Network Rail

Network Rail Limited
Annual report and accounts 2015

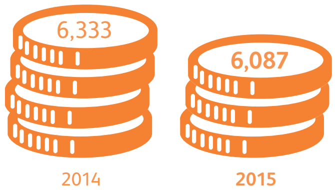
Working for you

Above: Project managers Rosie Majer and Tom Kirkham by the sea wall at Dawlish after successful reconstruction work on the railway.
Front cover: Night-time maintenance workers in railway tunnel.

OUR YEAR IN NUMBERS

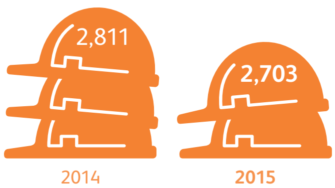
In this report we outline our performance during 2014/15, the first year of Control Period 5. Here is a snapshot of how we performed against a selection of key indicators.

£6,087m



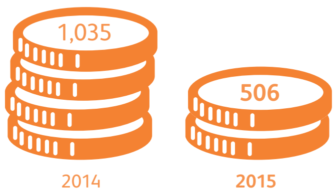
Revenue in the year
(2014: £6,333m)

£2,703m



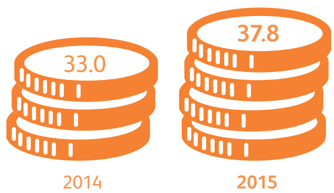
Operating costs*
(2014: £2,811m)

£506m



Profit before tax†
(2014: £1,035m)

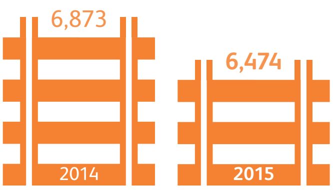
£37.8bn

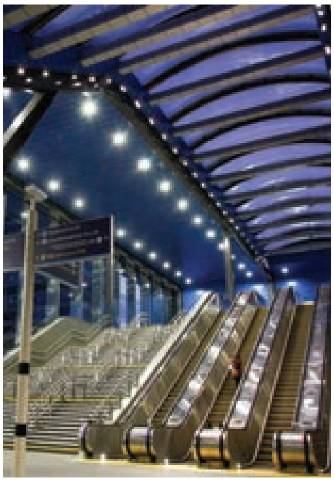


Net debt
(2014: £33.0bn)

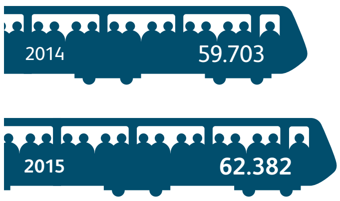
£6,474m

Capital expenditure
(2014: £6,873m)



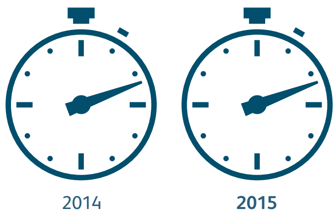


62.382km



Passenger km travelled
(bn)

89.7%

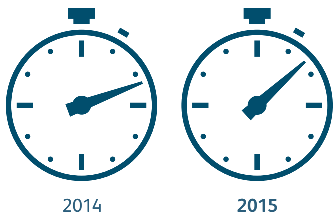


Passenger trains on time
(2014: 90.0%)

23.90

Freight moved
(bn net tonne km)

94.5%

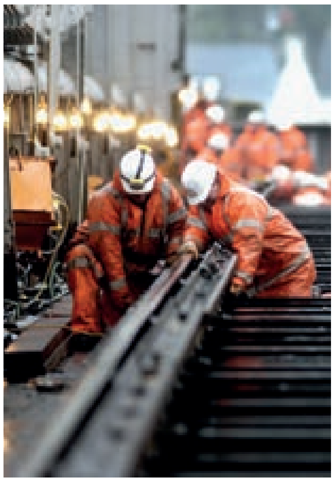


Freight trains on time
(2014: 93.2%)

71,237

Number of workforce safety close calls made against our target of 40,000

*Before depreciation and amortisation.
†We operate on a not-for-dividend basis, so our profits are reinvested in the railway.



OUR HIGHLIGHTS OF 2014/15

A selection of Network Rail's achievements during 2014/15 – just some of the ways we've been 'working for you' during the year.

TRANSFORMING THE RAILWAY AT READING

The £850m rebuilding of our station at Reading, and the infrastructure for several miles either side, has unlocked the biggest bottleneck on the main line out of London Paddington. This major project has unlocked capacity and made journeys smoother and more reliable for passengers. It was delivered under budget and ahead of schedule, and will enable Reading to become an increasingly important rail hub.

FASTEST GROWING RAILWAY IN EUROPE

In 2014/15, more people used Britain's railway than at any time in its history. Passenger journeys reached a record high of 1.65 billion – the result of a 70 per cent increase in passenger journeys in just 12 years. Yet not only is it the fastest-growing railway in Europe, it's also the safest.

SWIFT RESPONSE TO HARBURY LANDSLIP

Hundreds of engineers worked around the clock for almost six weeks to get services back up and running after a 0.3m tonne landslip at Harbury on the main line out of London Marylebone between Leamington Spa and Banbury. Thanks to their dedication and ingenuity we were able to re-open the railway three weeks ahead of schedule.

TAKING TRANSPARENCY TO THE NEXT LEVEL

Building on the success of our three-year transparency programme, we introduced a clearer, more detailed corporate scorecard with quarterly reporting on performance. We also set up the systems needed to be fully prepared for our new responsibilities under the Freedom of Information Act.

CABLE THEFT AT AN ALL-TIME LOW

Along with partners in the rail and utility sectors, we successfully lobbied for a change to the Scrap Metal Dealers Act to make it impossible for people who have stolen metal to sell it on anonymously. This change in regulation, along with our work with the British Transport Police, has helped to bring cable theft to its lowest ever recorded rate.

A COMMONWEALTH GAMES TO REMEMBER

Our people in Scotland pulled out all the stops to keep hundreds of thousands of spectators, athletes and officials moving during the 12-day Commonwealth Games. Glasgow Central station welcomed three times as many people as on a normal day and our maintenance teams worked hundreds of extra hours to keep the railway running smoothly, helping to make the Games a phenomenal success.

NORTH DONCASTER CHORD OPENS

We removed a major railway pinch point and significantly improved capacity by creating a flyover at Shaftholme near Doncaster. The flyover, which opened in June 2014, takes slow-moving freight trains up and over the busy East Coast main line rather than across it.

FIRST PART OF NORTHERN HUB COMPLETE

We reached the first milestone of the Northern Hub project by building a new platform at Manchester Airport station. Work was delivered 18 months ahead of schedule. The full project is set to be complete in 2019 and will allow up to 700 more trains each day to connect the cities of the North.

KEEPING BRITISH BUSINESS MOVING

Despite a six per cent increase in general freight traffic since 2013/14, our freight service achieved a leap in performance. It ended the year at 94.5 per cent against a target of 92.5 per cent, compared with 93.2 per cent against a target of 92.5 per cent in 2013/14.

To find out more visit:
www.networkrail.co.uk

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FOREWORD BY OUR CHAIR, RICHARD PARRY-JONES

Britain's railways continue to be a great success. Passenger numbers continue to rise rapidly, as has investment in the infrastructure to help meet that growing demand and to build a railway fit for 21st century Britain. This resurgence in the railways has been described as a renaissance, and in many respects it is.

WE OFTEN HAVE TO ASK PASSENGERS TO BEAR WITH US AND, OVERWHELMINGLY, THEY DO. IN RETURN, THEY EXPECT US TO DELIVER WHAT WE COMMIT TO.

SUCCESS, OF COURSE, WILL ALSO BE DEPENDENT ON THE HARD WORK AND DEDICATION OF THE MANY THOUSANDS OF PEOPLE WORKING FOR NETWORK RAIL, AND OUR PARTNERS AND CONTRACTORS.

While acknowledging the great strides made in the last two decades, we in the industry must also consider the experience of the person who really matters – the passenger. Rising passenger numbers mean more trains, which has drastically reduced the margin for error in terms of delays or cancellations when anything at all goes wrong. It has also made it more difficult to get a seat on the way to and from work.

As I wrote last year, we are engaged in a long-term transformation of our railway, and these benefits will not be realised overnight. Our significant investment in the rail infrastructure is designed to increase capacity in response to ever-increasing passenger numbers.

Every major project means some level of disruption and inconvenience, despite the considerable eventual benefits for passengers. We often have to ask passengers to bear with us and, overwhelmingly, they do. In return, they expect us to deliver what we commit to.

Above all, this means getting more trains running on time. We ended the last five-year control period in March 2014 well short of our target for punctuality, and received a substantial fine from our regulator as a result. The difficulties we had, though, have not disappeared. Punctuality is still not where any of us would want it to be. The executive team has developed a strategy to address the problem, but to succeed it will need to be backed up by a relentless focus on getting the basics right.

Our chief executive Mark Carne discusses in his review his passionate belief that safety performance and business performance go hand in hand. Mark's experience of another large and complex engineering industry has brought a valuable new perspective to the running of railways, including in particular an unwillingness to accept the levels of workforce injuries we see today. This focus, combined with the intense commitment of everyone at Network Rail, should bring the step change that is needed.

Success, of course, will also be dependent on the hard work and dedication of the many thousands of people working for Network Rail, and our partners and contractors. On behalf of the board, I would like to thank you for all that you have done this year.

In September 2014, the reclassification of Network Rail to the public sector was a significant change, particularly in its effect on our relationships with our funders and sponsors in government. At this early stage, it is difficult to make a full assessment of the extent of the impact of this change, though everyone is working to make it a success.

One result of reclassification was that in March 2015 Network Rail became subject to the Freedom of Information Act. The organisation already had a strong, ongoing commitment to transparency, so this is a logical next step for us. Society has a right to know what we do, how we take decisions and how we spend public money.

Richard Parry-Jones
Chair

IN SEPTEMBER 2014, THE RECLASSIFICATION OF NETWORK RAIL TO THE PUBLIC SECTOR WAS A SIGNIFICANT CHANGE, PARTICULARLY IN ITS EFFECT ON OUR RELATIONSHIPS WITH OUR FUNDERS AND SPONSORS IN GOVERNMENT.

There were also some changes to the board in 2014/15. Non-executive directors Keith Ludeman, Lawrie Haynes and Mike Firth have left; I would like to thank them for all their efforts on behalf of Network Rail. Sharon Flood was appointed as a non-executive director and has already brought a wealth of experience to bear as the board seeks to hold the executive accountable for its management of the organisation. Executive directors Simon Kirby and Robin Gisby have left Network Rail after years of sterling service. Francis Paonessa and Phil Hufton are their respective replacements. While Francis and Phil are not executive directors of the company, they are members of the executive committee and will seek to build on Simon's and Robin's records in the next phase of the organisation's life.

As always, there are challenges ahead for Network Rail and the industry as a whole. A particular issue is delivering major enhancements while running an increasingly congested network. To help address this, the board has established two temporary sub-committees addressing project delivery and supply chain efficiency.

The executive team at Network Rail is also single-minded in its commitment to tackling these problems. In turn, the board intends to challenge and scrutinise the team's work, but also to be supportive. This, I believe, is the right approach for long-term success.

Richard Parry-Jones

Richard Parry-Jones
Chair
10 June 2015

A MESSAGE FROM OUR CHIEF EXECUTIVE, MARK CARNE

When I became chief executive of Network Rail in early 2014, I already knew that the organisation had huge responsibilities and faced many challenges. I also knew that Britain needed us to succeed. For me, that was the appeal.

IN 2014/15 WE CARRIED MORE PASSENGERS THAN EVER, AND CARRIED OUT MORE ENHANCEMENTS OF THE NETWORK THAN IN ANY PREVIOUS YEAR IN THE COMPANY'S EXISTENCE.

IN TERMS OF TRAIN PUNCTUALITY, THE REALITY IS THAT TOO MANY TRAINS ARE CANCELLED AND TOO MANY ARE LATE. I DO NOT BELIEVE THIS IS ACCEPTABLE, OR JUST A FACT OF LIFE.

As we look back on 2014/15, we can take pride in many achievements. The year began with the reopening of the line at Dawlish, took in the opening of our station at Reading in July, and saw our exceptional advanced apprenticeship scheme celebrate its 10th anniversary. We carried more passengers than ever, and carried out more enhancements of the network than in any previous year in the company's existence. The asset reliability of the railway is five per cent better than last year – now at an all-time high.

It is no exaggeration to say that the railway has never been more important to Britain. More people are using it than at any time in its history, with growth levels that will lead to a further doubling in the next 25 years.

But this popularity causes challenges. On large parts of the network, at peak times, the railway is full and increasingly creaking under the strain. Our network, our stations and our platforms are now having to deal with more trains and more passengers than they were ever designed for. More trains means some timetables being squeezed to full capacity, with no slack in the system for delays of any sort. A single train stopping for 30 seconds longer than planned at rush hour can have a knock-on effect on dozens of trains, causing delay to thousands of passengers.

The unprecedented investment in the railways during Control Period 5 will enable more than 250 million additional passenger journeys per year. Network Rail has committed to deliver all this with minimal disruption to passengers by keeping the rail network open wherever possible for at least 18 hours per day, seven days a week. Access to the network for maintenance and improvement is extraordinarily limited, especially in locations where the usage is most intense. This creates huge challenges.

Although we have made some good progress in the first year of Control Period 5, our performance as a whole has not been where we want it to be. In terms of train punctuality, the reality is that too many trains are cancelled and too many are late. I do not believe this is acceptable, or just a fact of life. Passengers should be able to rely on us every time they get on a train.

In addition, the massive programme of enhancements to the network inevitably raises the level of disruption for passengers. We completed almost 300 projects on time over Christmas, with 15,000 of our people working tirelessly through the festive period. But this was entirely overshadowed by overruns on two projects that led to deeply unfortunate passenger disruption on services to and from Paddington, as well as chaos at Finsbury Park on 27 December. Likewise we failed, in the first few months of 2015, to anticipate how passenger services and passenger queuing might be affected at London Bridge and throughout the South East as we carried out a massive ongoing upgrade of the station and a number of lines going through it. Both cases have demonstrated the need for Network Rail to be far more focused on the possible implications for passengers when we are planning and executing our work.

Mark Carne inspecting the damage to the sea wall and railway line at Dawlish following severe winter storms in early 2014.

CHIEF EXECUTIVE'S REVIEW CONTINUED

Mark Carne with some of the apprentices representing each of the 10 years we've been running our Advanced Apprenticeship scheme, at an event at King's Cross station, London.

Passengers at platform 14 at Reading station, one of four new platforms added during redevelopment in 2014.

HM The Queen at the opening of our redeveloped station at Reading in July 2014.

I BELIEVE PASSIONATELY THAT SAFETY PERFORMANCE AND BUSINESS PERFORMANCE GO HAND IN HAND. IF WE FOCUS ON WHAT IT TAKES TO DO THINGS SAFELY, PERFORMANCE WILL FOLLOW.

Since joining Network Rail in early 2014, I have had a good look at how we organise ourselves within our existing structure, our performance measurement and accountability, our working practices and our reward structure. We have made improvements in all those areas:

- We have formalised the matrix management structure within our devolved organisation, clarifying roles and accountabilities
- I have strengthened key positions in my executive team, including people with proven experience of delivering structured continuous improvement (for example, Phil Hufton from Transport for London, Francis Paonessa from Bombardier and Graham Hopkins from Rolls Royce)
- For the first time we now have a single, clear scorecard deployed right through and across the organisation, which gives our people a direct line of sight of how corporate performance links to bonus outcomes
- We have also begun to deploy structured continuous improvement work practices such as performance visualisation.

But there is a long way to go. While working practices have improved at Network Rail, they have not kept pace with modern industrial practice seen elsewhere. This represents a major challenge but also a major opportunity to improve performance.

I believe passionately that safety performance and business performance go hand in hand. If we focus on what it takes to do things safely, performance will follow. After all, to do a job safely, it must be well planned, well led, and carried out by competent people using the right equipment in the right way. These same ingredients go to make up high performance. I knew this was true in the oil industry, and we have now shown that the routes in Network Rail with the most improved safety record also have the best train and financial performance.

We have seen some positive results in ensuring our passengers, staff and contractors get home safe every day, particularly in terms of close call reporting – our process for identifying safety risks. But too many tragic accidents involving our staff and contractors have been caused by behaviours and conditions that others have previously observed but did nothing to stop. Addressing the underlying factors that affect safety is therefore vitally important, and also embodies the caring culture I want to build at Network Rail.

So as I reflect on my first full year as chief executive of Network Rail, I see a huge amount of potential in the organisation as a whole. We need to improve against the key metrics we have agreed, but solely focusing on the hard numbers will not, of itself, be enough. I am determined to create an organisation in which everyone has the opportunity to deliver to their maximum potential, an organisation that is focused and rigorous, but also places real value on inclusiveness, caring, creativity, collaboration and teamwork. This kind of cultural shift is the way to embed lasting change.

Mark Carne
Chief executive
10 June 2015

HOW WE PERFORMED IN 2014/15

In 2014/15 we introduced a new approach to corporate reporting, based on a more detailed scorecard and quarterly reports. Our improved scorecard gives an at-a-glance summary of our achievements against key indicators and areas in which we need to do better.

Area	Bonus weighting	Full-year outturn		
Safety		Worse than target	Target	Better than target
Workforce safety – lost time injury frequency rate	5.0 %	0.568 0.515	0.486	0.458
Workforce safety – close calls	3.0 %	35,000	40,000	45,000 71,237
Workforce safety – close calls closed within 28 days (%)	2.0 %	40 %	47 % 50 %	60 %
Passenger safety	5.0 %	2.206	2.158	2.110 1.866
Level crossing risk reduction	5.0 %	11.99 11.62	11.36	10.73
Train performance		Worse than target	Target	Better than target
Public performance measure	12.0 %	89.7 % 90.0 %	91.1 %	91.6 %
Freight delivery	2.0 %	92.0 %	92.5 %	94.5 % 95.0 %
Financial performance		Worse than target	Target	Better than target
Financial performance measure	20.0 %	-234 £157m	0	+£157m
Investment		Worse than target	Target	Better than target
Top 10 IP renewals and enhancement milestones	7.5 %	6	8	10
All delivery plan enhancement milestones (%)	7.5 %	60 % 65 %	80 %	100 %
Asset management		Worse than target	Target	Better than target
Composite reliability index	7.5 %	1 %	6 % 7.52 %	10 %
Renewals (7 key volumes)	7.5 %	X ✓✓✓	✓✓✓✓✓	✓✓✓✓✓✓✓
Satisfaction		Worse than target	Target	Better than target
Customer	5.0 %	3.00 3.15	3.32	3.49
Passenger	5.0 %	81.0 % 81.4 %	83.3 %	86.0 %

Key to performance colours

- Below 'worse than target'
- Between 'worse than target' and 'target'
- Between 'target' and 'better than target'
- Above 'better than target'

118

We closed 118 level crossings

-7%

There were 311 near misses at level crossings involving pedestrians and road vehicles, a reduction of seven per cent on 2013/14

94.5%

For freight delivery we outperformed our regulatory target for the year, achieving 94.5 per cent against a target of 92.5 per cent

Workforce safety

Lost time injury frequency rate: a measure of the amount of time lost due to fatality and injury among Network Rail staff and contractors employed by Network Rail.

We did not meet either the 15 per cent LTIFR reduction target of 0.486 or the scorecard minimum of 0.515. There were 665 lost time injuries over 2014/15, compared to 720 in 2013/14.

Workforce close calls: any occurrence that had the potential to cause injury or damage. It can be an unsafe act or an unsafe condition.

71,237 close calls were reported. This comfortably exceeded both the target of 40,000 and the scorecard maximum of 45,000. Forty-seven per cent of these calls were closed in 28 days against a target of 50 per cent and a scorecard minimum of 40 per cent. This result excludes close calls managed through our contractors' systems.

Passenger safety – train accident precursor indicator model: this measures the underlying risk from train accidents to passengers, our workforce and members of the public, by tracking the occurrence of accident precursors such as broken rails.

In 2014/15 the target reduction in the passenger component of train accident risk – where Network Rail is the risk controller – was 10 per cent. The actual reduction achieved was 22 per cent. This was helped by less risk from weather-related causes, such as land slips and heat causing buckled rails, than in 2013/14.

Level crossing risk reduction – risk indicator model: a measure of the current level of risk recorded within the all level crossing risk model, nationally and by route.

We closed 118 level crossings in 2014/15. There was an eight per cent year-on-year reduction in level crossing risk (measuring benefits only). However, the scorecard target was not achieved. There were 311 near misses at level crossings involving pedestrians and road vehicles, a reduction of seven per cent on 2013/14.

Train performance

Public performance measure: the percentage of passenger trains arriving on time at the final destination. For long distance journeys 'on time' means within 10 minutes of scheduled arrival time, and for Regional and London & South East within five minutes of it.

At the end of 2014/15 passenger train punctuality in England and Wales stood at 89.7 per cent, 1.3 percentage points behind our committed target. In Scotland, punctuality stood at 90.5 per cent against a target of 92 per cent. At the train operator level performance was poor, with sixteen missing their punctuality targets and 12 missing their cancellations and significant lateness targets.

Freight delivery metric: the percentage of commercial freight trains that arrive at their destination within 15 minutes of booked arrival, or with less than 15 minutes delay caused by Network Rail or a non-commercial freight operator. All freight cancellations by Network Rail or a train operating company count as a fail.

We outperformed our regulatory target for the year, achieving 94.5 per cent against a target of 92.5 per cent.

Financial performance measure: represents the sum of Network Rail's income, expenditure and capital expenditure. We track our financial performance periodically and measure it against the baseline for income, operational expenditure and capital expenditure.

Our financial performance in 2014/15 was £234 million lower than planned. This was largely due to financial underperformance in renewals, notably in track, signalling and civils; net overspends across our enhancement portfolio; financial underperformance resulting from poor train punctuality; and lower than expected savings in operations and maintenance.

Investment

Top 10 IP renewals and enhancement milestones: the top 10 milestones in the renewals and enhancement work of our infrastructure projects (IP) group.

We achieved eight out of these top 10 milestones. Part of the Great Western electrification programme was delayed from January to May 2015. North West electrification saw two of its three phases delivered on time and a revised schedule for the third phase, which is now running to schedule.

All delivery plan enhancement milestones: our investment projects are managed using the Governance for railway investment projects (GRIP) approach, which has milestones at stages 3 and 6 of the 8-stage project process.

Of the 69 regulatory milestones planned in 2014/15, 45 were delivered on schedule and 24 were not.

Asset management

Composite reliability index: this index measures the short-term condition and performance of our assets including track, signalling, points, electrification, telecoms, buildings, structures and earthworks.

We achieved 7.52 per cent on the index, exceeding our target of six per cent.

Renewals (seven key volumes): our seven key volumes for renewals were plain line track; switches and crossings; signalling and equivalent units; underbridges; total earthworks; wire runs and conductor rail.

We achieved only one of the key volumes, in earthworks.

Satisfaction

Customer satisfaction: this metric shows how well Network Rail engages with its key customers, principally passenger train and freight operating companies in each of our eight routes. It is measured using the third-party 'Customer Satisfaction Survey'.

At 3.00, customer satisfaction fell short of both our target of 3.3 and the scorecard minimum of 3.15.

Passenger satisfaction: a metric based on the 'National Passenger Survey' commissioned by Passenger Focus, which provides a network-wide picture of passengers' satisfaction with rail travel. The survey is run twice a year – our performance is based on the yearly average.

Customer service failed to meet our target of 83.3, but met the scorecard minimum of 81.0 per cent.

GROUP FINANCE DIRECTOR'S REVIEW

This annual report marks the end of the first year of Control Period five (CP5), our five-year regulatory settlement. The settlement allows the Office of Rail and Road (ORR) and Network Rail to take a fresh look at how much money is needed to deliver the required outputs across the control period.

SAVINGS WE ACHIEVED OVER PRECEDING YEARS ARE BEING SHARED WITH OUR CUSTOMERS AND FUNDERS THROUGH LOWER CHARGES. CONSEQUENTLY, TURNOVER WAS £6,087M; £246M LOWER THAN 2013/14.

Part of building a sustainable railway is making it more affordable for tax payers, passengers and freight users. Coming into this control period Network Rail has been able to lower its charges as part of the new regulatory settlement, because of reductions in the underlying cost base and by reducing the returns required because of the existing equity built up in the business over the previous decade.

As a result of this drop in charges, profit before tax fell to £506m, compared to £1,035m last year.

Demand for the railway network continues to grow and Network Rail has delivered over £6bn of investment in the year to help meet this. Growth in the capability of the railway network will assist in making the railway of the future more affordable, by increasing capacity, as well as driving improvements in the country's economic wellbeing.

This year Network Rail continued to invest heavily in enhancing and renewing the network. The delivery of key projects such as Thameslink and Crossrail, Borders Rail and Edinburgh-Glasgow improvements, Reading and Birmingham New Street, as well as commencing some major electrification programmes, will provide a better railway for Britain.

This review will focus on the financial performance achieved by Network Rail in the first year of CP5. In particular focusing on:

- Revenue – how it has reduced from previous years, and income variations from train performance results and our property assets
- Operating costs – as revenue is largely determined by the regulatory regime the extent to which Network Rail has managed to reduce operating costs has a significant bearing on the operating profit
- Investment in new assets – is helping to deliver a network better able to cope with Britain's increasing demand for rail services
- Financing activities – as an arms-length public body it is important that Network Rail can demonstrate a strong financial framework; one that, despite challenges, remains on a stable footing to deliver the performance and investment required to drive the railway forward
- The challenges the company faces in delivering its CP5 targets, which has resulted in a reduction to the valuation of the railway network of £488m.

Patrick Butcher
Group finance director

£3,393m

We spent £3,393m, a record in terms of work delivered, (£3,198m: 2013/14) on enhancements increasing the capacity of the network

Revenue

This is the first year of a new five-year Control Period (CP5). As planned, our charges have been rebaselined by the ORR. Savings we achieved over preceding years are being shared with our customers and funders through lower charges. Consequently, revenue was £6,087m; £246m lower than 2013/14, despite continued increases in passenger and general freight traffic.

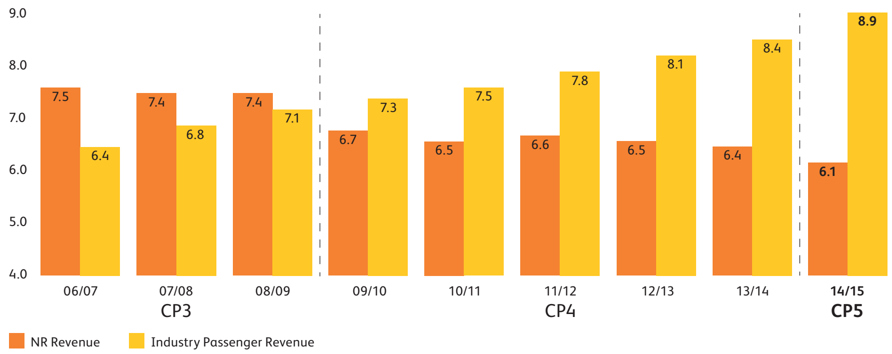
As the graph below illustrates, turnover has continued to decrease in real terms over the last eight years as a result of passing on the benefits of increased efficiency and stability to customers and taxpayers, through lower charges. Over the same period Great Britain passenger revenue has increased and now stands at over £8bn. As can be seen, Network Rail now takes a 7 per cent smaller share of the overall fare box than last year.

Performance and access regimes

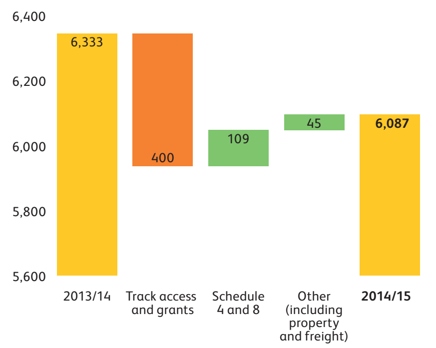
Track access and network grants reduced by £400m as a result of the regulatory determination. But not all Network Rail's income is fixed by the regulatory regime. Network Rail is at risk of reductions in receipts from train operators for worse than expected train performance.

When performance drops below the benchmarks determined by the ORR, Network Rail pays compensation to operators. Delays include those for planned engineering work and unplanned due to a variety of operational factors. Compensation paid to train operators reduced by £109m. The decrease in performance penalties reflects the recalibration of the performance regime by the regulator. Although delay minute benchmarks have reduced, the rates of compensation have also increased across nearly all operators.

Revenue (14/15 prices) (£bn)



Revenue movements since last year (£m)



Network Rail also generated an additional £45m of other revenue. This includes increases in freight revenue and property income. Freight revenue increased by £23m largely due to changes in the regulatory performance and charging regimes.

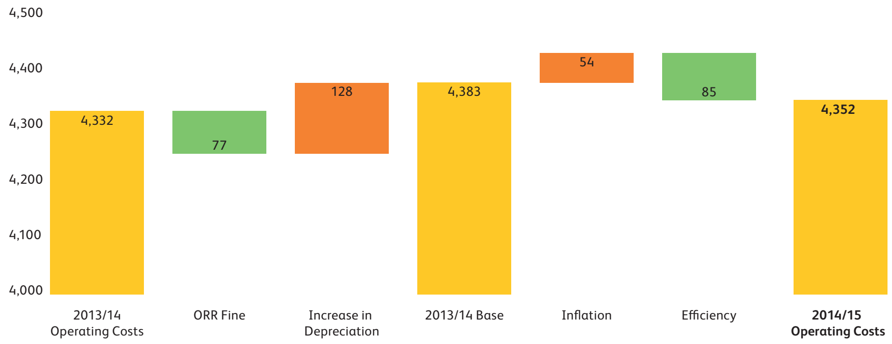
Property

During the year, property income grew by £18m (8 per cent) to £256m (2013/14: £238m).

The major drivers of this growth were the property enhancements programme, transfer of Reading and Bristol stations to Network Rail, retailer sales growth at our managed stations, rental income growth from our commercial estate portfolio and the acquisition of over 100 freight sites, from freight operating companies, with end user tenants.

GROUP FINANCE DIRECTOR'S REVIEW CONTINUED

Net Operating Costs (£m)



Significant property enhancements that completed during the year reinforce our strategy of creating 'destination stations' at our managed stations. These include a complete refurbishment of Victoria Place Shopping Centre, above Victoria Station in London, revitalising the environment and bringing in new brands to the Network Rail portfolio.

Operating costs

Because Network Rail's income is largely fixed by the regulatory regime, controlling operating costs is important in order to deliver operating profit.

Although net operating costs increased slightly this year by £20m to £4,352m (2013/14: £4,332m) this included a £128m increase in depreciation reflecting the high level of investment made in the network over the past year. Operating costs before depreciation and amortisation fell by £108m.

This was in part due to non-recurring costs in 2013/14 such as restructuring costs for the management efficiency programme and the provision for the ORR fine of £77m for long-distance train performance being below target. After allowing for general inflation at £54m this indicates efficiencies of around £85m in real terms.

Employee costs

Staff costs were stable in the year rising to £1,919m from £1,910m in 2013/14. The average number of employees rose slightly in the year to 35,457 (2013/14: 35,141). Network Rail insourced contractors to our high output track renewal (540 employees), structures inspection (80) and logistics teams (65), as well from strengthening our maintenance teams (450) such as the formation of an overhead electrification maintenance team ahead of the Western electrification project (80). These increases were largely offset by reductions from efficiency programmes.

The average salary received in the year fell slightly from £45,100 to £44,800. This reduction was partly driven by mix and partly by lower Long Term Incentive Plan payments.

Efficiency

One way to look at cost efficiency is the operating costs, before depreciation and amortisation per train mile. These costs are five per cent better than the previous year, reflecting the increase in the number of services run on the network and real term cost efficiencies achieved in the year. This growth, though clearly welcome, impacts the reliability of the train services as the network becomes more congested.

However, operating costs are only one part of the running costs. Significant challenges exist in achieving efficiencies in the per unit cost of renewing the component assets that make up the railway network. Over the past decade Network Rail has had a good record of achieving efficiencies, but as a consequence efficiencies in CP5 will be more difficult to achieve.

Investing in new assets

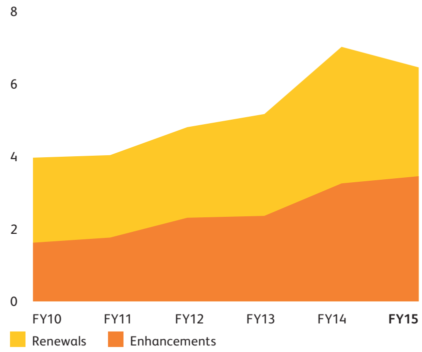
We invested £6,474m in the network in the year (2013/14: £6,873m), continuing the historically high levels of delivery.

We spent a record £3,393m (2013/14: £3,198m), on enhancements, increasing the capacity of the network. The portfolio includes major projects, such as Thameslink, Crossrail, Birmingham Gateway, Borders Rail and Great Western Electrification and smaller scale improvements works such as platform lengthening, power supply strengthening and providing and enhancing disabled access.

These projects are transforming the railway network and will make a major difference to rail users in London and South East England, Scotland, Wales as well as the Midlands and Northern England.

We have also invested £2,949m (2013/14: £3,701m) renewing both our railway's assets, such as track, signalling and civils, and in information management and asset information technologies. Renewals are largely financed through internally generated funds and enhancements through additional borrowing.

Capital Expenditure (£bn)



Financing activities

Following the decision to reclassify Network Rail as a public sector body (see page 48) the government decided that, to maximise overall taxpayer value for money, the group would cease to raise debt independently and instead borrow directly from the DfT. The policy applies to both the borrowing required for new investment and refinancing of existing debt.

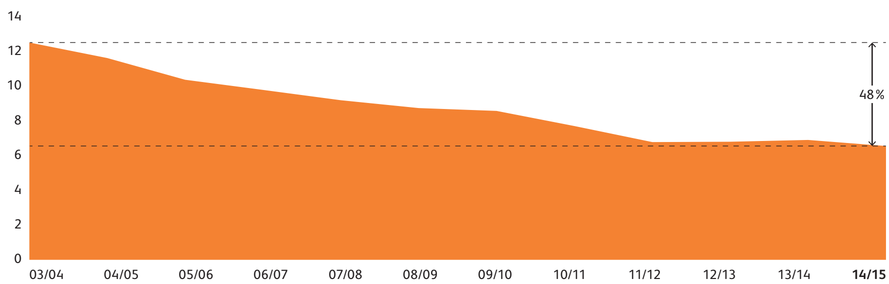
The regulatory settlement and DfT loan agreement provide strong security for future income and financing.

Borrowing

During the year ended 31 March 2015, Network Rail borrowed £6.45bn from the DfT. Part of this new debt was used to pay back existing bonds while the remainder was used to invest in the railway infrastructure. As a result, net debt rose from £32,987m to £37,759m.

Borrowing	2015 £m	2014 £m
Borrowing to invest	3,712	1,129
Borrowing to refinance	2,738	3,975
Bonds issued in year	–	5,104
DfT loan drawdown	6,450	–

Operating costs per train mile (2014/15 prices) (£)



Managing interest and foreign exchange risk
Network Rail manages its interest and foreign exchange risk by using derivative financial instruments (hedges). This is particularly important for Network Rail because, for example, a one per cent movement in interest rates would cause at least £350m of fluctuation in interest costs.

The group 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 (ie, 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 (ie, the loans). These losses on debt and derivatives valuations taken through the income statement were £41m (£304m gain in 2013/14). In addition, £942m of reduction in the value of interest rate swaps, used to control the cost of future borrowings, was posted to the hedge reserve as statistically effective cash flow hedges.

Deferred tax
Largely as a result of the continued high levels of capital expenditure in enhancing and renewing the railway network, Network Rail has considerable carried forward tax losses. These were previously carried as an asset on the balance sheet offsetting deferred tax liabilities. The losses would only be used once Network Rail had generated sufficient taxable profits.

In 2014/15 Network Rail derecognised this deferred tax asset (£597m) with respect to tax losses based on the uncertainty of future taxable profits. However these losses will still be available to set against future profits.

The key change in the year has been the reclassification of Network Rail as an arm's-length public body. This, when taken together with continued investment in the infrastructure, means that there is greater uncertainty with regard to when Network Rail will return to the level of taxable profits that will allow for the utilisation of tax losses based on the uncertainty of future taxable profits.

Network Rail will continue to monitor the probability of using available tax losses and may re-recognise its deferred tax assets if circumstances change such that it is probable that the assets will be utilised.

Retirement benefits
Retirement benefit obligations arise as Network Rail is party to two shared-cost defined benefit pension schemes. Costs are shared with pension scheme members on a 60:40 basis.

These results show that, like many other companies, Network Rail's share of the accounting deficit is widening to £1,505m (2013/14: £1,237m), although the actuarial valuation remains healthy and is indicating 99.1 per cent funding.

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 that have risen by 16.5 per cent in line with gains in the equity markets in 2014/15.

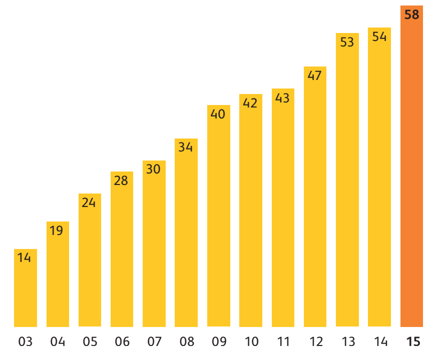
Accounting rules require that the total projected amounts that the scheme is obliged to pay out in the future are discounted to a present day liability using highly rated (AA) corporate bond indices. It is significantly cheaper to borrow now than it was last year, because long-term market interest rates have reduced. Therefore, 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.

The railway network
The railway network that we own and have a licence to operate is included in the accounts at a value that represents what a third-party purchaser would pay for it. The basis of this valuation is set out in Note 12 (page 103) to the accounts and comes from an assessment of the cash flows that are forecast to arise from the asset. The starting point for this valuation is the regulatory asset base (RAB). Subject to certain criteria established by the ORR, each year capital expenditure is added to the RAB and amortisation is deducted. The ORR can make deductions from the RAB in the event that we do not achieve our required outputs, for example not meeting required train performance or breaching a licence condition, or where the ORR wishes to make a retrospective funding adjustment.

As the valuation of the railway network is based on projected cash flows, we have considered the potential for underperformance in CP5, both in terms of the financial settlement and the required outputs.

