee recommended to the Board that at the AGM of Network Rail Limited in July 2009 it proposed the re-appointment of Deloitte as auditors until the conclusion of the AGM in 2010. It did recommend to the Board of the Company, however, that a tender process for the role of external auditor be considered during late 2009 in readiness for 2010. The tender process commenced in the autumn of 2009.

This process was undertaken in accordance with EU procurement requirements. Bid responses to the advertised tender request resulting in bid submissions were received from some of the major accountancy firms. Careful examinations of the bids took place including the use of objective scoring methodology and interviews by senior managers in Network Rail's Finance function, the Group Finance Director and the Chairman of the Audit Committee.

After reviewing the output from this tender process, in May 2010 the Committee recommended to the Board that PricewaterhouseCooper be presented for appointment as the Company's auditors at Network Rail Limited's AGM in July 2010. The Board accepted the recommendation. The Notice of the 2010 AGM of Network Rail Limited includes, therefore, a resolution to this effect.

The Treasury Committee
Members

Current members	From
Mike Firth (Chairman from December 2004)	December 2004
Steve Russell	July 2008

Previous members	From	To
Iain Coucher*	August 2007	November 2009
Patrick Butcher*	April 2009	November 2009

* In line with general policy adopted in November 2009 Executive Directors stepped down from all Board Committees.

The Chief Executive, Group Finance Director, Group Treasurer and Deputy Group Treasurer attend meetings by invitation.

Role The Committee's role is to review and satisfy itself as to the appropriateness of proposed treasury transactions including banking, cash management, debt raising and management and investment management.

Process The Committee conducts its responsibilities through a series of scheduled meetings. The Committee chairman reports on the Committee's activities to the Board meeting immediately following a Committee meeting. Between meetings, the Group Finance Director updates and discusses with the Committee chairman matters relating to the treasury activities.

Activities in 2009/10 During the year ended 31 March 2010, this Committee met twice and its principal activities included the following shown in the table below.

The Treasury Committee's activities in 2009/10

Meeting	Agenda item
November 2009	• Review of the current status of the debt issuance programme and investment portfolio • Review of a progress report on the current and forecast fixed:floating debt ratios and a valuation of the existing hedging portfolio • Review of the appropriate split between index-linked and nominal debt in relation to the debt portfolio strategy • Considering a paper setting out a proposal for revision of the terms of reference of the Committee.
February 2010	• Review of the current status of the debt issuance programme and investment portfolio • Review of a progress report on the current and forecast fixed:floating debt ratios and a valuation of the existing hedging portfolio • Considering a report on the status of the Treasury Risk Register • The annual review of the terms of reference of the Committee, the general effectiveness of the Committee and its composition.

The Policy & Performance Committee
Members

Current members	From
Rick Haythornthwaite (Chairman of Committee from January 2010)	January 2010
David Bailey	January 2010
Graham Eccles	March 2010
Lawrie Haynes	March 2010
David Higgins	April 2010
Steve Russell	January 2010

The Chief Executive and Director, Planning and Development, and occasionally with other Executive Directors, attend by invitation.

Role The role of the Committee includes:

- monitoring the quality, scope and integrity of the long and short-term planning
- monitoring operational and project risk management of the Company
- promoting within the Company a systems approach to resource and risk management
- seeking reassurance that performance metrics used in the Company are appropriate, for the purpose of seeking timely, effective solutions to the objectives of the Company
- monitoring the status of stakeholder goodwill and the Company's approach to stakeholder relationships, with particular emphasis on the Company's customers and their customers
- investigating or advising on the above or any related matters that are referred to it or as may appear to it to be necessary.

Process The Committee conducts its responsibilities through a series of scheduled meetings with a defined set of items of business for each meeting. The Committee chairman reports on the Committee's activities to the Board meeting immediately following a Committee meeting.

Activities in 2009/10 During the year ended 31 March 2010, this Committee met twice – having been set up at the end of 2009 and having its first meeting in January 2010 – and its principal activities are set out on page 70.

The Policy & Performance Committee's activities in 2009/10

Meeting	Agenda item
January 2010	• Receiving a paper on the key issues associated with the preparations for the next periodic review which will conclude in 2013 (PR13) and establishing the required outputs and funding for Control Period 5 (CP5) • Considering definition of two Key Performance Indicators and the latest performance in the two areas • Reviewing the current asset management capability and the improvements which can be expected over CP4.
March 2010	• Considering how rail can contribute to the national goals outlined in DfT's Delivering a Sustainable Transport System and outlines the emerging shape of the proposed long-term planning framework • Considering the potential improvements identified by AMCL, the independent reporter on Network Rail's asset management capability • Considering definition of two Key Performance Indicators and the latest performance in the two areas.

The Remuneration Committee
Members

Current members		From
Steve Russell (Chairman of Committee from July 2009)		September2007
David Bailey		October 2002
Yvonne Constance*		May 2005
Michael Firth		December 2004
Christopher Green*		June 2005
Rick Haythornthwaite		March 2009
Previous members	**From**	**To**
Ian McAllister	October 2002	July 2009
Ian Buchan	February 2006	March 2010
Jim Cornell (Chairman until July 2009)	October 2002	July 2009

* Stepping down from the Board in July 2010.

Role It determines appropriate levels of Directors' and senior executives' remuneration including their incentive scheme.

Process The Committee conducts its responsibilities through use of a series of scheduled meetings with a defined set of items of business for each meeting. The Committee chairman reports on the Committee's activities to the Board meeting immediately following a Committee meeting.

Activities in 2009/10 During the year ended 31 March 2010, this Committee met six times. Details of the activities during the year are set out in the Directors' remuneration report on page 31.

The Nominations Committee
Members

Current members		From
Rick Haythornthwaite (Chairman of Committee from July 2009)		March 2009
David Bailey		October 2002
Steve Russell		November 2008
Previous members	**From**	**To**
Ian McAllister (Chairman until July 2009)	October 2002	July 2009
Jim Cornell	October 2002	July 2009

The Human Resources Director attends meetings by invitation.

Role The role of the Committee includes:

- reviewing regularly the size, structure and composition of the Board (including use of suitable periodic performance evaluation processes) and making recommendations to the Board on any adjustments that may be deemed necessary and feasible (including on matters such as succession planning)
- evaluating the balance of skills, experience, independence and knowledge of the Board
- identifying and nominating candidates for appointment as Director for approval by the Board
- satisfying itself that appropriate succession plans and processes are in place for the appointments to the Board and to senior management positions.

Process The Committee conducts its responsibilities through meetings held as appropriate. The Committee chairman reports on the Committee's activities to the Board meeting immediately following a Committee meeting. Between meetings, the Committee chairman discusses matters of succession and recruitment with the other members of the Committee as required.

Activities in 2009/10 During the year ended 31 March 2010, this Committee met eight times. Details of the activities during the year are set out in the Nominations Committee Report on page 51.

The Executive Committee

Composition At executive level in the Company the Executive Committee is chaired by the Chief Executive, and comprises all the Executive Directors and a number of senior executives.

Role This Committee manages the functions of the business and implements the operational and financial objectives within limits set by the Board.

Process The Committee conducts its responsibilities through a series of scheduled meetings.

Activities in 2009/10 During the year ended 31 March 2010, the Executive Committee met 12 times and its principal activities included approval (within its delegated authority) and review of operational issues and activities of the Company including:

- the operational, financial and safety, health and environment performance of Network Rail
- reports into significant rail incidents
- Network Rail's budget for 2010/11
- investment projects and contract awards
- progress reports on significant projects and programmes
- route utilisation strategies
- the delivery plan
- development and content of the delivery plan
- Network Rail's risk management
- development of corporate key performance indicators
- Network Rail's industrial relations activities
- human resources policies and strategic plans
- the status and activities of the Transformation Programme
- Network Rail's regulatory matters.

Other management meetings

Additionally there is a defined structure of other executive steering groups and panels with terms of responsibilities focusing on specified aspects of the operational needs of the business with prescribed levels of authority.

Board effectiveness

A development and awareness programme for Directors exists which can be summarised as follows:

- an induction programme when they join the Board
- briefings on the business of Network Rail
- meetings with Members and opportunities to meet other stakeholders
- briefings on external technical matters.

Induction There is a comprehensive programme of induction for all new Directors aimed at equipping them so that they are fully conversant with their responsibilities as a Director and with the business of Network Rail. This includes briefing by the Group Company Secretary relating to Network Rail and the industry, guidance on Board procedures and corporate governance matters. Each Director is then provided with a manual of key documents and background information. The personal induction programme then includes separate sessions with each of the Directors, key senior managers and also sessions with key stakeholders. The sessions focus on the challenges, opportunities and risks faced by the business. Opportunities to visit operational sites are also provided. New Directors receive an induction on the safety, health and environmental matters of the Company. Further or follow-up meetings are arranged where a Director requires a deeper understanding on a particular issue.

Since their appointments during 2009/10, Rick Haythornthwaite and Patrick Butcher completed their induction and Janis Kong, Lawrie Haynes, Graham Eccles and David Higgins have been undertaking their programmes. The induction programmes for the last four new additions to the Board were reviewed by the Chairman.

Development Directors are then encouraged to update their skills, knowledge and familiarity with the Group through their on-going participation at Board and Committee meetings, and through regular meetings with senior managers, other employees and Members. Briefings are given to Board members by members of senior management on key projects, organisational functions and governance or assurance processes adopted within Network Rail including major projects, strategy review, contracts and procurement, organisational effectiveness, corporate development and information management.

Site visits are regularly scheduled for Non-Executive Directors to enable them to view first hand operational aspects of the business and to meet employees. In 2009/10 Non-Executive Director visits were arranged to King's Cross station redevelopment, Birmingham New Street station redevelopment and long welded rail steel works at Corus, Scunthorpe.

Additional personal development is available to all Directors. During 2009/10 arrangements were put in place for leadership development to be provided to the Executive Directors and other senior executives over the course of the next 12 months. Plans are also being made to introduce a structured annual review of personal development needs for each Board Director.

Training Ongoing professional development is provided to Directors each year. Directors receive briefings on relevant issues including new developments relating to corporate governance, company law and other new legislation.

Directors are also encouraged to attend externally organised seminars on a range of topics designed to assist in equipping Directors with awareness of current legal, risk management or corporate governance issues and trends.

The Audit Committee and Safety, Health and Environment Committee have commenced review of the specialised training to be provided to Directors on those Committees on an on-going basis. The Remuneration Committee will undertake a similar process in 2010/11 once the composition of this Committee has been finalised.

Board evaluation review

The effectiveness of the Board is vital to the success of Network Rail. Accordingly the Nominations Committee is charged by the Board to review annually the performance of the Board, its principal Committees and individual Directors. The policy adopted by the Nominations Committee is for external assistance also to be provided in conducting the review on a bi-annual basis. In the interim year the review is to be conducted internally by the Group Company Secretary. Details of the evaluation process for 2009/10 are set out in the Nominations Committee Report on pages 50 to 53.

Company Secretary

The Group Company Secretary is the secretary to the Board and all of the above Board committees and is responsible for advising each of these, through their chairman, on all governance matters. All Directors have access to the Group Company Secretary for advice on corporate governance, Board procedure and compliance matters. As well as supporting the Chairman with his responsibility for management of the Board and Board matters, the Group Company Secretary is also responsible for facilitating the induction and professional development of Board members and good flow of information within the Board, its Committees and between the Non-Executive Directors and senior management. The Group Company Secretary also acts as dedicated support to the Non-Executive Directors.

Advice

There is a procedure whereby Directors, wishing to do so in furtherance of their duties, may take independent professional advice at Network Rail's expense. No such advice was sought by any Director during 2009/10.

Conflict of interest management

Under the Companies Act 2006, Directors are under an obligation to avoid situations in which their interests can or do conflict, or may possibly conflict, with those of the company. In accordance with the Act, the Company's Articles of Association were amended to allow the Directors to authorise conflicts and potential conflicts, where appropriate. Procedures, already in place prior to the Companies Act 2006, were reviewed to ensure that they continue to be effective in relation to the disclosure of conflicts, the consideration and, if appropriate, the authorisation of conflicts by non-conflicted Directors. The Directors have not had need to exercise their powers to authorise any conflict of interest of any Director of Network Rail Limited during 2009/10.

Relations with Members and other stakeholders

Network Rail Limited does not have external shareholders. Instead it is owned by Members. Collectively Members and the wide range of other parties affected directly or indirectly in the activities of the Network Rail Group form very important stakeholders to both the Company and Network Rail Infrastructure Limited. The Company devotes, therefore, significant attention to the quality of its relationship with this diverse range of interests.

Delivering a specific improvement in stakeholder satisfaction does not form part of the regulated outputs that Network Rail is required to deliver. Notwithstanding this, the Board of Network Rail is extremely committed to, and recognises the importance of, developing and maintaining an ongoing relationship based on regular communication and dialogue with its wide range of stakeholders. Satisfying customers, users of the railway and other stakeholders must be at the heart of Network Rail's business delivery.

Various approaches are used to monitor the satisfaction of customers, rail users and other stakeholders within an overall performance management framework. For example, to monitor performance in this important area surveys of customer satisfaction for passenger and freight operators are undertaken each year. Similar surveys are produced for Network Rail's other stakeholders. Moreover, in 2009 customer satisfaction became a formal consideration under the Management Incentive Plan – see the Directors' remuneration report on pages 38 and 39 for details.

In summary the key relationship management activities are:

Members

A variety of forms of contact with Members of Network Rail is used to help Members hold the Board to account for the performance of the Group and to help Members to be aware of and understand developments within the business.

Members' role

It is the role of the Board of Directors of Network Rail to run the Company. It manages the Company for the Members and other stakeholders. Within the governance framework described above, the Directors provide leadership and management for the business as a whole being selected for their expertise, skills and experience for which they have legal responsibilities and duties.

The role of a Member is very different from that of a Director. Whilst Directors are responsible for the operation of the business including the decision-making as to how to deliver its obligations, the role of a Member, by contrast, is to hold the Board to account for its management of Network Rail. The way in which Members contribute to the delivery of a safe, reliable and efficient rail network is to perform effectively this different but important function.

The role of Members is similar to the role of shareholders in companies that have a share capital. In practice this means:

- **reviewing the overall performance (including safety) of Network Rail** against the operational and financial business plans published by Network Rail as well as against railway industry benchmarks. This is a **monitoring role** rather than an involvement in day-to-day management
- **holding the Board to account for its management of Network Rail** and in particular its achievement measured against its business plans
- **monitoring** Network Rail's management against **high standards of corporate governance**.

Unlike shareholders, whose objective is generally a return on capital, Members have a common objective – delivery of a safe and efficient rail network.

To assist Members to perform their role a set of ten principles has been drawn up which describes the basis of the role of Members and the measurement by which the Board of Network Rail can be judged in relation to how it runs the Company and against which the Board should be held to account. These principles are set out on page 55.

There are currently about 100 Members of Network Rail. Industry Members have a right of automatic membership if they meet the eligibility criteria set out in the Articles of Association. An independent panel, the Membership Selection Panel (MSP), oversees the process of publicising the opportunity to become a Public Member, analysing the applications and making recommendations to the Board of Network Rail for the appointment of individuals as Public Members. The Board can appoint as Public Members only individuals from those recommended by the MSP. Nevertheless the Board is not required to accept the recommendations of the MSP. The Board has never exercised this right to reject the recommendations of the MSP but if it were ever to do so it would publicise the fact and explain the basis for doing so.

The process by which the MSP selects individuals involves finding a blend of skills and experience from those whom the MSP considers to have appropriate experience of corporate governance. The MSP will identify, in the first instance, those who have demonstrated the active contribution they have made to the corporate governance of organisations with which they are involved and their ability to meet certain core competences. The MSP then considers the wider range of skills and experience candidates offer in order to achieve a blend of skills and experience.

