



OFFICE OF RAIL REGULATION

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13 February 2013

Group Company Secretary
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Network licence condition 4: consent of the Office of Rail Regulation

Background

1. On 21 January 2013, Network Rail Infrastructure Limited (Network Rail) wrote to the Office of Rail Regulation about consent under paragraph 1 of condition 4 of its network licence to the transfer of some assets including land and property structures to Network Rail from British Railways Board (Residuary) Limited (BRBR). Some of BRBR's functions would also transfer to a subsidiary of Network Rail.
2. You explained that this follows from the Government's 2010 review of public bodies and its proposed abolition of BRBR, which is wholly owned by the Department for Transport (DfT). The Public Bodies Act (the Act) provides a mechanism to achieve this.
3. You also explained that Network Rail proposes to covenant to reimburse the costs or losses incurred by its new subsidiary.
4. A copy of the letter is attached at Annex A.

Reasons for our consent

5. We concur with your view that management of the transferred operational sites and property could be considered as permitted business under condition 4. The three properties at Market Harborough, Hunslet and Glasgow have a clear operational use so these are captured within the definition of permitted business activities. Some of the structures sit above Network Rail's existing infrastructure and arrangements are in place to make sure these are structurally sound and do not adversely impact the operational railway.



6. We do not think that managing the seven railway war memorials to be transferred should be considered as ancillary to permitted business activities. However, given that Network Rail maintains other memorials as part of its managed stations portfolio and having had regard to our duties under section 4 of the Railways Act 1993, we consent for the purposes of paragraph 1 of condition 4 of the network licence to the proposed arrangement.

7. We may at any time modify or revoke this consent after consulting you it appears to us to be requisite or expedient to do so, having regard to the duties imposed on us by section 4 of the Railways Act.

A handwritten signature in black ink that reads "Robert M Plaskitt". The signature is written in a cursive style with a large, looped initial "R" and a long horizontal stroke at the end.

Rob Plaskitt

Annex A



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21 January 2013

Dear Tim

Consent to transfer BRB (Residuary) Limited property and assets to Network Rail

Background

The Government undertook a review of public bodies in 2010. The outcome of this review was the Public Bodies Review Programme which recommended the abolition of a number of public bodies, including BRB (Residuary) Limited ("BRBR") which is wholly owned by the Department for Transport (DfT).

BRBR was created on 24 January 2001 and by a transfer scheme dated 26 January 2001, the residual assets and functions of the British Railways Board were transferred to BRBR. Many of these assets have been disposed of to third parties, but some remain in BRBR's ownership.

The Public Bodies Act 2011 ("the Act") was enacted in order to provide for the abolition and merger of the various public bodies listed in the Schedules to the Act. BRBR is listed in Schedule 1 as a body to be abolished. The DfT has proposed that some of BRBR's assets including land and property structures (together with their corresponding functions) should be transferred to Network Rail. The original proposal was for the real estate assets and functions to be transferred to Network Rail Limited.

The DfT consulted on these proposals in May 2012. Network Rail responded to the consultation to confirm that subject to obtaining any such regulatory consents as may be required and agreeing how the ongoing operation, maintenance and renewal costs would be funded, Network Rail was the appropriate body to acquire these assets.

However, it has now been agreed that the transfer of the functions will be to a subsidiary of Network Rail Infrastructure Limited (NRIL) and the transfer of the real estate and assets will



be to NRIL; see below for the rationale behind this decision. Other real estate and assets will be transferred to London & Continental Railways, the Rail Safety & Standards Board, the Highways Agency and to DfT itself.

Section 1 of the Act provides that a Minister may by order abolish a body listed in Schedule 1, and transfer its functions to an eligible person. The only relevant eligible person is a Company Limited by Guarantee ("CLG"). Section 23 of the Act provides that a Minister may make a transfer scheme of property rights, assets and liabilities to an eligible person, or a body corporate. It should be specifically noted that there is no provision in the Act that gives Network Rail the ability to decline to accept any of the assets to be proposed to be transferred.

The effect is that there needs to be a Statutory Order (for the functions) and a transfer scheme (for the property rights, assets and liabilities). We have been informed by DfT that it currently intends to lay the Statutory Order before Parliament in March 2013 with a view to the transfer being completed in September 2013.