As a result, the valuation of the railway network was adjusted downwards by £488m (2013/14: £1,813m). This is because it was assessed that in advance of a formal update of our business plan there is a high risk of spending more per activity than the settlement allowed. We will keep under review with government and the rest of the industry whether parts of the current investment programmes should be rephased beyond CP5. A reduction in valuation has also been made for the impact of the like-for-like overspends and anticipated adjustments from the ORR for non-delivery of output.

Total Assets (£bn)



Post balance sheet events
There have not been any significant post balance sheet events, both adjusting and non-adjusting.

Summary
2014/15 has been a year of transition for Network Rail, and the first year of what is proving to be a very challenging control period settlement. Continued high level of capital investment has been maintained but it has proven to be difficult to achieve the ambitious efficiency and cost reduction targets. Additionally, regulatory outputs, particularly in train performance, have been missed.

The move into the public sector brings additional accountabilities for the organisation and in particular for Mark Carne as accounting officer (see page 48).

Nevertheless the fundamentals of the group remain strong. Profit before tax is £506m. The regulatory settlement and DfT loan agreement provide strong security for future income and financing. Our clear challenge is to continually improve, to enhance our capability to meet the challenges of the control period settlement.

Patrick Butcher
Group finance director
10 June 2015

ABOUT US

Network Rail owns and operates the railway infrastructure in England, Wales and Scotland. Find out more about what we do, how we are governed, how we are funded and our strategy for delivering a better railway for a better Britain.

OUR AIM IS A SAFE, RELIABLE AND EFFICIENT RAILWAY FOR PASSENGER AND FREIGHT TRAINS.

What we do

Network Rail owns and operates Britain's railway infrastructure, including tracks, signals, tunnels, bridges, viaducts, level crossings and stations. We also manage rail timetabling and 18 of the largest stations in England, Scotland and Wales.

We operate on a not-for-dividend basis, which means that we do not pay dividends to shareholders. Instead, we reinvest the profits we make into improving the railway.

Our aim is a safe, reliable and efficient railway for passenger and freight trains.

How we are governed and managed

As a public sector arm's length body, Network Rail retains the commercial and operational freedom to manage Britain's railway infrastructure within regulatory and control frameworks.

The diagram opposite shows the governance framework within which we operate.

Network Rail's board of directors provides the primary internal governance. For details of the directors, including their biographies, see page 44.

The board has delegated some of its powers to the six board committees shown in the diagram opposite.

The executive committee, comprising three executive directors and seven senior executives, manages the day-to-day running of Network Rail.

For details of the other five board committees, see pages 54 to 62.

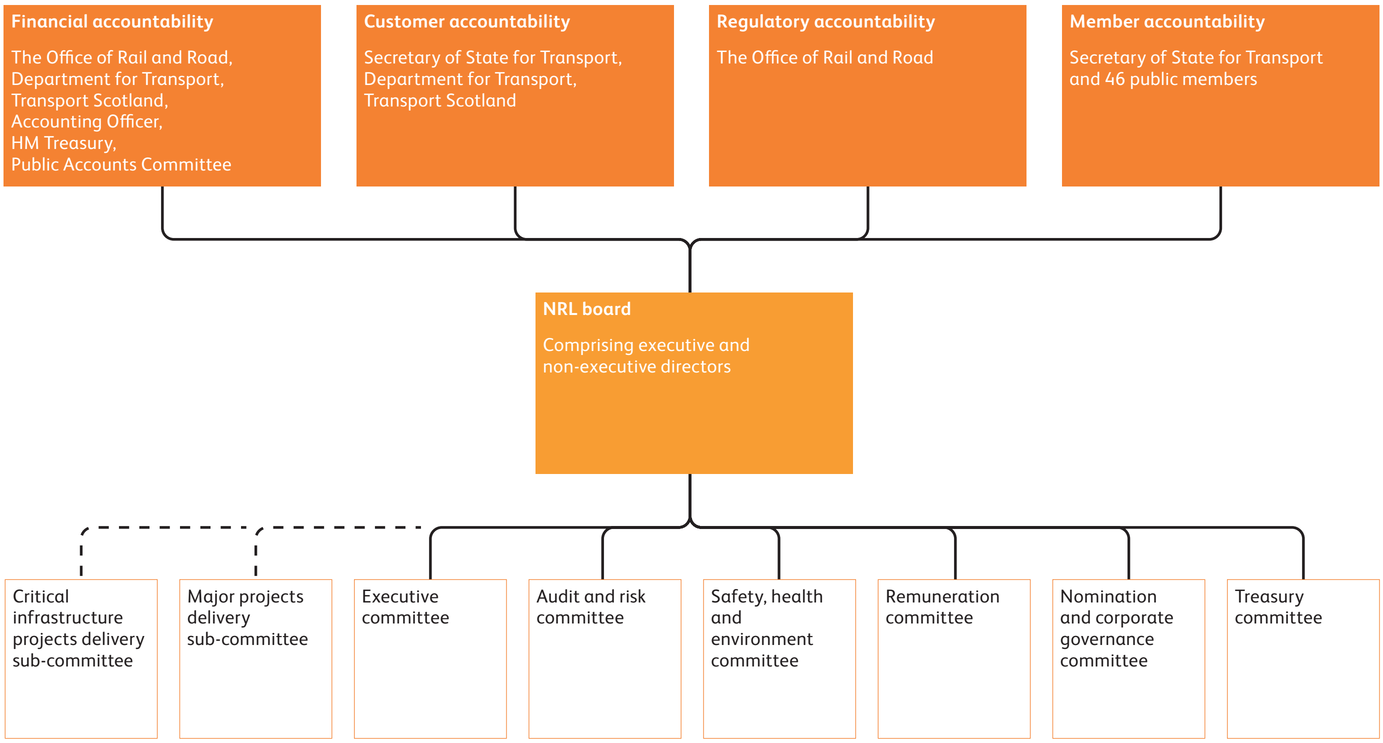
In early 2015 the board established two temporary sub-committees – the critical infrastructure projects delivery sub-committee and the major projects delivery sub-committee. For information on them, see page 47.

Our board is accountable to others in a number of ways:

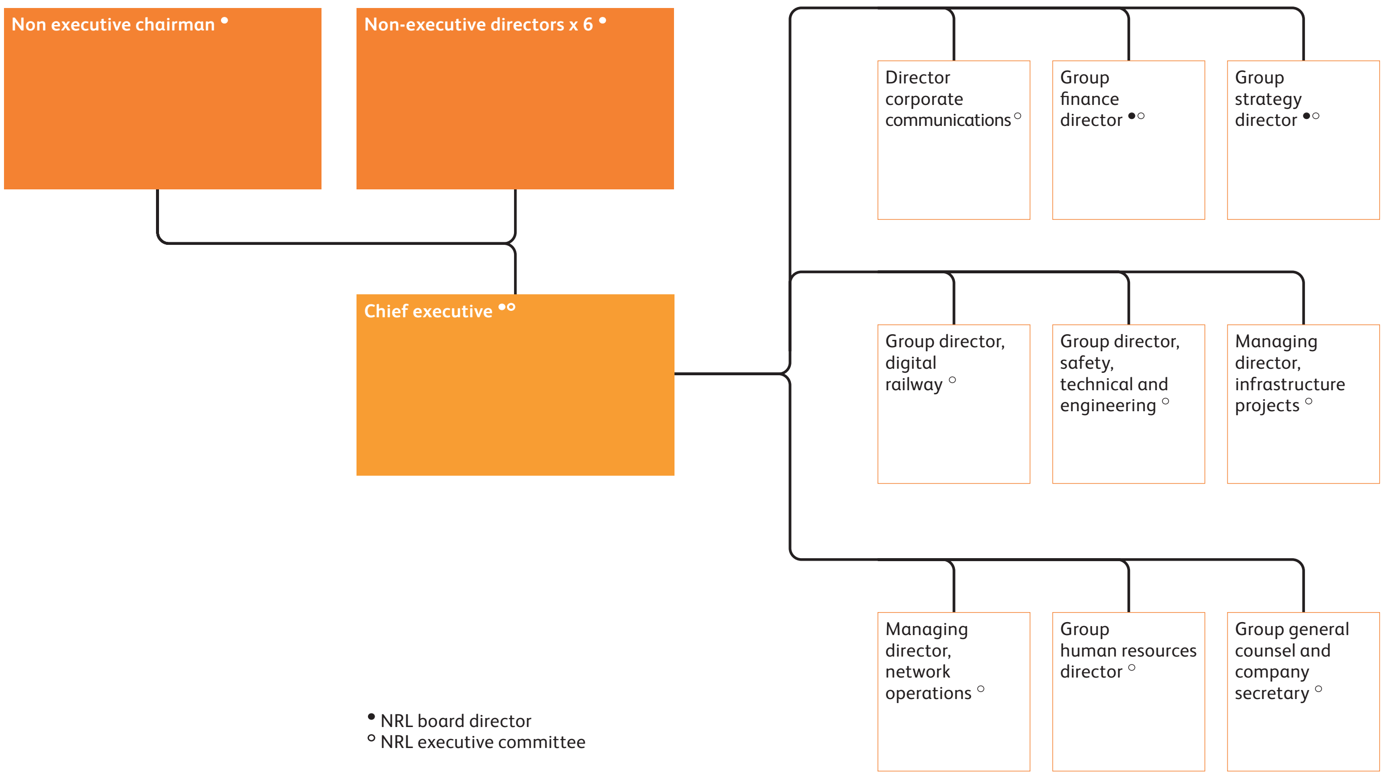
- **Financial** – we are accountable to a variety of groups for the way we spend our income. The Office of Rail and Road (the ORR) determines the income we receive from the Government and the outputs we must achieve during each five-year control period. In addition, our chief executive Mark Carne is our accounting officer and so is personally accountable to Parliament for Network Rail's stewardship of the public funds it receives
- **Regulatory** – we are accountable to the Office of Rail and Road for our health and safety performance
- **Membership** – the board is accountable to Network Rail's members for its leadership and management of the business. For more information about our members, see page 52.

The board's corporate governance report is shown on pages 43 to 80.

Our governance framework



How we are managed



WHO WE ARE CONTINUED

NATIONAL FUNCTIONS

- Network Operations
- Infrastructure Projects
- Safety, Technical and Engineering
- Group Strategy
- Digital Railway
- Corporate Services
- Corporate Communications

ROUTES

- Anglia
- London North Eastern and East Midlands
- London North Western
- Scotland
- South East
- Wales
- Wessex
- Western

THE EIGHT ROUTES ARE THE OPERATIONAL HEART OF NETWORK RAIL. THEY ARE SUPPORTED BY SEVEN NATIONAL FUNCTIONS THAT PROVIDE THE SERVICES AND SOLUTIONS THE ROUTES NEED TO DELIVER AND OPERATE A HIGH PERFORMANCE RAILWAY.

How we are organised

During 2012, Network Rail devolved responsibility for day-to-day operation of the railway to ten strategic routes, since reduced to eight. Our aim was to allow greater operational control at a local level and better alignment with the companies that run passenger and freight services on our infrastructure.

During 2014/15, we remained committed to devolution, but clarified and refined our approach to ensure that our central functions support the routes as effectively as possible. To achieve this, we have:

- Created a safety, technical and engineering function that integrates safety and sustainability into engineering and asset management.
- Integrated our capacity planning and group strategy function to create a single team for all aspects of network planning and timetabling, which will work closely with the routes to improve capacity management across the network.
- Defined a new digital railway function to provide the industry leadership and momentum to build an integrated strategy for the technological transformation of the railway.

How we operate

The eight routes are the operational heart of Network Rail. They are supported by seven national functions that provide the services and solutions the routes need to deliver and operate a high performance railway.

More information on the activities during 2014/15 of Network Operations (page 20), Infrastructure Projects (page 22), Safety, Technical and Engineering (page 26) and Property (page 30) can be found on the pages referenced.

Our business model

We are a public sector company that operates as a regulated monopoly. Our income is a mix of direct grants from the UK and Scottish Governments, charges levied on train operators that use our network and income from commercial property.

The governments specify what they need from Britain's railway and how much they can afford to contribute. Our independent regulator, the ORR, sets a framework that specifies the level of fixed income we are allowed to charge, as well as the prices for recovering the costs of wear and tear to our infrastructure caused by the trains using it.

The framework also includes flexible funding mechanisms which allow the level of enhancements to the railway to be varied over time. The charges we are allowed to pass on to train operators are determined so that they are fair and allow us to maintain a safe and reliable network, and deliver good customer service.

Providing mobility assistance to members of the public at Paddington station, London.

How we generate revenue
The sources of our income are:

68%

Network grants from the Department for Transport and Transport Scotland

68 per cent of our income for CP5 is in the form of network grants from government

28%

Track access income from train operating companies and freight operating companies

11 per cent of our income comes from fixed track access charges to operators, leaving 17 per cent coming from variable charges to train operators. Our income from operators is reduced by compensation paid to them under the performance regime

4%

Income from commercial property

Four per cent of our income comes from our national property and station retail portfolio of over 7,400 properties

How our revenue is determined

Network Rail is funded by government in five-year blocks called control periods. This annual report covers the first year of Control Period 5 (2014 to 2019).

The ORR assesses the efficient level of expenditure that we need to run our business and deliver the regulated outputs. It determines how much revenue we need, including an allowed return on our regulatory asset base – its assessment of the value of our assets. This takes into account other income that we receive (such as commercial income from property). Net revenue is received from access charges and network grants. Our regulatory agreements then allow us to determine the amount we are allowed to charge train operators.

The ORR calculates our revenue based on:

Cost of service – the regulator considers what costs an efficiently run company would incur to operate and maintain our network for each year of the control period. They vary and can include, for example, costs relating to employees, office rental, IT systems and taxes. The regulator determines what is considered an efficient cost and this may be different to the actual costs we incur.

Expenditure on renewals and enhancements – the regulator assesses the capital expenditure on renewals and enhancements that we need to undertake in the control period. This expenditure is added to the regulatory asset base in the year in which it is incurred.

Allowed return – the regulator calculates the allowed return on the regulatory asset base and allows us to recover through access charges. This therefore covers, among other things, the cost of financing our capital expenditure programme.

Performance against incentives – our regulatory framework includes incentives that are designed to encourage specific actions. Failing to achieve certain minimum targets may lead to a reduction in our allowed revenue.

Our strategy

Network Rail exists to continually improve the railway while delivering outstanding value for taxpayers. To achieve this, we are driving a strategy of structured continuous improvement, in partnership with our customers, suppliers and other stakeholders, making improved safety and improved performance go hand in hand. This includes better data management, visualisation and lean techniques, as well as better costing, contractor management and route client relationships to deliver capital projects.

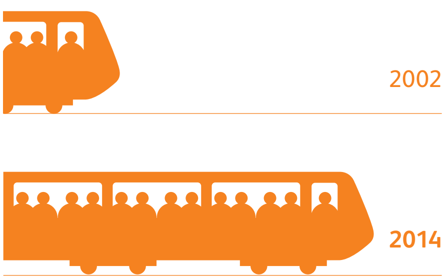
MAKING THE VERY MOST OF OUR EXISTING INFRASTRUCTURE

Despite the complex challenges of an increasingly busy network, we continually strive to make the very most of our infrastructure. We know how important a reliable, punctual and safe railway is to the passengers and businesses who depend on it every day. Our Network Operations group is at the forefront of this vital work.

IN 2014/15, THE NUMBER OF RAIL PASSENGER JOURNEYS REACHED A RECORD HIGH OF 1.65 BILLION. THERE HAS BEEN A 70 PER CENT INCREASE IN PASSENGER JOURNEYS IN JUST 12 YEARS, WITH THREE-QUARTERS OF THEM TAKING PLACE IN LONDON AND THE SOUTH EAST.

+70%

The increase in passenger journeys since 2002.



How we performed during the year

Train punctuality, which had suffered in recent years as congestion increased, has stabilised and is showing early signs of improvement. More people now arrive at their destinations on time than ever before. Our railway is the safest in Europe and passenger satisfaction remains among the highest of any major network.

Despite the many improvements in reliability, safety and efficiency in the last few years, we have a long way to go. Our focus is on accelerating the pace of improvement while dealing with the daily pressures of increasing congestion, delivering better punctuality and looking for ways to reduce costs further.

Freight services

In 2014/15 we exceeded our regulatory target for freight services, achieving 94.5 per cent against a target of 92.5 per cent. This was despite a six per cent increase in general freight traffic since 2013/14.

Passenger services

Passenger train performance continued to be a challenge as the impact of increasing congestion and disruption caused by some of our biggest projects has taken its toll. Services in England and Wales missed the public performance measure by 1.4 percentage points, mainly because of a lower level of performance in London and the south east. However, there were outstanding results in some areas, especially on our London North Eastern route and the main line into London King's Cross.

Early in 2015, Phil Hufton joined us from Transport for London to become the new managing director of Network Operations. He is driving through a programme of structured continuous improvement, with a relentless focus on getting the fundamental essentials of train performance right.

→ To find out more about our progress with redeveloping London Bridge station, see 'Infrastructure Projects' on page 22.

In Scotland, we missed our target by 1.5 percentage points. In July 2014, three times as many people as usual passed through Glasgow Central station during the 12 days of the Commonwealth Games. This huge temporary increase in passengers presented an additional challenge for us, but the team's unstinting work nevertheless helped to make the Games a great success.

Our work to make the Scotland timetable more robust has yet to filter down to better punctuality. A renewed focus on the basics and our new alliance with the train operator, Abellio, will help to drive the improvements needed.

While ever-increasing passenger growth is to be welcomed, it has presented challenges in terms of delivering both an effective service and improvements in efficiency. The impact of congestion on a network that is already almost full has had a major effect on train punctuality. This challenge, coupled with the impact of major project work, has proved more difficult to manage than we expected during 2014/15.

Freight train approaching Port of Felixstowe.

High-output train used for work on our infrastructure.

At the time of publication of this report, the ORR is investigating whether Network Rail did, or is doing, everything that we reasonably can to meet our licence conditions in relations to achieving our operational performance targets for Control Period 5 (CP5).

Structured continuous improvement

Our key objective for 2015/16 is to drive structured continuous improvement throughout the business with a clear, unerring focus on getting the basics right and using innovation and technology to help unlock efficiencies and further improvements.

We will place considerable emphasis on structured continuous improvement and roll out lean principles throughout Network Operations. We will also adopt best practice and benchmarking throughout our work, although the routes will continue to lead on their business accountabilities.

We have decided to take forward fewer initiatives than in 2014/15, to allow us to focus on those that will add the most value to the business. For example, safety and the safe work leader programme will be at the top of the list – our people and customers have the right to continue to work and travel in a safe environment.

In the first few months of 2015/16, this focus has helped deliver a halt to the slow decline in train punctuality seen over the past few years and the early shoots of improvement are starting to come through.

Key initiatives we are developing to support structured continuous improvement

Over the last year we have delivered a five per cent improvement in the reliability of our assets which are now more reliable than at any time in their history.

During CP5 we need to eliminate and/or mitigate the consequences of equipment failure, moving progressively from a 'respond and recover' regime to a 'predict and prevent' approach. To achieve this, we are increasing our understanding of how and at what rate assets degrade, enabling us to take the right decisions at the right time.

Our move to reliability-centred maintenance will involve introducing a range of tools designed to address cost, risk and performance, and embedding a culture where maintenance decisions are based on quality analysis.

Incident management

We are developing a more integrated approach to incident management across the network, involving industry specialists to help ensure that we have the right people at the right locations with plant, equipment and spares on site. Command, control and communications will be at the core of the new approach.

Managing incidents in this way will reduce the time it takes to get our teams to site and the time taken to fix problems. We will be able to deal with incidents, and their consequences, more quickly, leading to overall improvements in performance.

Safety hour

The aim of safety hour is to give our people a dedicated time to discuss health, safety and the environment, and other safety-related issues. By providing an opportunity for face-to-face discussions at all levels to address safety behaviours and conditions, it will help to improve our overall safety performance.

Depot project

Our depot project will help our teams to achieve their CP5 efficiency targets by creating the capacity in each depot to deliver more work with the resources they have. The project will focus on improving IT tools, skills and competencies in the depots, on the basis that this will lead to better decision-making and work planning.

Industry access planning

The industry access programme is an industry-wide approach to planning access to the railway infrastructure for maintenance, engineering work and train services. It is based on a proactive, joint access-planning process. The aim is to get the most out of the time we have to work on maintaining and working on our railway when trains are not running to keep it healthy and reliable.

Suicide prevention

We are implementing a number of initiatives, at route and national level, in a bid to reduce the impact of suicides on the railway. Many of these are driven by our partnership with the Samaritans, which, along with our work with the British Transport Police, Rail Delivery Group and others, is the leading influence on the rail industry's approach to suicide prevention.

In 2014/15 these initiatives included:

- Rolling out training in managing suicide contacts for front-line staff, and trauma support training for drivers and driver managers
- Preventative measures such as mid-platform fencing and signage at locations where there have been suicides or suicide attempts
- Working with local communities to predict and prevent potential suicide locations
- Trialling smart CCTV that can recognise different types of behaviour by movement and send out alerts when necessary
- Working with media outlets over their reporting of suicides on the railway, to help reduce the likelihood of copycat behaviour
- Launch of our online learning tool on suicide prevention and support
- Working with other third parties such as Public Health England to extend the reach of our work in this area

DELIVERING THE LARGEST RAIL INVESTMENT PROGRAMME IN MODERN TIMES

We are carrying out a £25bn programme of work to develop and enhance our rail infrastructure, to meet the needs of passengers and business throughout Britain.

WE ACHIEVED EIGHT OUT OF THE TOP 10 CORPORATE PROJECT DELIVERY MILESTONES EARLY OR ON TARGET IN 2014/15.

£5.1bn
Programme of works delivered in 2014/15

£1.9bn
of asset renewals

£3.2bn
of enhancement projects

What we achieved in 2014/15

As part of the largest railway investment programme in decades, our Infrastructure Projects division successfully delivered a £5.1bn programme of works in 2014/15, increasing the network's capacity, as well as improving its reliability and resilience. This work included:

- £1.9bn of asset renewals including 600km of track replacement and 700 new signalling units
- £3.2bn of enhancement projects, including work at Reading, Birmingham New Street station, the Borders Railway and on major projects for Thameslink and Crossrail.

We responded swiftly to a landslip at Harbury at the end of January 2015, completing the repairs in less than six weeks to allow the line between Leamington Spa and Banbury to re-open as soon as possible. This work included moving more than 0.3m tonnes of soil and rock.

In 2014/15 we delivered the biggest Christmas and New Year investment programme ever carried out on the rail network. 11,000 maintenance workers and engineers worked across 2,000 worksites on 300 projects. However, two significant over-runs caused considerable disruption for passengers at King's Cross and Paddington stations in London. We ensured that lessons were learnt from these incidents, as was shown by our pre-planning and strong delivery over Easter 2015.

Performance against project milestones

We achieved eight out of the top 10 corporate project delivery milestones early or on target in 2014/15. This included critical key-stage progress on the major programmes Thameslink and Crossrail, extensive station development works and complex signalling and electrification programmes.

As regards adherence to key project milestones, we achieved a schedule adherence rate of 79 per cent across all of our larger projects.

We delivered 65 per cent (45 out of 69) of regulatory enhancement milestones, which fell short of our target of 80 per cent. To help address this shortfall, we have developed an enhancement delivery improvement plan that will be implemented in 2015/16. Our performance shortfall in 2014/15 has in part led to the ORR investigating whether Network Rail did, or is doing, everything we reasonably can to meet our licence conditions in relation to delivering our enhancement projects portfolio.

Disruption caused by project work

As we rebuild the railway we inevitably cause disruption, even though we try to minimise it. Work on our major projects, such as London Bridge, reduce capacity, which in turn impacts on recovery and the network's resilience.

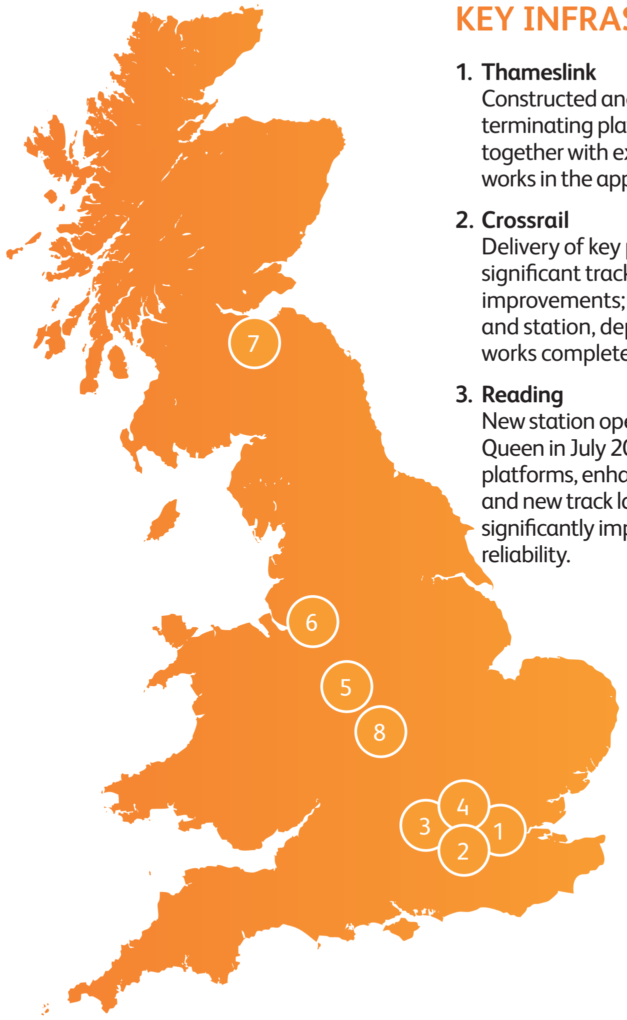
Panoramic aerial view showing the scale of our London Bridge station redevelopment.

London Bridge station redevelopment
Network Rail is transforming London Bridge station – the oldest in London – to help meet the capital's transport needs in the 21st century. The progress we made in 2014/15 included:

- completely reconstructing the low-level south side of London Bridge station and approach tracks
- constructing and opening four new platforms
- starting construction of two new Thameslink platforms and remodelling of the high-level side of the station
- installing a bridge to link the new Borough Viaduct to the station
- starting major construction work at Bermondsey to create a new junction that will be crucial to the success of the overall project.

Signal gantry being installed on the approach to London Bridge.

INFRASTRUCTURE PROJECTS CONTINUED



KEY INFRASTRUCTURE PROJECTS IN 2014/15

1. **Thameslink**
   Constructed and opened four low-level terminating platforms at London Bridge together with extensive track and signalling works in the approaches to the station.
2. **Crossrail**
   Delivery of key project milestones with significant track and overhead line improvements; signalling asset upgrades; and station, depot, bridge and subway works completed.
3. **Reading**
   New station opened by Her Majesty The Queen in July 2014, with four additional platforms, enhanced passenger facilities, and new track layouts and signalling, to significantly improve capacity and reliability.
4. **Watford**
   Signalling renewal critical to the West Coast mainline – delivering 132 new signalling units, new power supply and track renewals work both north and south of the junction and station.
5. **Birmingham Gateway**
   Construction works completed to enable September 2015 opening of the New Street station and Grand Central shopping destination, with an atrium designed to transform passenger experience.
6. **North West Electrification**
   27 miles of new electrified railway, allowing new services between Liverpool, Manchester and Wigan.
7. **Borders Railway**
   Ongoing delivery of 30 miles of new railway connecting Edinburgh Waverley Station to Tweedbank in the Scottish Borders, including seven new stations.
8. **Harbury**
   Restoration of the line between Leamington Spa and Banbury in just six weeks following a massive landslip near Harbury.

The term 'possession' refers to when a running railway line is blocked off, usually so that work by engineering trains can be carried out. In 2014/15, we handed back 98 per cent of all possessions on time or early, which was in line with our 2013/14 performance in this area.

Looking forward

The complexity of the projects we need to deliver in CP5, along with the continued high level of work planned, requires an ongoing focus on improvement.

Our move to new suppliers for track and the insourcing of the high-output track renewals team will allow us to continually improve our ability to renew track across the network and drive efficiency.

In addition, we will:

- Achieve efficiencies by reducing overheads, maximising people capacity and working collaboratively with our alliance partners within an environment of aligned efficiency targets
- Encourage greater collaboration with our partners and suppliers, to build a shared understanding of and focus on reducing cost, timely delivery, greater efficiency, and improved capability to manage risk
- Continue to target improvements in our safety record by embedding a culture of accountability, defining and applying safe systems of working, and by adopting new technology-driven solutions
- Ensure that we will only deliver change programmes if they will help us to mitigate identified risks or realise identified opportunities. For example, our programme to enhance PM3 (Projects, Portfolio, Programme Management) capability, as this will improve our planning processes and contingency management.

Main: Constructing the Doncaster Chord flyover, which takes freight trains over the East Coast main line to enable more passenger trains to run.

Above: The new 30-mile railway connecting Edinburgh Waverley station to Tweedbank in the Scottish Borders.

Right: Signalling renewal work near Watford, August 2014.

PROVIDING AN EXPERT SUPPORT SERVICE TO THE ROUTES

The safety, technical and engineering function provides an expert support service to our eight routes. It is Network Rail's single point of excellence and accountability for safety, health, sustainability, environment, engineering and asset management.

IT IS THROUGH EFFECTIVE LEARNING FROM CLOSE CALLS THAT FUTURE ACCIDENTS CAN BE PREVENTED. IN 2014/15 WE COMFORTABLY BEAT OUR TARGET FOR CLOSE CALLS REPORTED (71,237 AGAINST A TARGET OF 40,000).

Safety – how we performed in 2014/15

Passenger safety

This year the number of specified injuries and minor reportable accidents experienced by passengers on the railway fell significantly. However, changes in reporting requirements under the Reporting of Injuries, Diseases and Dangerous Occurrences Regulations (RIDDOR) 2013 mean that it is not possible to provide a direct comparison with our 2013/14 performance for passenger safety.

The passenger component of train accident risk, where Network Rail is the risk controller, decreased to 1.866 against a target of 2.158 fatalities and weighted injuries per annum. (The lower the score the better our performance.)

Slips, trips and falls are the main cause of passenger injuries at our 18 managed stations and, to reduce their number and severity, we continue to focus on managing crowd flow and influencing passenger behaviour. In 2014/15, at our managed stations, there was one passenger fatality and four RIDDOR specified injuries.

Workforce safety, health and wellbeing

Among our workforce, the lost time injury frequency rate at the end of 2014/15 was 0.568 against a target of 0.486, compared with 0.572 in 2013/14. There were two fatalities during the year. There were 95 RIDDOR specified injuries, compared with 121 major injuries in 2013/14 (of which 101 would be classified as a specified injury under the new RIDDOR guidelines). Slips, trips and falls remained the most common cases of accidents among the contractor workforce.

Close calls

It is through effective learning from close calls that future accidents can be prevented. Our close call system enables us to record and manage such incidents. In 2014/15, we comfortably beat our target for close calls reported, and 47 per cent of those close calls were closed in 28 days against a target of 50 per cent. (This result excludes close calls managed through our contractors' systems.)

A small proportion (3.5 per cent) of close calls relate to environmental issues. In 2014/15 we closed 66 per cent of these within 28 days, compared to 25 per cent in 2013/14.

Public safety

During 2014/15, there were 21 accidental adult fatalities across the network, nine of which occurred at level crossings, and one accidental child fatality at a level crossing. In addition, there were 294 suicides on the railway infrastructure.

Martin Power and Robert Duncan, construction managers on our Borders Railway project – the largest domestic railway to be built in Britain in 100 years.

SAFETY, TECHNICAL AND ENGINEERING CONTINUED

Train passing through full-barrier level crossing.

OUR SAFETY VISION

everyone home safe every day

- Our vision for safety is that everyone returns home safe every day – our passengers, our customers, and our people.
- Safety is at the core of everything we do – from the work of our board to that of every colleague at every depot, station, signal box and office.
- We believe that safety performance and business performance go hand-in-hand.

Level crossing risk

During 2014/15, we closed 118 level crossings. There was an eight per cent reduction in level crossing risk (measuring benefits only) during the year, but we did not achieve our target of 10 per cent. There were 311 near misses at level crossings with pedestrians and road vehicles, seven per cent fewer than in 2013/14.

Our aim is to reduce level crossing safety risk by 25 per cent in Control Period 5, through more level crossing closures and other risk reduction measures. We continue to focus our efforts on achieving the most cost-effective risk reduction, closing crossings wherever possible and ensuring that the public understand the risks of unsafe use of crossings.

Independent review of our safety culture and performance

In autumn 2014, we commissioned DuPont Sustainable Solutions to independently evaluate and benchmark our organisation's safety culture and performance. The review involved interviews with more than 200 staff and a number of site visits. It concluded that Network Rail had made significant progress in transforming safety since 2012, but there remain further opportunities for improvement. When benchmarking us against other organisations in the rail sector, the review found that the strength of our safety-reporting culture and our reported injury rate was above the sector average.

The review identified potential for improvement in the following areas:

- Leadership and accountability
- Employee engagement
- Managing interfaces between business units
- Change programmes, and
- Contractor management.

In response, our executive committee agreed an action plan that builds upon many existing work streams in Network Rail.

Key initiatives we have under way

Key to developing an inclusive safety culture at Network Rail will be a change in associated behaviours among our workforce. In 2014/15, as part of this work, we refreshed the Lifesaving Rules that we had introduced the previous year.

We also continued to implement our 10-point strategic plan for improving workforce safety and moving towards our target of eliminating workforce fatalities and major injuries. The plan includes a range of targeted interventions, including:

- Increasing clarity about people's roles and responsibilities when working trackside
- Investing in new technology to help ensure our people remain safe when working trackside
- Ways of ensuring that we treat people fairly when determining accountability for incidents
- Ways of implementing the learning gained from incidents
- Our approach to planning our work, and
- Ways of ensuring that our approach to safety is embedded in all our contractors' work practices.

One of our fleet of tilting wagons that enable us to transport pre-assembled infrastructure and track.

Asset management – how we performed in 2014/15

Throughout Control Period 5 (2014 to 2019), our measure of performance for asset management is the composite reliability index (CRI). Unlike the asset stewardship index used in Control Period 4, the CRI contains weightings that recognise that similar failures can differ significantly in their impact, depending on where they occur on the network.

In 2014/15, reliability improved across a range of key assets including points, track, signalling and electrical power.

However, telecoms assets experienced more failures than in 2013/14, principally as a result of software issues associated with implementing the new communications system between signallers and train drivers (Global Systems for Mobile Communications – Railway). New software was then tested and proved reliable and the train operating companies are now rolling it out to every train on the network.

We exceeded all of our improvement targets for the reliability of our buildings, structures (including bridges and tunnels) and earthworks (embankments and cuttings).

Key initiatives we have underway

Work towards accreditation under ISO 55000

We continue our overarching programme of improvement, addressing all aspects of how we manage our assets. We are working towards accreditation under ISO 55000, the International Standard Organisation's specification for the optimised management of physical assets. We contributed to the development of the specification as part of our patron role with the Institute of Asset Management.

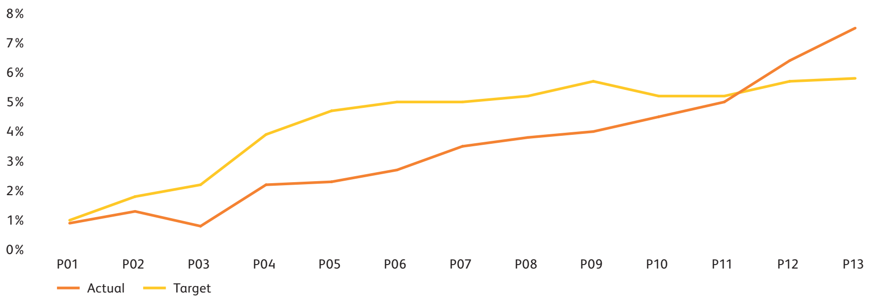
Increasing reliability

Other initiatives include further increasing the reliability of our assets and reducing the number and consequence of failures, whether track, points or signals. Achieving this will rely on a process of continuous improvement using targeted maintenance, lean techniques of working and the latest technology.

ORBIS and 'predict and prevent'

Network Rail's ORBIS programme (offering rail better information services) is key to our move from an approach based on 'respond and recover' to one of 'predict and prevent'. This significant investment in our asset information data and systems makes it easier to capture information through the deployment of hand-held devices and advanced train-borne systems. It gives us better information about how the network is performing, the condition our assets are in and helps us to understand where future investment should be targeted.

Composite Reliability Index (% improvement against baseline) 2014/15

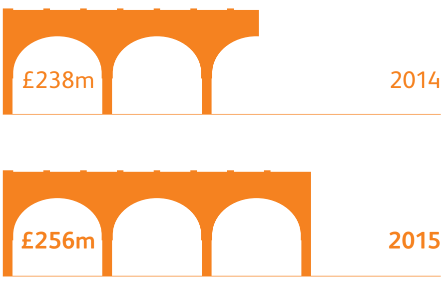


NETWORK RAIL PROPERTY

We provide high-quality professional property expertise that reduces industry costs, improves the passenger experience and creates great places for people, businesses and communities to thrive.

WE CONTINUE TO OPTIMISE OUR LAND USE TO FACILITATE THE EXPANSION OF THE NETWORK AND PROVIDE A GROWING AND IMPORTANT SOURCE OF FUNDING FOR THE RAILWAY.

+8%
Increase in income from Network Rail property



Our property's role in the future of the railway

The continued growth in rail travel is recognition of the level of service now offered to customers by the rail industry. It also reflects continued urbanisation, the need to be constantly in touch (the digital age) and society's drive towards a more sustainable future.

Our station and land assets will play a key role in the future growth of the rail network. Not only can we provide world-class modern station environments with the facilities expected by modern customers, but also the space for business and communities to grow and prosper. Furthermore, we continue to optimise our land use to facilitate the expansion of the network and provide a growing and important source of funding for the railway, thereby reducing the burden on tax payers.

Key initiatives we have underway

We have an ambitious growth agenda for Control Period 5 that will not only boost our income but also help to regenerate areas around our estate and bring more class-leading environments to rail passengers, colleagues, tenants and neighbours.

Over the next four years we will invest in improving our station facilities, enhancing the quality of our commercial assets and making our unique places extraordinary.

Our strategy is to use operational land to create development sites, and through partnering with developers, help regenerate our stations and surrounding areas, releasing capital to fund the railway.