Members' induction

Once appointed new Members attend a workshop to allow them to acquaint themselves with the Group and its businesses. The topics covered in the workshop can be summarised as follows:

- governance structure and their contribution as Members
- role of the Board
- update on the recent activities of the existing Members
- external governance debate and role of Network Rail's stakeholders in the debate
- the delivery outputs expected from Network Rail during the relevant control period.

Extensive resource material is also available to Members to familarise themselves with Network Rail and the rail industry provided by both Network Rail through the Members' dedicated website and its general website, as well as through other sources including the website of the ORR.

During membership

Members have available to them significant amounts of information about Network Rail and the rail industry. In particular Network Rail facilitates a wide range of communication methods whereby it provides information and enables Members to assess matters. The various forms of communication include:

- publication of full Annual Reports and Accounts
- publication of Interim and Preliminary Results
- the Annual General Meeting and other meetings of Network Rail Limited as required
- supply of key press releases, business documents and other material
- receipt of copies of the staff magazine
- regular meetings with Directors and senior Network Rail staff
- ability to attend periodical local briefings and site visits
- regular presentations on key issues
- provision of documents published by other bodies e.g. the ORR's quarterly monitor on Network Rail, key ORR consultation documents and other reports
- the services of a Network Rail employee dedicated to responding to enquiries and issues raised by Members (Members' Executive)
- a dedicated website for Members containing information about Network Rail and its governance, presentation material distributed at Members' meetings and a discussion forum facility for Members to share views. Within Network Rail this site is accessible by Members' Executive only
- a Members' only website for Members to discuss on-line between themselves. This site is not accessible by Network Rail.

Latest developments

Various new initiatives have been introduced during the year to enhance the flow of information and transparency between the Members and the Company including:

- the introduction of the Network Rail governance principles – see pages 54 and 55
- the launch of a quarterly governance letter written by the Chairman to encourage increased insight and debate amongst the Members on the governance of Network Rail through reporting on key governance topics including as the recent developments in governance structure, business performance, key Board and executive team decisions and other governance matters
- the enhanced independence of the Members' selection process by the removal of the requirement for a Non-Executive Director to be a member of the MSP
- the holding of focus meetings where Members have the opportunity to probe members of the Board on matters of governance as well as have the opportunity to get briefings on major topics and also enabling the Board to assess the views of Members on key matters of accountability
- the holding of twice a year meetings with the Chief Executive following announcement of half year and year end results to discuss with Members the key aspects of operational and financial performance
- the advanced publication and distribution of a schedule of Member events for the coming year – see opposite for details of the 2010 schedule.

The focus meetings arranged during 2009/10 were on a variety of specific topics during which Members discussed with a selection of Directors key aspects of Network Rail. The topics at these forums have included Directors' and senior management remuneration, risk management, asset management and the Members' selection process and planned changes to this. Presentation material used at these forums was also posted on the Members' website for all Members to access.

A table showing the key diary dates in 2010 for the members is detailed below:

Month in 2010	Event
January	Members' workshop
March	Chairman's governance letter
March	ORR Monitor Report
March	Interest rate hedging teleconference
April	Members' workshop
May	Members' site visit
June	Chairman's governance letter
June	ORR Monitor Report
June	Preliminary results
June	Members' discussion with the Chief Executive
June	Members' meeting with the ORR
July	AGM
September	Chairman's governance letter
September	ORR Monitor Report
September	Members' site visit
October	Members' workshop
November	Interim results
November	Chairman's governance letter
November	ORR Monitor Report
December	Members' half yearly meeting
December	Members' discussion with the Chief Executive

Members are encouraged to propose topics for briefing or discussion. Opportunities may also arise in each year for additional events – whether in the form of meetings, telephone conferences or other communication formats – at which topical matters can be discussed.

Members also have the opportunity to meet the Board both before and after the formal general meetings as well as to ask questions at the AGM of Network Rail Limited (including by submission of written questions in advance). Before the AGM Members are also encouraged to request areas of the business on which they would like presentations.

With the election in 2009 of a members' co-ordinator from amongst the Members, discussion now also takes place between the Chairman of the Board and the co-ordinator on the agenda contents for key meetings.

Meeting the Office of Rail Regulation

Members are invited to meet with the ORR, the rail industry's regulating body, at which they discuss the ORR's views on the current performance of Network Rail against its regulatory obligations.

Formal Company business

In line with best corporate governance practice, Network Rail Limited separates out the business of the AGM into single resolutions as required under the Code. Poll voting is adopted for all resolutions. The level of proxy votes received for the AGM is disclosed together with details of the votes for, against and the abstentions for each resolution. The chairmen of the Board committees are also available at the AGM to answer questions in relation to their committee's area of responsibility. The chairman of the MSP also attends the AGM for the same purpose of answering questions relating to the selection of new Public Members.

In addition and in line with best practice, the Notice of the AGM and any related papers are sent out to Members with the aim of arriving at least 20 business days before the date of the meeting to ensure that Members have sufficient time in which to consider the items of business. The next AGM will be held on 21 July 2010.

Members are also able to seek advice from the Group Company Secretary on how to exercise their rights under company law to requisition a resolution or a meeting. Some Members have used the right to requisition a resolution at each AGM in 2004 to 2008.

Attendance at Network Rail's AGM has been high for each year since its creation. In 2009, for example, 84 of the then current 106 Members voted. This is in line with the percentage of voting Members that Network Rail has benefited from in recent years. It is an impressive level of participation compared with the percentage of voting shareholders that a FTSE 100 company would typically expect at an AGM.

Review of the role of members

At the AGM in 2008 a resolution was requisitioned by a number of Members seeking to establish a temporary group of 12 Members to review the effectiveness of the corporate governance of Network Rail especially in relation to the Members. This resolution gained sufficient support at the AGM and was passed. Subsequently an election was held amongst Members to appoint the 12 members of the group known as the Members' Review Group (MRG). The MRG then conducted a number of activities considering the corporate governance of Network Rail including commissioning a survey by PricewaterhouseCooper of stakeholders, conducting a comparative analysis of the corporate structure of Network Rail with other corporate structures and a review of Network Rail's governance against certain corporate governance best practice.

The MRG reported back to all Members of Network Rail. Its final report was published to Members in July 2009 setting out a number of recommendations on enhancements to the governance of Network Rail. In November 2009 Members voted in favour of the following three of the recommendations of the MRG:

- the appointment of a Members' Co-ordinator
- the introduction of a web-based discussion site for Members only (the Members' only website)
- the provision by Network Rail to the Members of an adequate and reasonable budget for independent research and analysis.

These recommendations have been implemented. The Members' co-ordinator was elected from amongst the Members and now liaises with the Chairman of the Board of Directors on the agendas for Members meetings, and facilitates the agendas for the Members only meetings. The co-ordinator also has a role in moderating Members only meetings. The Members' only website has been launched and a budgeted sum is available to Members for research and analysis.

A fourth recommendation on the reduction of the number of Members was also voted upon but did not gain a majority of support and as such this suggestion has not been progressed.

Other stakeholders

The Company also recognises the importance of good relationships with its wider stakeholder base especially its customers – the passenger and freight train operators, its suppliers, funders and its own employees. Emphasis is placed, therefore, on developing existing relationships as well as expanding the breadth of relationships.

This includes the Chief Executive, other Executive Directors and functional Directors (together with many other senior managers) having regular meetings with representatives of the ORR (as both economic and safety regulator), passenger and freight train operators and other rail stakeholders. Scheduled meetings are held with the Department for Transport and train operators to discuss industry wide issues. Dialogue is continuous between both Executive Directors of Network Rail and throughout the Company with each of our customers – the passenger and freight operators. Dedicated executive resource is given to each customer. Monthly monitoring of performance on a customer by customer basis and on relationships between customers and Network Rail are reviewed by the executive management team. Action plans are drawn up with each customer seeking to address key issues as well as commitment by both parties to formal joint performance improvement plans.

Independent relationship surveys are conducted regularly with each of the Company's customers (the train operators), passengers and freight end users, suppliers and its employees (using an employee engagement survey – see pages 24 and 25 of the Directors' report for more detail).

In addition various forms of formal consultation with key stakeholders takes place on many aspects of Network Rail's activities, run either directly by Network Rail, by the ORR or by others.

2010 will also see an enhancement to stakeholder relationships through a number of the Board meetings being scheduled to be held outside London. These visits incorporate opportunities for feedback meetings with stakeholders. Furthermore, developing on the existing site visits schedule of the Non-Executive Directors, they are encouraged to visit at least one Network Rail site per quarter as well as maintain their relevant contacts related to the rail industry and its wide stakeholder base. Arrangements are also made for new Directors coming into Network Rail to meet with key stakeholders as part of their induction programme.

Network Rail needs to work closely with all types of community representatives and so, as part of its normal day-to-day routine activities, Network Rail regularly briefs many different bodies and individuals. This includes the

Company having a significant amount of contact with a wide range of elected representatives (Members of Parliament, Members of the Scottish Parliament, London Assembly and Welsh Assembly, Members of the European Parliament and others) as well as non-governmental organisations, pressure groups and campaigning organisations. This includes meetings to discuss issues facing the Company and those using the railways, both passengers and freight traffic nationally and regionally. Opportunity is also taken each year to explain to elected representatives the Company's business plans, performance and significant developments within the business. This is sometimes best achieved through the Company organising briefings and similar functions at which presentations are given as well as site visits.

The Network Rail Stakeholder Relations Code of Practice was launched in March 2010. This code of practice forms a fundamental part of how Network Rail intends to improve its business performance over the next five years and is firmly aligned with its ongoing programme to create a service culture within the Company. Network Rail aims to be seen as a great company to do business with and which delivers on its promises. The code of practice aims to go part of the way to satisfying this ambition, by recognising that in order to give stakeholders a better experience Network Rail needs to pre-empt and respond to their needs.

The overarching principle of the code of practice is that Network Rail will aim to deal with stakeholders:

- in an efficient and timely manner
- with the skill, diligence, prudence and foresight that is expected of us as a skilled and experienced network facility owner and operator.

Corporate responsibility

Corporate responsibility is also an important aspect of the role of Network Rail and one which it takes seriously. To support this, it has published a comprehensive Sustainability Policy which sets out its commitment, key goals and targets across social, economic and environmental sustainability.

On every notice board across Network Rail its Sustainability Policy statement appears, in which the Chief Executive sets out his commitment to delivering a responsible and sustainable railway.

Progress towards becoming a more responsible and sustainable company is reported in the Company's annual Corporate Responsibility Report. This includes:

- workplace issues like safety, health and wellbeing, talent, diversity and employee engagement
- community issues like charitable giving, community relations and community safety

Sustainability Policy

Social

Community
- Lineside neighbours and visual intrusion
- Social commitment
- Community relationships
- Heritage

Workplace – our people
- Employee relations
- Employee health
- Employee development
- Social inclusion

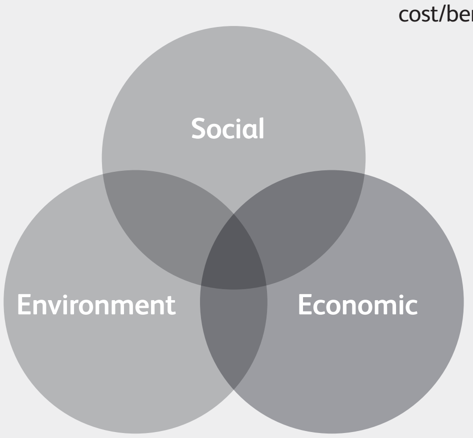
Marketplace – passengers
- Train service performance
- Safety and personal security
- Priorities, perception and experience
- Accessibility
- Travel information

Environment

- Air quality
- Noise and vibration
- Waste and pollution
- Land use and biodiversity
- Water and material use
- Climate change (including energy use)

Economic

Marketplace – customers, suppliers and funders
- Capacity
- Government policy and subsidy
- Purchasing and procurement
- Asset management (including climate change adaptation)
- Regional economic development
- Affordability and external cost/benefits to society



- marketplace issues like rail safety, or providing great travel environments and positive door-to-door journeys
- economic issues like encouraging modal shift or improving train service reliability and capacity
- environmental issues like reducing waste, improving energy efficiency, and protecting our natural habitats.

The next report will be published in the summer of 2010.

Strategic direction for corporate responsibility is provided by Network Rail's Corporate Responsibility Group in cross-functional meetings chaired by the Chief Executive. The group, which meets on a bi-monthly basis, is made up of senior representatives from within Network Rail. In February 2010 the terms of reference and remit of the group were reviewed and new members included. This group's remit includes:

- providing direction on the policy, strategy and objectives necessary to deliver Network Rail's sustainability goals across economic, social and environmental areas
- agreeing the measurable targets for sustainability and the specific activities and initiatives to deliver these targets
- monitoring the progress and success of these activities and providing priorities as appropriate.

Statement of Directors' responsibilities

The Directors are responsible for preparing the Annual Report and the financial statements. The Directors are required to prepare financial statements for the Group in accordance with International Financial Reporting Standards adopted for use in the European Union (IFRSs) and have also elected to prepare financial statements for the Company in accordance with IFRS. Company law requires the Directors to prepare such financial statements in accordance with International Financial Reporting Standards, the Companies Act 2006 and Article 4 of the IAS Regulation.

International Accounting Standard 1 requires that financial statements present fairly for each financial year the Company's financial position, financial performance and cash flows. This requires the faithful representation of the effects of transactions, other events and conditions in accordance with the definitions and recognition criteria for assets, liabilities, income and expenses set out in the International Accounting Standards Board's Framework for the Preparation and Presentation of Financial Statements. In virtually all circumstances, a fair presentation will be achieved by compliance with all International Financial Reporting Standards.

Directors are also required to

- select applicable accounting policies and apply them properly
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information
- provide additional disclosures when compliance with the specific requirements in IFRS is insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance
- prepare the accounts on a going concern basis unless, having assessed the ability of the Company to continue as a going concern, management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so.

The Directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and Group, for safeguarding the assets, for taking reasonable steps for the prevention and detection of fraud and other irregularities and for the preparation of the Directors' report and the Directors' remuneration report which comply with the requirements of the Companies Act 2006.

The Directors are responsible for the maintenance and integrity of the Company website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements differs from legislation in other jurisdictions.

On behalf of the Board of Network Rail

Hazel Walker
Group Company Secretary
3 June 2010

Independent auditors' report

to the Members of Network Rail Limited

We have audited the financial statements of Network Rail Limited for the year ended 31 March 2010 which comprise the Group Income statement, the Group and parent Company statements of comprehensive income, the Group and parent Company Balance sheets, the Group and parent Company cash flow statements, the Group statement of changes in equity and the related Notes 1 to 29. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union and as regards the parent company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and auditors

As explained more fully in the Directors' responsibilities statement, the Directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's (APB's) Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Group's and the parent Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the Directors; and the overall presentation of the financial statements.

Opinion on financial statements

In our opinion:

- the financial statements give a true and fair view of the state of the Group's and of the parent Company's affairs as at 31 March 2010 and of the Group's profit for the year then ended
- the Group financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union
- the parent Company financial statements have been properly prepared in accordance with IFRSs as adopted by the European Union and as applied in accordance with the provisions of the Companies Act 2006
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006 and, as regards the Group financial statements, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Companies Act 2006

In our opinion, the information given in the Directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Matters on which we are required to report by exception

We have nothing to report in respect of the following:

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or
- the parent Company financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Other matter

Whilst not required by law or regulation, the Directors have elected to publish such financial information as is required to be announced by a company admitted to the Official List of the UK Listing Authority. The Directors have asked us to perform the same audit of Directors' remuneration and review of corporate governance disclosures as would be required were the company to be admitted to the Official List. Accordingly:

- in our opinion, the part of the Directors' remuneration report to be audited has been properly prepared in accordance with the provisions of the Companies Act 2006 applicable to quoted companies
- we have nothing to report in respect of:
  - our duty to report if the Directors' remuneration report is not in agreement with the accounting records or returns
  - our review of the Directors' statement contained within Corporate governance statement in relation to going concern
  - our review of the part of the Corporate governance statement relating to the Company's compliance with the nine provisions of the June 2008 Combined Code specified for review by the auditor of a company admitted to the Official List.