Legal Structure

Under the Act, the property rights, assets and liabilities of BRBR can be transferred to any body corporate (such as NRIL) but the functions of BRBR can only be transferred to a CLG. Accordingly, NRIL has incorporated a subsidiary CLG named Network Rail (Assets) Limited (NR Assets) which is registered with company number 08225646. We therefore intend that the property rights assets and liabilities of BRBR will be transferred to NRIL by the transfer scheme and the functions of BRBR will be transferred to NR Assets by the transfer scheme. As we do not anticipate that this structure will require any significant internal reorganisation post-completion of the transfer scheme, we are of the view that the external legal costs associated with this structure will primarily be in the nature of Land Registry applications and fees.

During discussions with DfT, it has become apparent that DfT intends to include in the transfer scheme an obligation on NRIL, in favour of NR Assets, to maintain the assets and structures inherited from BRBR with a view to NRIL holding NR Assets harmless against any failure to do so (albeit we await the proposed wording from DfT). We understand that the DfT has adopted this approach on the basis that the statutory functions and liabilities will remain with NR Assets, a non-operational subsidiary, and as such DfT need to ensure that NR Assets has NRIL standing behind it in the event of any third party claim. DfT has asserted the right to include such an obligation on NRIL in the transfer scheme on the basis of section 23(6)(a) of the Act which states, "A transfer scheme may make consequential, supplementary, incidental or transitional provision and may in particular – (a) create rights, or impose liabilities, in relation to property or rights transferred;..." As such, Network Rail does

not believe that the imposition of such an obligation on NRIL is a matter which necessitates the need to obtain regulatory consent under the terms of the Network Licence. However, if ORR is of the view that specific consent is required, Network Rail invites ORR to provide specific consent under the terms of the Network Licence to allow the scheme to proceed.

In addition to the above, Network Rail in any event intends to put in place an agreement between NRIL and NR Assets which will provide that NR Assets will, at NRIL's request, exercise the statutory functions inherited from BRBR and in return NRIL will covenant to reimburse the costs or losses incurred by NR Assets in so doing. The main purpose of this agreement is to ensure that NRIL has the necessary powers to properly maintain and operate the relevant assets. Network Rail is of the view that such an arrangement may require ORR consent under Licence Condition 4.11 and 4.13 of the Network Licence. If ORR is of a similar view, Network Rail invites ORR to provide specific consent under the terms of the Network Licence to allow the scheme to proceed.

Assets/ Properties to be Transferred

The DfT's rationale for the proposed transfer to Network Rail is to correct apparent anomalies of property ownership arising from rail privatisation in 1994 and to transfer assets which might be expected to be owned by a national infrastructure manager or are of importance to the rail industry.

Where there is a benefit to the industry, we agree that certain assets should transfer to Network Rail. The assets will form part of the Network Rail Routes (seven are affected by this proposal) therefore the Directors of Route Asset Management and the National Liabilities team have been consulted and asked to evaluate each of the assets. While we are content with the proposed transfer, this is subject to agreeing issues of funding and such regulatory consents as may be required.

Annex 1 (attached) provides details of BRBR assets which are proposed to be transferred to Network Rail. These are grouped into the following categories:

Structures: there are 20 structures including abutments, over and under bridges, piers, embankments, viaducts and tunnels, the maintenance of which is critical to the safe running of the operational railway.

There are three large viaducts which do not exclusively span Network Rail's network and a large standalone viaduct which Network Rail engineers have estimated would cost a substantial amount to refurbish (numbered 8, 9 and 13 in Annex 1). Network Rail continues to discuss with DfT whether it would be a better solution for those structures not to be transferred to Network Rail, given the wider purpose of the structures and associated costs.

For the avoidance of doubt, the cost of operating and maintaining these assets are not set out in Annex 1.

Operational Sites: there are 17 operational sites, the transfer of which would correct anomalies of property ownership arising from rail privatisation. They are those which one might expect the national infrastructure owner to own or which have importance to the railway industry.

One example is Old Dalby Test Track (numbered 28 in Annex 1), a high speed electrified facility to test and trial passenger rolling stock, high speed and electrified infrastructure systems and is therefore capable of facilitating a wide range of innovation initiatives and future development. The site is complementary to Network Rail's High Marnham Innovation and Development Centre which is a lower speed facility.

It should also be noted that Network Rail has made use of the Old Dalby test track since railway privatisation for the purposes of calibrating its infrastructure maintenance fleet as the test track has a calibration rail. Calibration is a mandatory requirement in order to ensure the integrity of track monitoring data.

Properties: there are 3 properties which DfT has agreed should be transferred to Network Rail on the basis that they are required to assist with strategic railway improvements. These are:

- A former goods yard at Market Harborough with a connected railway siding over which Network Rail has a lease option. It is foreseeable in the future that Network Rail will seek to make line speed improvements to the adjacent Midland main line;
- A site at Hunslet, Leeds containing a number of sidings leased to Freightliner; and
- Eastfield maintenance depot, Glasgow: a regulated depot which is currently operated by First ScotRail.