Best station food and drink outlet in the world

The National Rail Passenger Survey revealed an increase in passenger satisfaction across all of our managed stations, with King's Cross, London, coming out on top with 95 per cent satisfaction. King's Cross also won the award for the best food and drink outlet at a station in the world (the Parcel Yard pub) at the annual international Airport and Rail Station Food and Beverage Awards 2014.

Retail outlets in the redeveloped King's Cross station, London.

£982m
Value of our investment property portfolio
2014 £856m

£256m
Commercial property income
2014 £238m

96.4%
Occupancy rates at our business space estate
2014 96.3%

547,500 sq ft
Rental space at our managed stations
2014 510,000 sq ft

+6.2%
Network Rail managed stations
British Retail Consortium +0.5%

Like-for-like retail sales growth from 1 April 2014 to 31 March 2015

Redeveloped railway arches at Prowse Place, Camden, London.

DELIVERING A RAILWAY FIT FOR THE FUTURE

In 2014/15 we continued to deliver services that improve Britain's economies and communities and the wider environment. In recognition of this, Network Rail was awarded four (out of five) stars in the 2015 Business in the Community Corporate Responsibility Index.

BY ADAPTING MOBILE FLASH BUTT WELDERS… WE CAN NOW FIX RAILS IN A QUARTER OF THE TIME AND WITH LESS DISTURBANCE TO OUR NEIGHBOURS.

Network Rail was awarded four (out of five) stars in the 2015 Business in the Community Corporate Responsibility Index

Environment

Managing our land and protecting our environment

During the severe winter of 2013/14, many trees fell onto the track resulting in train delays and risk of accidents. We assessed vegetation in all areas where trees had fallen and removed trees where the risk of future fall was unacceptable. This resulted in public and media scrutiny, and in some cases we needed to suspend work. We have put in place the necessary procedures to balance our biodiversity obligations with those of providing a safe, efficient railway.

Fixing defective rails used to be time consuming and noisy for our lineside neighbours. By adapting mobile flash butt welders, to make them lighter and quieter and to prevent them interfering with signalling and telecommunications equipment, we can now fix rails in a quarter of the time and with less disturbance to our neighbours.

Waste management

Because of increased volumes of renewals and enhancements to our network, the volume of waste we produced increased this year. However, we are reusing and recycling ever more materials such as ballast; this year we sent just 11.6 per cent of waste to landfill compared to 13.4 per cent in 2013/14.

The Borders Railway Project has used innovative design to remove the need for 0.3m tonnes of material. Around 0.7m tonnes of material has been reused to restore seven adjacent sites. The project is on course to divert almost 1.1m tonnes of material from landfill by its completion – the equivalent of a diversion rate of 98 per cent.

Our Scotland route has dramatically improved its waste management, reducing volumes by 10 per cent, increasing the percentage of waste recycled from 19 per cent to 66 per cent, and delivering almost 30 per cent reduction in associated costs.

Our carbon footprint

We are committed to reducing our carbon footprint and our spend on energy. However, the expansion of the network makes this particularly challenging and in 2014/15 our emissions increased by nine per cent.

We track 86 per cent of our non-traction energy consumption through automatic meter readings, enabling us to recover £3.2m in overcharges in 2014/15. We have renegotiated contracts to produce savings of £1.57m over two years and changed our energy contracts to buy from less carbon intensive sources. Furthermore, this year we produced over 744,000 kWh from renewable energy technologies on our estate.

We demonstrated a groundbreaking solution for bringing the benefits of electric trains to branch lines, where electrification itself is not feasible. We created an independently powered electric multiple unit by adding a lithium battery to a modified class 379 train. This passenger service ran between Harwich International and Manningtree stations and we are now evaluating data on performance.

19% → 66%
(2013/14) (2014/15)

Percentage of waste recycled by our Scotland route

10,997
Number of hours 815 of our people spent doing voluntary work for charity in 2014/15

Karen Chiles, Infrastructure maintenance protection coordinator, and Martyn Cox, tree surgeon, assess lineside vegetation in Birmingham.

Natural resources and embodied carbon
In 2014/15 we trialled the rail industry toolkit developed by the Rail Safety and Standards Board to measure and reduce embodied carbon on several projects, including alternative embankment stabilisation and footbridge construction methods.

Our Northern Hub programme team used carbon assessment techniques to inform the design and construction of the Ordsall Chord that will link Manchester Piccadilly and Manchester Victoria Stations. The opportunity to save 17,233 tCO^2e has been identified and implemented. On our Huyton and Roby scheme, between Liverpool and Manchester, the project team anticipates reducing the project's carbon footprint by up to 12 per cent by using lower carbon cement.

Weather resilience and adapting to climate change
We created our weather resilience and climate change programme in response to problems caused by the severe winter of 2013/14. In 2014/15 we published eight weather resilience and climate change adaptation plans, which explain how weather can affect the railway, the potential impact of changes in our climate, and what we are doing to mitigate the impacts of weather and climate change on our infrastructure.

The programme has also supported an update to the rail industry's process for working together during times of extreme weather, advice on lineside vegetation management and a trial to remotely monitor the condition of our embankments and manage the risk of landslides.

We are involved in forums that are finding solutions to flood risk in the south west of England – for example, in Exeter, Dawlish, the Somerset Levels, Plymouth and at Cowley Bridge Junction. We are also researching how changes to rainfall could affect the risk of river erosion of material at our bridges, so we can better manage these assets.

Social impact
When young people get onto our track, there is danger to them and disruption to us. There were more than 1,000 such incidents in 2013/14. Our Rail Life team explains how to stay safe around our network to young people and schools. In 2014/15 we partnered with the Football League Trust and 10 football clubs, including Leeds United and Portsmouth FC, to communicate key facts about railway safety to young people.

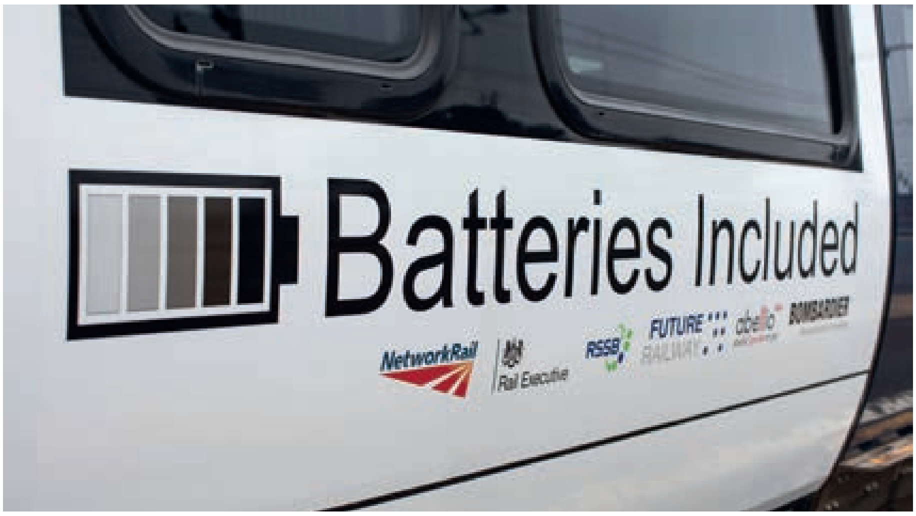
We continued to inspire tomorrow's workforce by working with students aged 11 to 18 years on careers guidance and science, technology, engineering and maths projects lasting between a few hours and eight weeks. In 2014/15 we ran programmes in Leicestershire, Glasgow, London and other areas.

We revised our approach to volunteering so that a wider range of charities can benefit from the five days of volunteer time that each of our people can contribute each year. In 2014/15, over 40 per cent of our volunteers' time was spent with projects that enabled them to be a caring neighbour, such as hospices and charities for disabled and homeless people. Volunteers also used their technical skills to support railway heritage and gardening, vegetation and wildlife projects.

This year we contributed more than £1.8m to our charity of choice, CLIC Sargent, through payroll giving, charity fundraising and in-kind giving. We helped other charities to raise over £784,000 through collections at our managed stations. We became a founding member of the Fundraising Standards Board's Railway Industry Charity Cash Collection Forum, to share knowledge and drive a consistent approach to charity collections at stations.

We recruited 204 new apprentices in 2014/15 and now directly employ a total of 591 apprentices. Several thousand more work within our supply chains – for example, on projects at Birmingham New Street, London Bridge and Crossrail.

HOW WE ACT RESPONSIBLY CONTINUED



Before and after percentages for people attending our 'Time to Change' awareness events:

27.4 → 44.6%

'strongly' agreed they would be comfortable discussing mental health issues at work

56 → 79%

'strongly' agreed that Network Rail cared for their health and wellbeing

Above and left: A battery-powered train we developed with industry partners, which could bring environmental benefits to branch lines.

Diversity and inclusion

To make our network more accessible, we have completed significant improvements to 150 stations since 2006, including installation of more than 1,000 lifts. In 2014/15 we consulted our built environment accessibility panel on the accessibility of redevelopments of many of our stations, including Leeds and Gatwick airports. We continue to employ disabled consultants to train our station staff, so that they better understand and can reduce the challenges faced by disabled passengers. We contributed to 'Working Together', a rail industry guide to encourage a better customer experience for rail passengers using wheelchairs, and are collaborating with public and industry bodies on a range of inclusive design initiatives.

Business in the Community awarded Network Rail 'silver' in their national benchmark surveys for gender and race diversity and inclusion. We were also awarded Positive about Disability accreditation by the Department for Work and Pensions.

This year we published our diversity and inclusion strategy, 'Everyone'. We grew our network of diversity champions, equality representatives, sponsors, local programme workstream leads and our six staff networks, which now have over 1,000 members. Over 2,000 of our managers have now been trained on inclusive leadership.

We have signed up to Barclays' Life Skills work experience programme, Your Life campaign and the Women In Science and Engineering's Ten Step Plan to get more women into engineering.

Our diversity profile

Percentage of workforce that is female	14.80%
Percentage of workforce that is Black, Asian and Minority Ethnic	6.10%
Percentage of workforce that is disabled (of staff who completed the question)	3.00%
Percentage of workforce that is lesbian, gay or bisexual (of staff who completed the question)	4.00%

Investing in our people

The health and wellbeing of our people

To help reduce preventable health conditions, we rolled-out mobile health kiosks where our people can check their body mass index, body fat level, blood pressure, heart rate and cardiovascular risk. More than 11,000 of them have used the kiosks already. We also launched a portal offering advice on health and wellbeing in a range of formats – videos, presentations, guides and podcasts.

On the mental health front, we worked with psychologists Robertson Cooper Ltd to develop an online tool through which an individual can get a basic assessment of their mental and physical wellbeing, and workplace stress risk factors, plus their own printable report. We held events nationwide to increase our people's awareness of Network Rail's public commitment to 'Time to Change', MIND's campaign to eliminate the stigma surrounding mental health issues.

Another major focus was educating front-line staff on the health risks of exposure to hand arm vibration. As a result, their engagement with our occupational health surveillance programme rose to 64 per cent (from 24% in 2012/13).

Engaging with our people

To build a high-performance culture, we need engaged employees who have the freedom to innovate and the confidence to challenge the status quo. The ways in which we facilitate this include the group intranet, regular management briefings, internal films, staff magazines and news bulletins. In addition, we hold annual business briefings at locations throughout Britain to update our people on the organisation's direction and give them the opportunity to challenge our directors and senior managers.

Above: Leson Blake, customer service assistant, mobility, at Birmingham New Street station.

Left: By October 2014 we had installed 1,000 lifts at stations to ensure easier access for passengers. Reading station passenger lift (courtesy of Stannah).

In response to feedback from our 2013/14 employee engagement survey, we redesigned our 'Engaging Managers' workshops to make them more interactive and developed a Sharepoint site that provides a wealth of engagement resources and tips. We launched an online tool on which people managers can record and share their engagement action plans – 500 had been recorded by March 2015. In addition, we set up project teams at a local level throughout the organisation, which have already developed and launched a variety of activities shaped by employee focus groups.

Developing our people

Recruitment, development and training are the cornerstones of our management system. We continue to review and enhance the processes we employ to ensure that we consider equality, disability, ethnicity, capability, competence and business needs as part of our recruitment and employment process. In addition, our policy is to offer training and career development to disabled people that is, as far as possible, identical to that offered to other employees.

We support a number of award-winning career-entry programmes to refresh our talent pipelines – for example, apprenticeships, graduate recruitment and sponsored MSc and HND courses.

BUILDING A TRANSPARENT AND ETHICAL ORGANISATION

We believe strongly in being transparent with our customers and stakeholders, and in behaving ethically in all areas of our business. For example, this year we proactively made more of our information publicly available than ever before and held our first ever ethical business behaviour panel discussion, led by Mark Carne.

Our transparency work

In April 2014 we asked people whether they thought we were a transparent organisation. Thirty-three per cent said that they thought we were.

While this is a promising start, we know that we have a long way to go to achieve our ambition of setting the standard for transparency. Our poll showed that now we are part of the public sector people expect us to be more open as a matter of course.

Freedom of information

In March 2015 we became subject to the Freedom of Information (FOI) Act. In less than seven months our implementation programme had put in place the people, systems and processes we need to manage requests for information. We see FOI as an opportunity to be more open and accountable, and our reputation for being transparent relies to a significant extent on managing our response to it in a positive way. As the number of requests we receive increases, so will our understanding of what people want to know about us, this insight will inform our wider transparency work.

Engaging others in our work

A key feature of the year for us was broadening our reach to a range of different audiences. Our bi-annual transparency debates are now an important focus of our work. They continue to attract interesting panel members, large audiences and a wide range of opinions. Our challenge panel – made up of experts from the private and public sectors – meets twice a year and has played a vital role in holding us to account in this area.

We have been more vocal about our transparency work: as well as launching a newsletter that provides a quarterly update on our work, we hosted a number of guest blog posts focusing on the benefits of transparency in business. Maintaining our proactive activity and ensuring our stakeholders remain engaged and as many people as possible are aware of our proactive work is even more important, now we are subject to the Freedom of Information Act.

By making changes to our web pages and publishing more relevant, accessible and interesting information, we have increased the number of hits to our datasets to over 60,000 a quarter. Our ‘delays explained’ series remains the most popular.

Proactive publication

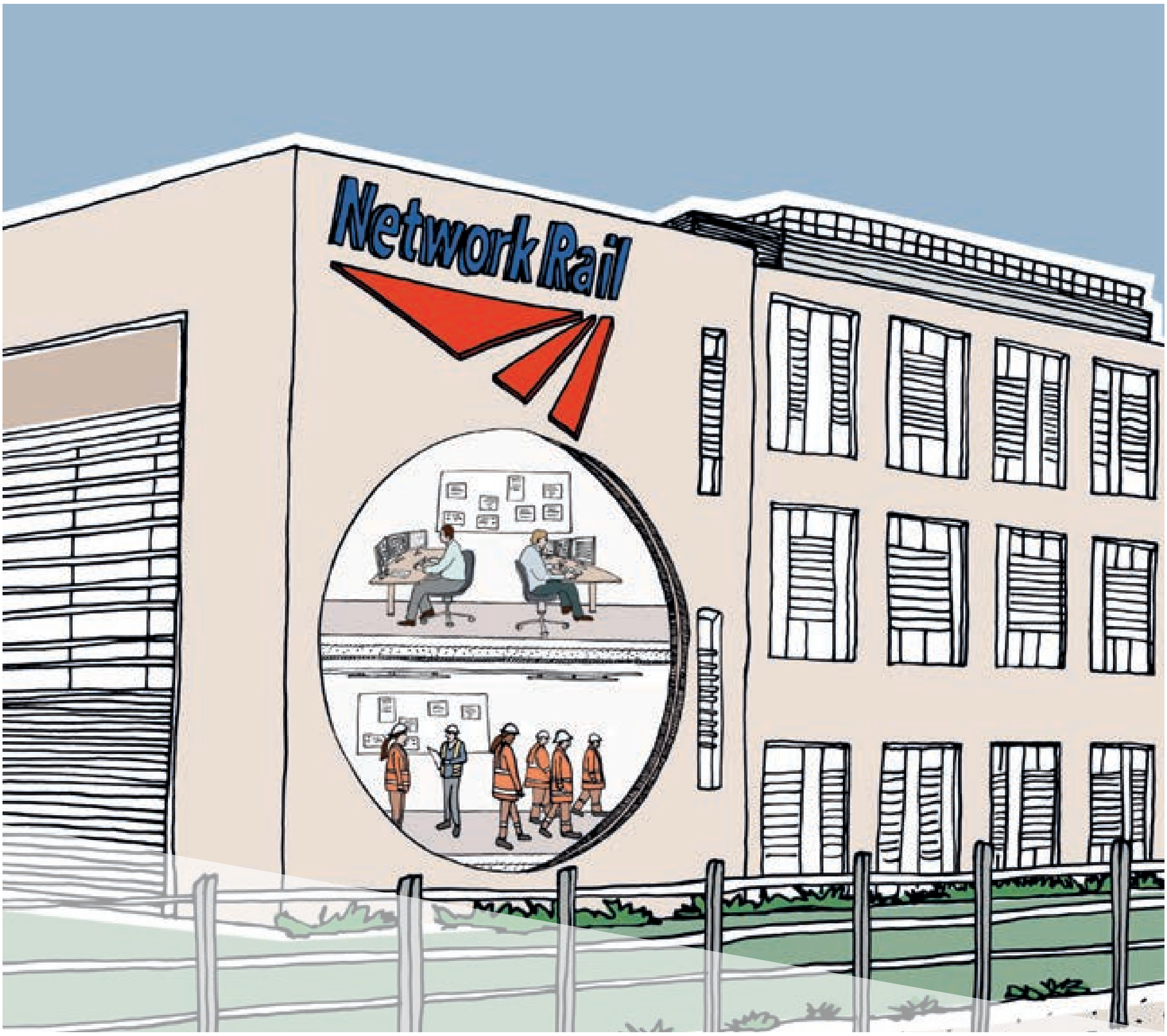
We exceeded our target for proactive publication in 2014/15. We published 34 new categories of information, and collaborated with Passenger Focus on our August 2014 release, which had a positive effect on coverage. Our real-time train running data feeds also remain popular, with the number of registered users increasing and with it the number of apps and web pages using the data. We ran the first cross-rail industry hackathon in conjunction with the Rail Delivery Group and the Association of Train Operating Companies, and have partnered with other organisations – such as Bloomberg and the Hack Train – to increase awareness of our open data feeds and help deliver real benefits and choice for passengers.

In 2015/16 we will be focusing on publishing even more new categories of information as part of our proactive publication scheme. We want to improve the quality and reliability of the data and information we publish, attracting more people to both. We will also be expanding our open culture work – achieving a baseline measure for the number of employees who think their teams work in an open way, and increasing on this over the year. By developing our work in this way, we will be able to make Network Rail even more open.

Ethical business behaviour

Our transparency and ethics day saw us get out into the company to talk about our way of working. As part of the day we held our first-ever ethical business behaviour panel discussion, headed up by chief executive Mark Carne. The panel of experts discussed the standards of business behaviour expected of everyone working at or on behalf of Network Rail. The event was a huge success in raising awareness of our code of business ethics.

2014 saw us introduce the Not So Superheroes to Network Rail. This group of characters showed our employees in a light-hearted way how breaching our code of



business ethics can damage the reputation of the group, as well as the individual concerned. Each month we introduced a new character highlighting a different example of unethical behaviour – ranging from Mrs Silence to the Diversity Destroyer. The campaign prompted a surge in reports to our Speak Out line and an increase in the number of enquiries to the ethics inbox.

We continued to show our support for employee whistleblowing by becoming a signatory of Public Concern at Work's First 100 campaign. The campaign was a result of a report conducted by the Whistleblowing Commission that recommended a statutory code of practice supporting whistleblowing arrangements for employers and employees. By becoming a signatory, we agreed to abide by the principles in the code of practice and work towards compliance.

In October 2014 we launched our refreshed policy on conflict of interest and outside activities. After the business had been briefed on the policy by HR, there was a 162 per cent increase in submissions on the declaration of interests register compared to the same three-month period in 2013/14.

Looking forward to 2015/16

Our biggest project next year will be delivering company-wide ethics training. This will take the form of e-learning for desk-based staff, video briefings for operational staff and face-to-face workshops for high-risk groups (those individuals with the highest exposure to ethical risk). The training will cover topics like anti-bribery, fraud and conflict of interest, with interactive dilemmas designed to enable people to make the right decisions even when the right course of action may not be clear-cut.

OUR APPROACH TO RISK MANAGEMENT

Our assets across the country work 24 hours a day seven days a week to provide a safe, reliable rail network. With so many assets working with often extreme environmental pressures, occasionally things break down.

WE IDENTIFY RISKS FROM A STRATEGIC VIEW (TOP DOWN) AND FROM THE OPERATIONAL ENVIRONMENT (BOTTOM UP) TO GIVE BETTER VISIBILITY OF RISK EXPOSURE ACROSS THE ENTERPRISE.

We are committed to rectifying issues quickly in order to maintain service provision. We are also committed to improving our assets through our enhancement and maintenance programmes. We recognise the impact of disruption on both the public and our commercial customers and strive to minimise disruption.

The purpose of our Enterprise Risk Management (ERM) approach is to mitigate risks to the delivery of a safe, reliable and cost-effective service to our customers. ERM supports the building of capability in all areas of the business to recognise both risk and opportunity early. Early recognition of risk allows us to work collaboratively and proactively with customers, stakeholders and suppliers to manage our extensive portfolio of works better. Structured continuous improvement (see page 21) enables us to constantly develop ways to improve.

Introduction

Across the group our approach to risk management balances the need to manage risks with identifying opportunities to improve performance through careful acceptance of some risk. We recognise our status as a regulated rail network infrastructure provider and the importance of maintaining essential service provision. We also recognise that things do not always go as planned and the overruns at Christmas 2014 reminded us of the need to manage potential impact to the travelling public better. We have looked hard at our assessment of risk within our works portfolio and taken steps to improve. Our Easter 2015 programme of works took a much harder look at risk reduction with a successful outcome. The nature of the Network Rail business is such that there are some significant risks. These are outlined in the 'Key Strategic Risks' section (page 40).

Embedded risk management processes

We take an enterprise wide approach to risk management and have in place an ERM framework for the identification, analysis, management and reporting of all risk to strategic objectives. The framework also takes account of operational risk and recognises the need for specialist approaches in areas such as safety, project management and information security. The use of a standard risk assessment matrix and defined risk appetite supports and enables the integration of the strategic and operational risk management approaches. Clear escalation criteria and the introduction of business assurance committees across the business provide the structure to enable visibility and challenge the management of risks.

While the ultimate responsibility for risk management rests with the board, it delegates the more detailed oversight of risk management and internal control principally to the audit and risk committee (see page 56) which reports the findings of its reviews to the board.

The audit and risk committee receives regular reports from the internal and external auditors and reviews progress against agreed action plans to manage identified risks.

Work at night to upgrade the rail network.

Detailed oversight of safety related risks is delegated to the safety, health and environment committee (see page 54).

The board's responsibilities for the internal control system

The board is responsible for our internal control systems and for reviewing their effectiveness. Such systems are designed to manage, rather than eliminate, the risk of failure to achieve strategic objectives. They can only provide reasonable (rather than absolute) assurance against material misstatement or loss.

The audit and risk committee, on behalf of the board, reviews the effectiveness of the systems of internal control under review and has done so throughout the year.

Monitoring and reviewing internal controls

Our Internal Audit function provides independent assurance on the adequacy and effectiveness of the system of internal control.

Following each internal audit, a report is produced showing the findings which are reported to senior management and any corrective action is agreed. Summaries of these reports and details of progress against action plans are presented to the audit and risk committee at each meeting for discussion and review.

In accordance with the Turnbull Guidance, an annual review of internal controls is conducted. The board has delegated authority to the audit and risk committee to monitor regularly internal controls and conduct the annual review. This review covers all material controls such as financial, operational and compliance, and also risk management systems in place throughout the year under review. No significant failings or weaknesses were identified from this review.

During the course of its review of the systems of internal control, the audit and risk committee 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 its internal control framework and uses the opportunity to review internal control processes against incidents when they arise in order to promote structured continuous improvement of our internal control systems.

Our Enterprise Risk Management process

The ERM framework provides a standardised approach to the identification, assessment, recording and reporting of significant risks. We analyse the possible causes of a risk and assess what the impact could be if the risk was to occur. By using standard risk assessment criteria based on our performance targets we are able to have a visible link to the achievement of objectives.

For each risk we identify current controls and their effectiveness to manage underlying causes and minimise consequences. The full risk assessment process is conducted using the BowTie methodology which provides a structured approach. We identify risks from a strategic view (top down) and from the operational environment (bottom up) to give better visibility of risk exposure across the enterprise.

Monitoring risk exposure and the effectiveness of the controls in place is an ongoing part of risk assessment. The introduction of early warning indicators is one of the current areas of improvement activity within the framework. The use of indicators and monitoring of controls will be enhanced greatly with the onset of business critical rules. The business critical rules framework underpins the management of risk by providing policy and means of control. Our Lifesaving Rules are the first 10 business critical rules. The rules are based on understanding what our top risks are, what we need to do to manage them and how to check we are managing them well.

Through the use of our risk appetite (see panel to the right) we understand better our capacity to manage risk outcomes and can make decisions on the need to enhance controls to further mitigate both likelihood and impact.

Identifying our categories of risks (ie, safety, performance, value) and who manages them

All strategic risks are mapped to performance reporting and strategic objectives. The assessment of risk is informed by the performance targets and the company's risk appetite statements. Each risk is allocated to an executive committee owner.

Network Rail has defined its risk appetite statements as follows:

'Network Rail has no appetite for safety risk exposure that could result in injury or loss of life to public, passengers and workforce. Safety drives all major decisions in the organisation. All safety targets are met and improved year on year.

In the pursuit of its objectives, Network Rail is willing to accept, in some circumstances, risks that may result in some financial loss or exposure including a small chance of breach of the loan limit. It will not pursue additional income generating or cost saving initiatives unless returns are probable.

The company will only tolerate low to moderate gross exposure to delivery of operational performance targets including network reliability and capacity and asset condition, disaster recovery and succession planning, breakdown in information systems or information integrity.

The company wants to be seen as best in class and respected across industry. It will not accept any negative impact on reputation with any of its key stakeholders, and will only tolerate minimum exposure ie, minor negative media coverage, no impact on employees, and no political impacts.'

RISK MANAGEMENT CONTINUED

KEY STRATEGIC RISKS

Risk Area: **Safety**

Risk	Risk owner	Current Actions	Planned
Failure to safeguard our workforce resulting in single and/ or multiple fatalities to Network Rail staff (employees and contractors)	Group STE director	• Lifesaving Rules refreshed by aligning them to the risks most likely to harm our workforce, with a renewed focus on taking personal responsibility • 71,000+ close calls reported against a target of 40,000 in 2014/15 with an average 28 day close out rate of 47 per cent • Establishing the role of safe work leader as the single accountable person on site for both safety and performance through the planning and delivering safe work programme • Ongoing development of the driving safety programme and publication of a new driving policy enforcing key risk controls including a prohibition on the use of motorcycles for company business • Successful award of new contingent labour contracts, with minimum health and safety provisions built in to drive improvements in the supply chain • Transport for London sign-up to Sentinel enabling the sharing of working hours and other safety critical information on one card for one railway	• Implement an electrical safety delivery programme focusing on improved isolation methods, better test equipment, clearer accountabilities and an improvement in competence/training • Establish a fatigue risk management programme aligned to a new policy and deliver a fatigue risk tool kit for line managers to help reduce stress and tiredness related incidents • An industry-wide common induction is to be mandated across all infrastructure projects – bringing all contractors into Sentinel and therefore creating a single card to drive out double shifting
Failure to adequately manage the railway infrastructure and prevent a major avoidable event eg, (collision, derailment etc.) leading to loss of life or major injury to passengers	Managing director, Network Operations	• Workshops held with professional heads (technical engineering) to identify key initiatives/ workstreams that contribute towards train accident risk reduction • 300+ tubular stretcher bars installed to improve track safety • Trials currently underway for key technology interventions such as remote monitoring for earthworks • A new control framework in the form of business critical rules rolled-out for plain line track • Development of a more consistent risk evaluation methodology for safety hazards, leading to an improved understanding of risks and prioritisation of improvement activities	• Continued roll-out of new control framework in the form of business critical rules to all asset systems • Implement drainage policy – targeting embankment stability and track bed stability • Roll-out of plain line pattern recognition – delivering a better understanding of track condition and track faults – increase volume of monitoring undertaken
Inadequate management of the interfaces between the public, passengers, trains and railway infrastructure leading to loss of life or major injury to the public and/or passengers	Group STE director	• 118 level crossings permanently closed • 9 crossings downgraded in status • 66 crossings temporarily closed, eliminating risk whilst permanent risk reduction measures are developed • Community safety strategy developed and key initiatives delivered including partnerships with Rail Life, a youth initiative to raise awareness of level crossing safety and other rail issues, local schools, youth groups and football league	• Closure of an additional 88 level crossings (subject to feasibility studies and liabilities negotiations) • Product approvals and enhancement programmes to deliver national roll-out of new systems • Enhancements to the level crossing risk model to improve the accuracy of risk modelling and calculations of level crossing risk • Development of a harmonised asset strategy focussed on improving asset management, introducing modular assets and promoting technological development; facilitating the introduction of automatic full barrier and other solutions • Targeted localised campaigns aimed at segmented user groups; eg, dog walkers, pedestrians and cyclists, farmers and landowners

Risk Area: **Performance**

Risk	Risk owner	Current Actions	Planned
Failure to achieve passenger and train operating company (TOC) and freight operating company (FOC) performance expectations for the control period	Managing director, Network Operations	• Timetable rules improvement programme strategy implementation to address root cause of Public Performance Measure (PPM) failures • Delivery of business critical rules, risk based maintenance and remote condition monitoring programmes • Regenerated understanding of the relationship of inputs to performance outputs • Periodic reviews and challenge of route/TOC performance delivery in line with trajectory • Quarterly review of TOC based performance strategies in order to maintain alignment and relevance between the input plans and performance outputs • Asset management plans underpinning the Composite Reliability Index and supporting a reduction of PPM failures • Fleet reliability improvement plans	• New five-year performance strategies developed collaboratively with routes and train operators • Timetable rules improvement programme to focus on improving the timetable and unlocking further operational performance • Establishment of wider right time railway groups in order to reduce performance failures from operational delivery • Development of specific station level improvement plans to neutralise the increasing impact of passenger crowding especially in the London and South East market sector • Strengthening of service recovery and contingency plans in order to reduce the spread of reactionary delays • Review delivering work within possessions (DWWP) framework and implement required improvements
We may be unable to sufficiently recover the infrastructure from a disruptive event (catastrophic asset failure, cyber-attack, extreme acts of weather etc.) within acceptable timescales	Managing director, Network Operations	• Design of a group-wide integrated approach to business continuity management • Design of a company-wide strategy to implement cyber and information security programmes aligning business areas, functions, technology platforms and governance frameworks	• Increased focus on improvement of incident management processes and procedures • Weather resilience and climate change programme board to continually assess vulnerability of assets • Further strategic and tactical investment to provide a more resilient network and systems landscape that will perform effectively under increased stress
Failure to adequately manage our assets and inability to demonstrate excellence in asset management	Group director, Digital Railway	• Major investment programme in asset information – ORBIS (Offering Rail Better Information Services), in order to improve asset information for better decision making and achieving targets • A business wide change programme to deliver improvements in asset management, through the achievement of an independently assessed excellence rating of 72 per cent by January 2018 • Measurement against the Asset Management Excellence Model (AMEM), an accepted and proven means of measuring progress in asset management capability • Whole life cost modelling integrated with asset policy development	• Cross functional programme to create alignment of maintenance initiatives to deliver improvements and consistency in how works are planned and executed • Conduct annual 'AMEM lite' assessments to demonstrate structured continuous improvements in asset management capability • Support 'AMEM lite' with an increase in the number of subject matter experts to become self-sufficient in the assessment process and to develop a progressively positive cultural change towards asset management

RISK MANAGEMENT CONTINUED

KEY STRATEGIC RISKS

Risk Area: **Value**			
Risk	**Risk owner**	**Current Actions**	**Planned**
Failure to plan or deliver the CP5 outcomes, including regulated outputs	Group finance director	• Improving the governance around all projects and programmes and confirming alignment with 2019 outcomes and strategic themes • The business review team setting up a central 'controlling' function for CP5 and beyond • Maintain strong union relationships reinforced by continuous dialogue • MSP4NR (Managing successful programmes for Network Rail) mandated across all major programmes key to delivering CP5 outputs	• Initiation of change portfolio group (CPG) to bring together a network of senior change leads from every relevant business unit in Network Rail • CPG accountability for the categorisation, prioritisation and rationalisation of the change portfolio to deliver the right outcomes • Initiation of an information governance improvement programme to enhance and strengthen current systems and processes to gain increased efficiency and data quality
There is a threat that the required critical resources (people, plant, materials and/ or access) will not be available to support the delivery of baseline programmes or additionally remitted work	Managing director, Infrastructure Projects	• Strategic planning forum to review supply versus demand and provide challenge and direction • Development of a national integrated plan for network rail and DWWP optimising use of resources • Foster strong union relationships with continuous dialogue • Enhanced governance arrangements	• Implementation of resource demand capture process • Consolidation and integration implementation • Resource category supply management • Enhance communications and reporting • Strategic vision (CP6 pipeline outline developed, future business capability requirements forecasting
We fail to develop and introduce the technology our business requires to deliver our strategic outcomes effectively and efficiently	Group director, Digital Railway	• Technical strategies developed and embedded into whole industry technology roadmaps • Technology governance structure in place • Relationships and associations to influence industry and research bodies	• Define behaviours and appropriate capabilities to deliver a suite of technology and innovation projects • Agree investment authority process, investment strategy and governance • Communications plan to identify and target key stakeholders

Directors' approval statement
The strategic report has been signed on behalf of the board of the company.

Richard Parry-Jones
Chair
10 June 2015

CORPORATE GOVERNANCE REPORT

OUR BOARD OF DIRECTORS

Richard Parry-Jones
Chairman (63)

Appointed to the board: 2012

Skills and experience
Richard has extensive experience of the transport and engineering industry having joined Ford Motor Company as an apprentice before working in multiple disciplines around the world, eventually becoming group vice president of global product development and chief technical officer. He has been recognised for his leadership of the development and introduction of breakthrough technologies in vehicle safety and sustainability. He is a fellow of the Royal Academy of Engineering, the Institution of Mechanical Engineers and the Royal Society of Statistical Science. Richard has been awarded a CBE for his services to the automobile industry.

Current external appointments
Non-executive director of Kelda Holdings Ltd, Kelda Eurobond Co Ltd and Yorkshire Water Services Ltd; Senior independent director of GKN PLC; honorary president of the High Speed Sustainable Manufacturing Institute; visiting professor of the faculty of Engineering at Loughborough University; council member of Bangor University.

Committee membership
Nomination and corporate governance committee; remuneration committee; safety, health and environment committee; treasury committee.

Mark Carne
Chief executive (56)

Appointed to the board: 2014

Skills and experience
Mark was formerly executive vice president for Royal Dutch Shell plc in the Middle East and North Africa, responsible for the company's business in a vital but volatile region at a time of significant political change. Before taking on that role he was executive vice president and managing director for BG Group plc in Europe and Central Asia. Mark joined BG from Shell where he worked in a variety of roles during a 21-year period – including responsibility for Shell's oil and gas platforms in the North Sea and as managing director for Brunei Shell Petroleum. Mark is a fellow of the Institution of Mechanical Engineers.

Current external appointments
Independent governor of Falmouth University; senior adviser for Adamant Ventures LLP ; senior railway executive for Rail Delivery Group Ltd.

Patrick Butcher
Group finance director (47)

Appointed to the board: 2009

Skills and experience
Patrick joined the company as group finance director. Patrick's former finance director positions include English Welsh and Scottish Railway (now DB Schenker), Mapeley, London Underground and King's College Hospital. His early career was at Deloitte & Touche as a management consultant and auditor. He is a member of the Institute of Chartered Accountants (South Africa). Until recently Patrick was a member of British Transport Police Authority.

Paul Plummer
Group strategy director (49)

Appointed to the board: 2008

Skills and experience
Paul joined the company in 2002 and is currently responsible for the group strategy and planning function. Prior to joining the company he was chief economist and director of Economics and Finance at the Office of Rail Regulation (now Office of Rail and Road). He has also held senior advisory positions at National Economic Research Associates, NM Rothschild and Accenture. He holds a degree and MSc in Economics.

Current external appointments
Director of the Rail Delivery Group Ltd (RDG); chair of the RDG sub committees on Planning and on Reform; president of the European Rail Infrastructure Managers; co-chair of PRIME (high level platform of rail infrastructure managers in Europe); council member of UK's Rail Supply Group.

Malcolm Brinded
Non-executive director (62)

Appointed to the board: 2010

Skills and experience
Malcolm had a 37-year career at Royal Dutch Shell plc, where he served 10 years on the main board, latterly as executive director responsible for Upstream International and prior to that for global Exploration and Production. Previously he was chairman of Shell UK. He is a fellow of the Institutions of Civil and Mechanical Engineers and of the Royal Academy of Engineering. He has honorary doctorates from Aberdeen and Robert Gordon Universities. Malcolm has been awarded a CBE for his services to the UK oil and gas industry. Malcolm therefore brings extensive engineering experience to the board, particularly in the fields of safety and major project delivery, two of the board's key strategic focus areas.

Standing left to right:
Malcolm Brinded, Suzanne Wise, Chris Gibb, Mark Carne, Patrick Butcher, Paul Plummer

Seated left to right:
Michael O'Higgins, Sharon Flood, Richard Parry-Jones, Janis Kong, Bridget Rosewell

Current external appointments
Non-executive director of CH2M Hill and BHP Billiton Plc; chairman of the Shell Foundation; vice president of the Energy Institute.

Committee membership
Chair of safety, health and environment committee; chair of major projects delivery committee.

Sharon Flood

Non-executive director (50)

Appointed to the board: 2014

Skills and experience
Sharon was most recently group chief financial officer and an LLP member of Sun European Partners LLP (an international private equity investment advisory firm), and prior to that was finance director of John Lewis department stores from 2005 to 2010. She has extensive financial experience and, prior to 2005, held a number of senior finance and strategy roles. Sharon's appointment to the board therefore strengthens the finance experience and customer focus on the board.

Current external appointments
Non-executive director and chair of audit and risk committee of Crest Nicholson PLC and Shelter, non-executive director of the Science Museum Group; présidente du conseil de surveillance of S.T. Dupont.