Andrew Kelly

Andrew Kelly (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Chartered Accountants
and Statutory Auditors

London, United Kingdom
3 June 2010

Income statement

for the year ended 31 March 2010

	Notes	Results pre debt and derivative revaluations 2010 Group £m	Debt and derivative revaluations (Note 8) 2010 Group £m	2010 Group £m	2009 Group £m
Revenue	3	**5,668**	**–**	**5,668**	6,160
Net operating costs	4	**(3,675)**	**–**	**(3,675)**	(3,604)
Operating profit		**1,993**	**–**	**1,993**	2,556
Property revaluation movements and profits on disposal		**62**	**–**	**62**	(138)
Total profits from operations	5	**2,055**	**–**	**2,055**	2,418
Investment revenue	7	**19**	**–**	**19**	112
Other gains and losses	8	**–**	**(477)**	**(477)**	(72)
Finance costs	9	**(1,197)**	**–**	**(1,197)**	(946)
Profit before tax		**877**	**(477)**	**400**	1,512
Tax	10	**(242)**	**134**	**(108)**	(911)
Profit for the year		**635**	**(343)**	**292**	601

All amounts in the current and prior years relate to continuing operations.

Under section 408 of the Companies Act 2006 the Group has elected to take the exemption with regard to disclosing the Company Income statement. The Company's net profit for the year was £nil (2009: £nil).

Statements of comprehensive income

for the year ended 31 March 2010

	2010 Group £m	2009 Group £m	2010 Company £m	2009 Company £m
Profit for the year	**292**	601	**–**	–
Losses on revaluation of the railway network	**(1,033)**	(113)	**–**	–
(Losses)/gains on movement in fair value of hedging derivatives	**(179)**	44	**–**	–
Recycling of balances in hedging reserve to other gains and losses in the income statement	**4**	4	**–**	–
Exchange differences on cash flow hedges taken to the hedging reserve	**154**	(391)	**–**	–
	(21)	(343)	**–**	–
Actuarial losses on defined benefit pension schemes	**(292)**	(281)	**–**	–
Tax relating to components of other comprehensive income	**376**	207	**–**	–
Other comprehensive expense for the year	**(970)**	(530)	**–**	–
Total comprehensive (expense)/income for the year	**(678)**	71	**–**	–

Statements of changes in equity

for the year ended 31 March 2010

Group	Revaluation Reserve £m	Other Reserve* £m	Hedging Reserve £m	Retained Earnings £m	Total £m
At 1 April 2008	**3,870**	**249**	**(72)**	**2,504**	**6,551**
Revaluation of the railway network	(113)	–	–	–	(113)
Transfer of deemed cost depreciation from revaluation reserve	(182)	–	–	182	–
Decrease in deferred tax liability on the railway network	82	–	–	(51)	31
Actuarial losses on defined benefit pension schemes	–	–	–	(281)	(281)
Deferred tax on actuarial losses	–	–	–	79	79
Increase in fair value of hedging derivatives	–	–	44	–	44
Exchange differences on cash flow hedges taken to the hedging reserve	–	–	(391)	–	(391)
Deferred taxation on all hedging reserve movements/retained earnings	–	–	98	–	98
Transfers					
Recycling of balances in hedging reserve to other gains and losses in the income statement	–	–	4	–	4
Deferred tax on transfers	–	–	(1)	–	(1)
Net profit for the year	–	–	–	601	601
At 31 March 2009	**3,657**	**249**	**(318)**	**3,034**	**6,622**
Revaluation of the railway network	(1,033)	–	–	–	(1,033)
Transfer of deemed cost depreciation from revaluation reserve	(147)	–	–	147	–
Decrease in deferred tax liability on the railway network	330	–	–	(41)	289
Actuarial losses on defined benefit pension schemes	–	–	–	(292)	(292)
Deferred tax on actuarial losses	–	–	–	82	82
Decrease in fair value of hedging derivatives	–	–	(179)	–	(179)
Exchange differences on cash flow hedges taken to the hedging reserve	–	–	154	–	154
Deferred taxation on all hedging reserve movements/retained earnings	–	–	7	–	7
Transfers					
Recycling of balances in hedging reserve to other gains and losses in the income statement	–	–	4	–	4
Deferred tax on transfers	–	–	(2)	–	(2)
Net profit for the year	–	–	–	292	292
At 31 March 2010	**2,807**	**249**	**(334)**	**3,222**	**5,944**

* Other reserves of £249m (2009: £249m) include the vesting reserve on privatisation.

There have been no changes in the Company equity and, therefore, no Company only reconciliation has been presented.

Balance sheets

at 31 March 2010

	Notes	2010 Group £m	2009 Group £m	2010 Company £m	2009 Company £m
Assets					
Non-current assets					
Intangible assets	11	**72**	73	**–**	–
Property, plant and equipment – the railway network	12	**36,629**	34,925	**–**	–
Investment property	13	**764**	700	**–**	–
Derivative financial instruments	20	**702**	768	**–**	–
Finance lease receivables	16	**8**	10	**–**	–
Interest in joint venture	14	**5**	5	**–**	–
Total non-current financial assets		**715**	783	**–**	–
		38,180	36,481	**–**	–
Current assets					
Inventories	15	**132**	88	**–**	–
Finance lease receivables	16	**2**	3	**–**	–
Trade and other receivables	17	**720**	813	**–**	–
Current tax assets		**6**	–	**–**	–
Derivative financial instruments	20	**297**	630	**–**	–
Cash and cash equivalents	24	**2,321**	1,723	**–**	–
		3,478	3,257	**–**	–
Total assets		**41,658**	39,738	**–**	–
Current liabilities					
Trade and other payables	18	**(3,043)**	(3,658)	**–**	–
Current tax liabilities		**–**	(18)	**–**	–
Bank loans and overdrafts	19	**(2,227)**	(1,776)	**–**	–
Derivative financial instruments	20	**(210)**	(73)	**–**	–
Short-term provisions	21	**(57)**	(9)	**–**	–
		(5,537)	(5,534)	**–**	–
Net current liabilities		**(2,059)**	(2,277)	**–**	–
Non-current liabilities					
Bank loans	19	**(23,385)**	(21,201)	**–**	–
Derivative financial instruments	20	**(507)**	(406)	**–**	–
Other payables	18	**(2,094)**	(1,841)	**–**	–
Retirement benefit obligation	28	**(985)**	(664)	**–**	–
Deferred tax liabilities	22	**(3,204)**	(3,467)	**–**	–
Obligations under finance leases	23	**(2)**	(3)	**–**	–
		(30,177)	(27,582)	**–**	–
Total liabilities		**(35,714)**	(33,116)	**–**	–
Net assets		**5,944**	6,622	**–**	–
Equity					
Revaluation reserve		**2,807**	3,657	**–**	–
Other reserve		**249**	249	**–**	–
Hedging reserve		**(334)**	(318)	**–**	–
Retained earnings		**3,222**	3,034	**–**	–
Total equity		**5,944**	6,622	**–**	–

The financial statements were approved by the Board of Directors and authorised for issue on 3 June 2010.

They were signed on its behalf by:

Iain Coucher Director

Patrick Butcher Director

Company reference number: 04402220

Statements of cash flows

for the year ended 31 March 2010

	Notes	2010 Group £m	2009 Group £m	2010 Company £m	2009 Company £m
Net cash generated from operating activities	24	**2,234**	2,811	**–**	–
Investing activities					
Interest received		**24**	78	**–**	–
Purchases of property, plant and equipment – the railway network		**(3,939)**	(4,601)	**–**	–
Proceeds on disposal of investment property		**1**	72	**–**	–
Capital grants received		**339**	191	**–**	–
Capital element of finance leases' receipts		**2**	3	**–**	–
Sale of financial investments		**–**	55	**–**	–
Acquistion of joint venture		**–**	(5)	**–**	–
Net cash used in investing activities		**(3,573)**	(4,207)	**–**	–
Financing activities					
Repayments of borrowings		**(1,416)**	(4,853)	**–**	–
Repayments of obligations under finance leases		**–**	(6)	**–**	–
New loans raised		**4,053**	6,373	**–**	–
Collateral (repaid to)/received from counterparties		**(508)**	1,062	**–**	–
Losses on derivatives not hedge accounted		**(192)**	–	**–**	–
Net cash generated from financing activities		**1,937**	2,576	**–**	–
Net increase in cash and cash equivalents		**598**	1,180	**–**	–
Cash and cash equivalents at beginning of the year		**1,723**	543	**–**	–
Cash and cash equivalents at end of the year		**2,321**	1,723	**–**	–

Notes to the financial statements

for the year ended 31 March 2010

1. General information

Network Rail Limited is a company incorporated in Great Britain and registered in England and Wales under the Companies Act 2006.

The Company registration number is 04402220.

The Company's registered office is situated at Kings Place, 90 York Way, London, N1 9AG.

The Company's principal activities are detailed in the Directors' report on pages 16 to 27.

Details of the Group's business activities, key events and changes during the year and likely future developments are contained in the Chairman's statement, the Chief Executive's review and the Group Finance Director's review. These financial statements should also be read in conjunction with the Corporate governance report and the Directors' remuneration report.

Presentation of the Income statement: exceptional debt and derivative revaluations

The Income statement has been presented in a three-column format in order to allow users to appreciate the impact on the results for the year of gains and losses arising from the revaluation of debt and derivatives. See Note 8 for further information.

2. Significant accounting policies

Basis of accounting

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) adopted for use in the European Union, and therefore comply with Article 4 of the EU IAS regulation.

The financial statements have been prepared on the historical cost basis, except for the revaluation of the railway network to a value determined using an income approach, the revaluation of investment properties, the measurement of certain financial assets and liabilities at fair value through profit and loss (FVTPL) and the measurement of derivative financial instruments at fair value.

The principal accounting policies adopted by the Directors are set out below.

Adoption of new and revised standards

IAS 1 (as revised in 2007) *Presentation of Financial Statements* was adopted in the current year and has introduced terminology changes (including revised titles for the financial statements) and changes in the format and content of financial statements. The adoption of this revision to IAS 1 has resulted in the inclusion of Statements of changes in equity as primary statements. The Statement of recognised income and expense is now presented as the Statement of comprehensive income and the Cashflow statement being presented as the Statement of cashflows.

The following new and revised Standards and Interpretations have also been adopted in these financial statements. Their adoption has not had any significant impact on the amounts reported in these financial statements but may affect the accounting for future transactions or arrangements.

Amendments to IFRS 1 and IAS 27	*First-time Adoption of International Financial Reporting Standards and Consolidated and Separate Financial Statements – Cost of an Investment in a Subsidiary, Jointly Controlled Entity or Associate*
Amendments to IFRS 2	*Share-based Payment – Vesting Conditions and Cancellations*
Amendment to IAS 23	*Borrowing Costs*
Amendments to IAS 32 and IAS 1	*Financial Instruments: Presentation and Presentation of Financial Statements – Puttable Financial Instruments and Obligations Arising on Liquidation.*
Amendments to IFRS 7	*Financial Instruments: Disclosures (Improving Disclosures about Financial Instruments)*
Amendments to IAS 39 and IFRS 7	*Financial Instruments: Recognition and Measurement and Financial Instruments: Disclosures regarding reclassifications of financial assets.*
Amendments to IFRIC 9 and IAS 39	*Reassessment of Embedded Derivatives and Financial Instruments: Recognition and Measurement*
IFRIC 12	*Service Concession Arrangements*
IFRIC 13	*Customer Loyalty Programmes*
IFRIC 14	*IAS 19 – The Limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction*
IFRIC 15	*Agreements on the Construction of Real Estate*
IFRIC 16	*Hedges of a Net Investment in a Foreign Operation*
IFRIC 17	*Distributions of Non-cash Asset to Owners (adopted in advance of effective date of 1 July 2009)*
IFRIC 18	*Transfers of Assets from Customers (adopted for transfers of assets from customers received on or after 1 July 2009).*
Improvements to IFRSs (2008)	

2. Significant accounting policies continued

At the date of authorisation of these financial statements, IFRS 8 *Operating segments* had been issued. The Company has chosen not to adopt this standard as the Company is outside the scope of IFRS 8.

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective (and in some cases had not been adopted by the EU):

Amendments to IAS 17	*Leases*
Amendments to IAS 27	*Consolidated and separate financial statements*
Amendments to IAS 39	*Financial Instruments: Recognition and Measurement (Eligible Hedged Items)*
Amendments to IFRS 2	*Share-based Payment*
Amendments to IFRS 3	*Business Combinations*
IFRIC 17	*Distribution of Non-cash Assets to Owners*
Improvements to IFRSs (2009)	

The Directors anticipate that the adoption of these Standards and Interpretations in the future periods will have no material effect on the financial statements of the Group.

Going concern

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Directors' report on pages 16 to 27. The financial position of the Group, its cash flows, liquidity position and borrowing facilities are described in the Group Finance Director's review on pages 10 to 15. In addition, Note 27 to the accounts included the Group's objectives, policies and processes for managing its capital; its financial risk management objectives; details of its financial instruments and hedging activities; and its exposures to credit, liquidity and foreign exchange risk.

The Group has considerable financial resources together with long term contracts with a number of customers and suppliers. As a consequence, the Directors believe that the Group is well placed to manage its business risks despite the current uncertain economic outlook.

After making enquiries, the Directors have a reasonable expectation that the Group has adequate resources to continue in operations existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

Basis of consolidation

The consolidated financial statements incorporate the financial statements of the Company and entities controlled by the Company. This includes special purpose financing companies which are not members of the Network Rail Group but are treated as subsidiaries in the Consolidated accounts of Network Rail Infrastructure Limited. All intra-group transactions, balances, income and expenses are eliminated on consolidation.

Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable. Revenue represents amounts derived from the management and provision of assets for the use in the operation of the railway and property rental income net of value added tax. Amounts recognised take account of any performance penalties or bonuses in respect of the year.

Revenue also includes supplements to the access charges and bonuses receivable from, less penalties payable to, customers. Operating expenditure includes additional contract amounts and bonuses payable to, less penalties receivable from, suppliers and the Office of Rail Regulation.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable. This is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Grants

Grants and other contributions received towards the cost of property, plant and equipment are included in trade and other payables as deferred income and released to the Income statement over the estimated useful economic life of the railway network. Revenue grants earned for the management and provision of railway network assets are credited to the Income statement in the period to which they relate.

Leasing

Leases are classified as finance leases when the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

2. Significant accounting policies continued

The Group as lessor

Amounts due from lessees under finance leases are recorded as receivables at the amount of the Group's net investment in the leases. Finance lease income is allocated to accounting periods so as to reflect a constant periodic rate of return on the Group's net investment outstanding in respect of the leases.

Rental income from operating leases and initial direct costs are recognised on a straight line basis over the term of the relevant lease.

The Group as lessee

Assets held under finance leases are recognised at their fair value as assets of the Group or, if lower, at the present value of the minimum lease payments. Each are determined at the inception of the lease. The corresponding liability to the lessor is included in the Balance sheet as a finance lease obligation. Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged to the Income statement, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Group's general policy on borrowing costs (see below).

Rentals payable under operating leases are charged to income on a straight-line basis over the term of the relevant lease.

Foreign currencies

Monetary assets and liabilities expressed in foreign currencies are translated into sterling at rates of exchange prevailing at the Balance sheet date. Foreign currency amounts are initially recorded at the rates of exchange prevailing on the dates of the transactions. Individual transactions denominated in foreign currencies are translated into sterling at the exchange rates prevailing on the dates payment takes place. Gains and losses arising on retranslation are, with the exception of the effective portion of foreign exchange gains or losses on debt instruments designated as hedging instruments in a cash flow hedge relationship, included in the Income statement for the period and are classified as either operating or financing depending on the nature of the monetary item giving rise to them.