Railway Memorials: there are 7 railway memorials which have importance to the railway industry and which might be expected to be owned by Network Rail, given that their existence results from incidents associated with the operational railway.

Funding

The values of the assets to be transferred are still being reviewed and it is DfT's view that there are benefits to Network Rail in receiving these assets and it has previously stated that the liabilities and assets which transfer will be neutral in terms of cost during CP4. In our response to DfT's consultation we set out that we had not seen any evidence that supported this assertion of cost neutrality or that we would be compensated through the benefits received in owning the properties. We are in ongoing negotiations with DfT in this regard.

We will need to take the costs of maintaining the assets into account as part of the next periodic review. Our Strategic Business Plan sets out more information on this matter.

Regulatory Consents

While Network Rail is in consultation with the DfT in relation to the BRBR transfer scheme and the implications of the transfer on the real estate, assets and functions outlined above, it must be acknowledged that ultimately Network Rail's consent to the statutory order and transfer scheme is not required for the same to have legal effect.

Therefore it is our view that the transfer to Network Rail will not require regulatory consent for the following reasons: -

1. Section 23(5)(a) of the Act states that, "The things that may be transferred under a transfer scheme include – (a) property, rights and liabilities that could not otherwise be transferred...."; and
2. The transfer to Network Rail of assets under a statutory transfer scheme does not amount to Network Rail conducting business or carrying out an activity within the meaning of Condition 4.1, as ultimately it is a unilateral transfer controlled by the DfT.

With that in mind, Network Rail does not believe the transfer of the assets to Network Rail can be considered as something which necessitates the need to obtain regulatory consent under the terms of the network licence.

Furthermore, Network Rail believes that the operation and maintenance of the properties, structures and operational sites all constitute permitted business activities under Condition 4 of the network licence as they are connected with the business of providing and operating Network Rail's network. The transfer of these sites to Network Rail will ensure that they can be maintained, renewed, replaced and improved as necessary and will assist Network Rail to improve and develop the railway infrastructure. While the war memorials will not provide any direct operational benefit, Network Rail considers that, they should be considered ancillary to permitted business activities, given their direct association with the operational railway.

Therefore for the reasons outlined above, Network Rail does not think it is necessary or appropriate to request specific consent or otherwise allocate any part of the acquisition to the de minimis facility. However, Network Rail is aware that ORR has expressed an initial view that the transfer of these assets is an activity for which specific consent is required. If ORR maintains this view then Network Rail invites ORR to provide specific consent under network licence condition 4.1(c) to allow the transfer to proceed. Given the nature of the railway

memorials in particular, it is also requested that ORR permits Network Rail to exclude them from the definition of 'relevant assets' under the network licence.

We have considered above the regulatory treatment of the transfer. However, we would distinguish that from the regulatory treatment of the arrangements between NRIL and NR Assets arising from the transfer, which may necessitate different treatment. In this regard, we would refer you to our comments under the "Legal Structure" heading of this letter and look forward to receiving your response.

The operational site at Old Dalby consists of a depot which is leased from Eos Inc. Limited to BRBR and sublet to Metronet. Under this arrangement Transport for London (TfL) observe and perform the tenant covenants following the transfer of business from Metronet to TfL in 2009. The test track is leased from BRBR to Metronet (now TfL). Licence Condition 5 provides that Network Rail is not to have a direct or indirect interest in the ownership or operation of railway vehicles in Great Britain. Network Rail believes that the acquisition of the test track (and depot) cannot create a legal or beneficial interest in a railway vehicle or the right to manage the affairs of any party who is interested in or operates a railway vehicle but is simply a property interest (as is Network Rail's interest in the High Marnham facility). For the avoidance of doubt Network Rail therefore believes that the transfer of this asset does not trigger a direct or indirect interest by Network Rail in rolling stock for which ORR consent would be required under Condition 5 of the Network Licence.

As noted above there are a few outstanding issues to be resolved with DfT. Despite this, Network Rail believes this letter should provide ORR with sufficient information in order to determine whether it agrees with Network Rail's view regarding the regulatory treatment of this transfer.

This letter is copied to Paul Plummer at Network Rail, John Larkinson at ORR and Malcolm Twite at DfT.

Yours sincerely

A handwritten signature in black ink, appearing to read 'K. Johnson', written in a cursive style.

Kara Johnson
Regulatory Specialist