Committee membership
Audit and risk committee; remuneration committee; treasury committee; critical infrastructure projects delivery committee.

Chris Gibb

Non-executive director (51)

Appointed to the board: 2013

Skills and experience
Chris is one of Britain's most experienced rail figures having worked in the industry for more than 34 years. After a career of operational roles in England, Scotland and Wales he became managing director, Wales and Borders Trains. He joined Virgin Trains as managing director, CrossCountry, before becoming chief operating officer in 2007, responsible for Virgin's West Coast safety, operations, stations and customer service. He retired from this role in November 2013. Chris's railway experience brings industry-specific experience to the board.

Current external appointments
Director of CLGR Limited and a member of Railway Pensions Scheme.

Committee membership
Remuneration committee; safety, health and environment committee; critical infrastructure projects delivery committee; major projects delivery committee.

Janis Kong

Non-executive director and senior independent director (64)

Appointed to the board: 2010

Skills and experience
Janis's executive management experience has been formed through a 33-year career with BAA, during which she held a number of senior operational roles including being a director of BAA Plc and chairman of both Heathrow Airport Ltd and 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. Janis has an honorary doctorate from the Open University and has been awarded an OBE for her services to transport and regional development. Janis's extensive management experience is invaluable in her role as the senior independent director.

BOARD OF DIRECTORS CONTINUED

Current external appointments
Chairman of Bristol Airport Ltd; non-executive director of South West Airports Limited, Kingfisher plc, Portmeirion Group PLC, TUI Travel PLC and Copenhagen Airports A/S.

Committee membership
Audit and risk committee;
chair of nomination and corporate governance committee; chair of critical infrastructure projects delivery committee.

Michael O'Higgins
Non-executive director (60)

Appointed to the board: 2012

Skills and experience
Michael has significant public sector and commercial experience. Michael has been chairman of the Pensions Regulator and the Audit Commission, managing partner at PA Consulting Group and a partner at PriceWaterhouse. He was also chair of Centrepoint, the youth homelessness charity. He has held visiting academic appointments at the London School of Economics, the Australian National University and Harvard University. Until recently Michael was a non-executive director and chair of audit at HM Treasury. The board recognises that the company's people are its major asset, and Michael brings his experience in this area and also of government relations to the board.

Current external appointments
Chairman of NHS Confederation, Investec Structured Products Calculus VCT plc; director of NHS Confederation (Employers) Company Limited and NHS Confederation Group Company Limited; non-executive director of Hedgehog (1) Limited; member of advisory board, Liaison Financial Services Limited and JustAccounts Limited.

Committee membership
Nomination and corporate governance committee; chair of remuneration committee; critical infrastructure projects delivery committee.

Bridget Rosewell
Non-executive director (63)

Appointed to the board: 2011

Skills and experience
Bridget is an economist and senior adviser of Volterra producing economic analysis across a range of sectors. Bridget is also chair of the risk committee for Ulster Bank. Past roles have included being chief economist and chief economic adviser to the Greater London Authority, executive chairman of Business Strategies Ltd, which was subsequently sold to Experian. She was also a founder of Oxford Economic Research Associates and previously held a position as an economics adviser to Chancellor Kenneth Clarke. She was also previously a non-executive director of the Department for Work and Pensions and Britannia Building Society. Bridget was awarded an OBE in 2013 for services to the economy. Until recently Bridget was a commissioner for the City Growth Commission. Bridget brings financial and economic expertise to the board.

Current external appointments
Senior adviser to Volterra Partners LLP; non-executive director of Ulster Bank Limited, Ulster Bank Ireland Limited and Crossco (1337) plc; member of The Royal London Mutual Insurance Society Limited's With Profits Committee.

Committee membership
Chair of audit and risk committee;
chair of treasury committee.

Suzanne Wise
Group general counsel and company secretary

Skills and experience
Suzanne is responsible for the legal corporate commercial function and is a member of the group executive. Suzanne has extensive in-house legal and corporate governance experience gained within the listed environment having joined the company from Premier Foods plc where she held the position of general counsel and company secretary. Prior to Premier Foods plc she was group head of legal at Gallaher Group plc. In her early career she was a solicitor in private practice.

Responsibilities
Suzanne leads the legal corporate commercial function which provides professional advice and guidance and sets the strategy, tone and direction in the areas of legal, commercial, company secretariat, transparency and business ethics. Legal corporate commercial provides the company with an effective corporate governance framework, leads the organisation in the appreciation and mitigation of legal and commercial risk, builds the company's legal capability and expertise and drives greater transparency and appreciation of business ethics and legal compliance.

Simon Kirby stepped down as an executive director on 18 May 2014.

Robin Gisby stepped down as an executive director on 27 February 2015.

Mike Firth, Lawrie Haynes and Keith Ludeman stepped down as non-executive directors on 18 July 2014.

DEAR MEMBER

The Network Rail board continues to believe that good corporate governance is an essential component of the effective management of the company.

To fulfil our vision of providing a safe, reliable and efficient railway, we have developed a strategy to improve the rail network, allowing faster, more frequent and more reliable journeys between Britain's towns and cities.

For Network Rail, having good corporate governance means that we have a solid base from which to deliver that strategy. Our framework of committees support the board by:

- Reviewing and commenting upon plans to deliver large infrastructure projects and programmes of enhancements to the railway
- Reviewing the company's policies and processes around safety, health and environmental issues, and
- Considering various of the company's internal policies that help employees to conduct their day-to-day tasks in an organised, safe and non-discriminatory environment.

In addition to the internal corporate governance processes that Network Rail adopts, the company also strives to adhere to the principles of the UK Corporate Governance Code 2012.

Reclassification of Network Rail

Network Rail was reclassified as a central government body from 1 September 2014. A Framework Agreement dated 1 September 2014 sets out how the Department for Transport and Network Rail will interact in terms of corporate governance and financial management.

Following reclassification Network Rail has become subject to governance provisions set out in documents such as HM Treasury's Managing Public Money (MPM). One provision of that document is that Mark Carne has been appointed as accounting officer for Network Rail. In that role, Mark must be able to assure parliament that Network Rail operates high standards of probity in the management of public funds.

Further information about reclassification can be found on page 48.

Board evaluation

The board undertook independent evaluations of its effectiveness in 2011 and 2012, and carried out its own internal review during 2013.

The UK Corporate Governance Code requires companies to undertake external board evaluation every three years. In 2014 Network Rail went beyond this requirement, and initiated a further independent review of the effectiveness of the board and its committees. That review was undertaken by independent experts, IDDAS.

The overall outcome of the IDDAS review was positive, commenting that the board as a whole had excellent skills and comprised talented and committed directors who each want to contribute to the development and enhancement of Network Rail.

The review highlighted two inter-related areas where it was recommended that the board take action, namely ensuring that the:

- Boundaries between executive and non-executive space are enforced, and
- Information provided to directors was appropriate in both quality and quantity.

Further information on the review process, outcomes and the actions being taken to address the recommendations, can be found on page 51.

London Bridge overcrowding and engineering overruns at King's Cross and Paddington

During 2014/15, passengers using London Bridge station faced problems with overcrowding due to improvement works being undertaken as part of the £6.5bn government-sponsored Thameslink Programme. This resulted in a lot of negative media coverage about Network Rail.

In addition, Network Rail was, understandably, heavily criticised following significant disruption caused to passengers using King's Cross and Paddington stations. That disruption occurred on the back of major engineering works over the Christmas period. Mark Carne instigated an immediate investigation into the root causes of the problems. The findings of that report were published on 12 January 2015, and can be found on the Network Rail website: www.networkrail.co.uk/news/2015/jan

Responding to these events, the board established two task force sub-committees:

(i) Critical infrastructure projects delivery (CIPD) committee – to review and assure the board on the delivery of critical infrastructure projects in the lead up to and through Easter 2015; and

(ii) Major projects delivery committee (MPDC) – to review the methodology and processes for defining the scope of major projects, the cost estimation and delivery processes and performance, as well as the process by which project funding is sought and approved and how performance is monitored and communicated internally and externally.

The engineering programme over Easter 2015 involved more than 14,000 men and women working around the clock over the four-day Easter weekend to deliver new station facilities, new platforms, new junctions and thousands of pieces of new, more reliable equipment. The works, with a value of around £100m, were completed successfully and on time, demonstrating the value that the task force committees had added to Network Rail's project management abilities.

CORPORATE GOVERNANCE REPORT CONTINUED

Reclassification
Network Rail was reclassified as a central government body in the UK national accounts and public sector finances from 1 September 2014. This was a statistical change driven by new guidance in the European System of National Accounts 2010 (ESA10).

A Framework Agreement dated 1 September 2014 details how the Department for Transport (DfT) and Network Rail (NR) would interact in terms of corporate governance and financial management.

The key principle behind the Framework Agreement was the preservation of NR's ability to continue to manage its business with the commercial freedom it requires to deliver outstanding value for the taxpayer and farepayer, within the regulatory and control frameworks appropriate for a company in the public sector.

Operational: NR and the DfT have worked together to ensure that reclassification has not impacted the way NR runs the network, nor the way in which infrastructure projects and enhancements are managed. Day-to-day responsibility remains with the executive, held to account by the board.

Financial: having determined that it offered the taxpayer better value for money than NR issuing debt in its own name, the Secretary of State for Transport (SoS) entered into a Loan Facility Agreement with Network Rail Infrastructure Limited to replace previous borrowing arrangements.

The £30.175bn loan facility will be used to fund the continuing programme of long-term investment in the national rail network as well as NR's CP5 financing requirements including refinancing. Accordingly, Network Rail Infrastructure Finance PLC does not have any current plans to issue further bonds or commercial paper. Its debt service obligations will be met through repayments of the intercompany loan by Network Rail Infrastructure Limited.

All of Network Rail's outstanding bonds continue to benefit from the direct and explicit guarantee from the UK Government under the Financial Indemnity Mechanism.

Governance: following reclassification the following matters became the preserve of the SoS: appointing or dismissing the board chair, approving the nomination and corporate governance committee's recommendation regarding the appointment of non-executive directors and setting the pay for the chair and non-executive directors.

NR is also now subject to general guidance documents which apply to public sector bodies, including Managing Public Money, the Audit and Risk Assurance Committee Handbook and the Code of Conduct for Board Members of Public Bodies. A full list of applicable guidance is included in the Framework Agreement.

For 2015/16 it is proposed, in accordance with the Framework Agreement, that the Comptroller and Auditor General be appointed as the company's independent external auditor to replace PricewaterhouseCoopers LLP.

Managing Public Money – Accounting Officer
Mark Carne as chief executive, was appointed as NR's accounting officer. In this role, Mark Carne is personally accountable to parliament for safeguarding the public funds available to Network Rail; for ensuring propriety, regularity, value for money and feasibility in the handling of those public funds; and for the day-to-day operations and management of Network Rail. In addition, he is required to ensure that Network Rail is run following the principles, rules, guidance and advice set out in Managing Public Money.

Additional responsibilities of the accounting officer, as set out in Managing Public Money, include:

- Signing the accounts, the annual report and the governance statement and
- Ensuring regularity and propriety; affordability and sustainability; value for money; control; management of opportunity and risk; learning from experience; and accounting accurately for the organisation's financial position.

Full details of the accounting officer's responsibilities are set out in Managing Public Money, a link to which can be found on NR's website: www.networkrail.co.uk/about-us/governance

Compliance with the provisions of the UK Corporate Governance Code 2012
The board considers that the company has complied with the UK Corporate Governance Code 2012 (Code) throughout the year.

The main headings below follow those set out in the Code.

Leadership and effectiveness
Network Rail Limited (NRL) is a not-for-dividend company that owns and operates Britain's railway infrastructure. NRL was reclassified from the private sector to the public sector on 1 September 2014.

As an arm's-length government body, Network Rail retains the commercial and operational freedom to manage Britain's railway infrastructure within effective regulatory and control frameworks.

NRL is accountable to the:

- Government – a framework agreement between NRL and the DfT sets out how NRL interacts with the Government in terms of financial management and corporate governance and
- Public members – who provide a secondary governance role holding the board to account for its leadership and management (see page 52).

The framework agreement is available on: www.networkrail.co.uk/about-us/governance/

Further information on the role of public members can be found on page 52 and also on: www.networkrail.co.uk/aspx/721.aspx

The board
NR works with the Office of Rail and Road to agree what NR must deliver during each five year control period, and the amount of money that NR has available to deliver those projects.

The board is responsible for establishing the strategy to deliver the outcomes required in each control period.

In setting the strategy, and monitoring progress towards delivering it, the board is also responsible for approving the group's risk management strategy (including the internal control policy and other major corporate policies, eg, health and safety).

Board composition
During the year the following board changes occurred:

Resignations: Mike Firth, Lawrie Haynes and Keith Ludeman did not seek re-election at the 2014 AGM and therefore resigned on 18 July 2014. Simon Kirby, managing director, Infrastructure Projects, resigned on 18 May 2014 and Robin Gisby, managing director Network Operations, resigned on 27 February 2015.

Appointments: Sharon Flood was appointed a non-executive director on 25 August 2014. Information on the recruitment and induction processes can be found on page 50.

At the date of this report, the NRL board consists of three executive and seven non-executive directors:

Executive directors
Mark Carne, chief executive
Patrick Butcher, group finance director
Paul Plummer, group strategy director

Non-executive directors
Richard Parry-Jones, chair
Malcolm Brinded
Sharon Flood
Chris Gibb
Janis Kong, senior independent director
Michael O'Higgins
Bridget Rosewell

Photographs and biographies of the board setting out their skills and experience can be found on pages 44-46.

Election and re-election of directors
All the directors will be presented to members for election or re-election at the 2015 AGM. All directors continue to perform effectively and demonstrate commitment to their respective roles.

Directors' conflicts of interest
Directors have a continuing obligation to update the board immediately on any changes to their potential or actual conflicts of interest. Relevant disclosure is considered at the beginning of each board meeting and directors are also required to complete an annual disclosure of conflicts using a questionnaire. Where a director has a potential or actual conflict of interest, procedures are in place to prevent the director from being involved in any decision-making process in relation to that interest. At the date of this report, there were no conflicts of interest.

It is appropriate to disclose that the reimbursement of expenses and cost of secretarial services for Richard Parry-Jones was made by payment of £33,732.22 (2014: £32,403.02) to RPJ Consulting Services Limited in which he has a material interest.

Role of the chair
The chair leads the board and is responsible for its effective functioning and promoting the highest standards of corporate governance. The chair encourages all directors to actively contribute to board meetings and sets the conditions for constructive relations between the executive directors and non-executive directors. He represents the company at its highest level and works with the chief executive to develop strategic relationships with major customers, political leaders and other stakeholders.

Role and responsibilities of the executive directors
The chief executive and executive directors have specific responsibilities for key parts of the business. They provide the non-executive directors with a wider and more immediate view of operational issues and prevent views and perception from becoming dominated by a single executive voice.

The role of the chief executive is to lead and manage the company within the strategy and business plan agreed by the board. He keeps the board informed as to the performance of the company and brings to its attention all matters that materially affect, or are capable of materially affecting, the achievement of the company's strategy. The chief executive provides clear and visible leadership in business conduct and promotes the requirement that all executive leaders are exemplars of the company's values. While the board is ultimately responsible for the success of the company, operational management is delegated to the chief executive and the executives working for him. The chief executive is accountable to the board for all elements of the company's business, and specifically for safety performance. Additionally, post-reclassification, the chief executive has been appointed to the role of accounting officer (see page 48).

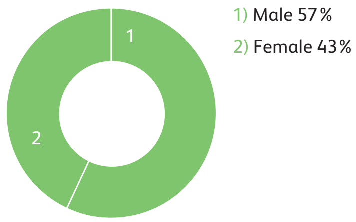
The chief executive chairs the executive committee which comprises all of the executive directors and seven other senior executives. It manages the functions of the business and implements the operational and financial objectives within limits set by the board.

The group finance director is responsible for a range of corporate services that support the whole business by providing business services, specialist expertise and advice. This includes: finance, contracts and procurement, human resources, information management, property and other services such as legal, tax and internal audit.

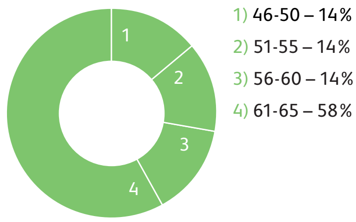
The group strategy director leads the group strategy and planning function which is responsible for developing medium- and long-term company strategy and plans and for the development and timetabling of the railway network. That team is responsible for making sure that the regulatory framework is understood and the company focuses on robust, sustainable and consistent deliverables that reflect the corporate goals. This work is central to driving good business planning practice in the business units to deliver our commitments and developing plans for the future.

Role of the senior independent director
The senior independent director is available to members if they have concerns where contact through the normal channels of chairman, chief executive or other executive directors has failed to resolve an issue or for which such contact is inappropriate. The senior independent director acts as a sounding board for the chairman and serves as an intermediary for the other directors when necessary. The senior independent director is responsible for the chairman's performance review.

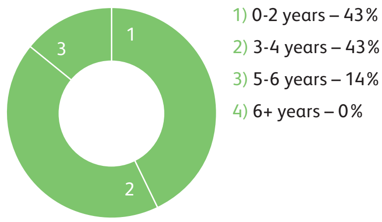
Non-executive directors – by sex



Non-executive directors – by age



Non-executive directors – by service



Role of the non-executive directors
The non-executive directors combine broad business and commercial experience from the rail and other industry sectors. They bring independence, external skills and challenge. This is critical for providing assurance that the executive directors are exercising good judgement in delivery of strategy and decision-making.

Information on the skills and experience of the non-executive directors can be found in the board biographies on pages 44 to 46.

Links to the statements of responsibility for each of the chair, chief executive, senior independent director and the non-executive directors can be found on the NRL website: www.networkrail.co.uk/about-us/board/

Board diversity
Each of the non-executive directors is considered to be independent by the board. The above charts show the composition of the non-executive directors by sex, age, and length of service.

CORPORATE GOVERNANCE REPORT CONTINUED

Induction case study – Sharon Flood
During September and October 2014 Sharon undertook a comprehensive induction programme, which included the following:

Meetings with NR executives: Sharon had one-to-one meetings with each of the non-executive directors and members of the executive committee. In addition, she met senior executives to discuss the company's property portfolio and associated issues, treasury matters and NR's approach to internal audit and risk management.

Meeting with members: Sharon attended a scheduled members' workshop. Topics discussed included reclassification, High Speed 2 and the role of the safety, health and environment committee in the review of safety risks,

Site visits to: Operational visits to London Bridge, Liverpool Street, Waterloo, Clapham Junction, Manchester Piccadilly and Bristol Parkway, encompassing stations, control rooms and maintenance delivery units. Sharon also attended the Bristol training centre to learn how the railway system operates and the complexities of how different operational functions work together. Sharon also met with various operational functions based at NR's Milton Keynes office.

Board recruitment and induction

During 2014, Sharon Flood was appointed as a non-executive director. Her appointment was managed internally by the nomination and corporate governance committee (NCGC) with support from the company secretary. An independent executive search firm, Ridgeway Partners, conducted the search.

Having regard to the other non-executive directors, the NCGC identified the knowledge, skills and experience that they thought would complement and enhance the composition of the board. In line with the NCGC's brief, a number of potential candidates were identified and interviewed by the search firm. A short list of recommended candidates was interviewed by Richard Parry-Jones, Keith Ludeman and Janis Kong.

Following recommendation by the NCGC the board appointed Ms Flood as a non-executive director in August 2014. Ms Flood will be seeking election as a director of the board for the first time at the 2015 AGM.

A comprehensive induction programme was created for Ms Flood, ensuring she had an appropriate introduction to NR for her level of knowledge and experience.

Board training and development

The board as a whole participates in a range of training and development sessions each year. During the year the primary focus was on the impact of reclassification (for more information see page 48) and how that would impact the group and the role of directors. In addition, directors received training on anti-bribery legislation and the Freedom of Information Act.

The board is supported by an executive committee, comprising the three executive directors and the seven senior executives who head up the key business functions.

Board meetings

The remit of the board is set out in the Matters Reserved for the Board document (which can be found on the website: www.networkrail.co.uk/about-us/board/). There are a number of items that only the board may decide upon.

Examples of such matters include:

- The group's overall strategy
- The annual and half-yearly financial statements of the group and company
- Material changes to the network licence
- Key pension matters
- Adequacy of internal control systems
- Major capital investments and expenditure
- Risk management strategy
- The appointment of directors (excluding the chair) and the company secretary and
- The performance reviews of the board and its committees.

There are also a number of powers that the board has delegated to its committees, and those delegated powers are set out in committee terms of reference and also the delegation of authorities policy. Reports from the committee chairs can be found on pages 54-62. Committee terms of reference are available on the website: www.networkrail.co.uk/about-us/board-committees/

As part of Network Rail's transparency commitment, minutes of NRL board meetings, once approved, are available on our website: www.networkrail.co.uk/transparency/datasets

Directors' attendance at board and committee meetings is shown below, in the format: actual attendance/maximum possible attendance:

Board and committee meeting attendance

Director	Board†	Nomination & corporate governance	Safety health & environment	Audit & risk	Treasury	Remuneration	Critical infrastructure projects delivery	Major projects delivery
Richard Parry-Jones*	9 / 9	4 / 4	5 / 5		4 / 4	6 / 6		
Malcolm Brinded*	8 / 9		5 / 5					4 / 4
Mark Carne	9 / 9							
Patrick Butcher	9 / 9							
Sharon Flood*	7 / 8			4 / 4	2 / 2	2 / 2	8 / 9	
Chris Gibb*	9 / 9		5 / 5			2 / 2	8 / 9	4 / 4
Janis Kong*	9 / 9	2 / 3	2 / 2	4 / 5			7 / 9	
Michael O'Higgins*	9 / 9	1 / 1		2 / 2		6 / 6	6 / 9	
Paul Plummer	9 / 9							
Bridget Rosewell*	9 / 9			5 / 5	4 / 4			

* non-executive
† in addition to the nine scheduled board meetings, there were also two telephone meetings called at short notice to discuss specific matters

Attendance at meetings

The board typically meets 10 times each year, and met nine times during 2014/15, including a one-day off-site strategy meeting. Additionally, the board met twice by telephone on specific matters.

Non-executive directors are also required to attend various committee meetings, as indicated in the table on page 50. As mentioned on page 47, two additional task force sub-committees were established in January 2015. The critical infrastructure projects delivery committee, which met weekly, discussed plans for works to be carried out over Easter and the two May bank holidays in 2015. The major projects delivery committee, which continues to meet every two weeks, is considering the end-to-end methodologies and processes behind the delivery of major projects. Representatives from the Office of Rail and Road and the Shareholder Executive (part of the Department for Business, Innovation and Skills) attend meetings by invitation.

In addition to board and committee meetings, the executive and non-executive directors regularly meet with NR's public members. These meetings, of which there were 15 in 2014/15, are designed to assist members fulfil their secondary governance obligation to hold the board to account. More information can be found on page 52 and also in the latest members' statement: www.networkrail.co.uk/aspx/5619.aspx

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. The non-executive directors held three such meetings during the year.

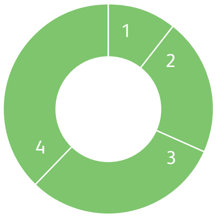
Senior executives and/or technical experts from within the business are from time to time invited to attend board meetings to assist the directors in understanding specific topics.

External parties may also be invited to attend board meetings where appropriate, for example the external auditor, major contractors and the British Transport Police.

Board time allocation

The chart below shows how the board allocated its time during meetings:

Allocation of time in board meetings 2014/15



During 2014/15, a relatively large amount of time was spent on governance, due to the group assessing the impact of reclassification and implementing the changes required.

Independent board evaluation 2014

During 2014/15, external consultancy IDDAS undertook an independent evaluation of the effectiveness of the NRL board and its committees.

The process involved one-to-one interviews with board members, following a structured questionnaire. IDDAS also attended one board and three committee meetings. The outcome from those interviews and the meeting observations were assessed against the pre-agreed evaluation scope, including performance against NR's strategic priorities and the functional effectiveness of the board and committees. IDDAS provided a written report of their observations, conclusions and recommendations. That report has been discussed by the board.

Overall, the board was found to have excellent skills and comprise talented and committed individuals, each of whom wanted to contribute to the development and enhancement of Network Rail.

The key findings of the IDDAS review and the plan to address them are identified below:

IDDAS key findings	Actions taken
1. there was an imbalance between the volume of information provided to the board and its clarity/ease of understanding	• a new corporate dashboard summary of performance against key metrics has been produced, which is updated each period and published on NR's website. See page 10 for the final outcome 2014/15 • executive committee members take a more active sponsorship role of papers presented to the board
2. allied to the above point, due to the volume of information provided to the board, there is a tendency for the board to become embroiled in executive management issues	• non-executive and executive directors commit to maintaining their respective roles and responsibilities, see page 49 for further information • the matters reserved for the board, committee terms of reference and delegated authority levels would be reviewed to determine whether they remained appropriate
3. for effective planning of board succession, a skills gap analysis is needed	• a skills matrix was developed and a gap analysis produced based on the results. These outcomes are being used for succession planning and, when appropriate, recruitment purposes • the nomination and corporate governance committee discuss the future structure and composition of the board (looking, say, two years hence) and discuss its findings with the board

CORPORATE GOVERNANCE REPORT CONTINUED

Directors' personal performance reviews
Both executive and non-executive directors, including the chair, have an annual performance review.

The process for executive directors is the same as that for other employees. Performance objectives are set following discussion with their line manager. There are regular review meetings throughout the year. A formal performance review at the end of the year results in a performance rating.

Regarding non-executive directors, the chair meets with each non-executive director throughout the year to discuss their performance, as well as having a more formal performance review meeting annually. While no specific objectives are set for non-executive directors, their performance is measured against the statement of responsibilities of non-executive directors, available at: www.networkrail.co.uk/about-us/board

The chairman's performance is assessed by the senior independent director in consultation with the other directors.

Accountability
Annual Report – fair, balanced and understandable
The board is accountable for ensuring that the annual report and accounts is 'fair, balanced and understandable'. Having reviewed the content of the annual report as a whole, the board believes that the content is fair, balanced and understandable and allows members to assess the group's performance and prospects. See page 58 for further information on the process underlying the board's view.

In addition, the board considers that it is appropriate for the 2014/15 group accounts to be prepared on the going concern basis. See page 80 for further information.

Determination and delivery of group strategy
The board is responsible for determining and delivering the business strategy of Network Rail and its subsidiaries. The strategy is designed to improve the rail network, allowing faster, more frequent and more reliable journeys between Britain's towns and cities.

In addition to discussing strategy at regular board meetings, the board holds a full-day meeting each year to discuss strategy.

To guide the development and delivery of group strategy, the board has identified four strategic priorities: safety, performance, capacity and cost.

More detail on the process surrounding Network Rail's strategy and business plans can be found in the Framework Agreement.

Key risks – how they are identified, assessed and monitored
The board is responsible for approving the group's risk management strategy including an appropriate internal control policy and other major corporate policies such as health and safety, environmental and business ethics.

On behalf of the board, the audit and risk committee reviews the group's risk profile, risk assessment processes, risk exposure and future risk strategy against the group's risk appetite, proposals for testing risk mitigation and control, and management's responsiveness to audit findings.

The audit and risk committee reports to the board on its activities after each meeting, and recommends proposed strategies and policies to the board for approval.

More information on Network Rail's approach to risk management can be found on page 38.

Other accountabilities
The board of Network Rail is accountable to a number of external bodies. Further information on our governance structure can be found on page 17.

Remuneration
The board's obligation is to ensure that Network Rail's remuneration policy is designed to attract and retain leaders of the necessary calibre, while fairly reflecting market rates for the skills and experience of the individual and recognising the need to ensure value for money for the funders of the Railway.

The board has delegated powers to meet this obligation to the remuneration committee. That committee's report can be found on pages 63 to 78.

Stakeholder engagement
The nature of NR's business requires it to engage with multiple stakeholders in a variety of different ways. Engagement with the primary stakeholder groups is discussed in more detail below.

However, in the normal course of business, and as part of NR's focus on good governance it is necessary to understand that NR also engages with:

- Local councils and communities – regarding works to railway lines, embankments, stations, level crossings, bridges, tunnels, environmental matters, etc
- Young people and schools – on how to stay safe around our network
- Students aged 11 to 18 years – on careers guidance and science, technology, engineering and maths projects.

Further information can be found on pages 32 to 35.

Members
Members perform a similar role to institutional investors in a listed public limited company, except that as NRL is a company limited by guarantee, members do not have any financial interest in the company.

Members hold the board to account for its management and leadership of the company by:

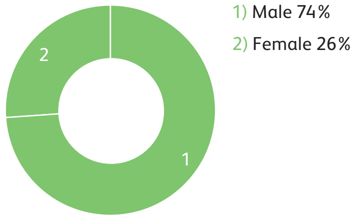
- Monitoring the performance of the board against high standards of corporate governance and regulatory, operational and financial targets
- Engaging with the board, in an informed and objective manner, on their performance
- Seeking assurance that governance procedures are designed to facilitate the delivery of strategic objectives and
- Entering into dialogue on matters that are an immediate subject of votes at general meetings.

As at 31 March 2015, the company had 46 public members (one of whom the members elect to be the members' co-ordinator), and the Secretary of State for Transport (SoS) as a special member. As a special member, the SoS has specific rights in relation to the company's constitution. The DfT also provides credit support in relation to the debt funding of the Network Rail group and has certain rights in that capacity.

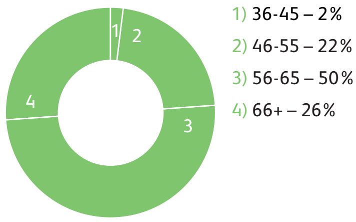
The latest members' statement can be found on NRL's website: www.networkrail.co.uk/aspx/5619.aspx

The following charts show the composition of the members (excluding the special member) by sex, age, and tenure:

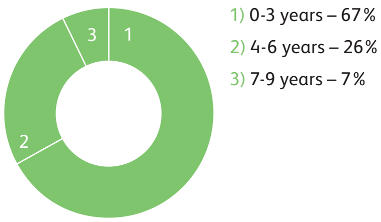
Member composition by sex



Member composition by age



Member composition by service



Further information on the role of members, and biographies of the current members are available on the NRL website.

Appointment of public members

Public members are recruited on an annual basis and are currently appointed for a three-year term. They are appointed in accordance with the membership policy, which is overseen by an independent membership selection panel and supported by Harvey Nash (a recruitment specialist).

On 26 November 2014, 12 new public members were appointed, five were re-appointed and seven retired.

Further information on the selection and recruitment of members is available on the NRL website: www.networkrail.co.uk/aspx/5624.aspx

Engagement with members

The relationship and engagement with members is managed by the group general counsel and overseen by the board chair. The chair regularly updates the board at its meetings on the company's engagement with members.

The Annual General Meeting (AGM)

The AGM provides another opportunity for the board to engage with members. Constructive board-member dialogue is facilitated throughout the event. The chief executive and group finance director present to members on past-year performance and future plans for the company. Members are able to submit written questions in advance of the meeting, enabling the directors to prepare a comprehensive response, as well as having the opportunity to ask ad hoc questions on the day.

The formal business of the AGM is considered by a number of separate resolutions. Poll voting is adopted for all resolutions with members having the option to vote either for or against a resolution, or to withhold their vote (although a withheld vote is not considered to be a vote in law). Final voting figures are announced to London Stock Exchange.

Richard Parry-Jones
Chair

Mark Carne
Chief executive,
in his role as accounting officer
10 June 2015

Resources and opportunities available to members during the year

Meetings
- Two half-yearly meetings to consider the interim and final results
- Four workshops to update members on a range of business issues
- Ten member engagement groups providing members with the opportunity to receive more in-depth briefings from the board and senior managers in five key strategic areas – safety, people, future, performance and finance and risk
- Two meetings with the Office of Rail and Road (ORR) to consider the regulator's view on the company's performance.

Publications
- Chair's quarterly governance letter detailing the board's strategic and governance developments
- Network Rail and ORR publications and press releases
- Railway industry periodicals.

Dialogue
- Scrutiny sessions with the board chair and non-executive directors to engage on the methods used for holding the executives to account
- Site visits to meet our operational teams – in 2014/15 this included a visit to Roby, Merseyside to learn more on electrification works, and a visit to the Forth Rail Bridge following its refurbishment.

Support
- Dedicated members' support team (who operate within a service level agreement)
- Members' website for secure document storage and correspondence among members
- Two-day residential induction for new members to enhance their understanding of their role and the company.

Members' voting at AGMs over a three-year period

	2012/13		2013/14		2014/15	
	No.	%	No.		No.	%
Voting	70	89%	38	93%	41	98%
Non-voting	9	11%	3	7%	1	2%

SAFETY, HEALTH AND ENVIRONMENT COMMITTEE REPORT

Malcolm Brinded,
Chair, safety, health and environment committee

Committee members

Malcolm Brinded
November 2010
(Chair since July 2013)

Richard Parry-Jones
April 2013

Chris Gibb
November 2013

Previous members during the year

Janis Kong
January 2010 to June 2014

Role of the committee

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 group.

The committee's responsibilities include:

- Considering significant corporate and individual safety, health and environment risks and whether management is managing these effectively
- Reviewing the structure and adequacy of safety, health and environment managerial committees within the company
- Reviewing the scope and results of any safety, health and environment audits, and their effectiveness, and
- Considering the major findings of internal and external investigations and management's response.

In respect of all of the above, where necessary making recommendations to the board.

Committee attendees

The chief executive, managing director, Network Operations, managing director, Infrastructure Projects, the Safety, Technical and Engineering director and group general counsel attend meetings by invitation. In addition, meetings are regularly attended by the director of safety and sustainable development risk and assurance.

Mick Cash, general secretary of the RMT Union attends the whole of each committee meeting. He participates in all topics for discussion. This aids scrutiny and challenge and enhances transparency of the work of the committee.

Representatives from the British Transport Police attended a meeting in January 2015 to discuss joint initiatives between a number of agencies to prevent, as far as possible, suicides and trespass on the railway.

Ian Prosser, director, railway safety at the Office of Rail and Road, attended two meetings of the committee to present and discuss the regulator's view on the company's safety performance.

Number of meetings held during 2014/15

The committee met five times during the year, in April, June, September and November 2014 and January 2015. The April 2014 committee meeting was followed with a site visit to Hooley Cutting in Sussex to learn more about the importance of vegetation management for maintaining a safe railway. For details of how many meetings committee members attended, please see page 50.

Principal activities of the committee during the year

Matters considered by the committee during the year included:

- The progress of the safety culture change programme, which was introduced to encourage and embed a culture of reporting actual and potential safety incidents, and the embedding of the Lifesaving Rules into Network Rail culture
- Safety, health and environment related incidents within Network Rail and contractor operations, the lessons learned from those incidents, and actions being taken to mitigate against a recurrence of similar incidents; learnings from notable international railway incidents were also reviewed
- Considering how contractors and sub-contractors working for Network Rail address safety matters among their workforce, including driving behaviours (eg, speeding, use of seatbelts, etc), drug and alcohol testing (both upon recruitment and randomly thereafter) and site safety
- Findings from corporate-level audits and agreed action plans
- Deep dive reviews into, amongst other things:
  - Safety at Network Rail managed stations (eg, slips, trips and falls, accidents while boarding or alighting trains, assaults at stations, etc)
  - Track system integrity (eg, monitoring and improving track system safety including switches and crossings to mitigate against potential derailment of trains)
  - The programme to reduce risk at level crossings – aiming to maximise CP5 risk reduction through the effectively targeted investment of circa £100m and to identify what additional investment and risk reduction might be achievable
  - The safety of earthworks (eg, management of cuttings, embankments, drainage) and structures (bridges and tunnels) and
  - Workforce health and wellbeing (eg, exposure of health hazards, mental health awareness and provision of online wellbeing assessments)
- The continuing work to develop and embed a more consistent risk evaluation methodology for safety hazards, which leads to improved understanding of risks and prioritisation of improvement activities
- Periodic reports on the progress of important safety, health and environment programmes and initiatives, and
- Progress towards significantly improving train accident risk and workforce safety.

Key aspects of the work of the committee on safety, health and environment is periodically reviewed and discussed with members in their safety engagement group, which meets twice a year.

In summary, the committee believes that the executive management of Network Rail has introduced a series of well targeted programmes designed to reduce major train accident risk and improve workforce safety. There is evidence that the desired safety culture is starting to become embedded in the business, although there is still much more progress to be made, especially with regard to workplace safety.

Planned activities of the committee during the coming year

During the coming year, the committee will continue to monitor the progress of the initiatives already under way to improve workforce safety, health and wellbeing, and passenger safety.

Particular areas of focus for 2015/16 will include:

- Ongoing development of the consistent risk evaluation methodology for safety
- Consideration of what additional initiatives and improvements will be needed to accelerate progress towards significantly reducing train accident, level crossing and workforce safety risk
- Further review of the safety performance, practices and policies of contractors used by Network Rail and
- The continuing focus on embedding a safety culture within the company, while also addressing the health and wellbeing of employees.

Malcolm Brinded
Chair, safety, health and environment committee
10 June 2015

AUDIT AND RISK COMMITTEE REPORT

Bridget Rosewell,
Chair, audit and risk committee

Committee members

Bridget Rosewell
July 2012 (Chair)

Janis Kong
January 2010

Sharon Flood
September 2014

Previous members during the year

Mike Firth*
December 2004 to July 2014
(chair January 2006 to July 2012)

Lawrie Haynes*
November 2010 to July 2014

Keith Ludeman*
July 2011 to July 2014

Michael O'Higgins
February 2013 to September 2014

*stepped down from the board and committee in July 2014

Role of the committee

The role of the committee is to review and discuss with management and the company's internal and external auditors the integrity of the financial statements of the Network Rail parent company, major subsidiary undertakings and the group as a whole.

The committee reviews and, where appropriate, makes recommendations to the board on internal controls including risk management, regulation, compliance and internal audit and also reviews the external audit process.

The committee monitors the integrity of the financial reporting and the audit process and monitors internal control systems including risk management, regulation and compliance. The committee makes recommendations to the board on the level of risk appetite acceptable to the company and oversees the process for the identification and management of risk. The committee is responsible for maintaining an appropriate relationship with the Internal Audit function and the independent external auditors. The committee reviews the policy and procedures whereby employees can raise, in confidence, concerns about possible improprieties.