Borrowing costs

Borrowing costs directly attributable to the construction of qualifying assets which are assets that necessarily take a substantial period of time to get ready for their intended use are added to the cost of those assets, until such time as the assets are substantially ready for their intended use.

All other borrowing costs are recognised in the Income statement in the period in which they are incurred.

Operating profit

Operating profit is stated before investment income, finance costs, other gains and losses and revaluation movements and profits on disposal of properties. A middle column has been presented to allow users to appreciate the impact of the revaluation of debt and derivatives on the results for the year. Not all hedging strategies qualify for hedge accounting and the Directors believe that by separating gains and losses arising from applying the valuation requirements of IAS 39, the users of this financial information will better understand the underlying performance of the Group.

Retirement benefit costs

Payments to the defined contribution retirement benefit scheme are charged as an expense as they fall due.

For the defined benefit scheme, the cost of providing benefits is determined using the Projected Unit Credit Method, with full actuarial valuations being carried out at least every three years and updates to these valuations carried out in intervening years.

The Group's share of the actuarial gains and losses are recognised in full in the period in which they occur. They are recognised outside the Income statement and presented in the Statement of comprehensive income (see Note 28).

Past service cost is recognised immediately to the extent that the benefits are already vested, and otherwise is amortised on a straight line basis over the average period until the benefits become vested.

The retirement benefit obligation recognised in the Balance sheet represents the present value of the defined benefit obligation, as adjusted for unrecognised past service cost, and as reduced by the fair value of scheme assets. Any asset resulting from this calculation is limited to past service cost, plus the present value of available refunds and reductions in future contributions to the plan.

2. Significant accounting policies continued

Tax

The tax expense represents the sum of the current tax payable and deferred tax. The Group's current tax liability is calculated using the tax rates that have been enacted or substantively enacted by the Balance sheet date.

Current taxes are based on the taxable results of the Group and calculated in accordance with tax rules in the United Kingdom.

Deferred tax is the tax expected to be payable or recoverable on the temporary differences that arise when tax authorities recognise and measure assets and liabilities with rules that differ from those of the consolidated accounts. Deferred taxes are calculated under the Balance sheet liability method at the rate of tax expected to prevail, subject to the rate being enacted or substantively enacted by that date, when the temporary differences reverse. Deferred tax is not discounted.

Deferred tax liabilities are recognised for all taxable temporary differences. Deferred tax assets are recognised on all deductible temporary differences to the extent that it is probable that there will be taxable profits available against which the temporary timing differences can be utilised.

Deferred tax assets and liabilities are not recognised if the temporary differences arise from the initial recognition of goodwill, non deductible goodwill or from initial recognition (other than a business combination) of other assets and liabilities in a transaction that affects neither the taxable profit or loss nor the accounting profit or loss.

Deferred tax is charged or credited in the income statement except when it relates to items charged or credited directly to equity. In this case the deferred tax is also dealt with in equity.

Property, plant and equipment – the railway network

The Group has one class of property, plant and equipment, being the railway network. This is the integrated network that the Group uses to deliver the operation, maintenance and renewal of Great Britain's national rail infrastructure, and constitutes one class of asset.

The Group has chosen the revaluation model in respect of measuring the value of the railway network. The fair value of the railway network is derived using an income approach. The income approach is based on a discounted future cash flow that assesses the value to the business of the net income stream of the railway network. Revaluations are reflected in equity.

The railway network is depreciated on a straight-line basis over its estimated remaining weighted average useful economic life. The estimated remaining weighted average useful economic life of the network is currently 30 years (2009: 30 years). The remaining weighted average useful economic lives are estimated annually, with external verification of the valuation and asset lives carried out where required.

Investment property

Investment property, which is property held to earn rentals and/or for capital appreciation, is stated at its fair value at the Balance sheet date. Gains and losses from changes in the fair value of investment property are included in the Income statement for the period in which they arise.

Research and development

Research and general development expenditure is charged to the Income statement as incurred. Expenditure on the development of specific projects is recognised only if all of the following conditions are met:

- an asset is created that can be identified
- it is probable that the asset created will generate future economic benefits
- the development cost of the asset can be measured reliably.

Intangible fixed assets

An intangible asset is only recognised if it is probable that future economic benefits will flow to the Group and its costs can be measured reliably. Intangible fixed assets are measured initially at purchase cost and are amortised on a straight-line basis. Licences are amortised over the length of their contractual agreement. Intangible fixed assets are tested for impairment at each Balance sheet date by comparing their carrying value and the expected discounted cash flows expected to arise from them over their contractual agreements. If the carrying value exceeds the discounted cash flows expected to arise from the assets, the carrying value would be impaired accordingly.

Inventories

Inventories are stated at the lower of cost and net realisable value. Cost comprises direct materials, direct labour costs and those overheads that have been incurred in bringing the inventories to their present location and condition. Cost is calculated using the weighted average method.

Financial instruments

Financial assets and financial liabilities are recognised on the Group's Balance sheet when the Group becomes party to the contractual provisions of the instrument.

2. Significant accounting policies continued

Financial assets

Financial assets are recognised and derecognised on a trade date where a purchase or sale of an investment is under contract whose terms require delivery of the investment within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those investments classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified as financial assets 'at fair value through profit or loss' (FVTPL), 'held-to-maturity' investments, 'available-for-sale' financial assets, and 'trade and other receivables'. Trade receivables do not carry any interest and are stated at their nominal value as reduced by appropriate allowances for estimated irrecoverable amounts, recognised in the income statement. The remaining assets are measured at subsequent reporting dates at fair value.

Financial assets at FVTPL

Financial assets are classified as at FVTPL where the asset is either held for trading or it is designated at FVTPL. Gains and losses arising from changes in fair value of these assets are recognised in the Income statement for the period. A financial asset is classified as held for trading if:

- it has been acquired principally for the purpose of selling in the near future; or
- it is part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

Held-to-maturity investments

Investments with fixed or determinable payments and fixed maturity dates and that the Group has the positive intent and ability to hold to maturity are classified as held-to-maturity investments. These investments are recorded at amortised cost less any impairment, with revenue recognised on an effective yield basis.

Available-for-sale financial assets

Gains and losses from changes in fair value of these assets are recognised directly in equity until the security is disposed of or is determined to be impaired. At this point the cumulative gain or loss previously recognised in equity is included in the Income statement for the period.

Impairment of financial assets

Financial assets, other than those at FVTPL, are assessed for indicators of impairment at each Balance sheet date. Financial assets at FVTPL are stated at fair value with any resultant gain or loss recognised in the Income statement. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

The carrying amount of the financial asset is reduced by the impairment loss directly for all financial assets with the exception of trade receivables, which are reduced by appropriate allowances for irrecoverable amounts. With the exception of available for sale investments, if, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the previously recognised impairment loss is reversed through the Income statement. The reversal is only made to the extent that the carrying amount of the investment at the date the impairment is reversed does not exceed what the amortised cost would have been had the impairment not been recognised.

Cash and cash equivalents

Cash and cash equivalents comprise bank balances held by the Group and money market deposit investments all denominated in sterling at varying rates. The carrying amount of these assets approximates their fair value.

Joint ventures

The results and assets and liabilities of joint ventures are incorporated in these financial statements using the equity method of accounting. Investments in joint ventures are carried in the Balance sheet at cost as adjusted by post acquisition changes in the Group's share of net assets of joint ventures, less any impairment in the value of individual investments. Losses of a joint venture in excess of the Group's interest in a joint venture are not recognised.

Financial liabilities and equity instruments

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements entered into. An equity instrument is any contract that evidences a residual interest in the assets of the group after deducting all of its liabilities.

2. Significant accounting policies continued

Financial liabilities at FVTPL

Financial liabilities are classified as at FVTPL where the financial liability is either held for trading or it is designated at FVTPL. A financial liability is classified as held for trading if:

- it has been incurred principally for the purpose of disposal in the near future; or
- it is a part of an identified portfolio of financial instruments that the Group manages together and has a recent actual pattern of short-term profit-taking; or
- it is a derivative that is not designated and effective as a hedging instrument.

A financial liability other than a financial liability held for trading may be designated as at FVTPL upon initial recognition if:

- such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise exist; or
- the financial liability forms a part of a group of financial assets or financial liabilities or both, which is managed and its performance is evaluated on a fair value basis; or
- it forms part of a contract containing one or more embedded derivatives and IAS 39 permits the entire combined contract to be designated as at FVTPL.

The Group derecognises financial liabilities when, and only when, the Group's obligations are discharged, cancelled or they expire.

Debt

Debt instruments not designated at FVTPL are initially measured at fair value, net of discount and direct issue costs. Finance charges, including premiums payable on settlement or redemption and direct issue costs are accounted for on an accrual basis to the Income statement using the effective interest rate method and are added to the carrying value of the debt instrument to the extent that they are not settled in the period in which they arise.

Trade payables

Trade payables are ordinarily not interest bearing and are stated at cost.

Derivative financial instruments and hedge accounting

The Group's activities expose it primarily to the financial risks of changes in interest rates and foreign currency exchange rates. The Group uses interest rate swaps and foreign exchange forward contracts to hedge these exposures. The use of financial derivatives is governed by the Group's policies approved by the Treasury Committee of the Board, which provide written principles on the use of financial derivatives.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each Balance sheet date.

The Group designates certain hedging instruments as either cash flow hedges or fair value hedges. Hedges of interest rate risk on firm commitments are accounted for as cash flow hedges. At the inception of the hedge relationship, the entity documents the relationship between the hedging instrument and the hedged item, along with its risk management objectives and its strategy for undertaking various hedge transactions. Furthermore, at the inception of the hedge and on an ongoing basis, the Group documents whether the hedging instrument that is used in a hedging relationship is highly effective in offsetting changes in fair values or cash flows of the hedged item.

Some derivatives, while complying with the Group's financial risk management policies, do not qualify for hedge accounting and are therefore classified as held for trading. Changes in the fair value of derivative financial instruments that do not qualify for cash flow hedge accounting are recognised in the Income statement as they arise.

Hedge accounting is discontinued when the hedging instrument expires or is sold, terminated, exercised, or no longer qualifies for hedge accounting. At that time, any cumulative gain or loss on the hedging instrument recognised in equity is retained in equity until the forecasted transaction occurs. If a hedged transaction is no longer expected to occur, the net cumulative gain or loss recognised in equity is transferred to the Income statement in the year.

Derivatives embedded in other financial instruments or other host contracts are treated as separate derivatives when their risks and characteristics are not closely related to those of host contracts and the host contracts are not carried at fair value, with gains or losses are reported in the Income statement.

Note 20 sets out details of the fair values of the derivative instruments used for hedging purposes. Movements in the hedging reserve in equity are detailed in the Statement of comprehensive income and in the Statement of changes in equity.

Fair value hedges

Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the Income statement immediately, together with any changes in the fair value of the hedged item that is attributed to the hedged risk. The change in the fair value of the hedging instrument and the change in the hedged item attributable to the hedged risk are recognised within 'Other gains and losses' in the Income statement.

2. Significant accounting policies continued

Cash flow hedges

Changes in the fair value of derivative financial instruments that are designated and effective as hedges of future cash flows are recognised directly in equity and the ineffective portion is recognised immediately within 'Other gains and losses' in the Income statement.

Provisions

Provisions are recognised when the Group has a present obligation as a result of a past event, and it is probable that the Group will be required to settle that obligation. Provisions are measured at the Directors' best estimate of the expenditure required to settle the obligation at the Balance sheet date, and are discounted to present value where the effect is material.

Critical accounting judgements and key sources of uncertainty

(i) Property, plant and equipment – the railway network: the estimate of the fair value of the railway network is based on an income approach using the regulatory asset base, which equates to the discounted future cash flow associated with the network, adjusted for the net present value of any variances from the Office of Rail Regulation's determination included in the Group's business plan. Further details are set out in Note 12.

(ii) Investment property – the investment property portfolio valuation is determined using an external valuation of 12 properties in the portfolio, comprising 10 per cent of the total valuation. King Sturge provide their assessment of yields for each of these properties (Jones Lang LaSalle performed the assessment in the prior year). These are then used to produce income multipliers and applied to the rental streams from each of the individual properties in the portfolio to form an overall valuation.

(iii) Retirement benefit obligations – the Group recognises and discloses its retirement benefit obligation in accordance with the measurement and presentational requirement of IAS 19 'Employee Benefits'. The calculations include a number of judgements and estimations in respect of the expected rate of return on assets, the discount rate, inflation assumptions, the rate of increase in salaries and life expectancy amongst others. Changes in these assumptions can have a significant effect on the value of the retirement benefit obligation. The key assumptions made are set out in Note 28.

(iv) Provisions – provisions are measured at the Directors' best estimate of the expenditure required to settle the obligation at the Balance sheet date, and are discounted to present value where the effect is material.

3. Revenue

	2010 Group £m	2009 Group £m
Franchised track access and grant income	**5,387**	5,799
Freight revenue	**52**	93
Property rental income	**206**	215
Other income	**23**	53
Revenue for the year	**5,668**	6,160
Other operating income (see Note 4)	**250**	232
Investment income (see Note 7)	**19**	112
	5,937	6,504

The net effect of the performance regimes on the results of the Group was net income of £42m (2009: £56m).

4. Net operating costs

	2010 Group £m	2009 Group £m
Employee costs (see Note 6)	**1,746**	1,656
Own costs capitalised	**(680)**	(662)
Other external charges (including infrastructure maintenance costs)	**1,730**	1,701
Other operating income	**(250)**	(231)
Net operating costs before depreciation	**2,546**	2,464
Depreciation and other amounts written off non-current assets	**1,193**	1,198
Capital grants amortised	**(64)**	(58)
Net operating costs	**3,675**	3,604

5. Profit from operations

Profit from operations is stated after charging/(crediting):

	2010 Group £m	2009 Group £m
Research and development costs expensed	**1**	1
Depreciation and other amounts written off property, plant and equipment	**1,193**	1,198
Amortisation of intangible fixed assets	**1**	1
Amortisation of capital grants	**(64)**	(58)
Profit on sale of properties	**(0.31)**	(70)
(Increase)/decrease in the fair value of investment properties	**(62)**	208
Cost of inventories recognised as an expense	**179**	192
Write downs of inventories recognised as an expense	**7**	–
Employee costs (see Note 6)	**1,746**	1,656
Amounts payable to auditors		
Fees payable to the Company's auditors for the audit of the Company's annual accounts	**0.04**	0.04
Fees payable to the Company's auditors for other services to the Group		
– The audit of the Company's subsidiaries pursuant to legislation	**0.35**	0.37
Total audit fees	**0.39**	0.41
Other services pursuant to legislation		
– Regulatory accounts audit and interim review	**0.12**	0.12
– Other	**0.02**	0.02
Total non-audit fees	**0.14**	0.14
Total amounts payable to auditors	**0.53**	0.55

6. Employee costs

The average number of employees (including Executive Directors) was:

	2010 Group Number	2009 Group Number
Management and operation of the railway	**37,153**	36,138

	2010 Group £m	2009 Group £m
Their aggregate remuneration comprised:		
Wages and salaries	**1,504**	1,415
Social security costs	**127**	121
Defined contribution pension costs (see Note 28)	**16**	18
Defined benefit pension costs – current service costs (see Note 28)	**99**	102
	1,746	1,656

7. Investment revenue

	2010 Group £m	2009 Group £m
Interest receivable on investments and deposits	**18**	111
Interest receivable on finance leases	**1**	1
	19	112

Investment revenue earned on financial assets analysed by category of asset, is as follows:

	2010 Group £m	2009 Group £m
Available-for-sale financial assets	**1**	1
Loans and receivables (including cash and bank balances)	**18**	111
	19	112

8. Other gains and losses

	2010 Group £m	2009 Group £m
Gains arising from ineffective portion of cash flow hedges	**9**	21
Losses arising from ineffective portion of cash flow hedges	**(77)**	(109)
Fair value losses on interest rate swaps transferred from equity	**(4)**	(4)
Losses arising from cash flow hedge accounting	**(72)**	(92)
Increase in fair value of fair value hedges	**181**	597
Increase in fair value of fair value hedged debt	**(107)**	(569)
Decrease in fair value of fair value hedged debt	**316**	–
Decrease in fair value of fair value hedges	**(394)**	–
(Losses)/profit arising from fair value hedge accounting	**(4)**	28
Increase in fair value of derivatives not hedge accounted	**30**	169
Increase in fair value of non-hedge accounted debt	**(8)**	(83)
Decrease in fair value of derivatives not hedge accounted	**(231)**	(94)
Realised losses arising from derivatives not hedge accounted	**(192)**	–
Losses arising from non-hedge accounting	**(401)**	(8)
Total other losses	**(477)**	(72)

No other gains and losses have been recognised in respect of loans and receivables or held-to-maturity investments other than those disclosed in Note 8 and impairment losses recognised/reversed in respect of trade receivables (see Notes 4 and 17). No gains or losses have been recognised on financial liabilities measured at amortised cost other than those disclosed in Note 9.