Following reclassification, the committee complies with the standards set out in HM Treasury's 'Audit and Risk Assurance Committee Handbook'.

Committee attendees

The chair of the board, chief executive, group finance director, director, risk and assurance, director, safety and sustainable development and group general counsel attend meetings of the committee by invitation. Two representatives from the independent auditors also attend each meeting and periodically meet with the committee members without executive management present. Periodically the director, risk and assurance meets with the committee without executive management present.

Number of meetings held during the year

The committee met five times during the year, in May, September and November 2014 and February and March 2015. For details of how many meetings committee members attended, please see page 50.

Principal activities of the committee during the year

Matters considered by the committee during the year included:

Internal controls and risk management

- Risk management reports, identifying high-level risks and the status of mitigation, current risk profile, changes to the risk profile during the year and the progress that has been made in relation to the key strategic risks
- Risk reviews of, among other things, critical resources, technology and innovation and business continuity (resilience) management
- The development and implementation of the Enterprise Risk Management system and
- A review of Network Rail's information governance and data quality improvement programme.

Further information on Network Rail's internal control system can be found on pages 38 and 39.

Financial reporting

- PwC's approach and scope of the audit work and the findings of their work
- The 2014/15 half yearly report and full year financial statements with focus on the reporting judgements contained within them and the basis for preparing the accounts on a going concern basis and
- Following reclassification, the proposed appointment of the Comptroller & Auditor General as external auditor to replace PwC, as set out in the Framework Agreement dated September 2014, to be effective for the 2015/16 financial year.

Internal audit

- The internal audit programme for 2015/16
- Any necessary changes to the management of NR's internal control, risk management and governance processes as a result of reclassification
- The output from, and progress against, the internal audit programme and
- Implementation of actions from internal audits, and outstanding actions.

Significant accounting judgements, key assumptions and estimates

With the support of the independent auditors, the committee assessed whether suitable accounting policies had been adopted, whether management had made appropriate estimates and judgements and disclosures were balanced and fair. The main areas of focus during the year are set out opposite.

Accounting judgements	How the committee addressed these judgements
Valuation of railway network and compliance with regulatory requirements The revaluation model used to measure the value of the railway network consists of a number of estimates and judgements made both by the company and the Office of Rail and Road (for example anticipated financial and operational outperformance in the control period).	Detailed reports from management were considered by the committee and the methodology applied to the revaluation model was also reviewed and agreed. The committee also challenged management and the independent auditors on: • The reasonableness of key judgements and estimates in respect of the forecast for the remainder of CP5. • The appropriate level of disclosures in the annual report and accounts around the valuation process and the related assumptions and judgements.
Risk of management override of internal controls	Reports on management's approach to implementing, operating and monitoring the system of internal control are considered by the committee on a regular basis. The committee considered a letter of responsibility from the chief executive regarding the standard of internal controls and integrity that has prevailed in the business during the financial year. The independent auditors have also focused attention on this area and provided satisfactory reporting to the committee on this matter.
Deferred tax It was considered whether it was still probable that Network Rail could expect to use its brought forward tax losses.	Reports indicated that the reclassification of Network Rail as a public body, when taken together with continued high levels of investment in the railway network, meant that it was hard to judge that Network Rail would return within a predictable period to the level of taxable profits that would allow for the utilisation of tax losses. It was agreed to derecognise deferred tax assets.
Valuation of investment properties Investment properties are stated at fair value. The valuations are based on assumptions and estimates that require judgement.	The committee agreed the appropriate methodology had been used. The methodology was consistent with prior years and included valuations and additional assistance from external valuation specialists. The valuations were reviewed by management and the external valuation specialists.
Hedge accounting and derivatives Forward starting interest rate swaps are accounted for as cash flow hedges where it is believed that future sterling issuances are highly probable.	The committee agreed with the assessment that it is highly probable that Network Rail will borrow more than required to utilise all the forward starting interest swaps. The borrowing agreement in place with the DfT is greater than the value of the interest rate swaps. Network Rail's CP5 capital investment programmes will use substantially all of the borrowing facility.
Pension assumptions The group operates defined benefit and defined contribution pension schemes. Valuation of these schemes is dependent on certain key assumptions and complex calculations. External actuaries are engaged to assist in advising on key assumptions and determining the value of the pension obligations.	The committee discussed the key assumptions, including the degree to which these were supported by professional advice from the actuaries. The independent auditors also focused attention on this area and provided reporting to the committee on this matter, following consultation with their own actuarial experts.

CORPORATE GOVERNANCE REPORT CONTINUED

Role of Internal Audit

The company has an Internal Audit function whose 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.

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 committee.

The committee receives regular reports on audit findings from the director, risk and assurance, who has direct access to the chair of the committee. Recommendations to improve the internal control framework are reported to the committee through this process.

Independent auditors' objectivity and independence

The committee has put in place safeguards to maintain the external auditors' objectivity and independence.

It has established a policy whereby employment of the independent auditors on work for the company is prohibited, other than for audit services or tax compliance services, without prior approval by the committee. The committee is responsible for the oversight of compliance with the policy and considers the infrequent requests to use the independent auditors for non-audit work.

In 2014/15 the fee for audit services was £0.7m and the fee for non-audit services was £nil.

To enhance independence and in line with established auditing standards, a new lead partner of the independent 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, reappointment and the remuneration of the independent auditors. PwC have been the group's independent auditors since 2010, when they were recommended by the committee to the board for appointment, following a re-tender of external audit services.

One impact of the reclassification of Network Rail as a central government body (see page 48 for further information), is that the Comptroller & Auditor General (C&AG) is proposed to be appointed as Network Rail's external auditor for the 2015/16 financial year. During 2015 the National Audit Office (NAO) presented both to a panel of management, the chair of the committee and an expert, and to the committee its approach to the Network Rail audit, and the expertise and experience it would bring to the role of external auditor.

Following that presentation, in May 2015 the committee recommended to the board that the C&AG be recommended for appointment as the company's auditors at the 2015 AGM. The board accepted their recommendation and the election of the C&AG as the group's independent auditors will be proposed at the 2015 AGM.

The committee's engagement with the independent auditors in respect to the 2014/15 financial statements

Prior to PwC commencing their audit of the 2015 annual financial results, the committee requested that the lead partner present to them their audit plan. The presentation covered PwC's proposed engagement with the group and how PwC have addressed prior feedback from both the committee and senior management. The presentation was critically considered by the committee and comments provided to the lead partner.

Network Rail satisfied themselves that the external audit process was effective by reviewing audit plans, approaches and critical judgements. PwC worked closely with management to plan the audit and accounting timetable in order to maximise effectiveness.

The committee's responsibilities for risk management

While the ultimate responsibility for risk management rests with the board it delegates the more detailed oversight of risk management to the committee which reports its findings to the board.

Further details on the risk management and assurance process are on pages 38 to 42.

The requirement for the annual report to be fair, balanced and understandable

The committee acknowledges that, taken as a whole, the annual report and accounts need to be fair, balanced and understandable in order to provide the information necessary for members to assess the company's performance, business model and strategy.

The committee advises the board on whether it believes that the annual report and accounts meet this requirement.

In order for the committee to make this assessment it considers reports received from management during the year, monitoring financial performance, and at year end in support of the financial statements. The committee also receives reports from the independent auditors on the findings of their annual audit. Formal review processes are in place to ensure the annual report and accounts are factually accurate.

Planned activities of the committee during the coming year

During the coming year, the committee will remain focused on the audit, assurance and risk process within the business, and maintain its oversight of financial and other regulatory requirements.

Particular areas of focus for 2015/16 will be:

- Ways of working and assurance following appointment of C&AG as the new Statutory Auditor
- Internal Audit and other assurance plans with particular focus on key strategic priorities and significant audit actions
- Integrity of internal controls including risk management, and
- Oversee the specific business presentations relating to the most significant risks within the group risk profile.

Bridget Rosewell
Chair, audit and risk committee
10 June 2015

TREASURY COMMITTEE REPORT

Bridget Rosewell
Chair, treasury committee

Committee members

Bridget Rosewell
July 2012 (chair)

Richard Parry-Jones
April 2013

Sharon Flood
September 2014

Previous members during the year

Mike Firth*
December 2004 to July 2014 (chair)

*stepped down from the board and committee in July 2014

Role of the committee

The committee's role is to:

- Review and satisfy itself as to the appropriateness of proposed treasury transactions including banking, cash management, and management of debt and investments
- Approve or recommend strategies and policies in relation to areas of treasury management, including liquidity management and forecasting, treasury internal control and governance policies
- Review the Treasury function's financial reporting and internal control procedures
- Review management's, the internal auditor's and external auditors' reports on the effectiveness of systems from internal financial control, financial reporting and risk management and
- Approve specific transactions in the areas of treasury responsibility.

However, since reclassification in September 2014 restrictions have been placed on group treasury activities in the areas of funding, investment management and financial risk management. In place of seeking funding in the financial markets, Network Rail is now financed via a Department for Transport Loan Facility (see page 48).

Committee attendees

The group finance director, group treasurer, head of treasury operations and group general counsel attend meetings by invitation.

Number of meetings held during the year

The committee met four times during the year, in May, July and November 2014 and February 2015. For details of how many meetings committee members attended, please see page 50.

Matters considered by the committee during the year included:

During 2014/15 the committee, amongst other things:

- Monitored existing debt issues and associated maturities, and cash flow forecasts
- Carried out the annual review of the adequacy and effectiveness of exiting treasury policies
- Considered and recommended to the board that NR enter into a loan agreement with the Department for Transport (DfT)
- Approved/agreed how interest rate pre-hedges should be utilised against DfT loan facility drawdowns to manage cash financing costs
- Noted the benefits of a number of potential strategic finance opportunities and agreed they should continue to be explored, and
- Requested information regarding potential litigation against banks relating to manipulation of FX / LIBOR rates but noted that fines from regulators were probably all that was practically achievable at present.

Planned activities of the committee during the coming year

Particular areas of focus for 2015/16 will be:

- Monitor existing debt issues and associated maturities, and cash flow forecasts
- Carry out the annual review of the adequacy and effectiveness of exiting treasury policies
- Review weighted average debt maturity policy with respect to its impact on CP5 financing costs
- Consider the appropriateness of potential changes currently being discussed with DfT, including the existing pre-funding mechanism, collateral arrangements and liability management, and
- Continue to consider the implications of any strategic finance opportunities that may be proposed to the Network Rail board.

Bridget Rosewell
Chair, treasury committee
10 June 2015

NOMINATION AND CORPORATE GOVERNANCE COMMITTEE REPORT

Janis Kong,
Chair, nomination and corporate governance committee

Committee members

Janis Kong
July 2010 (Chair)

Richard Parry-Jones
April 2013

Michael O'Higgins
September 2014

Previous member during the year

Keith Ludeman*
July 2012 – July 2013

*Stepped down from the board on 18 July 2014.

Role of the committee

The committee has two main areas of focus:

- Board composition and evaluation, and
- The effectiveness of non-financial corporate governance.

Committee attendees

The chief executive, group human resources director, corporate communications director and group general counsel attend meetings by invitation.

Number of meetings held during the year

The committee met four times during the year in April, June, September and October 2014. For details of how many meetings committee members attended, please see page 50.

Principal activities of the committee during the year

Recruitment of non-executive directors

At the June 2014 meeting, the committee finalised the replacement for Mike Firth, recommending Sharon Flood to be appointed to the board of directors. The board confirmed her appointment at the July 2014 board meeting and her appointment was effective from 24 August 2014. Members will be asked to appoint Sharon formally at the 2015 AGM.

Keith Ludeman and Lawrie Haynes stood down at the 2014 AGM, and the committee prepared a specification for a new non-executive director with railway experience. The search is ongoing and Ridgeway Partners, who have no connection with the company and are signatories to the Voluntary Code of Conduct for Executive Search Firms, have been appointed to identify candidates against this specification.

Board evaluation

Following the 2014 IDDAS review, the committee has been overseeing the implementation of the key findings of that review, including the revision of board paper formats to ensure clear, concise papers with articulated expectations and a focus on leaving operational matters to the executive where possible, to allow the board as a whole more time to focus on strategic matters.

In addition, IDDAS have been re-engaged to carry out a light touch review in 2015, to give an independent view on Network Rail's progress towards addressing the 2014 findings.

During 2014/15, the board also carried out an internal review. This consisted of an individual evaluation of each director with the chair and an evaluation of the chair's performance by the senior independent director. The non-executives also convened a special meeting to review the performance of the chair and fed back as part of the overall board evaluation.

CORPORATE GOVERNANCE REPORT CONTINUED

The committee also developed a policy on non-executive skills. The output of this policy is a skills matrix listing each non-executive's ability and experience in a range of competencies including: leadership, influencing, safety (mission critical), rail knowledge (mission critical), financial (mission critical), operational, strategic thinking and governance. The aim is to ensure that there are at least two non-executives with a good score in each mission critical area. Each non-executive director was scored 1-3, being a determinant of the overall depth of skills contained in the board in a particular field. This has also helped to identify any training that an individual non-executive director may require. An amendment to this matrix, to include the level of non-executive experience, is being introduced in 2015.

The committee also reviewed the ideal size of the board and the mix of executive and non-executive directors. Both this, and the policy referred to above will be used to plan the evolution of the board over the coming years. During the year under review, the committee also reviewed each committee, for composition, size and suitability of the chair.

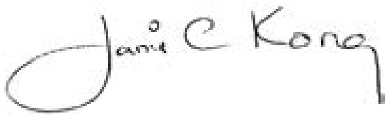
Planned activities of the committee during the coming year

During 2015, the committee will:

- Continue with its search for the remaining non-executive director position
- Review the 2015 IDDAS board effectiveness light touch review and subsequently make recommendations to the board regarding any key findings
- Review the non-financial internal controls implemented by the company, the company's ethics policy and performance and will continue to review the transparency performance, including freedom of information and the company's performance against its diversity and inclusion agenda, and
- Review the governance of all significant subsidiary companies, including board composition to ensure the subsidiary is well managed.

Succession planning

The committee received progress reports from senior management on the succession planning process with particular focus on senior key roles in the business. The committee recognises that effective talent management programmes and the enhancement of diversity and inclusion across all levels of the organisation is essential for the delivery of the company's long-term objectives.



Janis Kong
Chair, nomination and corporate governance committee
10 June 2015

DIRECTORS' REMUNERATION REPORT

DIRECTORS' REMUNERATION REPORT

Letter from the committee chair

It is my pleasure to present the 2015 directors' remuneration report from the Network Rail remuneration committee. The remuneration committee recognise that executive pay is an important issue for our stakeholders and remain committed to the highest standards of disclosure in this area. We operate in line with the remuneration reporting requirements which apply to UK listed companies and the provisions of the UK Corporate Governance Code.

At the 2014 AGM, our members approved the Network Rail Remuneration Policy (Policy) which sets out the parameters and the limits for how our directors are paid. The Policy was included in last year's directors' remuneration report and can also be viewed on our website www.networkrail.co.uk/RemunerationReport.pdf. A summary of the Policy, including how it will apply for next year, is set out on pages 74-76.

Our annual remuneration report explains the executive remuneration outcomes in respect of 2015 and will be subject to approval from our members at the 2015 AGM. Key points to note in respect of 2015 are:

- The executive remuneration framework at Network Rail has three simple components – salary, benefits/pension, and an incentive plan. The incentive plan is based on performance in the year and any payment is deferred in full for three years.
- The maximum incentive payment that can be paid to an executive director is 20 per cent of salary.
- There were no incentive payments made in respect of 2015 as performance was below expectations. This illustrates our commitment to performance pay.
- For 2015/16, there will be no salary increase for the executive directors.

The remainder of this introductory letter explains how executive remuneration is determined at Network Rail, summarises our stakeholder engagement activities, and provides further information on outcomes in respect of 2015.

Determining executive pay at Network Rail – best practice corporate governance

Network Rail operates under a corporate governance structure which is in line with best practice principles. The remuneration of the executive directors is determined by the remuneration committee and subject to approvals, as appropriate, from members and DfT as illustrated below.

Who is involved

Remuneration committee
Review and propose remuneration policy for executive directors.
Approve implementation decisions

Remco committee members:
Chair, Michael O'Higgins,
Richard Parry Jones,
Sharon Flood and Chris Gibb

The ORR
Reviews incentives to confirm they meet licence requirements.

Secretary of State
Approves policy prior to voting by members

Members
Provide feedback on policy proposals and vote on policy at the AGM

Policy

Remco – Determine policy for approval

↓

ORR – Confirms meets licence conditions

↓

Secretary of State – Approves policy

↓

Members – Approves policy through vote at AGM

Implementation

Remco – Following approval of policy make decisions each year on:

- Salary levels
- Setting and assessing performance targets and measures
- Arrangements for joiners and leavers
- The out-turn of incentive schemes (with input from relevant stakeholders, including the ORR)

Members – Vote on the annual remuneration report at the AGM

During the year, the committee has been operating within the Policy approved at the 2014 AGM, and making decisions about the out-turn of the annual incentive plan and the 2012-15 LTIP. The key items discussed by the committee were full details of the annual incentive plan for 2014/15 including measures and targets, reviewing the 2012-15 LTIP targets, reclassification and the UK corporate governance code of practice.

Stakeholder engagement

In 2014 the stakeholder engagement was focused on the application of the Policy approved at the 2014 AGM.

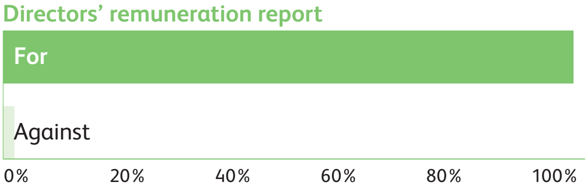
The committee engages with members as part of a regular and co-ordinated annual programme designed to share the information which informs the committee's decision making and to seek member feedback on key issues. During the year, this included workshops and meetings of the people engagement group, a sub-group of members introduced during 2013, which discusses a range of people-related issues including executive remuneration in greater depth. For more information on members, please see page 52.

In addition, there are regular discussions with the Office of Rail and Road (the ORR) to ensure that the incentive arrangements meet the licence conditions. Each year the regulator provides Network Rail with its assessment of performance during the year. This is used to inform the committee's decision on the outcome of the annual incentive plan.

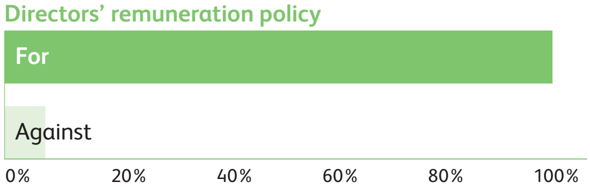
During the year, Network Rail was reclassified to the public sector in the national accounts. In light of this we have reviewed, with the Department for Transport (DfT), how engagement and assurance around remuneration should be strengthened to reflect government's increased stakeholder interests in the company. The framework agreement (www.gov.uk/government/uploads/system/uploads/attachment_data/file/349439/framework-agreement.pdf) agreed with the DfT and published in September 2014 sets out the adjustments that have been made to roles and accountabilities on both sides.

At the 2014 AGM, we received 98 per cent support from our members for the 2014 directors' remuneration report and 93 per cent support from our members for the 2014 policy.

Directors' remuneration report



Directors' remuneration policy



Implementation of the remuneration framework to deliver CP5

In 2014 the committee identified four principles on which the CP5 remuneration framework is based and these continue to underpin the approach:

- **Simple.** The framework should be simple and transparent for all stakeholders to understand
- **Competitive and fair.** Attracting and retaining leaders of the necessary calibre requires remuneration arrangements that are reasonable in the markets in which we compete for talent and which fairly reflect the market rate for the skills and experience of the individual. At the same time, we always remain cognisant of the need to ensure value for money for the funders of the railway, and to reflect the strong element of public interest in the business
- **Performance and safety.** There should be a performance-related element of the package which rewards performance in the areas that are most important for our stakeholders. There should be no reward for failure. Safety of the workforce, passengers and the general public is at the heart of everything we do and must be reflected in the remuneration framework
- **Aligned with employees.** Where possible, remuneration structures will be aligned across the organisation. All Network Rail employees continue to be eligible for incentive payments, determined using a consistent performance framework across the organisation.

Based on the principles above, the remuneration framework for executive directors introduced in 2015 was greatly simplified and is summarised below. No payments outside of this framework may be made. The key changes were to simplify the structure and dramatically reduce the maximum incentive opportunity from 160 per cent of salary to 20 per cent of salary.

Salary	Salaries are set at a level which reflects the skills and experience of the individual as well as the scope and responsibilities of the role. Salary increases over CP5 will normally be in line with that of other Network Rail employees
Benefits and pension	Participation on the same basis as other managerial positions in Network Rail
Incentive	One incentive plan based on the achievement of stretching annual performance targets aligned to the business scorecard (discussed on page 77) A maximum annual opportunity of 20 per cent of salary, subject to performance and any amount is deferred for three years, subject to safety and sustainability obligations over the period All Network Rail employees are eligible to participate, based on aligned business scorecard

DIRECTORS' REMUNERATION REPORT CONTINUED

Network Rail is large and complex and continues to need talented people to deliver the long-term objectives in CP5 and beyond outlined above, while remaining dedicated to ensuring the safety of our passengers, our workforce and the public on a daily basis. Remuneration needs to be appropriate to attract the right talent while recognising the company is publicly funded.

2015 outcomes

Pay for performance is one of the key principles of the remuneration policy, with no reward for failure. Alongside delivering the safe operation of the railway during the year, delivering significant enhancements and upgrades, the line to Dawlish was re-opened early in the year and the effects of the Harbury landslip were dealt with quickly and safely. However, overall performance during the year was below expectations.

The CEO decided to waive any opportunity for an incentive payment this year due to the delays over the Christmas period. The scorecard out-turn for the annual incentive plan (AIP) based on performance against the measures agreed at the start of the year was 22 per cent of the maximum opportunity, which would have triggered payments for eligible executive directors. However, the committee concluded that due to the overall level of performance achieved, they would not receive any payment under the annual incentive in respect of the year.

The 2012-15 LTIP was based on performance over the three year period ending in 2015. Targets in respect of train performance and financial efficiency were not met over this period. Performance against the project milestones targets were partially met and would have resulted in a payout of 8.2 per cent of the award. However, the remuneration committee concluded that the financial 'underpin' had not been met and therefore this award will lapse in full.

Deferred payments for the legacy 2009-12 LTIP were also due to be made during the year once the final assessment of CP4 performance had been completed. Significant achievements were made during the control period including passenger growth and a massive investment programme delivered largely to time and budget. However, financial efficiency and train performance progress made early in the control period was not sustained. Taking all of this into account, the committee increased the downward discretionary adjustment applicable to this award from 20 per cent to 40 per cent. The reduced deferred amount was due to be paid to the eligible executive directors, however all waived their payment and received no payment.

Full details of the out-turn and decision making about the AIP and LTIPs can be found in the sections on pages 67-70. No further LTIP awards will be made under the new remuneration framework described above.

Implementation in 2016

There are no changes proposed to the remuneration policy this year. As part of the review of incentives a business scorecard was introduced in 2014/15 to manage the different aspects of business performance that are important to Network Rail and its stakeholders. This has been a step change in the transparency of company performance, both internally and externally. The committee and the board recognise it is not yet fully embedded. Some refinements are being made for 2015/16 to give even greater clarity and visibility to what is important to Network Rail's overall business performance.

These are currently in discussion with the DfT, but it is proposed will include:

- A new measure, cancellations and significant lateness (CaSL), which is an important regulatory measure for Network Rail on train performance and
- A new measure for lineside neighbour satisfaction is also being introduced to reflect the importance of this important stakeholder group. The proposed scorecard including weightings is on page 78.

In 2015/16 salaries for executive directors will not be increased. Negotiations for the pay of other employee groups are ongoing with an offer of 2 per cent having been made for the largest bargaining group.

Changes to the UK Corporate Governance Code

In determining and implementing the executive remuneration framework at Network Rail, the committee operates in line with the requirements of the UK Corporate Governance Code ('Code'). During 2014/15, a revised version this Code was released and became effective on 1 October 2014. The committee reviewed the Network Rail remuneration framework and confirmed that it was in line with the requirements of the revised Code. Compliance with the Code now requires companies to have provisions to recover or withhold incentive payments to executive directors in circumstances where it is considered appropriate to do so. Under the new Network Rail incentive structure approved by members last year, any incentive payment earned in respect of performance in a financial year must be deferred in full for a period of three years over which it is subject to the terms of the 'safety and sustainability obligations' which allow the committee to withhold the full amount of any payment in a wide range of circumstances relating to safety and the sustainability of business performance (see details of the policy on page 76). The committee believes these provisions satisfy the requirements of the revised Code in this area.

Michael O'Higgins
Chair of the remuneration committee
10 June 2015

ANNUAL REMUNERATION REPORT

EXECUTIVE DIRECTOR REMUNERATION FRAMEWORK FOR 2015

This report has been prepared in accordance with the requirements of Schedule 8 of the Large and Medium-sized Companies and Groups (Accounts and Reports) (Amendment) Regulations 2013. Some of the disclosures in these sections, where indicated, have been audited.

Single total figure of remuneration for 2014/15 (audited)

The table below summarises all remuneration for the executive directors in respect of 2015 (and the prior year comparative). Further discussion of each of the components is set out on the pages which follow.

	Salary		Benefits[4]		Pension[5]		AIP		LTIP		Other[6]		Total	
£'000	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014	2015	2014
Mark Carne[1]	675	156	17	28	79	16	0	–	–	–	–	–	771	200
Patrick Butcher	410	401	16	15	133	155	0	51	0	–		300	559	922
Robin Gisby[2]	356	378	15	16	112	148	–	48	–	–		300	483	890
Simon Kirby[3]	51	378	2	15	16	149		48				300	69	890
Paul Plummer	362	355	17	17	168	150	0	45	0	–	–	–	547	567

1 Mark Carne was appointed to the board on 6 January 2014.
2 Robin Gisby left the board on 27 February 2015.
3 Simon Kirby left the board on 18 May 2014.
4 Benefits include car allowance, private medical cover, any annual travel subsidy, life insurance and relocation costs reimbursed.
5 Pension includes the value of all pension benefits receivable in respect of the relevant year. This includes both the supplementary cash allowance and a value from participation in the defined benefit or defined contribution pension arrangements (calculated in accordance with the methodology prescribed by the Regulations). Further details of these pension benefits are set out in the pensions section on page 71.
6 The other column contains the value of the one-off retention payments approved by members at the 2012 AGM and paid in 2014.

Management changes

The remuneration arrangements for Simon Kirby and Robin Gisby, who left the board during the year was determined by the committee in line with the company's established policies and principles of best practice. The arrangements are summarised below.

Robin Gisby	Stepped down from the Network Rail board on 27 February 2015 • Payment in lieu of notice was made • No other termination payment made • No eligibility for the 2014/15 incentive • Eligibility for the outstanding award under the 2012-15 LTIP lapsed under the terms of the plan to reflect cessation of employment as a Network Rail executive director during the performance period • His replacement is not a board appointment
Simon Kirby	Stepped down from the Network Rail board on 18 May 2014 • No termination payment made • No eligibility for the 2014/15 incentive • Eligibility for the outstanding award under the 2012-15 LTIP lapsed under the terms of the plan to reflect cessation of employment as a Network Rail executive director during the performance period • His replacement is not a board appointment

Incentive plan 2014/15 – annual incentive plan (audited)

The maximum potential AIP award for executive directors in 2015 was 20 per cent of salary. Stretching performance targets were set at the start of the year in the context of the business scorecard.

Performance in a number of areas fell short of our own expectations and stretching targets set at the beginning of the year. Train performance was lower than planned, which had an impact on financial performance. Renewals performance fell short and satisfaction, both customer and passenger, was not where it should be. On safety measures the target on reporting workforce close calls was met, although the percentage closed within 28 days was slightly below target. The reduction of underlying risk from train accidents to passengers, our workforce and members of the public exceeded the target. The target for achieving the top 10 milestones for enhancements and renewals was met. The freight delivery metric target was also exceeded. The committee's assessment of performance for 2015 is described in detail on page 68, and in the performance scorecard chart on page 10.

The CEO made a decision during the year to waive any opportunity for a bonus payment for 2014/15 because the impact on passengers of the Christmas over-runs was unacceptable.

In making the assessment for the other executive directors, the committee took into account the performance against target of each of the measures, an overall view of business performance and specific views from the audit and risk committee, the safety health and environment committee and the ORR. Based on this information, the committee agreed that business performance in 2014/15 did not meet the business plan agreed at the beginning of the year and that as the executive directors were instrumental in developing the business plan, they were also partly accountable for the gap in performance. The committee concluded that due to the overall level of performance achieved, the eligible executive directors would not receive any payment under the annual incentive in respect of the year.

The ORR assessment of overall performance correlates with the scorecard out-turn of performance. The ORR recognised that there has been four per cent growth of passenger journeys during the first three quarters of the year. They also recognised the scale of the challenge the company faces in delivering a major enhancement and renewals programme in CP5 while at the same time ensuring the continued safe and efficient operation of the network. The assessment of performance in the year highlighted a number of positive developments and successes as well as the areas where Network Rail performance fell short of the targets.

The areas where the ORR noted positive developments and successes during the year include more innovative approaches to risk control, the safety improvements that the tidy railway programme will enable and evidence of improvement in the management of risk at level crossings including the closure of around 120 higher risk crossings. They also note the significant improvement in train performance over the past 10 years and strong performance in the freight sector. A number of significant infrastructure enhancements were delivered in the first year of CP5 including upgrades to Reading and Edinburgh Haymarket stations and capacity improvements on the East Coast Mainline. In relation to asset management the composite reliability index (CRI) shows a reduction in the number of asset failure incidents and the ORBIS programme milestones for the year were delivered, which will result in significant improvements in the way asset information is collected, stored and utilised. In addition, the number of unplanned temporary speed restrictions has halved since the end of 2013/14. The ORR also noted that levels of disruption to passengers and freight users from planned engineering work were consistent with trajectories to meet the end of CP5 regulated targets.

The areas where the ORR noted that performance fell short of the targets aligns with the performance scorecard outcome including train performance. Financial performance was below both the regulatory measure and Network Rail targets. Over-running of engineering works on 27 and 28 December caused severe disruption to passengers travelling into or out of King's Cross and Paddington stations.

The committee also noted that the performance scorecard for 2014/15 did not fully align to the PR13 outputs, which was a concern raised by the ORR. This point was taken into account when determining the outcome for executive directors and also in developing the scorecard for 2015/16.

The safety, health and environment (SHE) committee noted that train accident risk has improved and the 10 per cent target met and good progress is being made in relation to action plans. Passenger safety at stations was good but the workforce safety target of a 15 per cent reduction was not met. Close calls reported has exceeded the target and the percentage being closed within 28 days is increasing. Positive steps have been made to improve the safety culture and performance through close call reporting and embedding the life saving rules. A recent independent safety assessment by Dupont benchmarked Network Rail's safety culture above that of comparator rail transportation industries. Over 100 level crossings were closed during the year and the risk has been reduced by 4.4 per cent. Overall the SHE committee concluded that as safety now represents 20 per cent of the overall scorecard and bonus, there should be no reduction to any bonus for specific safety reasons.

Long-term incentive plans (audited)

The interests of the executive directors in outstanding long-term incentive plan awards approved by members is summarised in this section. As discussed above, the incentive framework changed for CP5. These are the last legacy LTIPs.

2009-12 LTIP – earned and deferred

KEY FEATURES

- Awards approved by members at 2009 AGM
- Based on a performance period covering the three year period to 31 March 2012
- Vesting was based on financial value added (FVA) performance target, and assessment of overall business performance (including safety)
- Committee assessed performance and determined that 80 per cent of the maximum should vest, reflecting the delivery of £698m of FVA which was significantly ahead of the target
- Payment in two phases. First paid in April 2013 and second was due in 2014, subject to the ORR verification of FVA performance.
- Following final review overall vesting was further reduced to 60 per cent of the maximum
- Executive directors waived any entitlement, so the final payment was not made

As disclosed in detail in the 2013 directors' remuneration report, the committee determined that, based on the achieved performance in the period (as adjusted downwards by 20 per cent for safety and train performance in the period), so 80 per cent of the maximum vested.

The committee, mindful that the final FVA figure for the performance period could not be verified by the ORR until the end of CP4, made the decision to make the payments in two phases with 60 per cent of the payment being made initially and the remaining 40 per cent to be paid in 2014. The first payment was made in April 2013.

The second payment was deferred to provide a mechanism for any adjustments which may be required following final ORR verification of FVA. The control period finished on 31 March 2014, and the formal ORR view on FVA for the control period was published after the 2014 annual report was published. The committee reviewed overall business performance after the control period finished. They noted that significant progress had been made in level crossing closures and major projects during CP4 as well as growth in passenger numbers. However, the progress made during the early part of the control period on train performance and financial efficiency was not sustained in the latter part of the control period, resulting in lower financial performance. The ORR also gave their view of performance during the control period, which was taken into account by the committee. Having considered performance over the entire performance period, the committee decided to further increase the downward discretion from 20 per cent to 40 per cent.

All of the executive directors made a decision to waive their entitlement and therefore no payments were made to them.

The following table summarises the awards under the 2009-12 LTIP.

				During year/waived/lapsed**		Deferred amount
	Date of award*	Performance period	Deferred payment due at start of year	Payment of first tranche (April 2013)	Lapsed amount	Value
Mark Carne	No award					
Patrick Butcher	2009	2009-2012 (completed)	**112**	(168)	(112)	**Waived**
Robin Gisby	2009	2009-2012 (completed)	**106**	(158)	(166)	**Waived**
Simon Kirby	2009	2009-2012 (completed)	**106**	(158)	(106)	**Waived**
Paul Plummer	2009	2009-2012 (completed)	**99**	(149)	(99)	**Waived**

* Awards were made following member approval at the 2009 AGM.
** Columns illustrate the change in the outstanding value of the award to reflect the first payment of the vested amount to reflect the committee's assessment of performance and the amount which lapsed as a result of the committee's performance assessment (20 per cent of the total).

CORPORATE GOVERNANCE

2012-2015 LTIP

KEY FEATURES

- Awards approved by members at 2013 AGM
- Based on a performance period covering the three year period to 31 March 2015, which has now been completed
- Vesting based on performance in three areas: 50 per cent based on financial value added (FVA), 25 per cent based on PPM, and 25 per cent based on project milestones and underpins being met
- The underpins to the plan were not met and as a result no payments will be made.

The performance targets for this award are set out below and were discussed in detail in the 2013 directors' remuneration report.

		Performance measures		
	% of maximum	Cumulative FVA over FY13-FY15	PPM moving annual average	Project milestones
Proportion of award		50 %	25 %	25 %
Performance above expectations	25 %	£75m	92.5 %	Delivery above expectations
Exceptional performance	100 %	£450m or above	93.0 % or above	Exceptional delivery

No payment below the threshold performance level. For performance between the levels shown, vesting will be on a scaled basis.

The LTIP uses two underpins and the committee retains discretion to make a suitable downward adjustment to vesting levels if the underpins are not satisfied. This is to provide a safeguard such that performance in one area must not be achieved at the expense of the other. Any vesting on the operational measures is subject to a positive cumulative FVA over the period. Any vesting on the FVA measure is subject to the committee's assessment that key regulatory outputs have been sufficiently delivered.

Under the clawback provision, the committee has discretion to reduce or cancel an award at any time before vesting, if circumstances are considered appropriate. These include:
- Gross misconduct
- A material misstatement of the company's audited results
- An unacceptable level of safety performance. In the event of a catastrophic accident for which Network Rail was culpable, no LTIP would normally be payable to any Network Rail executive director
- A material failure of risk management
- A failure to comply with obligations set out in applicable contractual agreements
- Serious reputational damage to the Company as a result of the participant's misconduct.

The 2013 directors' remuneration report stated that as the plan spans two control periods, the targets would be verified once the determination was published and targets for the period in CP5 that this plan covers have been finalised. The committee reviewed the targets once the determination was finalised and concluded that no changes should be made to the targets as the targets originally set were still appropriate.

Of the three measures, two did not meet the target, FVA and PPM, and therefore no payment was triggered for them. The third measure, project milestones, achieved performance above the trigger with 82 per cent of project milestones being achieved.

Each measure is also subject to an underpin to vest. The project milestones measure has an underpin of positive cumulative FVA during the performance period. This underpin was not met and as a result the measure did not vest.

As none of the measures met both the threshold and underpin, the plan did not vest and no payments will be made to participants.

The following table summarises the outstanding awards under the 2012-15 LTIP. As shown, the awards to Robin Gisby and Simon Kirby lapsed under the terms of the plan to reflect cessation of employment as a Network Rail executive director during the performance period.

£000	Date of award*	Performance period	Maximum value of initial award	Changes since award**	Current maximum value of award
Mark Carne	Not eligible	–	**–**	–	**–**
Patrick Butcher	2013	2012-2015	**395**	(395)	**–**
Robin Gisby	2013	2012-2015	**371**	(371)	**–**
Simon Kirby	2013	2012-2015	**371**	(371)	**–**
Paul Plummer	2013	2012-2015	**338**	(338)	**–**

* Awards were made following member approval at the 2013 AGM.

** Illustrates the change in the outstanding value of the award to reflect awards lapsing on cessation of employment as a Network Rail executive director during the performance period.

Pension (audited)

Executive directors are eligible to participate in the Network Rail defined benefit pension schemes or defined contribution pension scheme on the same basis as other employees. Executive directors who have opted out of their respective pension arrangements to protect their lifetime allowance of £1.5m to 05/04/2014 (£1.25m from 06/04/2014) are eligible to receive a pension allowance on the same basis as other employees. This allowance is equivalent to the employer's pension contributions otherwise payable to the relevant pension scheme less the cost of providing continued life cover and less the employer National Insurance Contributions payable. In respect of salary above the Network Rail earnings cap (currently £149,400 but benefits were based on last year's value £145,800), executive directors and senior management may receive an additional pension allowance in the form of a cash salary supplement or contribution to a defined contribution scheme.

The table below sets out details for executive directors for 2015 in respect of all Network Rail pension benefits, split between the defined benefit and defined contribution/additional allowance. The value shown in the final column of this table is included as the pension column in the single total figure of remuneration on page 67.

	Defined benefit schemes					Other pension arrangements	
	Normal retirement age	Accrued pension at 31 March 2015 £000	Increase in accrued pension (net of inflation) during 2014	Transfer value of accrued pension at 31 March 2015	Value included in single figure table (A)*	Cash salary supplement or contribution to defined contribution scheme (B)	Total pension value reported in the single figure table (A+B)
Mark Carne	–	–	–	–	–	79	79
Patrick Butcher	65	12	0.2	179	4	129	133
Robin Gisby	60	40	0	841	0	112	112
Simon Kirby	60	25	0	279	0	16	16
Paul Plummer	60	36	3	388	66	102	168

Footnote: zero values have been shown where the inflation adjusted figure is negative.

The normal retirement age shows the age at which the director can retire without actuarial reduction.

Transfer values as at 31 March 2015 have been calculated in accordance with 'The Occupational Pension Schemes (Transfer Values) (Amendment) Regulations 2008'.

For the defined benefit schemes, the value shown in the Single Figure table (A) has been calculated in accordance with the Regulations by applying a multiplier of 20x to the increase in accrued pension (net of inflation) during the year. For the additional pension allowance (B), the value shown is the gross cash allowance/contribution in the year. The value shown in the single figure table is the sum of A and B.

Non-executive directors' fees

Under the framework agreement the Secretary of State sets the pay for the chair and non-executive directors of Network Rail. The fees for the non-executive directors remain unchanged and were last reviewed in 2013 and no increase was made at that time.

The table below summarises the remuneration for the non-executive directors in respect of 2015.

	Fees	
	2015	2014
Malcolm Brinded	60	57
Sharon Flood[1]	30	–
Mike Firth[2]	17	56
Chris Gibb	50	7
Lawrie Haynes[3]	15	53
Janis Kong	63	50
Keith Ludeman[4]	24	79
Michael O'Higgins	60	57
Richard Parry-Jones	250	250
Bridget Rosewell	67	60

1 Sharon Flood was appointed to the board on 25 August 2014.
2 Mike Firth stepped down from the board following the AGM on 18 July 2014.
3 Lawrie Haynes stepped down from the board following the AGM on 18 July 2014
4 Keith Ludeman stepped down from the board following the AGM on 18 July 2014.

Payments to former directors (audited)

There were no payments to former directors during 2014/15.

ANNUAL REMUNERATION REPORT CONTINUED

Payments for loss of office (audited)
Robin Gisby stepped down from the board on 27 February 2015. He received a payment in lieu of notice of £194,000, which is six months' pay in accordance with his contract. This payment was approved by the committee.

Outside appointments
The group is supportive of executive directors who wish to take on a non-executive directorship in order to broaden their experience and enhance their contribution to the company. Executive directors are normally required to seek approval from the committee to retain any fees they receive in respect of such appointments.

Additional disclosures
The following disclosures are required by the Regulations to provide additional context for considering executive remuneration.

Percentage change in remuneration
The table below shows the percentage change in the salary, benefits and AIP of the chief executive and all Network Rail employees from 2014 to 2015.

For the purposes of the table below, the annual change in the value of each of the components for the chief executive has been calculated using the data disclosed in the relevant columns of the single total figure of remuneration table on page 67.

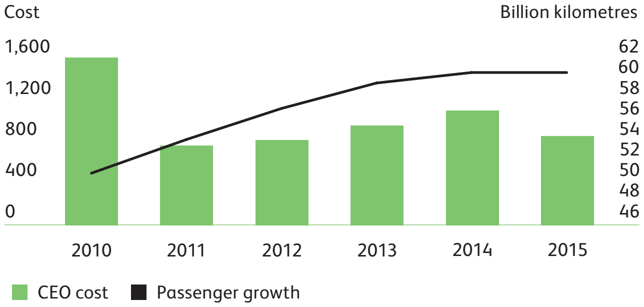
	Chief executive	All employees
Salary	0.0 %	2.44 %
Benefits	0.0 %	0.0 %
Bonus	-40 %	0.0 %

Salary review effective 1 January and 1 July 2014. Bonus is based on any changes to maximum opportunity.

Performance graph and table
Under the Regulations, companies are required to include a chart showing historic total shareholder return (ie, share price and re-invested dividends) over a six-year period alongside a table that shows the remuneration paid to the chief executive over the same period.

Network Rail has no listed shares and therefore cannot provide the required chart. However, in line with the principle of this disclosure, the chart below tracks the performance of Network Rail performance indicators over a six-year period and the table below provides remuneration data for the individuals occupying the role of chief executive for each financial year over the equivalent period.

Number of passenger kilometres travelled



	2015	2014		2013	2012	2011		2010
Chief executive	Mark Carne	David Higgins	Mark Carne	David Higgins	David Higgins	David Higgins	Iain Coucher	Iain Coucher
Single total figure of remuneration	£771k	£790k	£200k	£863k	£736k	£161k	£582k	£1,447k
AIP (% of maximum)	0 %	20.9 %	N/A	28.6 %	0 %	N/A	N/A	56.8 %
LTIP vesting (% of maximum)	N/A	N/A	N/A	N/A	N/A	N/A	N/A	47.8 %

David Higgins was appointed chief executive on 1 February 2011
Mark Carne was appointed chief executive on 24 February 2014
N/A indicates that there was no eligibility for an award vesting in respect of the relevant year.

Relative importance of spend on pay

Under the Regulations, companies are required to illustrate the relative importance of spend on pay by disclosing the total employee remuneration and returns to shareholders (ie, dividends and share buybacks) in the reporting year and the prior year. Network Rail is a not-for-dividend company and therefore cannot provide data on returns to shareholders. Therefore, in line with the principle of this disclosure, the table below includes other key Network Rail metrics to illustrate employee remuneration in the context of overall business activities.

	2015	2014	Change (%)
Total employee remuneration	£1,919m	£1,909m	0.5
Total expenditure	£9,391m	£9,772m	-4

Consideration of directors' remuneration – remuneration committee and advisers

The membership of the committee during the year comprised the following independent non-executive directors: Michael O'Higgins, Richard Parry-Jones, Chris Gibb and Sharon Flood. Chris and Sharon joined the committee on 25 September 2014.

The group general counsel is secretary to the committee. The committee is also supported by the director, human resources, head of reward and benefits and deputy company secretary. The chief executive attends meetings at the invitation of the committee. No individual is present when their own remuneration is being discussed.

In carrying out its responsibilities in line with best practice, the committee seeks independent external advice as necessary. During the year, the committee retained Deloitte LLP to provide independent advice on the major review of remuneration principles and the development of the CP5 remuneration framework. Deloitte had been appointed by the committee during 2012 following a selection process undertaken by the committee. The committee is comfortable that the Deloitte engagement partner and team provide objective and independent remuneration advice to the committee and do not have any connections with Network Rail that may impair their objectivity and independence. Deloitte is a founding member of the Remuneration Consultants Group and voluntarily operates under the code of conduct in relation to executive remuneration consulting in the UK. The code of conduct can be found at www.remunerationconsultantsgroup.com. During 2015, Deloitte provided independent advice to the committee in respect of the design and implementation of the CP5 remuneration framework, trends in corporate governance, and the adoption of new remuneration reporting requirements. The fees charged by Deloitte for the provision of independent advice to the committee during 2014/15 were £45,000. Deloitte also provide services to the group in respect of programme support to Network Operations, Digital Railway and the HR directorate, and property advice.

Key remuneration committee agenda items during the year

April 2014	• Remuneration policy • Review of directors' remuneration report • Incentives policy
May 2014	• Approval of 2013/14 AIP out-turn • Remuneration policy • Incentive targets for 2014/15 • Review of directors' remuneration report
June 2014	• 2012-15 LTIP targets and measures review (following CP5 determination)
September 2014	• Update on remuneration trends • Executive director objectives • Reclassification
November 2014	• Clawback and code of practice
March 2015	• Incentives • Benchmarking information

Statement of voting at annual general meeting

At the annual general meeting held on 18 July 2014, votes cast in respect of directors' remuneration were:

	Votes For		Votes Against			
Resolution	#	%	#	%	Total votes cast	Votes Withheld
Approval of directors' remuneration report for 2014	40	97.56%	1	2.44%	41	0
Approval of directors' remuneration policy for 2014	38	92.68%	3	7.32%	41	0
Approval of the management incentive plan	38	92.68%	3	7.32%	41	0

ANNUAL REMUNERATION REPORT CONTINUED

Remuneration policy summary for 2015/16

Principles which underpin the framework

Simple	Competitive and fair	Performance and safety	Aligned with employees
The framework should be clear and transparent for all stakeholders	Remuneration should appropriately reflect the skills and experience of the individual and the scope and complexity of the role. At the same time, should provide value for money for taxpayers and passengers	The incentive framework should reward exceptional performance in the areas most important for our stakeholders – such as safety, train performance and financial management. No reward for failure	The incentive structure is cascaded to all Network Rail employees to create an alignment throughout the business Business performance is consistently measured through the scorecard

Summary of remuneration policy for CP5

The structure of the remuneration framework for executive directors in CP5 is summarised below. No payments outside of this framework can be made following member approval of the policy at the 2014 AGM.

Fixed remuneration	Salary	• Salaries are set at a level that reflects the skills and experience of the individual as well as the scope and responsibilities of the role allowing the company to recruit the calibre of individual needed to lead the business. Salaries have not been increased in 2015 and therefore remain at 2014 rates: Mark Carne £675k Patrick Butcher £412k Paul Plummer £364k • In line with other employee groups, salaries are reviewed annually and increases will normally be in line with the typical salary increase for the overall employee population over the same period.
	Benefits	• Includes discounted rail travel and life insurance in line with all Network Rail employees, as well as car and healthcare benefits aligned with those for other management positions.
	Pension	• Eligible to participate in Network Rail pension schemes on the same basis as all employees • To provide a market competitive pension benefit, executive directors and senior managers may also receive a supplementary cash allowance of 10 per cent of salary above the Network Rail pension cap (30 per cent for existing executives).
Performance related	Incentive	• One incentive plan based on the achievement of stretching annual performance targets in the areas which our stakeholders care most about • All Network Rail employees are eligible to participate, based on aligned business scorecard • For executive directors, a maximum annual opportunity of 20 per cent of salary, subject to performance and any amount is deferred for three years, subject to safety and sustainability obligations over the period.

Any new appointments are based on the framework above. Should an executive director leave the business, there would be no reward for failure.

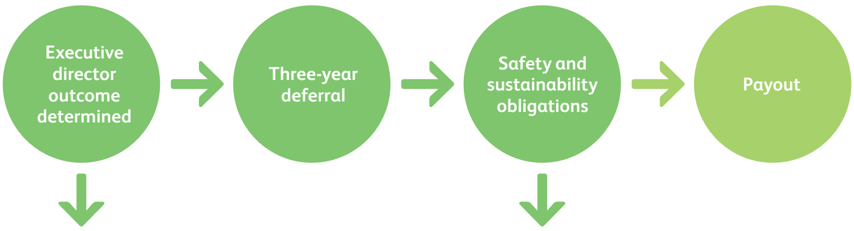
Further detail on the framework above is provided in the remuneration policy published last year (www.networkrail.co.uk/RemunerationReport.pdf) and in the following section.

Incentive structure for executive directors – aligned to the things which matter for stakeholders

Performance target framework common business performance scorecard

Corporate performance scorecard, which is split between long-term stewardship of the railway and annual operating performance

Measures aligned with CP5 regulatory targets and areas that matter most to stakeholders



Half of the incentive is based on the corporate scorecard and half based on targets specific to the business unit or area of responsibility for each executive director. This allows incentive payments to reflect the performance of different business areas

The committee takes into account overall business performance in the year including safety performance and may adjust outcome on this basis. In the event of a serious incident for which Network Rail was responsible, no incentive would normally be payable to any executive director

Any amount earned is deferred for a period of three years, in line with best practice

To pay any deferred amount, the committee must confirm the safety and sustainability obligations over the period have been met. To the extent that they are not met, the committee can reduce the deferred amount

ANNUAL REMUNERATION REPORT CONTINUED

Safety and sustainability obligations

The payment of any deferred amount is subject to the committee's confirmation that the safety and sustainability obligations described below have been met. In the event that the obligations are not met, the committee may reduce the value of the deferred amount (including to zero), or impose further conditions which must be fulfilled prior to payment.

Details of how the committee had undertaken the assessment prior to payment of an award would be disclosed in the relevant annual remuneration report.

- **Safety.** In the event of a serious safety incident over the deferral period which impacts passengers, workforce, or the general public, for which Network Rail was responsible, the committee has discretion to reduce the deferred amount(s) which may be payable to an executive director (including to zero)
- **Sustainability of business performance.** The committee must confirm that performance delivered in the performance year has been appropriately sustained over the deferral period. No specific targets would apply for this assessment, but the committee would consider the following indicators:
  - Material downturn in a metric. The committee's assessment of the extent to which performance in each of the metrics under the balanced scorecard (including safety) has been appropriately sustained in the years following the performance year. A consistent and material downturn in performance for a particular metric following the performance year may indicate performance has not been appropriately sustained
  - Undermining long-term stewardship. Determination by the committee that annual operating performance targets have not been achieved as a result of actions which could undermine effective stewardship and performance of the railway network over the long term
  - Overall CP5 consistency. Incentive payouts in respect of CP5 which, in aggregate, are consistent with overall performance in CP5 against the regulatory objectives.
- **Other circumstances:**
  - A material misstatement of the company's audited financial results and disclosed operational performance
  - A material failure of risk management, or a failure to comply with obligations set out in applicable contractual agreements (including the network licence, the access agreements or other relevant contracts)
  - Gross misconduct
  - Serious reputational damage to the company as a result of the participant's misconduct or otherwise.

Balanced scorecard business performance targets for 2016

The following table summarises the proposed specific business performance measures for executive directors for the 2016 financial year, based on the framework described above.

The business scorecard used to measure performance every period is translated into incentive plan measures and targets across the business.

After the first year of the scorecard the committee and board undertook a review and concluded that a number of minor refinements should be made.

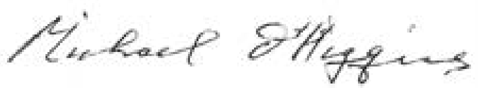
The proposed changes are summarised in the table below:

Change	Reason
Introduction of cancellations and significant lateness, England and Wales (CaSL)	CaSL is an important business measure for Network Rail and is an important regulatory measure. Given this importance, it was felt that it should be included as a core performance measure
Investing in the railway and financial performance measures – a specific measure of financial performance of investment projects incorporated into the financial performance measure	The financial performance measure will be split into two parts, one of which will specifically be a measure of the financial performance of the investment projects measure. Financial performance will continue to have a 20 per cent weighting, with 5 per cent specifically on investment projects. To reflect this change, the overall investing in the railway measure will reduce to 10 per cent
Satisfaction measure – increase weighting to 15 per cent and specifically introduce a new measure of lineside neighbour satisfaction	The current satisfaction measure which forms 10 per cent of the overall incentive opportunity in the scorecard includes customer (TOC) satisfaction and passenger survey results. Network Rail recognises that their lineside neighbours are also an important stakeholder group in terms of satisfaction and is therefore proposing to introduce an additional measure for lineside neighbour satisfaction. All of the satisfaction measures will have equal weighting: Customer (TOC) survey results – 5 per cent Passenger survey results – 5 per cent Lineside neighbours – 5 per cent
Safety measures – separate calculation of workforce close calls and closure of close calls within 28 days	Safety measures form 20 per cent of the overall scorecard for incentive purposes and no changes are being made to this. Currently close calls and closure of close calls form one quarter of this measure. For FY16 these will be separated out. The safety measures will therefore be: Lost time injury frequency rate – 5 per cent Workforce close calls – 3 per cent Close calls closed within 28 days – 2 per cent Train accident precursor indicator model, passenger – 5 per cent Level crossing risk indicator model – 5 per cent

ANNUAL REMUNERATION REPORT CONTINUED

The framework of the 2015/16 scorecard is detailed below, including measures and weightings. The targets will be published on the website once finalised with stakeholders.

Area	Performance measure	Weighting
Safety		
Workforce safety	Lost time injury frequency rate (LTIFR)	5.0%
Workforce safety	Workforce close calls recorded	3.0%
Workforce safety	Close calls closed within 28 days	2.0%
Passenger safety	Passenger component of train accident risk where Network Rail is the risk controller	5.0%
Level crossing risk reduction	Benefits only as measured by the level crossing risk indicator model	5.0%
Train performance		
PPM	National	12.0%
CaSL	England and Wales	6.0%
Freight	Freight delivery metric (FDM)	2.0%
Financial performance		
Financial performance measure	Total efficiency generated (£m) excluding enhancements	25.0%
Financial performance measure	Enhancements only (£m)	5.0%
Investment		
Top 10 IP renewals and enhancement milestones	Key milestones of top 10 renewals and enhancement projects	5.0%
All delivery plan enhancement milestones (%)	Interim and completion milestones of all enhancement projects	5.0%
Asset Management		
CRI (composite reliability index)	Total	7.5%
Renewals (seven key volumes)	Volumes	7.5%
Satisfaction		
Customer	Survey results	5.0%
Passenger	Survey results	5.0%
Lineside neighbours	Level of awareness about disruption amongst lineside neighbours who experienced disruption in past 12 months. Response to 'To what extent would you speak highly or critically of Network Rail?'	5.0%



Michael O'Higgins
Chair of the remuneration committee
10 June 2015

DIRECTORS' REPORT

Disclosures regarding business performance and activities that were previously part of the directors' report are now contained in the strategic report (pages 4 to 42) and corporate governance report (pages 43 to 80) to increase their prominence.

Directors

The directors who served during the year and held office at the date of signing the financial statements are detailed on pages 44 to 46.

Directors' conflicts of interest

In accordance with company law and the company's articles of association, the directors have the power to authorise any matter which would or might otherwise constitute or give rise to a direct or indirect conflict of interest. However, such authority can only be exercised if the director has declared his actual or potential conflict of interest to the board. At the date of this report there were no conflicts of interest.

Directors' & Officers' (D&O) liability insurance

During 2014/15 the company held a D&O liability insurance policy. That policy covers directors and officers of the company against the costs of defending proceedings brought against them in their capacity as a director or officer of the company.

Directors' indemnities

In accordance with company law and the company's articles of association, every director and officer of the company is indemnified by the company against any liability incurred in connection with any negligence, default, breach of duty or breach of trust in relation to the company. This excludes any liability to the company and any fine imposed in criminal proceedings or any penalty payable to a regulatory authority. This also excludes any liability incurred by the director in defending criminal proceedings in which he/she is convicted or in defending civil proceedings brought against the director or officer by the company, in which judgement is given against the director or officer.

Political donations

In line with company policy, no donations to political parties were made during the year (2014: £nil).

The company needs to work closely with all types of community representatives and has a significant amount of contact with a wide range of elected representatives (including members of Parliament, Scottish Parliament, London Assembly and Welsh Assembly) as well as with non-governmental organisations, pressure groups and campaigning organisations. Meetings are held to discuss both the company's issues and the issues of passengers and freight users on a national and regional scale.

Opportunity is also taken each year to explain to elected representatives the company's business plans, performance and significant developments within the business.

Investing in research and development

Technology and innovation is fundamental to the company's success in CP5 and beyond.

During the year the group charged £1m to the income statement (2014: £1m) on research and development. Other costs relating to significant development work have been capitalised in property, plant and equipment.

Auditors

For 2015/16 it is proposed, in accordance with the Framework Agreement, that the Comptroller and Auditor General be appointed as the group's independent external auditor to replace PricewaterhouseCoopers LLP (see page 58). This will be voted on by members at the 2015 AGM.

Statement of directors' responsibilities

The directors are responsible for preparing the annual report, the directors' remuneration report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the group and company financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the group and the company and of the profit or loss of the group for that period. In preparing these financial statements, the directors are required to:

- Select suitable accounting policies and then apply them consistently
- Make judgements and accounting estimates that are reasonable and prudent
- State whether applicable IFRSs as adopted by the European Union have been followed, subject to any material departures disclosed and explained in the financial statements.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the company's transactions and disclose with reasonable accuracy at any time the financial position of the company and the group and enable them to ensure that the financial statements and the directors' remuneration report comply with the Companies Act 2006 and, as regards the group financial statements, Article 4 of the IAS Regulation. They are also responsible for safeguarding the assets of the company and the group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

DIRECTORS' REPORT CONTINUED

The directors consider that the annual report and accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for members to assess the company's performance, business model and strategy.

Each of the directors in office at the date of this report, whose names and functions are listed on pages 44-46 confirm that, to the best of their knowledge:

- The group financial statements, which have been prepared in accordance with IFRSs as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and profit of the group
- The directors' report contained in the annual report includes a fair review of the development and performance of the business and the position of the group, together with a description of the principal risks and uncertainties that it faces.

Disclosure of information to the independent auditors

Each of the directors at the date of approval of this report confirms that:

- So far as the director is aware, there is no relevant audit information of which the company's auditor is unaware
- The director has taken all steps that he or she ought to have taken as a director in order to make the director aware of any relevant audit information and to establish that the company's auditor is aware of that information.

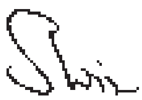
Going concern

The group's business activities, together with the factors likely to affect its future development, performance and position are set out in the 'strategic report' section on pages 4 to 42. 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 12 to 15. In addition, Note 25 to the accounts includes 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.

After making enquiries, the directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

The directors' report has been signed on behalf of the board of the company.



Suzanne Wise
Group general counsel and company secretary
10 June 2015

FINANCIAL STATEMENTS AND NOTES

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF NETWORK RAIL LIMITED

Report on the financial statements

Our opinion

In our opinion:

- Network Rail Limited's group financial statements and company financial statements (the financial statements) give a true and fair view of the state of the group's and of the company's affairs as at 31 March 2015 and of the group's loss and the group's and the company's cash flows for the year then ended
- the group financial statements have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union
- the 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 and
- the financial statements have been prepared in accordance with the requirements of the Companies Act 2006.

What we have audited

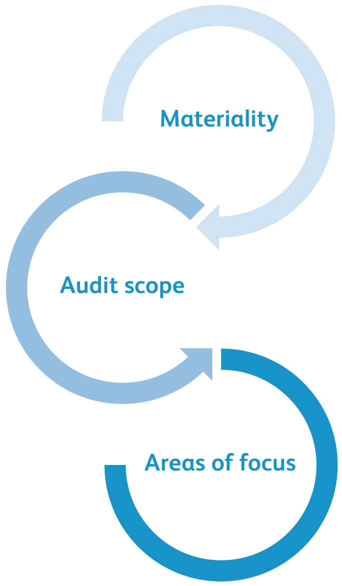
Network Rail Limited's financial statements comprise:

- the group and company balance sheets as at 31 March 2015
- the group income statement and statement of comprehensive income for the year then ended
- the group and company statement of cash flows for the year then ended
- the group and company statements of changes in equity for the year then ended and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and IFRSs as adopted by the European Union and, as regards the company financial statements, as applied in accordance with the provisions of the Companies Act 2006.

Our audit approach



Materiality

- Overall group materiality: £50 million (2014: £50 million) which represents approximately 0.1 % of the group's total assets.

Audit scope

- The group audit team carried out the audits of the complete financial information of Network Rail Infrastructure Limited (the group's main operating company) and Network Rail Infrastructure Finance PLC (the group's financing company), as well as of the consolidation.

Areas of focus

- Plant, property and equipment – valuation of railway network – including any adjustments for anticipated underperformance for the remainder of the control period
- Appropriate recording of capital expenditure – including consideration of whether expenditure is operating or capital in nature
- Recognition of deferred tax assets in view of uncertainty over availability of future taxable profits
- Valuation of defined benefit pension scheme assets and liabilities – including assessment of the appropriateness of the actuarial assumptions adopted
- Valuation of derivative financial instruments which are used to hedge the group's exposure to fluctuations in interest, foreign exchange and RPI rates

The scope of our audit and our areas of focus

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) (ISAs (UK & Ireland)).

We designed our audit by determining materiality and assessing the risks of material misstatement in the financial statements. In particular, we looked at where the directors made subjective judgements, for example in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits we also addressed the risk of management override of internal controls, including evaluating whether there was evidence of bias by the directors that represented a risk of material misstatement due to fraud.

The risks of material misstatement that had the greatest effect on our audit, including the allocation of our resources and effort, are identified as 'areas of focus' in the table below. We have also set out how we tailored our audit to address these specific areas in order to provide an opinion on the financial statements as a whole, and any comments we make on the results of our procedures should be read in this context. This is not a complete list of all risks identified by our audit.

Area of focus	How our audit addressed the area of focus
Plant, property and equipment – valuation of railway network See also note 12 and the audit committee report on page 56. The railway network is revalued at each reporting date to its fair value. The valuation model used is an income based approach which acts as a proxy for a discounted cash flow. The valuation model is complex and involves significant management estimates and judgements about the delivery of capital enhancement and renewal projects, train performance, efficiency and method and cost of financing over the remainder of Control Period 5 (CP5) ending on 31 March 2019, against the delivery plan set by the Office of Rail and Road (ORR). Projections about the future are inherently uncertain and some of the judgements made in the valuation model are highly subjective. Given the level of spend in any control period, changes to the assumptions or any external factors can have a highly material impact on the valuation. Also, if the ORR were to disallow certain expenditure from earning a return due to deferrals or inefficiencies, or to impose penalties on Network Rail, then this would need to be reflected in the model and would affect the valuation.	We checked that the model was mathematically accurate and were satisfied that the financial information was consistent with the underlying books and records. We performed detailed work over the material elements of the revaluation movements in the year and were able to obtain appropriate explanations and evidence for the assumptions adopted. We also assessed the reasonableness of the key judgements and estimates behind the inputs to the model in respect of future performance across CP5. We obtained management's delivery plan for CP5, and concluded that it was reasonable based on discussions with key members of management regarding its achievability. We then held discussions with Arup, the regulator's independent reporter, on the findings of their work in respect of efficiency measures in CP5 and checked how they were reflected in the valuation. Finally we were satisfied that the disclosures in the financial statements around the valuation process and the related assumptions and judgements were clear and balanced.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF NETWORK RAIL LIMITED CONTINUED

Area of focus	How our audit addressed the area of focus
Appropriate recording of capital expenditure See also note 12 and the audit committee report on page 56. Due to the nature of Network Rail's business and the construction contract method of accounting, there is an element of judgement in the measurement of work-in-progress and therefore capital spend, on a project-by-project basis and as a whole. There is also a risk of incorrect classification between operating and capital expenditure. With total spend in the year of £6,474 million and a capital accrual of £1,565 million at 31 March 2015, these judgements may have a material impact on the financial statements. Furthermore the recording of capital expenditure as additions also has a direct impact on the valuation of the network. See the previous area of focus.	We tested controls over the group's Governance for Railway Investment Projects (GRIP) process and found that for the sample tested it allowed the group to track the status of each capital project accurately. We also performed testing over the purchases to payables cycle, with a particular focus on capital items, work done in respect of on-going projects and the value of capital accruals, obtaining sufficient evidence on the controls for our audit of capital expenditure. We also tested the classification of spend as either capital or operating for a sample of items. We tested controls over the booking of costs to projects and for selected projects and supplemented this with tests of detail over costs booked to projects. We found no material exceptions in our testing. We also carried out detailed procedures on a sample of projects that provided us with satisfactory evidence over the accuracy of cut-off and accruals.
Recognition of deferred tax assets See also note 22 and the audit committee report on page 56. As at 31 March 2014, the group had a deferred tax asset of £597 million in respect of trading losses; this asset was written off in the year because changes in the group's circumstances gave rise to doubts over its recoverability. These circumstances include the reclassification by the Office of National Statistics of Network Rail as a public body and discussions held with the Department for Transport as to whether Network Rail will generate sufficient future taxable profits, due to uncertainty over the future regulatory return that the ORR will determine for future control periods.	We reviewed management's taxable profit forecasts with reference to the CP5 delivery plan, and concluded that it was appropriate to derecognise the deferred tax asset on the grounds that there was not sufficient certainty that there would be sufficient future taxable profits. We challenged management's assumptions included within the forecast and confirmed the mathematical accuracy of the forecast. We also considered the accuracy of management's budgeting process by looking at the evidence of the actual performance in CP4 against the initial delivery plan and did not identify any factors to contradict the approach taken.
Valuation of defined benefit pension scheme assets and liabilities See also note 26 and the audit committee report on page 56. The group participates in defined benefit pension schemes and Network Rail's share is a net liability of £1,505 million as at 31 March 2015. The valuation of the pension scheme liabilities requires significant levels of judgement and technical expertise in choosing appropriate assumptions. Changes in assumptions (including salary increases, inflation, discount rates and mortality) can have a material impact on the calculation of the liabilities.	We evaluated the assumptions adopted by management in respect of calculating the pension scheme liabilities. This included comparison of the key assumptions (discount and inflation rates, salary increases and mortality rates) to our own benchmarks, which reflect national and industry averages. We were able to confirm that the assumptions were within reasonable ranges based on market conditions at the balance sheet date. We confirmed the existence and valuation of the pension scheme assets to third party confirmations from the scheme custodians. We also tested the underlying information provided to the group's actuaries back to supporting evidence without noting any material issues.
Valuation of derivative financial instruments See also note 20 and the audit committee report on page 56. The group has a number of financial instruments in place which are recorded at a fair value of £272 million (liability). This includes foreign exchange forwards, interest rate swaps and cross currency interest rate swaps, which are used to reduce volatility over Network Rail's £38,548 million debt. Determining the fair values of these financial instruments requires judgements and assumptions in particular in relation to future interest and exchange rates. Changes in these assumptions can have a material impact on the valuation of financial instruments.	We tested the existence of financial instruments, agreeing a sample to contracts and obtaining confirmations from the relevant counterparties. We tested IT controls for the systems that the contract data is maintained within and where the valuation calculations are performed. We considered the reasonableness of the forward looking assumptions, agreeing to third party data and performed independent valuations for a sample of Network Rail's financial instruments. No material issues were noted in our testing.

How we tailored the audit scope

The group is structured across ten geographic routes which make up the UK's railway network, together with corporate, network operations, business services, infrastructure projects, property, treasury business units and tax. From a legal perspective, the majority of operations are within Network Rail Infrastructure Limited. The treasury business is in a separate legal entity, Network Rail Infrastructure Finance PLC, and there are further small legal entities including a consultancy business and a company that manages the maintenance of non-owned stations. The group is a consolidation of these legal entities.

Accordingly, based on size and risk characteristics, we determined that our audit work would be performed on the complete financial information of Network Rail Infrastructure Limited and Network Rail Infrastructure Finance PLC. This work was undertaken by the group audit team with no component auditor involvement. This work covered substantially all of the group's assets and pre-tax profits and, together with the procedures performed at the group level, gave us the evidence we needed for our opinion on the group financial statements as a whole.

Materiality

The scope of our audit was influenced by our application of materiality. We set certain quantitative thresholds for materiality. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and on the financial statements as a whole.

Based on our professional judgement, we determined materiality for the financial statements as a whole as follows:

Overall group materiality £50 million (2014: £50 million).	
How we determined it Approximately 0.1 % of total assets.	
Rationale for benchmark applied Network Rail Limited is a regulated company whose returns are driven off its Regulatory Asset Base and determined by the ORR. Accordingly, consistent with the previous year, we believe that an asset based measure is the most appropriate benchmark to use in determining materiality for the group financial statements.	

We agreed with the Audit Committee that we would report to them misstatements identified during our audit above £2.5 million (2014: £2.5 million) as well as misstatements below that amount that, in our view, warranted reporting for qualitative reasons.

Going concern

The directors have voluntarily complied with Listing Rule 9.8.6(R)(3) of the Financial Conduct Authority and provided a statement in relation to going concern, set out on page 108, required for companies with a premium listing on the London Stock Exchange.

The directors have requested that we review the statement on going concern as if the company were a premium listed company. We have nothing to report having performed our review.

As noted in the directors' statement, the directors have concluded that it is appropriate to prepare the financial statements using the going concern basis of accounting. The going concern basis presumes that the group and company have adequate resources to remain in operation, and that the directors intend them to do so, for at least one year from the date the financial statements were signed. As part of our audit we have concluded that the directors' use of the going concern basis is appropriate.

However, because not all future events or conditions can be predicted, these statements are not a guarantee as to the group's and company's ability to continue as a going concern.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF NETWORK RAIL LIMITED

Other required reporting

Consistency of other information

Companies Act 2006 opinions

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

ISAs (UK & Ireland) reporting	
The directors have chosen to voluntarily comply with the UK Corporate Governance Code (the Code) as if the company were a premium listed company. Under ISAs (UK & Ireland) we are required to report to you if, in our opinion:	
• Information in the Annual Report is: – materially inconsistent with the information in the audited financial statements; or – apparently materially incorrect based on, or materially inconsistent with, our knowledge of the group and company acquired in the course of performing our audit; or – otherwise misleading.	We have no exceptions to report arising from this responsibility.
• the statement given by the directors on page 52 in accordance with provision C.1.1 of the Code, that they consider the Annual Report taken as a whole to be fair, balanced and understandable and provides the information necessary for members to assess the group's and company's performance, business model and strategy is materially inconsistent with our knowledge of the group and company acquired in the course of performing our audit.	We have no exceptions to report arising from this responsibility.
• the section of the Annual Report on page 56, as required by provision C.3.8 of the Code, describing the work of the Audit Committee does not appropriately address matters communicated by us to the Audit Committee.	We have no exceptions to report arising from this responsibility.

Adequacy of accounting records and information and explanations received

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

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept by the company, or returns adequate for our audit have not been received from branches not visited by us; or
- the company financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Other voluntary reporting

Opinion on additional disclosures

Directors' Remuneration Report

The company voluntarily prepares a Directors' Remuneration Report in accordance with the provisions of the Companies Act 2006. The directors have requested that we audit the part of the Directors' Remuneration Report specified by the Companies Act 2006 to be audited as if the company were a quoted company.

In our opinion, the part of the Directors' Remuneration Report to be audited has been properly prepared in accordance with the Companies Act 2006.

Matters on which we have agreed to report by exception

Corporate governance statement

The company has chosen voluntarily to comply with the UK Corporate Governance Code. The directors have requested that we review the parts of the Corporate Governance Statement relating to the company's compliance with the ten provisions of the UK Corporate Governance Code specified for auditor review by the Listing Rules of the Financial Conduct Authority as if the company were a premium listed company. We have nothing to report having performed our review.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 79, 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 and express an opinion on the financial statements in accordance with applicable law and ISAs (UK & Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

What an audit of financial statements involves

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 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.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Annual Report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Jonathan Hook (Senior Statutory Auditor)
for and on behalf of
PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London
10 June 2015

INCOME STATEMENT
FOR THE YEAR ENDED 31 MARCH 2015

	Note	2015 Group £m	2014 Group £m
Revenue	3	**6,087**	6,333
Net operating costs	4	**(4,352)**	(4,332)
Operating profit		**1,735**	2,001
Property revaluation movements and profits on disposal		**140**	96
Profit from operations	5	**1,875**	2,097
Finance income	7	**10**	20
Other gains and losses	8	**(41)**	304
Finance costs	9	**(1,338)**	(1,386)
Profit before tax		**506**	1,035
Tax*	10	**(882)**	221
(Loss)/profit after tax for the year		**(376)**	1,256

* The tax charge in the year includes the derecognition of previously recognised deferred tax assets of £597m. The prior year tax credit includes a £235m credit relating to “prior year adjustments” and £220m credit for the enactment of corporation tax rate reduction.

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 result for the year was £nil (2014: £nil).

STATEMENT OF COMPREHENSIVE INCOME
FOR THE YEAR ENDED 31 MARCH 2015

	Note	2015 Group £m	2014 Group £m
(Loss)/profit for the year		**(376)**	1,256
Other comprehensive (expense)/income:			
Items that will not be reclassified to profit or loss			
Loss on revaluation of the railway network	12	**(488)**	(1,813)
Actuarial (loss)/gain on defined benefit pension schemes	26	**(159)**	140
Tax relating to components of other comprehensive income	22	**122**	320
Total items that will not be reclassified to profit or loss		**(525)**	(1,353)
Items that may be reclassified to profit or loss			
(Loss)/gain on movement in fair value of cash flow hedge derivatives		**(982)**	172
Reclassification of balances in the hedging reserve to the income statement		**73**	218
Tax relating to components of other comprehensive income	22	**19**	(124)
Total items that may be reclassified to profit or loss		**(890)**	266
Other comprehensive expense for the year		**(1,415)**	(1,087)
Total comprehensive (expense)/income for the year		**(1,791)**	169

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 MARCH 2015

Group	Revaluation reserve £m	Other reserve* £m	Hedging reserve £m	Retained earnings £m	Total equity £m
Balance at 31 March 2013	2,890	249	(188)	5,062	8,013
Profit for the year	–	–	–	1,256	1,256
Other comprehensive income/(expense) for the year:					
Impact of change in tax rate	159	–	(9)	(17)	133
Revaluation of the railway network	(1,813)	–	–	–	(1,813)
Transfer of deemed cost depreciation from revaluation reserve	(84)	–	–	84	–
Decrease in deferred tax liability on the railway network	228	–	–	(17)	211
Actuarial gain on defined benefit pension schemes	–	–	–	140	140
Deferred tax on actuarial gain	–	–	–	(33)	(33)
Increase in fair value of hedging derivatives	–	–	172	–	172
Deferred tax on all hedging reserve movements/retained earnings	–	–	(115)	–	(115)
Reclassification of balances in hedging reserve to the income statement	–	–	218	–	218
Total comprehensive (expense)/income for the year:	(1,510)	–	266	1,413	169
Balance at 31 March 2014	**1,380**	**249**	**78**	**6,475**	**8,182**
Loss for the year	–	–	–	(376)	(376)
Other comprehensive (expense)/income for the year:					
Revaluation of the railway network	(488)	–	–	–	(488)
Transfer of deemed cost depreciation from revaluation reserve	(42)	–	–	42	–
Decrease in deferred tax liability on the railway network	98	–	–	(9)	89
Actuarial loss on defined benefit pension schemes	–	–	–	(159)	(159)
Deferred tax on actuarial loss	–	–	–	33	33
Decrease in fair value of hedging derivatives	–	–	(982)	–	(982)
Deferred tax on all hedging reserve movements/retained earnings	–	–	19	–	19
Reclassification of balances in hedging reserve to retained earnings	–	–	13	(13)	–
Reclassification of balances in hedging reserve to the income statement	–	–	73	–	73
Total comprehensive (expense)/income for the year:	**(432)**	**–**	**(877)**	**(482)**	**(1,791)**
Balance at 31 March 2015	**948**	**249**	**(799)**	**5,993**	**6,391**

* Other reserves of £249m (2014: £249m) include the vesting reserve on privatisation.

There has been no movement in the current or prior year affecting the statement of changes in equity for the company.