The gain/loss arising on adjustment for the hedged item in a designated fair value hedge accounting relationship, the change in fair value of debt designated as fair value through profit and loss, and the exchange differences on retranslation of foreign currency debt forms part of the net gains/losses on other financial liabilities carried at amortised cost and relates to debt issuances disclosed in Note 19.

The overall size of the debt and derivative movements will be significantly affected by the real interest rate hedging activities with regard to future index-linked debt issuance. This hedge of the real interest rate does not qualify for hedge accounting under IAS 39 and a one per cent move in the real interest rate will cause a change in the valuation of these hedge instruments by approximately £418m.

Debt and derivative revaluations
The Income statement has been presented in a three-column format in order to allow users to appreciate the impact of the revaluation of debt and derivatives on the results for the year. Not all hedging strategies qualify for hedge accounting and the Directors believe that by separating gains and losses arising from applying the valuation requirements of IAS 39, the users of this financial information will better understand the underlying performance of the Group.

Those items that have been identified for disclosure as changes in debt and derivative valuations are explained above.

9. Finance costs

	2010 Group £m	2009 Group £m
Interest on bank loans and overdrafts	**8**	66
Interest on bonds issued under the Debt Issuance Programme	**1,057**	681
Interest on debt issued under Medium Term Note Programme	**–**	180
Interest on obligations under finance leases	**13**	14
Expected return on assets less interest on liabilities in respect of defined benefit pension schemes	**40**	15
Other interest	**174**	102
Total borrowing costs	**1,292**	1,058
Less: amounts included in the cost of qualifying assets	**(95)**	(112)
Total finance costs	**1,197**	946

Borrowing costs are included in the costs of qualifying assets to the extent that the asset is financed by the Group. The average rate used during the year was 5.9 per cent (2009: 5.0 per cent).

10. Tax

	2010 Group £m	2009 Group £m
Current tax:		
UK Corporation tax at 28% (2009: 28%):		
Corporation tax charge	**(1)**	(10)
Less advance corporation tax (ACT) set-off	**–**	9
Corporation tax liability	**(1)**	(1)
Prior year credit	**8**	–
Total current tax	**7**	(1)
Deferred tax:		
Deferred tax at 28% (2009: 28%)		
Current year charge	**(120)**	(418)
Abolition of Industrial Building Allowances	**–**	(524)
Prior year credit	**5**	32
Total deferred tax	**(115)**	(910)
Total tax	**(108)**	(911)

10. Tax continued

The tax charge for the year can be reconciled to the profit per the Income statement as follows:

	2010 Group £m	2009 Group £m
Profit before tax	**400**	1,512
Tax at the UK corporation tax rate of 28% (2009: 28%)	**108**	423
Adjustments in respect of prior years	**(13)**	(32)
Change of corporation tax rate	**–**	–
Abolition of Industrial Building Allowances	**–**	524
Permanent differences	**13**	5
Advance corporation tax previously written off	**–**	(9)
Tax charge for the year	**108**	911

In addition to the amounts charged to the Income statement, deferred tax relating to the revaluation of the railway network amounting to £289m (2009: £31m) has been charged directly to equity. Movements on the hedging reserve amounted to £7m credit (2009: £98m credit). Movements relating to retirement benefit obligations amounted to a £82m credit to equity (2009: £79m credit).

Deferred tax is calculated at a rate of 28 per cent (2009: 28 per cent). 28 per cent (2009: 28 per cent) is also used for the reconciliation above as the tax charge is substantively deferred tax.

UK corporation tax is calculated at 28 per cent (2009: 28 per cent).

The Group has £39m (2009: £34m) of surplus ACT carried forward (including a release in relation to the prior period). No deferred tax asset has been provided in respect of this amount as it is uncertain that it can be utilised against tax liabilities in the foreseeable future.

The legislation introducing the abolition of Industrial Buildings Allowances was enacted in the previous financial year and this liability was fully reflected in that year's accounts, as shown above. The types of asset which qualified as an industrial building were stations, embankments, sea walls, depots and goods yards.

11. Intangible assets

Group	Concessions £m
Cost	
At 1 April 2008	**78**
Fully written down licences de-recognised in the year	–
At 1 April 2009 and 31 March 2010	**78**
Amortisation	
At 1 April 2008	(4)
Charge for the year	(1)
Fully written down licences de-recognised in the year	
At 1 April 2009	**(5)**
Charge for the year	(1)
At 31 March 2010	**(6)**
Carrying amount	**72**
At 31 March 2010	**72**
At 31 March 2009	73

The intangible assets above are held by the Company's wholly owned subsidiary Network Rail (CTRL) Limited.

The concession to run the operations, maintenance and renewal business of the Channel Tunnel Rail Link is being amortised over 84 years, to 2086.

12. Property, plant and equipment – the railway network

	Group £m	Company £m
Valuation		
At 1 April 2008	31,443	–
Additions	4,743	–
Depreciation charge for the year	(1,198)	–
Transfers from investment property	50	–
Revaluation in the year	(113)	–
At 1 April 2009	**34,925**	**–**
Additions	3,920	–
Depreciation charge for the year	(1,193)	–
Transfers from investment property	10	–
Revaluation in the year	(1,033)	–
At 31 March 2010	**36,629**	**–**

In the prior year ended 31 March 2009 Ove Arup and Partners reviewed Network Rail Infrastructure Limited's engineering assessment of the serviceable economic lives of the major asset categories that comprise the railway network and their depreciated replacement cost. They confirmed in writing to the Directors that the basis upon which the assessment had been prepared was reasonable.

Given the interdependency of the assets comprising the railway network, the Group has concluded that the railway network is a single cash-generating unit and that its fair value is the estimated future cash flows that will be generated in perpetuity, discounted at the Group's pre-tax cost of capital, as set by the Office of Rail Regulation (ORR) in its Access Charges Review. The estimate of the fair value is based on the regulatory asset base (RAB) which is based on a discounted future cash flow calculation adjusted for the net present value of any variances from the ORR's determination included in the Group's business plan. This takes into account: the provisional ORR RAB balance; any regulatory out/under-performance derived by comparing future income and expenditure projections, in the Group's Business Plan, against the regulatory settlement; assets funded directly by third party contributions rather than RAB funded; and an adjustment to reflect that a subset of this valuation is disclosed separately as investment properties.

The unimpaired depreciated replacement cost of the network (after excluding the replacement cost of embankments, cuttings and tunnels) is estimated at £75bn (2009: £75bn).

The depreciation charge for any year is calculated using the average carrying value for the year and the estimated weighted average remaining useful economic life of the railway network. The weighted average remaining economic life of the railway network was calculated using the engineering assessment of serviceable economic lives, of the major categories that comprise the railway network. The estimated remaining weighted average useful economic life of the network is currently 30 years (2009: 30 years). The change in asset lives from 25 to 30 years was adopted from 1 October 2008 in the last financial year. This change resulted in a lower depreciation charge, by £126m, for the last six months of the year ended 31 March 2009 than if the lives had remained at 25 years. After taking into account deferred taxation the effect on profit after tax was £91m.

As at 31 March 2010 the comparable valuation of the railway network according to the historic cost convention is £32,157m (2009: £29,273m).

As at 31 March 2010 and 31 March 2009 it is not possible to identify the undepreciated capitalised interest or the undepreciated finance leases, within the net book value of fixed assets. The undepreciated interest capitalised since the date of adoption of the network value as deemed cost on 1 April 2002 was £457m (2009: £376m). No finance leased assets have been acquired since 1 April 2002.

At 31 March 2010, the Group had entered into contractual commitments in respect of capital expenditure amounting to £1,436m (2009: £1,667m).

13. Investment property

	Group £m	Company £m
Fair value		
At 1 April 2008	949	–
Additions	12	–
Transfers to property, plant and equipment	(50)	–
Disposals	(3)	–
Decrease in fair value in the year	(208)	–
At 1 April 2009	**700**	**–**
Additions	13	–
Transfers to property, plant and equipment	(10)	–
Disposals	(1)	–
Increase in fair value in the year	62	–
At 31 March 2010	**764**	**–**

The fair value of the Group's investment properties at 31 March 2010 has been arrived at on the basis of a valuation carried out at that date by King Sturge, external valuers not connected with the Group (in the year ended 31 March 2009, Jones Lang Lasalle were the Group's external valuer), and by a chartered surveyor working for Network Rail.

The valuation, which conforms to International Valuation Standards, was arrived at by, firstly, the external valuation of the 12 largest properties amounting to 10 per cent of the total valuation. Secondly, the balance of the estate, amounting to 6,413 properties, was valued using the Beacon method. The portfolio was analysed into homogenous classes of property and areas. King Sturge independently assessed the appropriate yield to be adopted within each of the portfolio classes and areas in order to enable the directors to estimate market values by applying the adopted yields to the net rental income in accordance with a traditional UK investment property valuation.

The property rental income earned by the Group from its investment property, all of which is leased out under operating leases, amounted to £69m (2009: £75m). Direct operating expenses arising on the investment properties in the year amounted to £3m (2009: £4.2m).

The Group's investment properties are let on a tenant repairing basis. The Group's maintenance obligations are limited to common areas and vacant property units.

14. Investment in subsidiaries: Company

	At cost £m
Investment in subsidiaries at 1 April 2008, 1 April 2009 and 31 March 2010	**–**

The Company's subsidiaries are set out below:

Directly owned	Country of incorporation	Proportion of all classes of issued share capital owned by the Company	Principal activity
Network Rail Holdco Limited	Great Britain	100%	Holding company
Network Rail CP Finance PLC	Great Britain	100%	Dormant
Rail Safety & Standards	Great Britain	Company limited by guarantee	Dormant
Railway Safety	Great Britain	Company limited by guarantee	Dormant
Held through subsidiary			
Network Rail Infrastructure Limited	Great Britain	100%	Management of UK railway infrastructure
Network Rail Insurance Limited	Guernsey	100%	Insurance
Network Rail (CTRL) Limited	Great Britain	100%	Holds St Pancras concession and CTRL Railway Services Agreement
Network Rail Development Limited	Great Britain	100%	Holds 49.95% of the property joint venture Solum Regeneration LP
Solum Regeneration (GP) Limited	Great Britain	50%	Holds 0.1% of the property joint venture Solum Regeneration LP
Network Rail (Spacia) Limited	Great Britain	100%	Dormant
Network Rail (Stations) Limited	Great Britain	100%	Dormant
Network Rail (Projects) Limited	Great Britain	100%	Dormant
Network Rail (Property) Limited	Great Britain	100%	Dormant
Spacia (2002) Limited	Great Britain	100%	Dormant
Network Rail Pension Trustee Limited	Great Britain	Company limited by guarantee	Administration of defined contribution pension scheme
Shares held by a trustee			
Network Rail MTN Finance PLC	Great Britain	Shares held by HSBC Trustee (C.I.) Limited	Dormant
Network Rail Infrastructure Finance PLC	Great Britain	Shares held by HSBC Trustee (C.I.) Limited	Administration of Debt Issuance Programme

The shares in Network Rail MTN Finance PLC and Network Rail Infrastructure Finance PLC are held by HSBC Trustee (C.I.) Limited for charitable purposes. The sole purpose of these companies is to act as special purpose funding vehicles. The companies are treated as subsidiaries for accounting purposes as proceeds from debt issuances are on lent to Network Rail Infrastructure Limited and are used to finance the activities of the Company and to refinance the existing debt of the Group.

Network Rail Infrastructure Finance PLC issues debt under the Debt Issuance Programme. Network Rail MTN Finance PLC is now dormant but formerly issued debt under the Medium Term Note Programme.

The Company's joint venture is set out below:

Joint venture	Country of incorporation	Proportion of all classes of capital owned by the Company	Principal activity
Solum Regeneration LP	Great Britain	50%	Property development

Aggregated amounts relating to joint ventures	**2010 £m**	2009 £m
Current assets	**5**	5

15. Inventories

	2010 Group £m	2009 Group £m
Raw materials and consumables	**132**	88

As at 31 March 2010 a provision of £18m was held in respect of inventories (2009: £13m).

16. Finance lease receivables

	Minimum lease payments		Present value of minimum lease payments	
	2010 Group £m	2009 Group £m	**2010 Group £m**	2009 Group £m
Amounts receivable under finance leases:				
Within one year	**3**	4	**2**	3
In the second to fifth years inclusive	**7**	9	**6**	7
After five years	**2**	3	**2**	2
	12	16	**10**	12
Less: unearned finance income	**(2)**	(3)	**n/a**	n/a
Present value of minimum lease payments receivable	**10**	13	**10**	12
Analysed as:				
Current finance lease receivables (recoverable within one year)	**2**	3	**2**	3
Non-current finance lease receivables (recoverable after one year)	**8**	10	**8**	9
	10	13	**10**	12

The Group has entered into finance lease arrangements with third parties for various types of telecommunications equipment. Leases are due to expire in 2017/18.

The interest rate inherent in the leases is fixed at the contract date for all of the lease term. The average effective interest rate contracted is approximately 8.4 per cent (2009: 8.4 per cent) per annum.

Finance lease receivable balances are secured over the equipment leased. The Group is not permitted to sell or repledge the collateral in the absence of default by the lessee.

The fair value of the Group's finance lease receivables at 31 March 2010 is estimated at £9m (2009: £11m) using a 3.5 per cent (2009: 4.8 per cent) discount rate based on the current average cost of capital.

17. Other financial assets

Trade and other receivables	2010 Group £m	2009 Group £m	2010 Company £m	2009 Company £m
Trade receivables	**313**	373	**–**	–
Capital grants receivable	**94**	110	**–**	–
Other taxation and social security	**27**	–	**–**	–
Other receivables	**85**	59	**–**	–
Prepayments and accrued income	**201**	271	**–**	–
	720	813	**–**	–

Trade receivables include an allowance for estimated irrecoverable amounts from the supply of services of £18m (2009: £14m). This allowance has been made by reference to past default experience. Average debtor days were 58 days (2009: 53 days).

The Directors consider that the carrying value of trade and other receivables approximates their fair value. All balances are non-interest bearing and denominated in sterling. The Group provides fully for receivables overdue by over six months because historical experience is that such receivables are generally not recoverable. All other trade receivables are provided for on the basis of estimated irrecoverable amounts, determined by reference to past default experience.