BALANCE SHEETS
AT 31 MARCH 2015

	Note	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Assets					
Non-current assets					
Intangible assets	11	**67**	68	**–**	–
Property, plant and equipment – the railway network	12	**54,091**	49,833	**–**	–
Investment property	13	**982**	856	**–**	–
Derivative financial instruments	20	**721**	637	**–**	–
Finance lease receivables	16	**–**	1	**–**	–
Other receivables	17	**109**	135	**–**	–
Interest in subsidiaries and joint ventures	14	**42**	27	**–**	–
		56,012	51,557	**–**	–
Current assets					
Inventories	15	**198**	173	**–**	–
Finance lease receivables	16	**1**	2	**–**	–
Trade and other receivables	17	**1,475**	915	**–**	–
Current tax assets		–	4	**–**	–
Derivative financial instruments	20	**50**	11	**–**	–
Cash and cash equivalents		**313**	1,253	**–**	–
		2,037	2,358	**–**	–
Total assets		**58,049**	53,915	**–**	–
Liabilities					
Current liabilities					
Trade and other payables	18	**(3,151)**	(3,886)	**–**	–
Current tax liabilities		**(2)**	–	**–**	–
Borrowings	19	**(3,133)**	(2,707)	**–**	–
Derivative financial instruments	20	**(5)**	(277)	**–**	–
Provisions	21	**(50)**	(143)	**–**	–
		(6,341)	(7,013)	**–**	–
Net current liabilities		**(4,304)**	(4,655)	**–**	–
Non-current liabilities					
Borrowings	19	**(35,415)**	(31,308)	**–**	–
Derivative financial instruments	20	**(1,038)**	(387)	**–**	–
Other payables	18	**(4,129)**	(3,297)	**–**	–
Retirement benefit obligation	26	**(1,505)**	(1,237)	**–**	–
Deferred tax liabilities	22	**(3,230)**	(2,491)	**–**	–
		(45,317)	(38,720)	**–**	–
Total liabilities		**(51,658)**	(45,733)	**–**	–
Net assets		**6,391**	8,182	**–**	–
Equity					
Revaluation reserve		**948**	1,380	**–**	–
Other reserve		**249**	249	**–**	–
Hedging reserve		**(799)**	78	**–**	–
Retained earnings		**5,993**	6,475	**–**	–
Total equity		**6,391**	8,182	**–**	–

*The company has £1 share capital and £1 investment on its balance sheet

The financial statements on pages 88 to 130 were approved by the board of directors and authorised for issue on 10 June 2015.

They were signed on its behalf by:

Mark Carne
Chief executive

Patrick Butcher
Group finance director

Company registration number: 4402220

STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED 31 MARCH 2015

	Note	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Cash flows from operating activities					
Cash generated from operations	23	**3,514**	3,793	**–**	–
Interest paid*		**(1,208)**	(1,077)	**–**	–
Income tax received		**4**	4	**–**	–
Net cash generated from operating activities		**2,310**	2,720	**–**	–
Investing activities					
Interest received		**10**	20	**–**	–
Purchases of property, plant and equipment		**(6,745)**	(6,263)	**–**	–
Proceeds on disposal of property		**33**	41	**–**	–
Capital grants received		**503**	227	**–**	–
Net cash outflows from joint ventures		**(15)**	(15)	**–**	–
Capital element of finance lease receipts		**1**	2	**–**	–
Net cash used in investing activities		**(6,213)**	(5,988)	**–**	–
Financing activities					
Repayments of borrowings	19	**(2,738)**	(3,975)	**–**	–
Proceeds from borrowings	19	**6,450**	5,104	**–**	–
Increase in collateral posted	19	**(690)**	(22)	**–**	–
Decrease in collateral held	19	**(11)**	(143)	**–**	–
Cash received on settlement of derivatives		**3**	–	**–**	–
Net cash generated from financing activities		**3,014**	964	**–**	–
Net decrease in cash and cash equivalents		**(889)**	(2,304)	**–**	–
Cash and cash equivalents at beginning of the year		**1,202**	3,506	**–**	–
Cash and cash equivalents at end of the year		**313**	1,202	**–**	–
Cash and cash equivalents comprise:					
Cash, short-term bank deposits, commercial paper and money market deposits		**313**	1,253	**–**	–
Bank overdrafts		–	(51)	**–**	–
		313	1,202	**–**	–

* Balance includes the net interest on derivative financial instruments

NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 MARCH 2015

1. General information

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

The company registration number is 4402220.

The company's registered office is situated at 1 Eversholt Street, London, NW1 2DN, United Kingdom.

The company's and its subsidiaries' (together 'the group') principal activities are detailed in the 'Who we are' section on pages 16 and 19.

Network Rail is organised as a single operating segment for financial reporting purposes.

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 European Union International Accounting Standard regulation, and in accordance with interpretations of the IFRS Interpretation Committee.

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. The policies have been consistently applied to the years presented.

Reclassification of Network Rail

In December 2013, the Office for National Statistics announced the reclassification of Network Rail as a Central Government Body in the UK National Accounts and Public Sector Finances with effect from 1 September 2014. This is a statistical change driven by new guidance in the European System of National Accounts 2010 (ESA10). The reclassification does not have any impact on the group's financial reporting requirements under IFRS.

Adoption of new and revised standards

The following accounting standards and amendments to accounting standards have been adopted by the group for the first time for the financial year beginning on 1 April 2014 and not had a material impact on the group:

i) IFRS 11'Joint Arrangements'

ii) The amendment to IAS 32 on Financial instruments asset and liability offsetting.

iii) The amendment to IAS 39 'Financial instruments: Recognition and measurement', on novation of derivatives and hedge accounting.

The following accounting standards have not been early adopted by the group but will become effective in future years and are considered to have a material impact on the group that has yet to be assessed:

i) Amendment to IAS 19 (Revised) 'Employee benefits', on defined benefit plans effective from 1 July 2014, but endorsed by the EU from 1 February 2015. Employee contributions that are linked to service, but do not vary with the length of the employee service are to be deducted from the cost of benefits earned in the period that the service is provided. However, employee contributions that vary according to the length of service must be spread over the service period. Employee contributions not linked to service are reflected in the measurement of the balance sheet liability.

ii) IFRS 9 'Financial Instruments'. The standard addresses the classification, measurement and recognition of financial assets and liabilities.

There are no other IFRS or IFRS Interpretation Committee interpretations not yet effective that would be expected to have a material impact on the group.

2. Significant accounting policies continued

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 'Who we are' section on pages 16 and 19, and 'Business unit summaries' on pages 20 and 31. 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 12 to 15. In addition, Note 25 to the accounts includes 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.

After making enquiries, the directors have a reasonable expectation that the company and the group have adequate resources to continue in operational existence for the foreseeable future. Accordingly, they continue to adopt the going concern basis in preparing the annual report and accounts.

Basis of consolidation

Subsidiaries are all entities (including structured entities) over which the group has control. The group controls an entity when the group is exposed to, or has rights to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. Transactions with non-controlling interests that do not result in a loss of control are accounted for as equity transactions. In terms of subsidiaries the group:

- Consolidates subsidiaries from the date on which control passes to the group and deconsolidates from the date control ceases;
- Changes the accounting policies of subsidiaries, where necessary, to ensure consistency with the policies adopted by the group;
- Eliminates intercompany transactions and balances in the group results.

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 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 and rebates payable to, customers and stakeholders. Operating expenditure includes additional contract amounts and bonuses payable to, less penalties receivable from, suppliers and the Office of Rail and Road.

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.

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.

2. Significant accounting policies continued

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 is 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 the income statement 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 the exchange rates prevailing at the balance sheet date. Foreign currency amounts are initially recorded at the exchange rates prevailing on the dates of the transactions. Gains and losses arising on retranslation are 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 finance income, finance costs, other gains and losses, and revaluation movements and profits on disposal of properties. For the year ended 31 March 2015, the income statement has been simplified by removing the three column format as it was felt that the previous format was causing an unnecessary level of complexity.

Retirement benefit costs

Payments to the defined contribution retirement benefit scheme are charged as an expense as they fall due.

For the defined benefit schemes, 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 current service cost and plan administration expenses are recognised as an operating expense in the consolidated income statement.

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.

The net interest cost is the charge in the year on the net defined benefit liability. The charge reflects the passage of time and is recognised as a finance cost in the income statement.

Past service cost and credits are recognised immediately in the consolidated income statement.

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.

The group reflects its share of the contribution in the financial statements. The IAS 19 deficit, service cost and interest cost therefore represent 60 per cent of the total for each of the schemes. Further details on the retirement benefit schemes are provided in Note 26.

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 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 accounted for within 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.

Valuation methodology

The railway network is carried in the balance sheet at its fair value. As there is no active market in railway infrastructure assets, the company has derived the fair value of the railway network using an income approach. The income approach assesses the discounted future cash flows that are expected to be generated by the railway network, including an assessment of under and outperformance. This valuation is carried out twice a year and revaluation gains and losses are reflected in other comprehensive income.

Depreciation

The railway network is depreciated on a straight-line basis over its estimated weighted average remaining useful economic life. The estimated weighted average remaining useful economic life of the network is currently 30 years (2014: 30 years). The remaining useful economic lives of network assets 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 capitalised 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 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 assets are measured initially at purchase cost and are amortised on a straight-line basis. Cost includes the original purchase price of the asset and the costs attributable to bringing the asset to its working condition for its intended use. Licences and concessions are amortised over the length of their contractual agreement. Intangible 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.

2. Significant accounting policies continued

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.

Financial assets

Financial assets are classified as financial assets at fair value through profit or loss (FVTPL), 'available-for-sale' financial assets, and 'loans and 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 fair value through profit or loss (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 a derivative that is not designated and effective as a hedging instrument.

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 reduced.

The carrying amount of the financial asset is reduced by the impairment loss for all financial assets with the exception of trade receivables, which are reduced by appropriate allowances for irrecoverable amounts. 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, commercial paper and money market deposit investments at varying rates. The carrying amount of these assets approximates their fair value.

Joint ventures

The results and net assets 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 and 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

Financial liabilities are classified according to the substance of the contractual arrangements entered into.

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 is a derivative that is neither designated nor effective as a hedging instrument.

A financial liability, other than a financial liability held for trading, is designated as FVTPL upon initial recognition if such designation eliminates or significantly reduces a measurement or recognition inconsistency that would otherwise exist, in line with International Accounting Standard 39 *Financial Instruments: Recognition and Measurement*, paragraph 9. Certain bonds, as set out in Note 19, are designated at FVTPL. These bonds are hedged by derivative financial instruments as part of a documented risk management strategy. By recognising these bonds and derivatives at FVTPL the recognition inconsistencies that would otherwise exist with regard to these risk management strategies are significantly reduced.

The group derecognises financial liabilities when, and only when, the group's obligations are discharged, cancelled or expire.

2. Significant accounting policies continued

Debt

Debt instruments not designated at FVTPL are initially measured at fair value, net of discount and direct issue costs, and subsequently recognised at amortised cost. 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, cross-currency 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. Derivatives are presented on the balance sheet in line with their maturity date.

The group designates certain hedging instruments as either cash flow hedges or fair value 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 value 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.

Cashflow hedge accounting is discontinued when the hedging instrument expires, is sold, terminated, exercised or no longer meets the criteria for hedge accounting. Where the hedging instrument no longer meets the criteria for hedge accounting, the cumulative gain or loss on the hedging instrument that remains recognised directly in equity from the period when the hedge was effective remains in equity until the forecast transaction occurs.

In the instance where cashflow hedge accounting is discontinued since the forecast transaction is no longer expected to occur, the cumulative gain or loss on the hedging instrument that remains recognised directly in equity from the period where the hedge as effective is recognised in the income statement.

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 being 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 changes in equity and in the statement of comprehensive income.

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, 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.

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 in other comprehensive income, 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.

2. Significant accounting policies continued

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 flows associated with the network, adjusted for the net present value of any variances from the Office of Rail and Road's determination included in the group's business plan. Further details are set out in Note 12.

(ii) Investment property – an element of the investment property portfolio valuation is determined using the Beacon method. Jones Lang LaSalle provided their assessment of yields for 13 properties in the portfolio. 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. Further details are set out in Note 13.

(iii) Retirement benefit obligations – the group recognises and discloses its retirement benefit obligation in accordance with the measurement and presentational requirement of IAS 19 (Revised) '*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 among 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 26. The total contribution rate payable under the Railway Pension Scheme (RPS) and the Career Average Revalued Earnings (CARE) scheme is normally split in the proportion 60:40 between the group and the members, respectively. The group reflects its share of the contribution in the financial statements.

(iv) Hedge accounting – Forward starting sterling interest rate swaps are accounted for as cashflow hedges where it is believed that future sterling issuances are highly probable.

(v) Taxation – The tax base of additions to property, plant and equipment is calculated for financial accounting purposes. The relevant tax computation is finalised, following publication of the statutory accounts. During this time, additional analysis can be undertaken which may give rise to a prior year adjustment. Typically such adjustments are not material and relate to further analysis of the eligibility of expenditure for tax relief, principally through capital allowances.

The group recognises and discloses its deferred tax assets in accordance with IAS 12. Where it is considered to be probable that deferred tax assets can be matched to future taxable profits then deferred tax assets are recognised, or offset against the overall deferred tax provision as appropriate. This evaluation requires significant judgements to be made, including the uncertainty of the availability of future taxable profits. Further details are set out in Note 10.

3. Revenue

	2015 Group £m	2014 Group £m
Franchised track access and grant income	**5,729**	6,020
Freight revenue	**75**	52
Property rental income	**256**	238
Other income	**27**	23
Revenue	**6,087**	6,333

The effect of the performance regimes was a net loss of £109m (2014: net loss of £218m) which led to a reduction in revenue of the respective amount. In the year ended 31 March 2014 rebates of £110m and £32m were paid to the Department for Transport and Transport Scotland respectively. There were no rebates in the year ended 31 March 2015.

4. Net operating costs

	2015 Group £m	2014 Group £m
Employee costs (see Note 6)	**1,919**	1,910
Own costs capitalised	**(731)**	(739)
Other external charges (including infrastructure maintenance costs)	**1,857**	1,873
Other operating income and recoveries	**(342)**	(233)
Net operating costs before depreciation and amortisation	**2,703**	2,811
Depreciation	**1,732**	1,603
Capital grants amortised	**(83)**	(82)
Net operating costs	**4,352**	4,332

In the year ended 31 March 2014 other external charges include a provision for a financial penalty of £77m arising from an order made by the ORR in respect of the 2014 long distance punctuality target. In the year ended 31 March 2015 £24m of this provision was released.

5. Profit from operations

Total profit from operations is stated after charging/(crediting):

	2015 Group £m	2014 Group £m
Research and development costs expensed	**1**	1
Amortisation of intangible assets	**1**	1
Profit on sale of properties	**(32)**	(37)
Increase in the fair value of investment properties	**(108)**	(59)
Cost of inventories recognised as an expense	**205**	205
Write downs of inventories recognised as an expense	**1**	3

Amounts payable to auditors		
Fees payable to the company's auditors for the audit of the company and consolidated financial statements	0.5	0.5
Fees payable to the company's auditors for audit related services		
– The audit of the company's subsidiaries	0.1	0.1
– Regulatory accounts audit and interim review	0.1	0.1
Total amounts payable to auditors	0.7	0.7

In the financial years ended 31 March 2015 and 2014 there were no fees payable to the company's auditors in respect of non-audit related services.

6. Employee costs

The monthly average number of employees (including executive directors) was:

	2015 Group Number	2014 Group Number
Management and operation of the railway	**35,457**	35,141

	2015 Group £m	2014 Group £m
Their aggregate remuneration comprised:		
Wages and salaries	**1,587**	1,584
Social security costs	**155**	151
Defined contribution pension costs (see Note 26)	**13**	13
Defined benefit pension costs – current service costs (see Note 26)	**164**	162
Total employee costs	**1,919**	1,910

During the year ended 31 March 2015, the key management personnel were comprised of seven directors; two of which left during the year. Three of these directors are executive directors and full details of their remuneration are included within the annual remuneration report on pages 63 to 78. The remaining two directors had aggregate short-term employee benefits payable of £0.4m and aggregate post-employment benefits payable of £0.1m. No other benefits were paid to these two individuals.

In the year ended 31 March 2014, all key management personnel were executive directors, and full details of their remuneration are included within the annual remuneration report on pages 63 to 78.

7. Finance income

	2015 Group £m	2014 Group £m
Interest receivable on investments and deposits	**10**	20
	10	20

Finance income earned on financial assets analysed by category of asset, is as follows:

	2015 Group £m	2014 Group £m
Loans and receivables (including cash and bank balances)	**10**	20
	10	20

8. Other gains and losses

	2015 Group £m	2014 Group £m
Net ineffectiveness arising from cash flow hedge accounting	**(96)**	6
Fair value gain/(loss) on fair value hedges	**719**	(540)
Fair value (loss)/gain on carrying value of fair value hedged debt	**(689)**	540
Gain arising from fair value hedge accounting	**30**	–
Net decrease in fair value of non-hedge accounted debt	**2**	54
Gain on derivatives not hedge accounted	**23**	244
Gain arising from non-hedge accounting	**25**	298
Total other (losses)/gains	**(41)**	304

No other gains and losses have been recognised in respect of loans and receivables other than those disclosed in this note. No gains or losses have been recognised on financial liabilities measured at amortised cost other than those disclosed in Note 9.

The movements in the hedged risk adjustment on fair value hedged debt, the movement in fair value of debt designated as fair value through profit and loss and exchange differences on retranslation of foreign currency debt that form part of the above total other gains and losses are in relation to debt issuances disclosed in Note 19.

9. Finance costs

	2015 Group £m	2014 Group £m
Interest on bank loans and overdrafts	**17**	21
Interest on loan issued by Department of Transport	**74**	–
Interest on bonds issued under the Debt Issuance Programme	**862**	957
Interest on derivative instruments	**97**	257
Defined benefit pension interest cost	**53**	54
Debt Issuance Programme financial indemnity fee	**361**	240
Other interest	**2**	1
Total borrowing costs	**1,466**	1,530
Less: capitalised interest	**(128)**	(144)
Total finance costs	**1,338**	1,386

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 3.7 per cent (2014: 4.4 per cent).

10. Tax

	2015 Group £m	2014 Group £m
Current tax:		
Corporation tax charge	**1**	4
Less advance corporation tax set-off	**-**	(3)
Adjustment in respect of prior years	**1**	-
Total current tax	**2**	1
Deferred tax:		
Current year charge	**836**	233
Effect of rate change	**–**	(220)
Adjustments in respect of prior years	**44**	(235)
Total deferred tax	**880**	(222)
Total tax charge/(credit)	**882**	(221)

The tax charge/(credit) for the year can be reconciled to the profit per the income statement as follows:

	2015 Group £m	2014 Group £m
Profit before tax	**506**	1,035
Tax at the UK corporation tax rate of 21 per cent (2014: 23 per cent)	**106**	238
Adjustments in respect of prior years	**50**	(235)
Effect of rate change	**–**	(220)
Income not subject to tax	**(133)**	(1)
De-recognition of deferred tax assets - brought forward	**597**	–
De-recognition of deferred tax assets - current year	**267**	–
Advance corporation tax previously written off	(5)	(3)
Tax charge/(credit) for the year	**882**	(221)

UK corporation tax is calculated at 21 per cent (2014: 23 per cent). Further reductions to the UK tax rate have been announced and substantively enacted and will reduce the rate to 20 per cent by 1 April 2015.

The group have £25m (2014: £30m) of surplus advance corporation tax carried forward (including a release in relation to the prior year). No deferred tax asset has been provided in respect of this amount.

Under IAS12 deferred tax assets can only be recognised where it is probable that taxable profits will be available against which the deferred tax asset can be utilised. In the year Network Rail has derecognised the deferred tax asset in respect of tax losses. During the year, Network Rail has been reclassified as a Central Government Body. As a consequence of a change in assumptions in the second half of the year regarding the uncertainty over the regulatory determination of income in future control periods, it is no longer considered probable that Network Rail will return to the level of taxable profits that would have allowed for the continued recognition of the deferred tax assets. Consequently, the deferred tax assets of £864m (£597m carried forward losses and £267m current year losses) in respect of tax losses have been derecognised.

'Income not subject to tax' in the year is mainly due to the timing differences arising from accounting for derivatives and their associated tax charges/credits.

11. Intangible assets

Group	Concession £m
Cost	
At 1 April 2013, 31 March 2014 and 31 March 2015	78
Accumulated amortisation	
At 1 April 2013	(9)
Charge for the year	(1)
At 31 March 2014	**(10)**
Charge for the year	(1)
At 31 March 2015	**(11)**
Carrying amount	
At 31 March 2015	**67**
At 31 March 2014	68

The intangible assets above relate to the concession to run the operations, maintenance and renewal business of the Channel Tunnel Rail Link, and are held by the wholly owned company Network Rail (High Speed) Limited.

Intangible assets are being amortised over the life of the licence of 83 years to 2086. Amortisation is charged to net operating costs in the income statement.

12. Property, plant and equipment – the railway network

	Group £m
Valuation	
At 1 April 2013	46,411
Additions	6,873
Transfer to investment property	(35)
Depreciation charge for the year	(1,603)
Revaluation in the year	(1,813)
At 31 March 2014	**49,833**
Additions	6,474
Transfer from investment property	4
Depreciation charge for the year	(1,732)
Revaluation in the year	(488)
At 31 March 2015	**54,091**

Given the interdependency of the assets comprising the railway network, the group has concluded that the railway network is a single class of asset. The railway network is carried at its fair value, which is measured as the estimated future cash flows that are expected to be generated in perpetuity, discounted at a pre-tax rate of return, as set by the independent rail regulator, (the ORR), in its *"Periodic Review 2013: Determination of Network Rail's outputs and funding 2014-19"*. This rate reflects the risks and opportunities that exist in the regulated market for railway infrastructure assets and equates to the cost of capital for this market.

The Regulatory Asset Base (RAB) is a proxy for the present value of future cash flows

As there is no active market in railway infrastructure assets, the group has derived the fair value of the railway network using an income approach. The income approach assesses the discounted future cash flows that would be generated by the railway network using a market rate of return. This valuation is carried out twice a year and revaluation gains and losses are reflected in other comprehensive income.

The income approach to determining the fair value of the railway network involves using the RAB, which is a proxy for a discounted cash flow calculation, adjusted for forecast performance variations.

12. Property, plant and equipment – the railway network continued

The RAB is used by the ORR to set Network Rail's charges to customers and is a proxy for the present value of future cash flows. Annual income (receivable as track access charges and the network grant) comprises three elements:

a) Efficient operating and maintenance costs – paid to Network Rail as they are expected to be incurred.

b) RAB amortisation – capital expenditure is added to the RAB as incurred in order to spread the cost to customers and stakeholders of investment in the railway network over many years. The ORR allows Network Rail to recover these costs through amortisation of the RAB.

c) Allowed return – calculated by applying the rate of return permitted by the ORR (based on its assessment of the market's cost of capital) to the RAB balance. The ORR has determined that for CP5 it will not provide Network Rail with a full market cost of capital. The ORR believes that because Network Rail is primarily funded by debt supported by the Financial Indemnity Mechanism it is not necessary to provide a return on equity. A change in the rate of return affects the allowed return element of Network Rail's income, but the RAB is not affected. The ORR has confirmed that a conventionally funded market participant would receive an allowed return equal to the full market cost of capital.

When valuing the network, management considers the value a knowledgeable willing party would place on the network in an arm's length transaction. We have applied the market cost of capital determined by the ORR in calculating the value of the network to a conventionally funded third party.

The RAB is a proxy for the present value of the future cash flows because the net cash flow that a conventionally funded market participant would earn is the RAB multiplied by the rate of return allowed by the regulator, which reflects the risks and opportunities that exist in the regulated market for railway infrastructure assets. This rate equates to the market's pre-tax cost of capital.

Discount rate

The discount rate used in the income approach is the pre-tax rate of return set by the ORR. The ORR performs a periodic review every five years, which leads to the setting of the appropriate rate for the five-year period. The ORR's method encompasses advice from consultants, comparisons to similar infrastructure assets and discussions with Network Rail. Management believes this cost of capital reflects the assumptions that a market participant would make in arriving at a discount rate.

Should the ORR amend the permitted rate of return in future quinquennial reviews, the regulator would raise or lower the permitted charges to customers so as to achieve the new rate of return. In other words, the cash flows would change but the RAB would not.

The rate of return set by the regulator is, at each quinquennial review date, consistent with the market discount rates for infrastructure assets. Movements in the market cost of capital within a review period would have a small effect on the valuation of the railway network. However, at the start of the next review period, the regulator will re-evaluate the rate of return and reset it to the market rate. Changes in the fair value of the railway network resulting from movements in the market rate would not be permanent – only lasting until the next review.

The group's valuation includes a reassessment of this rate to determine whether it continues to reflect conditions in the market in between review dates. This assessment is by reference to movements in observable market data, including the risk-free cost of borrowing, and changes in the weighted average cost of capital of listed utility companies with similar gearing ratios.

The following table shows the effect of changes in the market discount rate on the carrying value of the railway network and on the depreciation charge. The analysis only considers the effects of movements in the market discount rate until the end of the control period (2019), and not in perpetuity. This is because the regulator performs a review every five years, so the rate applicable to the income streams derived from the railway network will be rebased to the market every five years. The effects of changes in the market discount rate apply equally to increases and to decreases in discount rates.

12. Property, plant and equipment – the railway network continued

	Change in cost of capital (basis points)	31 March 2015	31 March 2014
Change in fair value	25	**£528m**	£623m
	50	**£1,056m**	£1,245m
Percentage change in fair value	25	**1.0%**	1.3 %
	50	**2.0%**	2.5 %
Change in annual depreciation charge	25	**£18m**	£21m
	50	**£35m**	£42m

These sensitivities are calculated by reference to the RAB used to determine a return, equal to the regulatory determination of the cost of capital, as set out in the ORR's "*Periodic Review 2013: Determination of Network Rail's outputs and funding 2014-19*". Twenty-five and fifty basis points were chosen as management's assessment of reasonably possible changes in the market cost of capital.

The sensitivities calculated are the discounted additional income or expense that could arise if the actual cost of capital varied from the regulatory cost of capital between quinquennial reviews.

Forecast performance variations

The semi-annual valuations include a review of changes in cash flow estimates and an assessment of current operational and economic conditions, as well as operational and political risk. These changes are reflected in the valuation so that the resulting fair value of the railway network remains current throughout the five years between periodic reviews.

Critical judgements

The valuation also includes the following critical judgements:

a) Cash flows remain stable and robust. In determining a fair value, management must consider what a knowledgeable, willing party would value the network at in an arm's length transaction. The regulatory financial framework has remained robust and stable over recent years, although for the next control period the ORR has determined that it will not provide Network Rail with a return on equity as Network Rail is primarily debt funded. The ORR has committed to providing a market cost of capital return to a conventionally funded owner and operator of the network and the fair value calculation has been prepared on that basis.

b) The residual value of the railway network is considered immaterial to assessing its annual depreciation charge. This is because evidence from other disused parts of the railway network indicates that the residual value is negligible and includes significant onerous obligations. In addition, the value of the land on which the railway network stands is immaterial to the value of the assets that comprise the network.

c) The valuation includes an assessment of the likely ORR determination in respect of the financial consequences of potential out or underperformance against the regulatory determination in the future. The valuation downward in the year is largely the result of projected and actual financial underperformance against the regulatory determination. Currently, the valuation includes around £1,006m of projected financial underperformance which will crystallise in the income statement or result in the ineligibility of additions to the RAB. During this financial year £249m of capital expenditure was incurred that was not eligible for RAB addition.

12. Property, plant and equipment – the railway network continued

Depreciated replacement cost

In the 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.

The inflation-adjusted depreciated replacement cost of the network (after excluding the replacement cost of embankments, cuttings and tunnels) is estimated at £89.3bn (2014: £87.5bn).

As at 31 March 2015 the comparable valuation of the railway network according to the historical cost convention is £52,255m (2014: £47,468m).

As at 31 March 2015 and 31 March 2014 it has not been possible to identify the depreciated capitalised interest or the undepreciated finance leases within the net book value of non-current assets. The undepreciated interest capitalised since the date of adoption of the network value at deemed cost on 1 April 2002 was £1,017m (2014: £889m). No finance leased assets have been acquired since 1 April 2002.

The depreciation charge for the 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 useful economic life of the railway network was calculated using the engineering assessment of serviceable economic lives of the major categories of asset that comprise the railway network. The estimated weighted average remaining useful economic life of the network is currently 30 years (2014: 30 years).

At 31 March 2015, the group had entered into contractual commitments in respect of capital expenditure amounting to £3,405m (2014: £5,693m).

13. Investment property

	Group £m
Fair value	
At 1 April 2013	751
Additions	15
Disposals	(4)
Transfer from property, plant and equipment	35
Decrease in fair value in the year	59
At 31 March 2014	**856**
Additions	23
Disposals	(1)
Transfer to property, plant and equipment	(4)
Increase in fair value in the year	108
At 31 March 2015	**982**

The market values of the group's investment properties at 31 March 2015 have been arrived at on the basis of a valuation carried out at that date with Jones Lang LaSalle, external valuers not connected with the group. The fair value of the group's investment property portfolio is deemed to be the market value .

The valuation, which conforms to International Valuation Standards, was arrived at by splitting the portfolio between one-off individual properties to be valued separately and the remainder of the portfolio to be valued under the Beacon method.

Jones Lang LaSalle provided independent valuations of 17 one-off individual properties (2014: 16) , amounting to 15 per cent (2014: 14 per cent) of the total valuation. The balance of the estate was valued under the Beacon method by splitting the portfolio into 13 homogeneous classes (2014: 13) of property and areas, assuming that the current passing rent received from these properties are in line with market rent. Jones Lang LaSalle independently assessed the appropriate yield to be adopted within each of these classes and areas. This enabled the directors to estimate market values by applying the provided yields to the net rental income from these properties, in accordance with a standard 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 £84m (2014: £80m). Direct operating expenses arising on the investment properties in the year amounted to £6m (2014: £6m).

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. Investments in subsidiaries and joint ventures

Principal subsidiaries affecting the amounts shown in the financial statements are included in the list below.

Principal subsidiaries	Country of incorporation	Proportion of all classes of issued share capital owned	Principal activities
Network Rail Infrastructure Limited	Great Britain	100 %	Operation, maintenance and renewal of the national railway infrastructure
Network Rail Insurance Limited	Guernsey	100 %	Insurance
Network Rail Holdco Limited*	Great Britain	100 %	Holding company of Network Rail Infrastructure Limited
Network Rail (High Speed) Limited	Great Britain	100 %	Holds St Pancras concession and High Speed Railway Services Agreement
Network Rail Development Limited	Great Britain	100 %	Holds 49.95 % of each of the property joint ventures Solum Regeneration Limited Partnership and Solum Regeneration Epsom Limited Partnership
Network Rail Pension Trustee Limited	Great Britain	Company limited by guarantee	Administration of defined contribution and CARE defined benefit pension schemes
Network Rail Consulting Limited	Great Britain	100 %	International rail consultancy
Network Rail Certification Body Limited	Great Britain	100 %	Conformity assessment services to the rail industry
Network Rail (VY1) Limited	Great Britain	100 %	Holds land required for works access
Network Rail (VY2) Limited	Great Britain	100 %	Holds land required for works access

Shares held by a trustee			
Network Rail Infrastructure Finance PLC	Great Britain	Shares held by HSBC Trustee (C.I.) Limited	Issuer of the Debt Issuance Programme

* Directly owned by Network Rail Limited company.

The shares in Network Rail Infrastructure Finance PLC are held by HSBC Trustee (C.I.) Limited, for charitable purposes. The sole purpose of this company is to act as a special purpose funding vehicle. The company is treated as a subsidiary for accounting purposes as proceeds from debt issuances are lent on to Network Rail Infrastructure Limited and are used to finance the activities and to refinance the existing debt of the group.

Joint ventures	Country of incorporation	Proportion of all classes of issued share capital owned	Principal activities
Solum Regeneration (GP) Limited	Great Britain	50 %	Holds 0.1 % of the property joint venture Solum Regeneration Limited Partnership
Solum Regeneration Epsom (GP) Limited	Great Britain	50 %	Holds 0.1 % of the property joint venture Solum Regeneration (Epsom) Limited Partnership
Solum Regeneration Limited Partnership	Great Britain	50 %	Property development
Solum Regeneration (Epsom) Limited Partnership	Great Britain	50 %	Property development
Solum Regeneration Christchurch LLP	Great Britain	50 %	Property development
The Station Office Network LLP	Great Britain	50 %	Provides flexible office space, meeting rooms and virtual offices
West Hampstead Limited Partnership	Great Britain	50 %	Property development
Doddle Ltd*	Great Britain	50 %	Parcel collection services

* New joint venture entered into during the year.

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14. Investment in subsidiaries and joint ventures continued

	2015 Group £m	2014 Group £m
At 1 April	**27**	12
Investment in joint venutures	**22**	15
Share of (loss)/profit	**(7)**	–
At 31 March	**42**	27

15. Inventories

	2015 Group £m	2014 Group £m
Raw materials and consumables	**198**	173

As at 31 March 2015 a provision of £26m was held in respect of inventories (2014: £33m).

16. Finance lease receivables

	Minimum lease payments		Present value of minimum lease payments	
	2015 Group £m	2014 Group £m	**2015 Group £m**	2014 Group £m
Amounts receivable under finance leases:				
Within one year	**1**	2	**1**	2
In the second to fifth years inclusive	**–**	2	**–**	1
	1	4	**1**	3
Less: unearned finance income	**–**	(1)	**n/a**	n/a
Present value of minimum lease payments receivable	**1**	3	**1**	3
Analysed as:				
Current finance lease receivables	**1**	2	**1**	2
Non-current finance lease receivables	**–**	1	**–**	1
	1	3	**1**	3

The group has entered into a finance lease arrangement with a third party to sell various types of telecommunications equipment. The lease is due to expire in 2017. The interest rate inherent in the lease is fixed at the contract date for all of the lease term. The average effective interest rate contracted is approximately 8.4 per cent per annum for the life of the lease.
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 2015 is estimated at £1m (2014: £4m) using a 1.07 per cent (2014: 1.78 per cent) discount rate based on the average cost of capital associated with the remaining life of the lease.

17. Trade and other receivables

Non-current assets: other receivables	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Regulatory income receivable	**109**	135	**–**	–

Current assets: trade and other receivables	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Trade receivables	**226**	294	**–**	–
Capital grants receivable	**75**	86	**–**	–
Other taxation and social security	**143**	149	**–**	–
Other receivables	**59**	128	**–**	–
Collateral placed with banking counterparties	**726**	36		
Prepayments and accrued income	**246**	222	**–**	–
	1,475	915	**–**	–

Trade receivables include an allowance for estimated irrecoverable amounts from the supply of services of £12m (2014: £16m). This allowance has been made by reference to past default experience. Average debtor days were 50 days (2014: 36 days).

The directors consider that the carrying value of trade and other receivables approximates to 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.

The group's credit risk is primarily attributable to its trade receivables. Around 95 per cent of the group's income is received from train operating companies and in the form of revenue grants from Government. Franchises are issued to train operating companies by the Department for Transport in England and Wales and Transport Scotland in Scotland. The group believes that amounts receivable from Government and the train operating companies represent a high level of credit quality. This is because in the extraordinary circumstance that a train operating company were to be unable to meet its obligations then provisions in the franchise agreements allow the Department for Transport 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 amounts totalling £49m (2014: £25m) 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 32 days (2014: 34 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:

	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Past due by 1 – 28 days	**35**	19	**–**	–
Past due by 29 – 56 days	**7**	2	**–**	–
Past due by 57 – 84 days	**1**	1	**–**	–
Past due by 85 – 180 days	**6**	3	**–**	–
	49	25	**–**	–

Trade receivables of £11m (2014: £15m) are overdue by six months or more, and have been fully provided for.

18. Trade and other payables

Current liabilities: trade and other payables	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Trade payables	**534**	601	**–**	–
Collateral received from banking counterparties	**250**	261	**–**	–
Payments received on account	**23**	19	**–**	–
Other payables	**295**	353	**–**	–
Other interest accruals	**240**	210	**–**	–
Other accruals and deferred income	**1,809**	2,442	**–**	–
	3,151	3,886	**–**	–

The average credit period taken for trade purchases is 28 days (2014: 25 days).

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	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Capital grants deferred income	**3,089**	2,668	**–**	–
Other payables	**1,040**	629	**–**	–
	4,129	3,297	**–**	–

19. Borrowings

	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Net borrowings by instrument:				
Cash and cash equivalents*	**313**	1,253	**–**	–
Collateral placed with counterparties	**726**	36	**–**	–
Collateral received from counterparties	**(250)**	(261)	**–**	–
Commercial paper	–	(255)	**–**	–
Overdrafts	–	(51)	**–**	–
Bank loans	**(476)**	(469)	**–**	–
Bonds issued under the Debt Issuance Programme (less unamortised premium, discount and fees)	**(31,622)**	(33,240)	**–**	–
Borrowings issued by the Department for Transport	**(6,450)**	–	**–**	–
	(37,759)	(32,987)	**–**	–
Movement in net borrowings:				
At the beginning of the year	**(32,987)**	(30,358)	**–**	–
Decrease in cash and cash equivalents	**(940)**	(2,253)	**–**	–
Decrease/(increase) in overdrafts	**51**	(51)	**–**	–
Proceeds from borrowings	**(6,450)**	(5,104)	**–**	–
Repayments of borrowings	**2,738**	3,975	**–**	–
Capital accretion	**(226)**	(298)	**–**	–
Exchange differences	**23**	304	**–**	–
Movement in collateral placed with counterparties	**690**	22	**–**	–
Movement in collateral received from counterparties	**11**	143	**–**	–
Fair value and other movements	**(669)**	633	**–**	–
At the end of the year	**(37,759)**	(32,987)	**–**	–
Net borrowings are reconciled to the balance sheet as set out below:				
Cash and cash equivalents*	**313**	1,253	**–**	–
Collateral placed with counterparties (included in trade and other receivables)	**726**	36	**–**	–
Collateral received from counterparties (included in trade and other payables)	**(250)**	(261)	**–**	–
Borrowings included in current liabilities	**(3,133)**	(2,707)	**–**	–
Borrowings included in non-current liabilities	**(35,415)**	(31,308)	**–**	–
	(37,759)	(32,987)	**–**	–

* Includes collateral received from derivative counterparties of £250m (2014: £261m).