17. Other financial assets continued

The Group's credit risk is primarily attributable to its trade receivables. Around 95% of the Group's income is received from train operating companies (TOCs) and in the form of revenue grants from Government. Franchises are issued to TOCs by the Department for Transport (DfT) in England and Wales and Transport Scotland in Scotland. The Group believes that amounts receivable from Government and the TOCs represent a high level of credit quality.This is because in the extraordinary circumstance that a TOC was financially distressed and unable to meet its obligations then provisions in the franchise agreements allow the DfT to take over services at any time. Before accepting any other new customer, the Group uses an external credit scoring system to assess the potential customer's credit quality.

Included in the Group's trade receivable balance are debtors with a carrying value of £14m (2009: £22m) which are past due at the reporting date for which the Group has not provided as there has not been a significant change in the credit quality and the amounts are still considered recoverable. The Group does not hold collateral over these balances. The average age of these receivables is 73 days (2009: 57 days).

The following table shows the age of financial assets for the Group which are past due and for which no specific provision has been raised:

	2010 Group £m	2009 Group £m	**2010 Company £m**	2009 Company £m
Past due by 1–28 days	**5**	15	**–**	–
Past due by 29–56 days	**5**	2	**–**	–
Past due by 57–84 days	**3**	1	**–**	–
Past due by 85–180 days	**1**	4	**–**	–
	14	22	**–**	–

18. Trade and other payables

Current liabilities: Trade and other payables	**2010 Group £m**	2009 Group £m	**2010 Company £m**	2009 Company £m
Trade creditors	**637**	738	**–**	–
Collateral held from banking counterparties	**554**	1,062	**–**	–
Payments received on account	**14**	18	**–**	–
Other taxation and social security	**–**	8	**–**	–
Other creditors	**459**	331	**–**	–
Other interest accruals	**311**	302	**–**	–
Other accruals and deferred income	**1,068**	1,199	**–**	–
	3,043	3,658	**–**	–

The average credit period taken for trade purchases is 48 days (2009: 47 days).

In the prior year 'Other taxation and social security' included the Current tax liability of £18m at Group level. In the current year this amount (an asset of £6m) has been presented separately on the face of the Balance sheet.

Before accepting new suppliers, and upon letting significant contracts, the Group evaluates suppliers creditworthiness using external credit scoring systems and other relevant data.

The Directors consider that the carrying value of trade and other payables approximates to their fair value. All balances are ordinarily non-interest bearing and denominated in sterling.

Non-current liabilities: Other payables	**2010 Group £m**	2009 Group £m	**2010 Company £m**	2009 Company £m
Deferred development income	**18**	38	**–**	–
Capital grants deferred income	**1,954**	1,678	**–**	–
Other payables	**122**	125	**–**	–
	2,094	1,841	**–**	–

19. Bank loans and overdrafts

	2010 Group £m	2009 Group £m	2010 Company £m	2009 Company £m
Bank loans and overdrafts	**1,320**	1,323	**–**	–
Bonds issued under the Debt Issuance Programme (less unamortised discount and fees)	**24,292**	21,469	**–**	–
Kreditanstalt für Wiederaufbau working capital facility	**–**	185	**–**	–
	25,612	22,977	**–**	–
The borrowings are repayable as follows:				
On demand or due within one year	**2,227**	1,776	**–**	–
Due within one to two years	**2,363**	4,882	**–**	–
Due within two to five years	**1,990**	1,069	**–**	–
Due in more than five years	**19,032**	15,250	**–**	–
	25,612	22,977	**–**	–
Less: amounts repayable within one year (shown under current liabilities):				
Bank loans and overdrafts	**(106)**	(4)	**–**	–
Bonds issued under the Debt Issuance Programme (less unamortised discount and fees)	**(2,121)**	(1,587)	**–**	–
Debt issued under Medium term Note Programme (less amortised discount and fees)	**–**	–	**–**	–
Kreditanstalt für Wiederaufbau working capital facility	**–**	(185)	**–**	–
Amounts repayable within one year	**(2,227)**	(1,776)	**–**	–
Amounts repayable after more than one year	**23,385**	21,201	**–**	**–**

All borrowings are denominated in or swapped into sterling.

19. Bank loans and overdrafts continued

Bonds issued under the Debt Issuance Programme are analysed as follows*:

	2010 Group £m	2009 Group £m	**2010 Company £m**	2009 Company £m
1.085% sterling index linked bond due 2052	**106**	102	**–**	–
0% sterling index linked bond due 2052	**102**	101	**–**	–
1.003% sterling index linked bond due 2051	**20**	20	**–**	–
0.53% sterling index linked bond due 2051	**102**	100	**–**	–
0.517% sterling index linked bond due 2051	**101**	101	**–**	–
0% sterling index linked bond due 2051	**108**	103	**–**	–
0.678% sterling index linked bond due 2048	**101**	98	**–**	–
1.125% sterling index linked bond due 2047	**3,411**	1,303	**–**	–
0% sterling index linked bond due 2047	**67**	66	**–**	–
1.1335% sterling index linked bond due 2045	**41**	–	**–**	–
1.5646% sterling index linked bond due 2044	**227**	227	**–**	–
1.1565% sterling index linked bond due 2043	**46**	–	**–**	–
1.1795% sterling index linked bond due 2041	**57**	–	**–**	–
1.2219% sterling index linked bond due 2040	**225**	226	**–**	–
1.2025% sterling index linked bond due 2039	**62**	–	**–**	–
4.6535% sterling bond due 2038	**100**	100	**–**	–
1.375% sterling index linked bond due 2037	**3,876**	3,514	**–**	–
7.05% US dollar bond due 2036	**–**	21	**–**	–
6.91% US dollar bond due 2036	**–**	21	**–**	–
4.75% sterling bond due 2035	**1,223**	1,218	**–**	–
1.6492% sterling index linked bond due 2035	**343**	341	**–**	–
4.375% sterling bond due 2030	**869**	869	**–**	–
1.75% sterling index linked bond due 2027	**3,035**	2,010	**–**	–
4.57% Norwegian krone bond due 2026	**16**	16	**–**	–
4.615% Norwegian krone bond due 2026	**58**	58	**–**	–
1.9618% sterling index linked bond due 2025	**288**	288	**–**	–
4.75% sterling bond due 2024	**726**	724	**–**	–
2.28% Japanese yen bond due 2021	**73**	71	**–**	–
2.315% Japanese yen bond due 2021	**74**	71	**–**	–
2.15% Japanese yen bond due 2021	**72**	70	**–**	–
2.76% Swiss franc bond due 2021	**193**	173	**–**	–
4.625% sterling bond due 2020	**996**	994	**–**	–
4.4% Canadian dollar bond due 2016	**333**	291	**–**	–
6% Australian dollar bond due 2016	**294**	248	**–**	–
4.875% sterling bond due 2015	**993**	989	**–**	–
3.5% US dollar bond due 2013	**821**	865	**–**	–
1.75% US dollar bond due 2013	**656**	–	**–**	–
4.875% sterling bond due 2012	**997**	994	**–**	–
2% US dollar bond due 2012	**669**	692	**–**	–
4.375% sterling bond due 2011	**449**	449	**–**	–
5.25% US dollar bond due 2011	**691**	742	**–**	–
3% US dollar bond due 2011	**658**	697	**–**	–
5.5% Australian dollar bond due 2010	**513**	410	**–**	–
5.125% sterling bond due 2010	**500**	499	**–**	–
3.875% US dollar bond due 2009	**–**	698	**–**	–
4.875% US dollar bond due 2009	**–**	889	**–**	–
	24,292	21,469	**–**	–

* Amounts are shown net of unamortised discount and fees.

19. Bank loans and overdrafts continued

Bank loans and overdrafts are analysed as follows:

	2010 Group £m	2009 Group £m	2010 Company £m	2009 Company £m
Index-linked European Investment Bank due 2037	**384**	383	**–**	–
Royal Bank of Scotland (novated from HSBC Bank) due 2019 repayable by instalments	**208**	206	**–**	–
Barclays Bank due 2017 repayable by instalments	**50**	53	**–**	–
Royal Bank of Scotland due 2017 repayable by instalments	**69**	69	**–**	–
5.57% European Investment Bank due 2013	**203**	204	**–**	–
5.77% European Investment Bank due 2012	**305**	306	**–**	–
6.42% European Investment Bank due 2011	**101**	102	**–**	–
	1,320	1,323	**–**	–

The weighted average interest rates on borrowings at 31 March 2010 and 31 March 2009 were as follows:

	2010 Group %	2009 Group %	2010 Company %	2009 Company %
Bank loans and overdrafts	**5.41**	5.04	**–**	–
Debt issued under the Debt Issuance Programme	**4.82**	4.63	**–**	–

At 31 March 2010 and 2009 the Group had the following undrawn committed borrowing facilities.

	2010 Drawn £m	2010 Undrawn £m	2010 Total £m	2009 Drawn £m	2009 Undrawn £m	2009 Total £m
Working capital facility	**–**	**1,000**	**1,000**	–	1,000	1,000
Standby facility A	**–**	**4,000**	**4,000**	–	4,000	4,000
	–	**5,000**	**5,000**	–	5,000	5,000

Undrawn committed facilities expire as follows:

	2010 Group £m	2009 Group £m
Within one year	**1,000**	1,000
Within one to two years	**–**	–
Within two to five years	**4,000**	4,000
	5,000	5,000

In addition the Secretary of State for Transport has provided unlimited financial indemnity in respect of borrowings under the Debt Issuance Programme.

20. Derivative financial instruments

	2010 Group Fair value £m	2010 Group Notional amounts £m
Cash flow hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	**445**	**1,512**
Fair value hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	**437**	**1,786**
Non-hedge accounted derivatives		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	**104**	**198**
Forward starting real interest rate swaps and gilt locks	**12**	**300**
Forward starting cross-currency swaps	**1**	**22**
	999	**3,818**
Included in non-current assets	**702**	**2,924**
Included in current assets	**297**	**894**
Derivative financial instrument assets	**999**	**3,818**
Cash flow hedges		
Interest rate swaps	**(141)**	**1,551**
Forward starting interest rate swaps	**(359)**	**6,690**
Fair value hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	**(7)**	**668**
Non-hedge accounted derivatives		
Forward starting real interest rate swaps and gilt locks	**(210)**	**2,152**
Forward starting cross-currency swaps	**–**	**46**
	(717)	**11,107**
Included in current liabilities	**(210)**	**2,173**
Included in non-current liabilities	**(507)**	**8,934**
Derivative financial instrument liabilities	**(717)**	**11,107**

Bank loans are analysed as follows:

	2010 Group Fair value £m	2010 Group Notional amounts £m	2009 Group Fair value £m	2009 Group Notional amounts £m
Cash flow hedges				
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	**445**	**1,512**	586	2,044
Forward starting interest rate swaps	**(359)**	**6,690**	(282)	7,000
Interest rate swaps	**(141)**	**1,551**	(103)	2,966
Fair value hedges				
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	**430**	**2,454**	569	2,444
Forward starting cross-currency swaps	**–**	**–**	47	547
Non-hedge accounted derivatives				
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	**104**	**198**	89	228
Forward starting cross-currency swaps	**1**	**68**	10	66
Forward starting real interest rate swaps and gilt locks	**(198)**	**2,452**	3	4,735
	282	**14,925**	919	20,030

21. Provisions: Group

	£m
At 1 April 2008	12
Additional provision in the year	2
Utilisation of provision	5
At 1 April 2009	9
Reclassification in the year	40
Additional provision in the year	10
Utilisation of provision	(2)
At 31 March 2010	57
Included in current liabilities	57
Included in non-current liabilities	–
	57

The Group has provided against a number of commercial claims from third parties arising from interpretations of legal contracts or past events for which settlement is expected to be achieved in the next year, but could be deferred to future years depending on the legal interpretation of rights and responsibilities under the contracts as well as commercial negotiation. The provisions that have been recorded represent the Director's best estimate of the expenditure required to settle the obligation, often with the benefit of legal advice.

Contingent liability

Provisions are measured at the Directors' best estimate of the expenditure required to settle the obligation at the balance sheet date. The nature of these claims means that there is some uncertainty with regard to the value that they will be settled at. If the outcomes of the claims are different to the assumptions underpinning the Directors' best estimates then a further liability may arise.

The Group's lawyers have advised that the provisions for the claims are realistic and no further provision is made for contingent liabilities as the directors do not consider there is any probable loss and, in accordance with paragraph 92 of IAS 37, the Directors consider that further disclosure regarding the nature and amount of the disputes beyond that disclosed here could be expected to prejudice seriously the position of the Group.

22. Deferred tax

The following are the major deferred tax liabilities and assets recognised by the Group and movement thereon during the current and prior years.

Group	Accelerated tax depreciation £m	Revaluation of railway network £m	Short-term timing differences including retirement benefit obligations £m	Derivatives £m	Tax losses £m	Total £m
At 1 April 2008	2,692	1,754	(109)	(25)	(1,547)	2,765
Charge to income	623	–	(0)	3	284	910
(Credit) to equity	–	(31)	(79)	(98)	–	(208)
At 1 April 2009	**3,315**	**1,723**	**(188)**	**(120)**	**(1,263)**	**3,467**
Charge/(credit) to income	91	–	(10)	24	10	115
(Credit) to equity	–	(289)	(82)	(7)	–	(378)
At 31 March 2010	**3,406**	**1,434**	**(280)**	**(103)**	**(1,253)**	**3,204**

Certain deferred tax assets and liabilities have been offset. The following is the analysis of the gross deferred tax balances:

	2010 £m	2009 £m
Deferred tax liabilities	**4,840**	5,038
Deferred tax assets	**(1,638)**	(1,571)
	3,202	3,467

Network Rail Infrastructure Limited has a potential deferred tax asset relating to the disposal of the track bed which is carried at zero in the accounts. It is not possible to determine reliably the tax base of the asset which would be determined by negotiation with HM Revenue & Customs and therefore it has not been possible to reliably quantify the potential deferred tax asset.

23. Obligations under finance leases

	Minimum lease payments 2010 Group £m	2009 Group £m	Present value of minimum lease payments 2010 Group £m	2009 Group £m
Amounts payable under finance leases:				
In the second to fifth years inclusive	**1**	2	**1**	2
After five years	**1**	2	**1**	1
	2	4	**–**	3
Less: future finance charges	**–**	(1)	**n/a**	n/a
Present value of lease obligations	**2**	3	**2**	3
Less: amounts repayable within one year (shown under current liabilities)	**–**	–	**–**	–
Amounts repayable after more than one year	**2**	3	**2**	3

The Group leases certain fixtures and fittings under finance leases from third parties. All lease obligations are denominated in sterling. The fair value of the Group's lease obligations approximates their carrying amount. The Group's obligations under finance leases are secured by the lessors' charges over the leased assets. For the year ended 31 March 2010, the effective borrowing rate was 7.4 per cent (2009: 7.4 per cent). Interest rates are fixed at contract date. All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rent payments.

24. Notes to the statements of cash flows

	2010 Group £m	2009 Group £m	2010 Company £m	2009 Company £m
Operating profit	**1,993**	2,556	**–**	–
Adjustments for:				
Depreciation of the railway network	**1,193**	1,198	**–**	–
Amortisation of capital grants	**(64)**	(58)	**–**	–
Amortisation of intangible assets	**1**	1	**–**	–
Increase/(decrease) in provisions	**48**	(3)	**–**	–
Operating cash flows before movements in working capital	**3,171**	3,694	**–**	–
Increase in inventories	**(44)**	(24)	**–**	–
Decrease/(increase) in receivables	**67**	(85)	**–**	–
(Decrease)/increase in payables	**(29)**	139	**–**	–
Cash generated from operations	**3,165**	3,724	**–**	–
Income taxes paid	**(20)**	(9)	**–**	–
Interest paid	**(911)**	(904)	**–**	–
Net cash generated from operating activities	**2,234**	2,811	**–**	–

Cash and cash equivalents

Cash and cash equivalents (which are represented as a single class of assets on the face of the Balance sheet) comprise cash at bank, collateral and money market deposit investments, all of which are on call with the exception of £6m of short term deposits with an average term of one day (2009: six) from the Balance sheet date. In 2009/10 cash and money market deposits had an average maturity of six days (2009: 29) from the Balance sheet date.