19. Borrowings continued

	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
1.085% sterling index linked bond due 2052	**124**	123	**–**	–
0% sterling index linked bond due 2052	**130**	121	**–**	–
1.003% sterling index linked bond due 2051	**23**	23	**–**	–
0.53% sterling index linked bond due 2051	**120**	118	**–**	–
0.517% sterling index linked bond due 2051	**120**	119	**–**	–
0% sterling index linked bond due 2051	**130**	122	**–**	–
0.678% sterling index linked bond due 2048	**118**	116	**–**	–
1.125% sterling index linked bond due 2047	**5,191**	5,144	**–**	–
0% sterling index linked bond due 2047	**81**	73	**–**	–
1.1335% sterling index linked bond due 2045	**48**	47	**–**	–
1.5646% sterling index linked bond due 2044	**271**	264	**–**	–
1.1565% sterling index linked bond due 2043	**54**	53	**–**	–
1.1795% sterling index linked bond due 2041	**66**	65	**–**	–
1.2219% sterling index linked bond due 2040	**267**	261	**–**	–
1.2025% sterling index linked bond due 2039	**72**	71	**–**	–
4.6535% sterling bond due 2038	**100**	100	**–**	–
1.375% sterling index linked bond due 2037	**5,063**	5,011	**–**	–
4.75% sterling bond due 2035	**1,228**	1,227	**–**	–
1.6492% sterling index linked bond due 2035	**406**	396	**–**	–
4.375% sterling bond due 2030	**871**	870	**–**	–
1.75% sterling index linked bond due 2027	**5,019**	4,988	**–**	–
4.615% Norwegian krone bond due 2026*	**52**	56	**–**	–
4.57% Norwegian krone bond due 2026*	**15**	16	**–**	–
1.9618% sterling index linked bond due 2025	**343**	334	**–**	–
4.75% sterling bond due 2024	**735**	733	**–**	–
3% sterling bond due 2023	**397**	397		
2.76% Swiss franc bond due 2021	**208**	203	**–**	–
2.315% Japanese yen bond due 2021*	**63**	64	**–**	–
2.28% Japanese yen bond due 2021*	**63**	64	**–**	–
2.15% Japanese yen bond due 2021*	**63**	63	**–**	–
4.625% sterling bond due 2020	**998**	998	**–**	–
1.75% US dollar bond due 2019**	**684**	599	**–**	–
0.875% US dollar bond due 2018**	**1,167**	1,023	**–**	–
Floating rate US dollar bond due 2017**	**337**	300	**–**	–
0.75% US dollar bond due 2017**	**836**	737	**–**	–
1% sterling bond due 2017	**747**	746	**–**	–
6% Australian dollar bond due 2016	**257**	278	**–**	–
4.4% Canadian dollar bond due 2016	**266**	271	**–**	–
0.625% US dollar bond due 2016**	**839**	775		
1.25% US dollar bond due 2016**	**679**	607	**–**	–
1.125% sterling bond due 2016*	**504**	499	**–**	–
Floating rate sterling bond due 2016	**600**	599	**–**	–
0.625% US dollar bond due 2015**	**1,011**	900	**–**	–
4.875% sterling bond due 2015	**1,256**	1,266	**–**	–
1.25% sterling bond due 2015	–	1,499	**–**	–
0.875% US dollar bond due 2015**	–	901	**–**	–
	31,622	33,240	**–**	–

* Bonds treated as fair value through profit and loss.
** Bonds in a fair value hedge arrangement.
All other bonds are shown net of unamortised discount and fees.

19. Borrowings continued

Bank loans are analysed as follows:

	2015 Group £m	2014 Group £m	2015 Company £m	2014 Company £m
Index-linked European Investment Bank due 2036 (£228m) and 2037 (£226m)	**454**	443	**–**	–
Barclays Bank due 2017 repayable by instalments	**22**	26	**–**	–
	476	469	**–**	–

At 31 March 2015 and 2014 the group had the following undrawn committed borrowing facilities:

	2015 Drawn £m	2015 Undrawn £m	2015 Total £m	2014 Drawn £m	2014 Undrawn £m	2014 Total £m
Standby facility A	**–**	**–**	**–**	–	4,000	4,000
Department for Transport loan facility	**6,450**	**23,725**	**30,175**	–	–	–
	6,450	**23,725**	**30,175**	–	4,000	4,000

Undrawn committed facilities expire as follows:

	2015 Group £m	2014 Group £m
Within one year	**–**	–
Within two to five years	**23,725**	–
After five years	**–**	4,000
	23,725	4,000

On 4 July 2014 the Secretary of State for Transport provided the group with a loan facility of £30,175m expiring on 31 March 2019. On 1 September 2014 the group terminated its standby facility A. In addition the Secretary of State for Transport has provided unlimited financial indemnity in respect of borrowings under the Debt Issuance Programme which expires in 2052.

20. Derivative financial instruments

	2015 Group	
	Fair value £m	Notional amounts £m
Derivative financial instrument assets		
Cash flow hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	228	581
Forward starting interest rate swaps	–	–
Fair value hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	399	5,161
Non-hedge accounted derivatives		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	69	198
Interest rate swaps	71	3,633
Forward foreign exchange contracts	4	71
	771	9,644
Included in non-current assets	721	8,670
Included in current assets	50	974
	771	9,644
Derivative financial instrument liabilities		
Cash flow hedges		
Interest rate swaps	(59)	583
Forward starting interest rate swaps	(779)	13,282
Fair value hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	–	–
Non-hedge accounted derivatives		
Interest rate swaps to hedge debt issued under the Debt Issuance Programme	(198)	4,033
Forward foreign exchange contracts	(7)	130
	(1,043)	18,028
Included in current liabilities	(5)	214
Included in non-current liabilities	(1,038)	17,814
	(1,043)	18,028

20. Derivative financial instruments continued

	2014 Group	
	Fair value £m	Notional amounts £m
Derivative financial instrument assets		
Cash flow hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	246	581
Forward starting interest rate swaps	308	11,519
Fair value hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	3	606
Non-hedge accounted derivatives		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	79	198
Interest rate swaps	12	4,000
Forward foreign exchange contracts	–	65
	648	16,969
Included in non-current assets	637	13,405
Included in current assets	11	3,564
	648	16,969
Derivative financial instrument liabilities		
Cash flow hedges		
Interest rate swaps	(68)	583
Forward starting interest rate swaps	(59)	5,835
Fair value hedges		
Cross-currency swaps to hedge debt issued under the Debt Issuance Programme	(322)	5,534
Non-hedge accounted derivatives		
Interest rate swaps to hedge debt issued under the Debt Issuance Programme	(212)	6,400
Forward foreign exchange contracts	(3)	229
	(664)	18,581
Included in current liabilities	(277)	7,353
Included in non-current liabilities	(387)	11,228
	(664)	18,581

21. Provisions

	Legal £m	Restructuring £m	Other £m	Total £m
At 1 April 2014	4	4	135	143
Charge for the year	5	–	8	13
Utilised in the year	–	(3)	(59)	(62)
Release for the year	(4)	–	(40)	(44)
At 31 March 2015	**5**	**1**	**44**	**50**

Included in current liabilities	50

Included in other provisions at 1 April 2014 was the maximum possible financial penalty of £77m in respect of the missed 2014 long distance punctuality target. During the financial year £53m was paid to the Office of Rail and Road in relation to the financial penalty and £24m was released. At 31 March 2015, £36m of other provisions relates to lease provisions (2014: £36m).

The group has also provided against a number of claims 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 directors' best estimate of the expenditure required to settle the obligation, with the benefit of legal advice.

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.

Contingent liability

ORR has launched investigations to establish whether Network Rail did or is doing everything reasonably practicable to meet its licence conditions:

- In relation to achieving its operational performance targets for CP5; and
- In relation to delivering its CP5 enhancement project portfolio.

The outcome of these investigations is uncertain. It is possible that this could result in enforcement action or financial penalties. It is not possible at this stage to measure with sufficient reliability the potential financial consequences of any action that could arise from these investigations.

22. Deferred tax

The following are the deferred tax liabilities and assets recognised by the group and movement thereon during the current and prior year.

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 2013	3,173	1,218	(353)	(182)	(947)	2,909
(Credit)/charge to income	(696)	–	2	122	350	(222)
(Credit)/charge to other comprehensive income	–	(370)	50	124	–	(196)
At 1 April 2014	**2,477**	**848**	**(301)**	**64**	**(597)**	**2,491**
(Credit)/charge to income	274	–	30	(21)	(267)	16
(Credit)/charge to other comprehensive income	–	(89)	(33)	(179)	–	(301)
De-recognition of deferred tax asset to income	–	–	–	–	864	864
De-recognition of deferred tax asset to equity	–	–	–	160	–	160
At 31 March 2015	**2,751**	**759**	**(304)**	**24**	**–**	**3,230**

Certain deferred tax assets and liabilities have been offset. The following is the analysis of the gross deferred tax balances:

	2015 £m	2014 £m
Deferred tax liabilities	**3,534**	3,389
Deferred tax assets	**(304)**	(898)
	3,230	2,491

22. Deferred tax continued

Under IAS 12 deferred tax assets can only be recognised where it is probable that taxable profits will be available against which the deferred tax asset can be utilised. In the year Network Rail has derecognised the deferred tax asset in respect of tax losses and derivatives. During the year, Network Rail has been reclassified as a Central Government Body. As a consequence of a change in assumptions in the second half of the year regarding the uncertainty over the regulatory determination of income in future control periods, it is no longer considered probable that Network Rail will return to the level of taxable profits that would have allowed for the continued recognition of the deferred tax assets. Consequently, the deferred tax assets in respect of tax losses of £864m (£597m carried forward losses and £267m current year losses) and derivatives of £160m has been derecognised.

23. Notes to the statement of cash flows

	2015 Group £m	2014 Group £m	**2015 Company £m**	2014 Company £m
Profit before tax	**506**	1,035	**–**	–
Adjustments for:				
Property revaluation movements and profits on disposal	**(140)**	(96)	**–**	–
Fair value loss/(gain) on derivatives and debt	**41**	(304)	**–**	–
Net interest expense	**1,328**	1,366	**–**	–
Depreciation of the railway network	**1,732**	1,603	**–**	–
Amortisation of capital grants	**(83)**	(82)	**–**	–
Amortisation of intangible assets	**1**	1	**–**	–
Movement in retirement benefit obligations	**56**	56	**–**	–
(Decrease)/increase in provisions	**(93)**	135	**–**	–
Operating cash flows before movements in working capital	**3,348**	3,714	**–**	–
Increase in inventories	**(25)**	(16)	**–**	–
Decrease/(increase) in receivables	**157**	(289)	**–**	–
Increase in payables	**34**	384	**–**	–
Cash generated from operations	**3,514**	3,793	**–**	–

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, commercial paper and money market deposit investments, all of which are on call with the exception of short-term deposits. There were no short term deposits held as at 31 March 2015 (2014: £163m with an average term of 22 days from the balance sheet date). Cash and money market deposits had an average maturity of 35 days (2014: ten days) from the balance sheet date.

24. Operating lease arrangements

The group as lessee	2015 Group £m	2014 Group £m
Minimum lease payments under operating leases recognised in the income statement in the year	**47**	28

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:

	2015 Group £m	2014 Group £m
Within one year	**42**	33
In the second to fifth years inclusive	**94**	115
After five years	**19**	30
	155	178

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 required for maintenance and renewal activities.

The group as lessor

Operating lease rentals earned in the year by the group were £279m (2014: £263m). This amount includes property rental income of £256m (2014: £238m), as disclosed in Note 3.

At the balance sheet date, the group had contracted with customers for the following future minimum lease payments:

	2015 Group £m	2014 Group £m
Within one year	**390**	334
In the second to fifth years inclusive	**903**	594
After five years	**2,219**	1,291
	3,512	2,219

25. Funding and financial risk management

Introduction

The group is almost entirely debt financed. Debt has been issued through the 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 existing debt has been issued by Network Rail Infrastructure Finance PLC under the Debt Issuance Programme which is rated AAA by Standard & Poor's, Aa1 (stable outlook) by Moody's and AA+ (stable outlook) by Fitch. The Debt Issuance Programme is supported by a financial indemnity from the Secretary of State for Transport which expires in 2052.

Debt has been 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.

Reclassification of Network Rail

In December 2013, the Office for National Statistics announced the reclassification of Network Rail as a Central Government Body in the UK National Accounts and Public Sector Finances with effect from 1 September 2014. This is a statistical change driven by new guidance in the European System of National Accounts 2010 (ESA10).

As part of Network Rail's formal reclassification to the public sector, an arrangement was agreed whereby funding would be provided by the DfT in the form of a loan made directly to Network Rail Infrastructure Limited, to fund the continuing programme of long-term investment in the national rail network. Network Rail Infrastructure Finance PLC does not anticipate issuing further bonds in the foreseeable futures and its debt service obligations would be met through repayments of the intercompany loan by Network Rail Infrastructure Limited.

All of the outstanding bonds under the Debt Issuance Programme, including nominal and index-linked benchmarks and private placements in all currencies, will continue to benefit from the direct and explicit guarantee from the UK Government under the Financial Indemnity Mechanism.

Externally imposed capital requirements

The Network Rail group is almost entirely debt financed and therefore manages its debt as the key part of its capital. Network Rail manages its debt in relation to the Regulatory Asset Base (RAB). 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 debt 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 service additional debt that may arise from losses incurred).

25. Funding and financial risk management continued

The RAB and regulatory debt are reconciled to property, plant and equipment (in Note 12) and net debt (in Note 19) as follows:

	2015 £m	2014 £m
Net debt per Note 19	**(37,759)**	(32,987)
Revaluations and remeasurements	**1,254**	687
Regulatory net debt	**(36,505)**	(32,300)

The RAB used to calculate the debt to RAB ratio is:

	2015 £m	2014 £m
Railway network per Note 12	**54,091**	49,833
Investment properties per Note 13	**982**	856
Capital grant funded assets	**(2,979)**	(2,688)
Other fair value adjustments	**957**	1,946
RAB	**53,051**	49,947

The debt to RAB ratio at 31 March 2015 and 2014 was as follows:

	2015	2014
Debt: RAB ratio	**68.8%**	64.7%

The debt to RAB ratio is based on regulatory net debt, which recognises debt at hedged rates.

The group's subsidiary, Network Rail Infrastructure Limited, owns and operates Britain's rail network under licence from the ORR. The licence imposes conditions on the company with regard to its net debt. Should the value of the company's qualifying net debt exceed 75 per cent of the ORR's RAB then the ORR will be formally notified.

25. Funding and financial risk management continued

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 2015 and 31 March 2014.

The fair values of the financial assets and liabilities are recorded at the amount at which the instrument could be exchanged 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 where balances were not already held at fair value:

- Bank loans – based on market data at the balance sheet date and the net present value of discounted cash flows
- Certain 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.

For cash and cash equivalents, finance lease receivables, trade and other payables and trade and other receivables, fair value equates to carrying value.

	2015		2014	
Group	**Carrying value £m**	**Fair value £m**	Carrying value £m	Fair value £m
Financial assets				
Cash and cash equivalents as loans and receivables	**313**	**313**	1,253	1,253
Other non-derivative financial assets				
Finance lease receivables	**1**	**1**	3	4
Investment property	**982**	**982**	856	856
Plant, property and equipment - the railway network	**54,091**	**54,091**	49,833	49,833
Trade and other receivables (less prepayments and accrued income and other taxation and social security)	**1,195**	**1,195**	679	679
Derivatives				
Derivatives designated as cash flow hedging instruments	**228**	**228**	554	554
Derivatives designated as fair value hedging instruments	**399**	**399**	3	3
Other derivatives as fair value through profit and loss	**144**	**144**	91	91
Total derivatives	**771**	**771**	648	648
Total financial assets	**57,353**	**57,353**	53,272	53,273
Financial liabilities				
Financial liabilities held at amortised cost				
Overdraft	**–**	**–**	(51)	(51)
Commercial paper	**–**	**–**	(255)	(255)
Bank loans	**(476)**	**(753)**	(469)	(617)
Bonds issued under the Debt Issuance Programme	**(30,862)**	**(35,654)**	(32,479)	(33,375)
Borrowings issued by Department for Transport	**(6,450)**	**(6,624)**	–	–
Financial liabilities designated as fair value through profit and loss				
Bonds issued under the Debt Issuance Programme	**(760)**	**(760)**	(761)	(761)
Total borrowing	**(38,548)**	**(43,791)**	(34,015)	(35,059)
Trade and other payables at amortised cost	**(3,951)**	**(3,951)**	(4,262)	(4,262)
Derivatives				
Derivatives designated as cash flow hedging instruments	**(838)**	**(838)**	(127)	(127)
Derivatives designated as fair value hedging instruments	**–**	**–**	(322)	(322)
Other derivatives as fair value through profit and loss	**(205)**	**(205)**	(215)	(215)
Total derivatives	**(1,043)**	**(1,043)**	(664)	(664)
Total financial liabilities	**(43,542)**	**(48,785)**	(38,941)	(39,985)

25. Funding and financial risk management continued

Derivatives

The group (including the group's special purpose financing company, 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, through a treasury sub-committee (the treasury committee), has approved and monitors 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 have 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.

For debt designated as fair value through profit and loss (FVTPL) there has been no change in carrying value as a result of changes in the group's credit risk. The gains in the income statement arising from the remeasurement of FVTPL debt items of £2m (2014: £54m gain) are all attributable to changes in market risk.

The credit risk with regard to all classes of derivative financial instruments entered into before 1 January 2013 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 members of the banking group are required to post collateral on positive mark to market swaps above the threshold. In December 2012 the group entered into new collateral agreements in respect of derivative trades entered into after 1 January 2013. Under the terms of the new agreements Network Rail posts collateral on adverse net derivative positions with its counterparties. The new agreements do not contain a provision for thresholds; as such Network Rail or its counterparties are required to post collateral for the full fair value of net out of the money positions. At 31 March 2015 the fair value of collateral held was £250m (2014: £261m). 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. The balance of collateral posted by the group at 31 March 2015 was £726m (2014: £36m).

The group does not have any significant credit risk exposure to any single counterparty and has considered the creditworthiness of debtors. For further detail on the creditworthiness of customers and suppliers, see Notes 17 (Trade and other receivables) and 18 (Trade and other payables).

The group considers its maximum exposure to credit risk to be the sum of its financial assets as set out on page 121.

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 10 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 and therefore no sensitivity analysis is produced.

25. Funding and financial risk management continued

Interest rate and inflation 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 £32,072m (2014: £29,277m) is arranged at or swapped into fixed interest rates and exposes the group to fair value interest rate risk. Other borrowings were arranged at or swapped into floating rates, thus exposing the group to cash flow interest rate risk.

The group has forward starting interest rate swaps with a notional value of £13,282m which hedge the interest rate on forecast borrowings in CP5. The weighted average rate on these swaps is 2.88 per cent.

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.

Sensitivity analysis

This sensitivity analysis has been determined based on the exposure to interest rates and inflation for both derivative and non-derivative financial 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 and inflation.

	Group 31 March 2015		Group 31 March 2014	
	Impact on the income statement £m	**Impact on equity £m**	Impact on the income statement £m	Impact on equity £m
1 % increase in the interest rate	**(435)**	**(513)**	(101)	447
1 % increase in the GBP RPI on index linked bonds	**(170)**	**–**	(172)	–

A one per cent decrease in the above rates would have an equal and opposite effect.

Interest rate sensitivities have been calculated by comparing the average rates of the derivative financial instruments to the market rate for similar instruments.

The impact of a change in GBP RPI has been calculated by applying a change of one per cent to the RPI at the balance sheet date to the carrying value of the index linked bonds.

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 £5,729m (2014: £6,020m) of revenue which is far in excess of an index-linked interest expense of £239m (2014: £232m). 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 continue to be the case. Therefore, the natural hedge that exists between finance costs and revenue mitigates the risk of RPI movements.

25. Funding and financial risk management continued

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 minimising credit risk on surplus cash.

The group manages liquidity risk by maintaining sufficient cash and facilities to cover at least one year's working capital requirement by continuously monitoring forecast and actual cash flows. 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 2015					
Non-derivative financial liabilities					
Bank loans and overdrafts	**(10)**	**(10)**	**(30)**	**(1,010)**	**(1,060)**
Bonds issued under the Debt Issuance Programme					
– Sterling denominated bonds	**(2,126)**	**(709)**	**(1,346)**	**(6,069)**	**(10,250)**
– Sterling denominated index-linked bonds	**(236)**	**(241)**	**(761)**	**(36,243)**	**(37,481)**
– Foreign currency denominated bonds	**(1,365)**	**(2,182)**	**(2,781)**	**(467)**	**(6,795)**
Loan from the Department for Transport	**(187)**	**(187)**	**(5,302)**	**(1,748)**	**(7,424)**
Trade and other payables	**(2,671)**	**(921)**	**–**	**–**	**(3,592)**
Derivative financial liabilities					
Net settled derivative contracts	**(60)**	**(107)**	**(456)**	**(394)**	**(1,017)**
Gross settled derivative contracts – receipts	**1,365**	**2,181**	**2,745**	**59**	**6,350**
Gross settled derivative contracts – payments	**(1,252)**	**(1,770)**	**(2,561)**	**(47)**	**(5,630)**
	(6,542)	**(3,946)**	**(10,492)**	**(45,919)**	**(66,899)**

Group	Within 1 year £m	1-2 years £m	2-5 years £m	5+ years £m	Total £m
31 March 2014					
Non-derivative financial liabilities					
Bank loans and overdrafts	(315)	(9)	(34)	(981)	(1,339)
Bonds issued under the Debt Issuance Programme					
– Sterling denominated bonds	(1,794)	(2,128)	(1,859)	(6,265)	(12,046)
– Sterling denominated index-linked bonds	(234)	(241)	(768)	(40,688)	(41,931)
– Foreign currency denominated bonds	(992)	(1,254)	(4,456)	(494)	(7,196)
Trade and other payables	(3,423)	(519)	–	–	(3,942)
Derivative financial liabilities					
Net settled derivative contracts	(216)	(65)	(186)	253	(214)
Gross settled derivative contracts – receipts	992	1,254	4,422	–	6,668
Gross settled derivative contracts – payments	(1,042)	(1,293)	(4,368)	–	(6,703)
	(7,024)	(4,255)	(7,249)	(48,175)	(66,703)

25. Funding and financial risk management continued

Offsetting financial assets and liabilities

a) Financial assets

The following financial assets are subject to offsetting, enforceable master netting arrangements and similar agreements.

Group	Gross amounts of recognised financial assets £m	Gross amounts of recognised financial liabilities set off in the balance sheet £m	Net amount of financial assets presented in the balance sheet	Related amounts not set off in the balance sheet		Net amount
				Financial instruments	Cash collateral received	
31 March 2015						
Derivative financial assets	**771**	**–**	**771**	**(542)**	**(156)**	**73**

Group	Gross amounts of recognised financial assets £m	Gross amounts of recognised financial liabilities set off in the balance sheet £m	Net amount of financial assets presented in the balance sheet	Related amounts not set off in the balance sheet		Net amount
				Financial instruments	Cash collateral received	
31 March 2014						
Derivative financial assets	648	–	648	(345)	(168)	135

b) Financial liabilities

The following financial liabilities are subject to offsetting, enforceable master netting arrangements and similar agreements.

Group	Gross amounts of recognised financial liabilities £m	Gross amounts of recognised financial assets set off in the balance sheet £m	Net amount of financial liabilities presented in the balance sheet	Related amounts not set off in the balance sheet		Net amount
				Financial instruments	Cash collateral paid	
31 March 2015						
Derivative financial liabilities	**(1,043)**	**–**	**(1,043)**	**542**	**501**	**–**

Group	Gross amounts of recognised financial liabilities £m	Gross amounts of recognised financial assets set off in the balance sheet £m	Net amount of financial liabilities presented in the balance sheet	Related amounts not set off in the balance sheet		Net amount
				Financial instruments	Cash collateral paid	
31 March 2014						
Derivative financial liabilities	(664)	–	(664)	345	(57)	(376)

Cash flow hedges

Contractual payments on derivatives designated as cash flow hedges impact the income statement and will all have matured by 2027.

Borrowings

Details of the group's undrawn committed facilities and types of debt instrument used can be found in Note 19.

25. Funding and financial risk management continued

Fair value measurements recognised in the balance sheets

The following table provides an analysis of 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 (ie, as prices) or indirectly (ie, derived from prices).
- 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).

	2015			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Property, plant and equipment – the railway network	–	–	54,091	54,091
Investment properties	–	–	982	982
Derivative financial assets	–	771	–	771
Financial assets held at amortised cost	–	1,509	–	1,509
Assets	–	2,280	55,073	57,353
Derivative financial liabilities	–	(1,043)	–	(1,043)
Financial liabilities designated at fair value through profit and loss	(760)	–	–	(760)
Financial liabilities designated at amortised cost	(34,716)	(12,266)	–	(46,982)
Liabilities	(35,476)	(13,309)	–	(48,785)
Total	(35,476)	(11,029)	55,073	8,568

	2014			
	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Property, plant and equipment – the railway network	–	–	49,833	49,833
Investment properties	–	–	856	856
Derivative financial assets	–	648	–	648
Financial assets held at amortised cost	–	1,936	–	1,936
Assets	–	2,584	50,689	53,273
Derivative financial liabilities	–	(664)	–	(664)
Financial liabilities designated at fair value through profit and loss	(761)	–	–	(761)
Financial liabilities designated at amortised cost	(32,669)	(5,891)	–	(38,560)
Liabilities	(33,430)	(6,555)	–	(39,985)
Total	(33,430)	(3,971)	50,689	13,288

The fair value of level 2 derivatives is estimated by discounting the future contractual cash flows using appropriate yield curves based on quoted market rates as at the current financial year end.

Property, plant and equipment

We have classified the valuation of the rail network as Level 3. As explained in Note 12, the network's fair value is the estimated future cash flows that will be generated in perpetuity, discounted at the regulatory cost of capital, as set by the ORR in its Periodic Review. The cost of capital at which cash flows are discounted is the key unobservable input in the valuation. The full market cost of capital determined by the ORR is 4.31 % for the current control period, arrived at through advice from consultants, comparisons to similar infrastructure assets and discussions with Network Rail.

An increase in the market cost of capital would lead to a decrease in the valuation of the rail network and vice versa. However, the impact would be limited to the current control period as the regulator would re-evaluate the allowed return and reset it to the market rate at the next quinquennial review.

25. Funding and financial risk management continued

Investment properties

Property valuations are by their nature subjective, as they are made on the basis of assumptions made by the valuer. They too have been classified as Level 3 and the key inputs to the valuations, defined as 'unobservable' by IFRS 13, are analysed in the table below.

	Fair value at 31 March 2015	Estimated rental value per sq. ft Minimum £	Estimated rental value per sq. ft Maximum £	Estimated rental value per sq. ft Weighted average £	Equivalent yield Minimum %	Equivalent yield Maximum %	Equivalent yield Weighted average %
Valuation Technique:							
One-off valuation	**152**	**2.30**	**303.04**	**38.70**	**4.2**	**10.0**	**6.4**
Beacon method*	**830**	**n/a**	**n/a**	**n/a**	**5.5**	**12.5**	**8.6**

* The Beacon methodology splits all the properties within the portfolio into 13 homogenous groups. The properties in each group are valued by applying a yield to the annual rent (passing or void) for the property. Yields applied are on the basis that the property is rack rented ie, the current passing rent received from these properties are in line with market rent. As such, an estimated rental value per square feet for these properties is not available.

All other factors being equal, a higher yield would lead to a decrease in the valuation of a property and an increase in the current or estimated future rental stream would have the effect of increasing the capital value, and vice versa. However, there are interrelationships between the unobservable inputs which are influenced by market conditions, which would impact the changes in fair value.

A review of the categorisation of the assets and liabilities into the three levels is made at each reporting date. There were no transfers between Level 1 and Level 2 fair value measurements, and no transfers into or out of Level 3 fair value measurements in the current or prior years.

26. Retirement benefit schemes

Defined contribution schemes

On 1 April 2004 the group introduced a defined contribution pension scheme, the Network Rail Defined Contribution Pension Scheme (NRDCPS). This is an auto-enrollment scheme for all new employees of Network Rail, except those who have the legal right to join the Railway Pension Scheme (RPS), in compliance with regulations made under the Pensions Act 2008. Any employee who wishes to transfer from the Network Rail Section of the RPS to the NRDCPS is entitled to do so.

At 31 March 2015, the NRDCPS had 9,097 members (2014: 8,510) and the average employer contribution rate in the year was 4.3 per cent (2014: 6.5 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 among 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 of 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, 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.

Qualified actuaries Towers Watson have valued the schemes on an IAS 19 (Revised) basis at 31 March 2015 and 31 March 2014.

The contributions required to fund the RPS and the CARE scheme are reassessed every three years, following completion of actuarial valuations (by the Scheme Actuaries). Under the terms of the Pensions Act 2004, the Trustee and each employer must agree the methods and assumptions used to calculate the 'Technical Provisions', ie, assets required to meet the Section's liabilities. The assumptions agreed are typically weaker than those used for IAS 19 purposes in current market conditions, so the minimum funding requirement in itself requires no further adjustment to the IAS 19 obligations below. However, the regulatory regime may, depending on legal advice received at the appropriate time, mean that a future employer's accounting surplus would need to be restricted.

26. Retirement benefit schemes continued

The RPS and CARE schemes are both shared cost in nature, so the cost of benefits being earned and the cost of funding any shortfall in the schemes are normally split in the proportion 60:40 between the group and the members. In practice the contributions are adjusted at each triennial valuation to reflect the funding position of the schemes at that time. The group reflects its share of the contribution in the financial statements. The IAS 19 deficit, service cost and interest cost therefore represent 60 % of the total for each of the schemes.

The group reviewed its pension arrangements in 2012 resulting in an alternative benefit scale in the RPS for members who joined after 30 June 2012. Employees who were members of the Section as at 1 July 2012 were given the option to continue accruing on the existing benefit scale or to opt to accrue on the alternative scale. Those that opted to continue on the existing basis are referred to as "RPS 60 members" and those who changed to the new structure, as well as post 30 June 2012 joiners, are referred to as "RPS 65 Members".

The group pays contributions of 14.04 per cent of Section Pay for RPS 60 members and 10.5 per cent of RPS 65 Section Pay for RPS 65 members. The members pay contributions of 9.36 per cent of Section Pay for RPS 60 members and 7.0 per cent of RPS 65 Section Pay for RPS 65 members. These rates are expected to continue until 30 June 2018, barring any adjustments required in conjunction with the 2013 Actuarial Valuation, when the employer contribution rates will revert to 60 % of the long-term joint contribution rate of 21.8 % of Section Pay for RPS 60 Members and 16.1 % of Section Pay for RPS 65 Members. Future rates are subject to review following the completion of the actuarial valuation at 31 December 2013 which is currently being progressed. The equivalent rates for the CARE scheme are 10.9 per cent for group contributions and 7.9 per cent for member contributions and these are being reviewed in conjunction with an actuarial valuation as at 31 March 2015 which is currently being undertaken.

The estimated amounts of contributions expected to be paid by the group and members to the schemes during the year ended 31 March 2016 are £124m and £70m respectively. 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.

	2015 %	2014 %
Key assumptions used:		
Discount rate	**3.4**	4.4
Expected rate of price inflation and CARE benefit increases (RPI measure)	**2.9**	3.3
Future earnings increases*	**3.9**	4.3
Future pension increases – RPS (CPI measure)	**1.9**	2.3

* Inclusive of a promotional salary scale of 0.5 per cent per annum. From 31 March 2012 promotional salary increases are assumed to apply only in respect of service after the date of promotion.

	2015		2014	
	Males	**Females**	Males	Females
Average life expectancy for mortality tables used to determine defined benefit obligations:				
– Member aged 65 now (pension under £9,300 pa or pensionable pay under £35,000 pa)	**20.9**	**22.7**	20.7	22.6
– Member aged 65 now (others)	**23.3**	**24.5**	22.9	25.0
– Member aged 65 in 20 years' time (pension under £9,300 pa or pensionable pay under £35,000 pa)	**23.2**	**25.1**	23.1	25.1
– Member aged 65 in 20 years' time (others)	**25.5**	**26.8**	25.1	27.4

For the Network Rail Section of the RPS the discounted mean term of the Defined Benefit obligation is 20 years, for the CARE scheme it is 33 years.

Amounts recognised in income in respect of the group's pension arrangements are as follows:

	2015 £m	2014 £m
Current service cost – defined contribution (see Note 6)	**13**	13
Current service cost – defined benefit (see Note 6)	**164**	162
Interest cost	**53**	54
	230	229

The current service cost has been included in employee costs, the net interest scheme deficit has been included in finance costs.

Amounts recognised in the statements of comprehensive income in respect of the group's pension arrangement are as follows:

	2015 £m	2014 £m
Loss/(gain) on defined benefit obligation due to experience	**7**	(35)
Loss/(gain) on defined benefit obligation due to assumption changes	**452**	(99)
Return on plan assets greater than discount rate	**(300)**	(6)
Actuarial loss/(gain) on defined benefit pension scheme	**159**	(140)

The cumulative amount of actuarial losses recognised in other comprehensive income was £1,007m (2014: £848m).

26. Retirement benefit schemes continued

The amount included in the balance sheet arising from the group's obligations in respect of its defined benefit schemes is as follows:

	2015 £m	2014 £m
The defined benefit obligation is made up as follows:		
Active members	**(4,423)**	(4,004)
Deferred pensioner members	**(769)**	(581)
Retired members	**(2,387)**	(1,826)
Present value of defined benefit obligation	**(7,579)**	(6,411)
Fair value of scheme assets	**5,071**	4,350
Deficit in the scheme	**(2,508)**	(2,061)
Group's share (60%) of the scheme deficit recognised in the balance sheet	**(1,505)**	(1,237)

This amount is presented as a non-current liability in the balance sheet.

Cumulative gains or losses are recognised in equity.

Expected future benefit payments from the Network Rail Section, based on data from the 2013 formal valuation and the 31 March 2015 IAS 19 assumptions are as follows:

	£m
Benefits expected to be paid within 12 months	139
Benefits expected to be paid between 2 to 3 years	293
Benefits expected to be paid between 4 to 6 years	525
Benefits expected to be paid between 7 to 10 years	882
Benefits expected to be paid between 11 to 15 years	1,394
Benefits expected to be paid in over 15 years	12,068

Movements in defined benefit plan assets and liabilities (including members' share)

	Asset £m	Liabilities £m	Deficit £m
At 1 April 2013	4,117	(6,229)	(2,112)
Current service cost including members' share*	–	(271)	(271)
Interest on pension deficit*	182	(272)	(90)
Administration expenses	(8)	–	(8)
Return on plan assets greater than the discount rate	11	–	11
Actuarial loss arising from changes in financial assumption	–	165	165
Actuarial loss arising from experience adjustments	–	59	59
Regular contributions by employer	119	–	119
Contributions by employees	66	–	66
Benefits paid	(137)	137	–
At 1 April 2014	**4,350**	**(6,411)**	**(2,061)**
Current service cost including members' share	–	(276)	(276)
Interest on pension deficit	192	(279)	(87)
Administration expenses	(7)	–	(7)
Return on plan assets greater than the discount rate	499	–	499
Actuarial gain arising from changes in financial assumption	–	(817)	(817)
Actuarial gains and losses on defined benefit obligation due to demographic assumptions	–	64	64
Actuarial gain arising from experience adjustments	–	(11)	(11)
Regular contributions by employer	121	–	121
Contributions by employees	67	–	67
Benefits paid	(151)	151	–
At 31 March 2015	**5,071**	**(7,579)**	**(2,508)**

The actual return on scheme assets was £691m (2014: £193m).

26. Retirement benefit schemes continued

The analysis of the scheme assets and the expected rate of return at the balance sheet date was as follows:

	Fair value of assets		Percentage of assets	
	2015 £m	2014 £m	**2015 %**	2014 %
Equity instruments	**4,474**	3,884	**88.23**	89.29
Debt instruments – Government	**336**	277	**6.62**	6.37
Debt instruments – non-Government	**227**	178	**4.48**	4.09
Property	**2**	–	**0.04**	–
Other	**32**	11	**0.63**	0.25
	5,071	4,350		

The group is exposed to a number of risks relating to the scheme including assumptions not being borne out in practice. The most significant risks are as follows:

Asset volatility
There is a risk that a fall in asset values is not matched by corresponding reduction in the value placed on the defined benefit obligation scheme (DBO). The scheme holds a proportion of growth assets, which are expected to outperform corporate or government bond yields in the long term, but gives exposure to volatility and risk in the short-term.

Change in bond yields
A decrease in corporate bond yields will increase the value placed on the scheme defined benefit obligation, although this will be partially offset by an increase in the value of the scheme's corporate bond holdings.

Inflation risk
The majority of the scheme's DBO is linked to inflation where higher inflation will lead to higher value being placed on the DBO. Some of the scheme assets are either unaffected by inflation or loosely correlated with inflation (eg, growth assets), meaning that an increase in inflation will generally increase the deficit.

Life expectancy
An increase in life expectancy will lead to an increased value being placed on the scheme's DBO. Future mortality rates cannot be predicted with certainty.

Actuarial assumption sensitivity
The discount rate is set by reference to market conditions at the reporting date, and can vary significantly between periods.

The earnings increases are linked to inflation and so set by reference to market conditions at the reporting date.

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:

	2015 £m	2014 £m
Discount rate		
Change in defined benefit obligation at year end from a 25 basis points increase	**(353)**	(277)
Change in defined benefit obligation at year end from a 25 basis points decrease	**372**	291
Mortality		
Change in defined benefit obligation from a one year increase in longevity	**244**	156
Change in defined benefit obligation from a one year decrease in longevity	**(237)**	(153)
Earnings increase		
Change in defined benefit obligation at year end from a 25 basis points increase	**147**	80
Change in defined benefit obligation at year end from a 25 basis points decrease	**(142)**	(79)
Price inflation (CPI measure)*		
Change in defined benefit obligation at year end from a 25 basis points increase	**375**	296
Change in defined benefit obligation at year end from a 25 basis points decrease	**(357)**	(283)

* Including consistent increases to RPI, salary growth and RPI/CPI related pensions assumptions.

COMPANY INFORMATION

CALENDAR 2015/16

31 March 2015	Year end
11 June 2015	Preliminary results announced for full year to 31 March 2015
26 November 2015	Results for half-year announcement to 30 September 2015*
31 March 2016	Year end

*The announcement date is not yet confirmed and may change

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