25. Analysis of changes in net debt

	At 1 April 2009 £m	Cash flows £m	Non cash movements £m	Capital accretion £m	Amortisation of discount £m	Fair value remeasurements £m	Foreign exchange movements £m	**At 31 March 2010 £m**
Cash and cash equivalents*	661	1,106	–	–	–	–	–	**1,767**
Borrowings due within one year	(1,776)	1,189	(1,971)	(2)	(2)	231	104	**(2,227)**
Borrowings due after one year	(21,201)	(3,826)	1,974	(345)	(7)	(30)	50	**(23,385)**
Obligations under finance leases	(3)	1	–	–	–	–	–	**(2)**
	(22,319)	**(1,530)**	**3**	**(347)**	**(9)**	**201**	**154**	**(23,847)**

	At 1 April 2008 £m	Cash flows £m	Non cash movements £m	Capital accretion £m	Amortisation of discount £m	Fair value remeasurements £m	Foreign exchange movements £m	At 31 March 2009 £m
Cash and cash equivalents*	543	118	–	–	–	–	–	661
Borrowings due within one year	(5,082)	4,853	(1,059)	–	(5)	(235)	(248)	(1,776)
Borrowings due after one year	(15,267)	(6,373)	1,063	(54)	(10)	(417)	(143)	(21,201)
Obligations under finance leases	(9)	6	–	–	–	–	–	(3)
Financial investments	55	(55)	–	–	–	–	–	–
	(19,760)	(1,451)	4	(54)	(15)	(652)	(391)	(22,319)

* Excludes collateral held of £554m (2009: £1,062m).

26. Operating lease arrangements

The Group as lessee	**2010 Group £m**	2009 Group £m	**2010 Company £m**	2009 Company £m
Minimum lease payments under operating leases recognised in Income statement in the year	**66**	62	**–**	–

At the Balance sheet date, the Group had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2010 Group £m	2009 Group £m	**2010 Company £m**	2009 Company £m
Within one year	**38**	33	**–**	–
In the second to fifth years inclusive	**77**	62	**–**	–
After five years	**70**	62	**–**	–
	185	157	**–**	–

Operating lease payments largely represent rentals payable by the Group for certain of its office properties. Leases are negotiated for an average term of seven years and rentals fixed for an average of three years. In addition rentals are paid for land adjacent to the railway as required for maintenance and renewal activities.

The Group as lessor

Operating lease rentals earned in the year by the Group was £466m (2009: £551m). This amount includes property rental income of of £206m (2009: £215m), as disclosed in Note 3, and a portion of track access income (being income earned from station and depot leases to train operating companies).

At the Balance sheet date, the Group had contracted with customers for the following future minimum lease payments:

	2010 Group £m	2009 Group £m	**2010 Company £m**	2009 Company £m
Within one year	**315**	442	**–**	–
In the second to fifth years inclusive	**739**	1,148	**–**	–
After five years	**1,022**	1,365	**–**	–
	2,076	2,955	**–**	–

27. Funding and financial risk management

Introduction

Network Rail Limited is a company limited by guarantee without shareholders. The Group is almost entirely debt funded. Debt is issued through a special purpose financing company (Network Rail Infrastructure Finance PLC) which is not a member of the Network Rail Limited Group but is treated as a subsidiary for accounting purposes. The majority of the Group's debt is issued by Network Rail Infrastructure Finance PLC under the Debt Issuance Programme (DIP) which has been highly rated (AAA by Standard & Poor's, Aaa by Moody's and AAA by Fitch). The DIP is supported by a financial indemnity from the Secretary of State for Transport which expires in 2052.

The DIP allows access, through a single platform, to the widest possible sources of funding, at the lowest possible cost, including the long term capital markets. This gives Network Rail a stable base for funding a continuing programme of long-term investments in the national rail network. Debt is issued in a number of currencies and a range of maturities which gives rise to interest rate, foreign currency and inflation risk. Financial risk management aims to mitigate these risks (see below).

Externally imposed capital requirements

The Regulatory Asset Base (RAB) is the Regulator's valuation of Network Rail's assets. This is an important business ratio because the value of the RAB and the amount of debt that the business can sustain are, generally speaking, closely related. Network Rail's debts cannot exceed the value of the RAB; a debt to RAB ratio of significantly less than 100 per cent indicates that the business is more robust to future cost shocks (because it is more likely to be able to sustain the additional debt that would arise from any losses incurred).

The Group owns and operates Britain's rail network under licence from the Office of Rail Regulation (ORR). The licence imposes conditions on the Group with regard to its net debt. Should the value of the Group's qualifying net debt exceed 85 per cent of the ORR's RAB then the ORR will be formally notified.

The Group's debt to RAB ratios at 31 March 2010 and 2009 were as follows:

	2010	2009
Debt: RAB ratio	63.9 %	70.0 %

Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised in respect of each class of financial asset, financial liability and equity instrument are disclosed in Note 2 to the financial statements.

Summary table of financial assets and liabilities

The following table presents the carrying amounts and the fair values of the Group's financial assets and liabilities at 31 March 2010 and 31 March 2009.

The fair values of the financial assets and liabilities are included at the amount at which the instrument could be exchanged for in a current transaction between willing parties, other than in a forced or liquidation sale. The following methods and assumptions were used to estimate the fair values:

- cash and cash equivalents – approximates to the carrying value
- working capital facility – approximates to the carrying value because of the short maturity of these instruments
- bank loans and overdraft – based on market data at the Balance sheet date and the net present value of discounted cash flows
- bonds issued under the Debt Issuance Programme – based on market data at the Balance sheet date. Where market data is not available valuations have been obtained from dealing banks
- loans and receivables and payables – approximates to the carrying value
- lease receivables/obligations – approximates to the carrying value
- derivatives – based on market data at the Balance sheet date.

27. Funding and financial risk management continued

Group	2010 Carrying value £m	2010 Fair value £m	2009 Carrying value £m	2009 Fair value £m
Financial assets				
Cash and cash equivalents	**2,321**	**2,321**	1,723	1,723
Other non-derivative financial assets				
Finance lease receivables	**10**	**10**	13	13
Trade and other receivables	**493**	**493**	542	542
Derivatives				
Derivatives designated as cash flow hedging instruments	**445**	**445**	596	596
Derivatives designated as fair value hedging instruments	**437**	**437**	616	616
Other derivatives	**117**	**117**	186	186
Total derivatives	**999**	**999**	1,398	1,398
Total financial assets	**3,823**	**3,823**	3,676	3,676
Financial Liabilities				
Financial liabilities held at amortised cost				
Obligations under finance leases	**(2)**	**(2)**	(3)	(3)
Working capital facility	**–**	**–**	(185)	(185)
Bank loans and overdrafts	**(1,319)**	**(1,382)**	(1,323)	(1,425)
Bonds issued under the Debt Issuance Programme*	**(21,163)**	**(22,873)**	(18,107)	(18,693)
Financial liabilities designated as fair value through profit and loss				
Bonds issued under the Debt Issuance Programme*	**(3,129)**	**(3,129)**	(3,362)	(3,362)
Total borrowing	**(25,613)**	**(27,386)**	(22,980)	(23,668)
Trade and other payables	**(3,165)**	**(3,165)**	(3,801)	(3,801)
Derivatives				
Derivatives designated as cash flow hedging instruments	**(500)**	**(500)**	(395)	(395)
Derivatives designated as fair value hedging instruments	**(7)**	**(7)**	–	–
Other derivatives	**(210)**	**(210)**	(84)	(84)
Total derivatives	**(717)**	**(717)**	(479)	(479)
Total financial liabilities	**(29,495)**	**(31,268)**	(27,260)	(27,948)

* Amounts are shown net of unamortised discount and fees.

Derivatives

The Group (including the special purpose financing vehicle, Network Rail Infrastructure Finance PLC) uses derivative financial instruments to reduce exposure to foreign exchange risk and interest rate movements. The Group does not use derivative financial instruments for speculative purposes. Certain derivatives are designated as hedges, and those derivatives that are not hedge accounted are fair valued immediately through the Income statement. The Group has a comprehensive risk management process.

The Board of Network Rail Limited through a treasury sub-committee (the Treasury Committee) have approved and monitor the risk management processes, including documented treasury policies, counterparty limits, controlling and reporting structures.

The use of derivative instruments can give rise to credit and market risk. Market risk is the possibility that future changes in foreign exchange rates and interest rates may make a derivative more or less valuable. Since the Group uses derivatives for risk management, market risk relating to derivative instruments will principally be offset by changes in the valuation of the underlying assets, liabilities or transactions being hedged.

Credit risk

The credit risk for all classes of derivative financial instruments and other funds is limited because counterparties are banks with high credit ratings assigned by international credit-rating agencies. The Treasury Committee authorises the policy for setting counterparty limits based on credit ratings. The Group spreads its exposure over a number of counterparties, and has strict policies on how much exposure can be assigned to each counterparty. The concentration and amount of the Group's investments varies depending on the level of surplus liquidity the Group chooses to hold at any point in time. However, because of the strict criteria governing counterparty suitability the risk is mitigated. The Treasury Committee also authorises the investment and borrowing instruments that can be used.

27. Funding and financial risk management continued

For debt designated as fair value through profit and loss there has been no change as a result of credit risk changes. The losses in the Income statement arising from the re-measurement of FVTPL debt items of £8m (2009: £83m) are all attributable to changes in market risk.

The credit risk with regard to all classes of derivative financial instruments is limited because Network Rail has arrangements in place which limit each bank to a threshold (based on credit ratings), which if breached requires the bank to post collateral in cash or eligible securities. The thresholds were reviewed by the Treasury Committee in the year and the members of the banking group are required to post collateral on positive mark to market swaps above their threshold. At 31 March 2010 the fair value of collateral held was £554m (2009: £1,062m). The Group is the beneficial owner of this collateral. The Group is free to invest or otherwise utilise the collateral at its discretion, subject to acting within the authority sanctioned by the treasury committee.

Receivables consist of a small number of counterparties. The Group does not have any significant credit risk exposure to any single counterparty and has considered the creditworthiness of debtors. For futher detail on the creditworthiness of customers and suppliers, see Notes 17 (Trade and other receivables) and 18 (Trade and other payables).

Foreign exchange risk

Network Rail is exposed to currency risks from its investing, financing and operating activities. Foreign exchange risk for all currencies is managed by the use of forward exchange contracts and currency swaps to limit the effects of movements in exchange rates on foreign currency denominated liabilities.

It is estimated that a general increase of ten percentage points in the value of any currency against sterling would have no material effect on the Group's profit before tax or equity due to all currency positions being 100 per cent hedged.

Interest rate risk

The Group is exposed to changes in interest rates as funds are borrowed at both fixed and floating interest rates. The hedging strategy approved by the Treasury Committee defines the appropriate mix between fixed and floating borrowings. Cross-currency and interest rate swap contracts are used to manage the fixed/floating ratio.

Debt with a carrying value of £23,968m (2009: £22,311m) is arranged at or swapped into fixed interest rates and exposes the Group to fair value interest rate risk. Other borrowings were arranged at floating rates, thus exposing the Group to cash flow interest rate risk.

The maturity of interest rate swaps is shown in the derivative maturity table on page 112.

The Group has notional values of £6,690m (2009: £7bn) of forward stating interest rate swaps which hedge Control Period 4. The average rate on these swaps is 5.05 per cent (2009: 5.03 per cent). The Group also has notional values of £325m (2009: £325m) of real rate swaps with an average real rate of –0.28 per cent (2009: –0.28 per cent) and notional values of £2,127m (2009: 4,410m) of gilt locks with an average real rate of 1.35 per cent (2009: 1.10 per cent).

The sensitivity analysis below has been determined based on the exposure to interest rates for both derivative and non-derivative instruments at the Balance sheet date. A one per cent increase or decrease represents management's assessment of the reasonably possible changes in average interest rates.

Sensitivity analysis

If average interest rates had been one per cent higher and all other variables were held constant, the Group's profit before tax for the year ended 31 March 2010 would remain the same (2009: increase of £10m) comprised of increased finance costs on the Group's debt of £9m (2009: £6m) and increased interest reveivable on the Group's cash balances of £9m (2009: £16m).

If average interest rates had been one per cent higher and all other variables were held constant, the Group's profit before tax for the year ended 31 March 2010 would remain the same (2009: decrease by £6m).

The Group's sensitivity to interest rates has decreased during the period as the majority of new long-term debt raised in the year were issued at fixed or inflation-linked interest rates and control period hedges have been used to fix debt which was floating at the prior year's balance sheet date. In addition average cash balances and short term investments have reduced.

Inflation rate risk

The Group has certain debt issuances which are index-linked and so are exposed to movements in inflation rates. The Group does not enter into any derivative arrangements to hedge its exposure to inflation in relation to its index-linked debt, but rather to mitigate the effects of inflation on the Group's retail price index-linked revenue streams.

The sensitivity analysis below has been determined based on the exposure to inflation rates for both derivative and non-derivative instruments at the Balance sheet date. A one per cent increase or decrease represents management's assessment of the reasonably possible changes in inflation rates.

27. Funding and financial risk management continued

Sensitivity analysis

If the Retail Price Index (RPI) had been one per cent higher and all other variables were held constant, the Group's finance costs for the year ended 31 March 2010 would increase by £120m (2009: £69m) and other than a corresponding movement in the profit and loss reserve there would be no impact upon equity.

If RPI had been one per cent higher and all other variables were held constant, the Group's finance costs for the year ended 31 March 2010 would increase by £120m (2009: £69m) and other than a corresponding movement in the profit and loss reserve there would be no impact upon equity.

The Group's sensitivity to inflation rates has increased during the period due to further issuances of index-linked debt instruments.

The Group believes that the above analysis is unrepresentative of the risks inherent in issuing index-linked debt. Franchised track access and grant income constitute £5,387m (2009: £5,799m) of revenue which is far in excess of an index-linked interest expense of £150m (2009: £64m). Currently, these sources of income are contractually index-linked and whilst there is no absolute contractual guarantee for future regulatory control periods that this will continue the Group is highly confident that this will remain to be the case. Therefore, the natural hedge that exists between finance costs and revenue mitigates the risk of RPI movements.

Liquidity risk management

The ultimate responsibility for liquidity risk management rests with the Board of Directors. The policy manual ratified by the Treasury Committee includes an appropriate liquidity risk management framework covering the Group's short, medium and long-term funding and liquidity management requirements. Treasury is subject to regular internal audits. Treasury provides sufficient liquidity to meet the Group's needs, while reducing financial risks and prudently maximising interest receivable and credit risk on surplus cash.

The Group manages liquidity risk by maintaining sufficient facilities to cover at lease one year's working capital requirement by continuously monitoring forecast and actual cash flows and matching maturity profiles of financial assets and liabilities. Included in Note 19 is a description of additional undrawn facilities that the Group has at its disposal to further reduce liquidity risk.

The following table details the Group's remaining contractual maturity for its financial liabilities. The table has been drawn up on the undiscounted cash flows of financial liabilities based on the earliest date on which the Group can be required to pay and, therefore, differs from both the carrying value and the fair value. The table includes both interest and principal cash flows.

Group	Within 1 year £m	1-2 years £m	2-5 years £m	5+ years £m	**Total £m**
31 March 2010					
Sterling denominated DIP bonds	**1,277**	**1,282**	**699**	**7,591**	**10,849**
Sterling denominated index-linked bonds	**169**	**175**	**574**	**35,056**	**35,974**
Effect of interest rate swaps on sterling denominated bonds	**(209)**	**–**	**1**	**19**	**(189)**
	(40)	**175**	**575**	**35,075**	**35,785**
Foreign currency denominated bonds	**1,341**	**1,521**	**1,688**	**1,185**	**5,735**
Effect of foreign currency swaps on foreign currency denominated bonds	**(366)**	**(830)**	**(209)**	**(314)**	**(1,719)**
Effect of interest rate swaps on foreign currency denominated bonds	**44**	**12**	**37**	**76**	**169**
	1,019	**703**	**1,516**	**947**	**4,185**
Bank loans and overdrafts	**155**	**49**	**596**	**1,763**	**2,563**
Effect of interest rate swaps on bank loans and overdrafts	**9**	**3**	**6**	**–**	**18**
	164	**52**	**602**	**1,763**	**2,581**
Working capital facility	**–**	**–**	**–**	**–**	**–**
Finance lease liabilities	**–**	**–**	**1**	**1**	**2**
Trade and other payables	**2,732**	**122**	**–**	**–**	**2,904**
	5,152	**2,334**	**3,393**	**45,377**	**56,306**
Effect of discount/financing costs/derivatives	**(193)**	**151**	**(1,402)**	**(26,344)**	**(27,788)**
	4,959	**2,485**	**1,991**	**19,033**	**28,518**

27. Funding and financial risk management continued

Group	Within 1 year £m	1-2 years £m	2-5 years £m	5+ years £m	**Total £m**
31 March 2009					
Sterling denominated DIP bonds	327	1,277	1,748	7,824	11,176
Sterling denominated index-linked bonds	124	127	404	22,773	23,428
Effect of interest rate swaps on sterling denominated bonds	7	–	–	20	27
	131	127	404	22,793	23,455
Foreign currency denominated bonds	1,808	1,261	2,601	1,359	7,029
Effect of foreign currency swaps on foreign currency denominated bonds	(399)	(783)	(458)	(437)	(2,077)
	1,409	478	2,143	922	4,952
Bank loans and overdrafts	54	155	623	1,436	2,268
Effect of interest rate swaps on bank loans and overdrafts	1	–	–	–	1
	55	155	623	1,436	2,269
Working capital facility	189	–	–	–	189
Finance lease liabilities	–	–	1	2	3
Trade and other payables	3,374	125	–	–	3,499
	5,485	2,162	4,919	32,977	45,543
Effect of discount/financing costs/derivatives	269	2,846	(3,849)	(17,725)	(18,459)
	5,754	5,008	1,070	15,252	27,084

Cash flow hedges

The following table shows the contractual maturities of payments under cash flow hedges for the Group:

Cash flow hedging reserve	**2010 Group £m**	**2010 Company £m**	2009 Group £m	2009 Company £m
Less than one year	**(287)**	**–**	73	–
One to two years	**–**	**–**	(204)	–
Two to five years	**101**	**–**	(197)	–
More than five years	**71**	**–**	280	–
	(115)	**–**	(48)	–

Borrowings

Details of the Group's undrawn committed facilities and types of debt instrument used can be found in Note 19.

Hedge ineffectiveness

At 31 March 2010 the Group has recognised £68m (2009: £88m) of ineffectiveness arising from the Groups' cash flow hedges in the Income statement.

27. Funding and financial risk management continued

Derivative maturity

The interest rate and foreign exchange derivatives have the following maturities:

Group	2010 Group Fair value £m	2010 Group Notional amounts £m	2009 Group Fair value £m	2009 Group Notional amounts £m
Interest rate derivatives				
Less than one year	**464**	**1,487**	12	6,135
One to five years	**149**	**1,966**	(48)	658
More than five years	**366**	**779**	(345)	7,908
	979	**4,232**	(381)	14,701
Foreign exchange derivatives				
Less than one year	**(209)**	**2,127**	547	1,802
One to five years	**(377)**	**7,633**	494	2,718
More than five years	**(111)**	**933**	260	809
	(697)	**10,693**	1,301	5,329

Forward Foreign Exchange Contracts

Oustanding contracts on 31 March 2010

	Average exchange rate	Foreign currency £m	Notional value £m	Fair value £m
Buy Sterling	**1**	**16**	**16**	**–**
Sell Sterling	**1**	**52**	**52**	**1**

	Average exchange rate	Local currency m	Notional value £m	Fair value £m
Buy Euros	**1.15**	**26**	**23**	**1**
Buy Swiss francs	**1.61**	**46**	**29**	**–**
Sell Euros	**1.13**	**2**	**1**	**–**
Sell Swiss francs	**1.60**	**23**	**14**	**–**
Forward foreign exchange asset				**1**

All outstanding forward foreign exchange contracts on 31 March 2010 settle within one year.

Oustanding contracts on 31 March 2009

	Average exchange rate	Foreign currency £m	Notional value £m	Fair value £m
Buy Sterling				
Less than 12 months	1	1	1	0
Sell Sterling				
Less than 12 months	1	62	62	9
1 to 2 years	1	6	6	1

	Average exchange rate	Local currency m	Notional value £m	Fair value £m
Buy Euros				
Less than 12 months	1.26	57	45	7
1 to 2 years	1.31	7	5	1
Buy Swiss francs				
Less than 12 months	1.84	30	17	2
1 to 2 years	1.95	2	1	0
Sell Euros				
Less than 12 months	1.25	1	1	0
Forward foreign exchange asset				**10**

27. Funding and financial risk management continued

Fair value measurements recognised in the statement of financial position

The following table provides an analysis of financial instruments that are measured subsequent to initial recognition at fair value, grouped into Levels 1 to 3 based on the degree to which the fair value is observable:

- Level 1 fair value measurements are those derived from quoted prices (unadjusted) in active markets for identical assets or liabilities
- Level 2 fair value measurements are those derived from inputs other than quoted prices (included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices or indirectly (i.e. derived from prices); and
- Level 3 fair value measurements are those derived from valuation techniques that include inputs for the asset or liability that are not based on observable market data (unobservable inputs).

	2010			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets at FVTPL				
Derivative financial assets	–	999	–	999
	–	999	–	999
Financial Liabilities at FVTP				
Derivative financial liabilities	–	(717)	–	(717)
Financial liabilities designated at FVTPL	(3,129)	–	–	(3,129)
	(3,129)	(717)		(3,846)
Total	(3,129)	282	–	(2,847)

There were no transfers between Level 1 and 2 during the year.

28. Retirement benefit scheme

Defined contribution schemes

With effect from 1 April 2004 Network Rail introduced a defined contribution pension scheme, the Network Rail Defined Contribution Pension Scheme (NRDCPS). This scheme is offered to all new employees of Network Rail, except those who have the legal right to join the Railway Pension Scheme (RPS). Any employee who wishes to transfer from the Network Rail Section to the NRDCPS is entitled to do so.

At 31 March 2010, the NRDCPS had 9,904 members (2009: 10,418) and the average employer contribution rate in the year was 5.2 per cent (2009: 5.9 per cent).

Defined benefit schemes

The principal pension scheme in which the Group participates is the Railway Pension Scheme (RPS), which was established by statutory instrument, commenced on 1 October 1994 and is a funded defined benefit arrangement. The assets and liabilities under the predecessor scheme, the British Rail Pension Scheme (BRPS), were transferred to the RPS on that date. The RPS is an industry-wide scheme for all eligible employees within the railway industry. There are different sections within it for different employers. The assets and liabilities of each section are identified separately from those of the other sections. The Group has its own section, the Network Rail Shared Cost Section (the Network Rail Section). This scheme, the assets of which are held separately from the Group, is contributory and provides pensions related to pay at retirement.

The assets transferred to the RPS from the BRPS on 1 October 1994 were apportioned amongst the various sections of the RPS in accordance with the methods and assumptions specified in The Railways Pensions (Transfer and Miscellaneous Provisions) Order 1994 (the 'Transfer Order') which effected the transfer. The amount credited to the Network Rail Section included a share of the surplus at that time.

Since 1 April 2004, new members can only join the Network Rail Section of the RPS after completing five years' service. Benefits for existing members and employees joining up to and including 31 March 2004 were not affected by the revised eligibility rules of the Network Rail Section. In addition to closing the scheme to new entrants the Group announced its decision to cap its contribution to British Railways Additional Superannuation Scheme (BRASS) matching at current levels for existing employees and to dispense with matching for new employees. The Group will continue to match regular contributions but will not increase them in cash terms in the future.

On 1 November 2008 Network Rail launched a third pension scheme – the Career Average Revalued Earnings (CARE) Scheme, which is available to all employees. The CARE scheme will run alongside the existing RPS and NRDC schemes.

Qualified actuaries Towers Watson have valued the schemes on an IAS 19 basis at 31 March 2010 and 31 March 2009.

The total contribution rate payable under the RPS and the CARE scheme is normally split in the proportion 60:40 between the Group and the members. The Group reflects its share of the contribution in the financial statements.

The Group and members pay contributions of 17 per cent (2009: 17 per cent) and 11.4 per cent (2009: 11.4 per cent) of section pay respectively as at 31 March 2010 to RPS. The equivalent rates for the CARE scheme are 10.8 per cent and 7.2 per cent.

28. Retirement benefit scheme continued

If a surplus or deficit arises, the provisions in the rules mean that the Group and members benefit from or pay for this respectively in the proportion 60:40.

	2010 %	2009 %
Key assumptions used:		
Discount rate	**5.55**	6.70
Expected return on equity assets	**7.70**	8.10
Expected return on bond assets	**4.50**	3.40
Expected return on property assets	**6.10**	5.80
Expected rate of price inflation	**3.65**	3.20
Future earnings increases*	**4.65**	4.70
Future pension increases	**3.65**	3.20

* Inclusive of a promotional salary scale of 0.5 per cent per annum.

	2010		2009	
	Males	**Females**	Males	Females
Average life expectancy for mortality tables used to determine defined benefit obligations:				
– Member aged 65 now (pension under £8,500 pa or pensionable pay under £30,000 pa)	**19.8**	**21.7**	19.8	21.7
– Member aged 65 now (others)	**21.5**	**22.7**	21.5	22.7
– Member aged 65 in 20 years' time (pension under £8,500 pa or pensionable pay under £30,000 pa)	**22.2**	**23.2**	22.2	23.2
– Member aged 65 in 20 years' time (others)	**23.7**	**24.2**	23.7	24.2

Amounts recognised in income in respect of the Group's pension arrangements are as follows:

	2010 £m	2009 £m
Current service cost – defined contribution	**16**	18
Current service cost – defined benefit	**99**	102
Interest cost	**139**	153
Expected return on scheme assets	**(99)**	(138)
	155	135

The current service cost has been included in employee costs, the expected return on scheme assets less interest on liabilities has been included in finance costs.

Amounts recognised in the Statement of comprehensive income in respect of the Group's pension arrangement are as follows:

	2010 £m	2009 £m
Loss/(gain) on defined benefit obligation	**688**	(350)
(Gain)/loss on scheme assets	**(396)**	631
Total loss recognised in the Statement of comprehensive income	**292**	281

The cumulative amount of actuarial losses recognised in other comprehensive income was £738m (2009: £446m).

The amount included in the Balance sheet arising from the Group's obligations in respect of its defined benefit schemes is as follows:

	2010 £m	2009 £m
The defined benefit obligation is made up as follows:		
Active members	**(3,314)**	(2,242)
Deferred pensioner members	**(360)**	(242)
Retired members	**(1,128)**	(833)
Present value of defined benefit obligation	**(4,802)**	(3,317)
Fair value of scheme assets	**3,160**	2,211
Deficit in the scheme	**(1,642)**	(1,106)
Group's share (60%) of the scheme deficit recognised in the Balance sheet	**(985)**	(664)

28. Retirement benefit scheme continued

This amount is presented in the Balance sheet as follows:

Included in non-current liabilities	**(985)**	(664)
	(985)	(664)

Cumulative gains or losses are recognised in equity.

Movements in the present value of retirement benefit obligations (including members' share) in the current year were as follows:

	2010 £m	2009 £m
At 1 April	**(3,317)**	(3,572)
Current service cost including members' share	**(175)**	(183)
Interest cost	**(231)**	(254)
Actual benefit payments	**68**	104
Actuarial gains and losses	**(1,147)**	588
Past service cost	**–**	–
At 31 March	**(4,802)**	(3,317)

Movements in the present value of fair value of retirement benefit scheme assets (including members' share) in the current year were as follows:

	2010 £m	2009 £m
At 1 April	**2,211**	2,955
Expected return on scheme assets	**164**	231
Actuarial gains and losses	**660**	(1,051)
Contributions from scheme members	**67**	58
Contributions from employer	**126**	122
Actual benefit payments	**(68)**	(104)
At 31 March	**3,160**	2,211

The actual return on scheme assets was £824m (2009: £820m loss).

The analysis of the scheme assets and the expected rate of return at the Balance sheet date was as follows:

	Expected return		Fair value of assets		Percentage of assets	
	2010 %	2009 %	**2010 £m**	2009 £m	**2010 %**	2009 %
Equity instruments	**7.70**	8.10	**2,509**	1,675	**79.40**	75.76
Debt instruments	**4.50**	3.40	**374**	305	**11.84**	13.79
Property	**6.10**	5.80	**270**	225	**8.54**	10.18
Other	**4.00**	4.00	**7**	6	**0.22**	0.27
			3,160	2,211		

The expected return on assets assumption was determined as the average of the expected returns on the assets held on the accounting date. The rates of return for each class are set out in the table above and were determined as follows:

- equities and property: the rate adopted is consistent with the median assumption used in Towers Watson's Asset Liability Modelling work
- bonds: the overall rate has been set to reflect the yields on the bond holdings
- other assets: this class is mostly made up of cash holdings and the rate adopted reflects current short-term returns on such deposits.

28. Retirement benefit scheme continued

Actuarial assumption sensitivity

The discount rate is set by reference to market conditions at the reporting date, and can vary significantly between periods.

The mortality assumptions used are set by considering the experience of the scheme's members, and by making an allowance for possible future improvements in longevity. Mortality assumptions are difficult to set accurately, and forecasting rates of future mortality improvement is inevitably speculative.

The following table shows the effect of changes in these assumptions upon the defined benefit obligation:

	2010 £m	2009 £m
Discount rate		
Change in defined benefit obligation at year end from a 25 basis points increase	**224**	153
Change in defined benefit obligation at year end from a 25 basis points decrease	**236**	161
Mortality		
Change in defined benefit obligation from a one year increase in longevity	**144**	80
Change in defined benefit obligation from a one year decrease in longevity	**149**	83

The history of experience adjustments is as follows:

	2010 £m	2009 £m	2008 £m	2007 £m	2006 £m
Present value of defined benefit obligations	**(4,802)**	(3,317)	(3,572)	(3,424)	(3,234)
Fair value of scheme assets	**3,160**	2,211	2,955	3,010	2,635
Deficit in the scheme	**(1,642)**	(1,106)	(617)	(414)	(599)
Group's share (60%) of the scheme deficit recognised in the Balance sheet	**(985)**	(664)	(370)	(248)	(359)
Experience adjustments on scheme liabilities					
Amount (£m)	**32**	151	(114)	(14)	(67)
Percentage of scheme liabilities	**0.67%**	4.55%	3.19%	0.41%	2.07%
Experience adjustments on scheme assets					
Amount (£m)	**396**	(631)	(222)	52	229
Percentage of scheme assets	**12.53%**	(28.54)%	(7.51)%	1.73%	8.69%

The estimated amounts of contributions expected to be paid by the Group and members to the scheme during the year ended 31 March 2011 are £132m and £72m.

29. Related party transactions

Transactions between the Company and its subsidiaries, which are related parties, have been eliminated on consolidation and are not disclosed in this note.

The Company considers its key management personnel to be its directors. Details of their remuneration can be found in the Directors' remuneration report on pages 30 to 49. The Company has no other related party transactions.

Company information

Calendar 2010/11

31 March 2010	Year end
3 June 2010	Preliminary results announcement for full year to 31 March 2010
21 July 2010	Annual General Meeting of Network Rail Limited
November 2010	Results for half-year announcement to 30 September 2010
31 March 2011	Year end

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