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31 March 2010

Ms Hazel Walker  
Group Company Secretary  
Network Rail Infrastructure Limited  
Kings Place,  
90 York Way  
London N1 9AG

Dear Hazel

## **Notice of modification of Network Rail Infrastructure Limited's network licence**

Network Rail Infrastructure Limited ("Network Rail") has been granted a network licence ("the licence") under section 8 of the Railways Act 1993 ("the Act") subject to conditions contained in the licence.

In accordance with section 12(2) of the Act, on 26 February 2010, ORR gave notice of its proposal to modify the licence to:

- (a) revise the limits to the level of financial indebtedness;
- (b) simplify the limits to the level of financial indebtedness by removing the higher group of limits, which were an absolute restriction on the level of financial indebtedness;
- (c) simplify the restrictions on the levels of financial indebtedness for the Network Rail group of companies by just restricting the level of financial indebtedness of the consolidated Network Rail;
- (d) require that Network Rail should notify us immediately in writing if it becomes aware of any circumstance that means it is no longer complying, or that causes it to no longer have the reasonable expectation that it is likely to comply, with condition 3.1 and (where applicable) condition 3.2 of the licence; and to
- (e) amend the definitions of financial indebtedness and RAB.

The notice published by ORR set out the reasons for the modifications and their effect. It required any representations or objections to the modifications to be made to it on or before 26 March 2010.



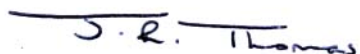
ORR has considered the representations or objections which were duly made and not withdrawn.

The licence holder has given its consent to the modifications.

### **Modifications**

Under section 12(1) of the Act and with the consent of the licence holder, I therefore modify the licence by deleting condition 3 of Network Rail's licence in its entirety and replacing it with the new condition 3 of Network Rail's licence as set out in Schedule 1 of this notice. There will also be related changes to the definition of RAB in condition 11 of Network Rail's licence as set out in schedule 2 of this notice. These modifications will take effect on 1 April 2010.

Yours sincerely

A handwritten signature in blue ink, appearing to read "J. R. Thomas", with a horizontal line drawn above the first part of the signature.

**John Thomas**

## **Schedule 1: New condition 3 of Network Rail's licence.**

### **3 Financial indebtedness**

- 3.1 Except with the written consent of ORR, the licence holder shall use reasonable endeavours to ensure that at any time the total amount of financial indebtedness of the licence holder, any subsidiaries of the licence holder, Network Rail Infrastructure Finance and any subsidiaries of Network Rail Infrastructure Finance shall not exceed the limits applicable at that time that are shown in table 3.1 which are determined by dividing that financial indebtedness by the Value of the RAB at that time.

**Table 3.1: Limits to the level of financial indebtedness expressed as a percentage of the Value of the RAB**

<b>Financial year</b>	<b>Limit</b>
2009-10	70.0%
2010-11	70.0%
2011-12	72.5%
2012-13	75.0%
2013-14	75.0%

- 3.2 If at any time the total aggregate amount of financial indebtedness of the licence holder, any subsidiaries of the licence holder, Network Rail Infrastructure Finance and any subsidiaries of Network Rail Infrastructure Finance exceeds the limits set out in condition 3.1 applicable to that financial year the licence holder shall, within such time periods as ORR may notify as being appropriate in the circumstances:
- (a) provide to ORR details of the steps it intends to take to reduce the amount to those limits or below;
  - (b) take those steps; and
  - (c) provide to ORR evidence that it has taken those steps.

3.3 The licence holder shall:

- (a) provide, from time to time as requested by ORR and in any event every year in the regulatory financial statements the licence holder prepares pursuant to condition 11, confirmation that, in respect of the financial year to which the statements relate, it has complied, and, in respect of the following financial year, it is not aware of any circumstances which will prevent it complying and it is likely to comply, with condition 3.1 and (where applicable) condition 3.2 and, if so requested by ORR, evidence in support of that confirmation; and
- (b) notify ORR immediately in writing if at any time the licence holder becomes aware of any circumstance that means it is no longer complying, or that causes it no longer to have the reasonable expectation that it is likely to comply, with condition 3.1 and (where applicable) condition 3.2.

3.4 The licence holder shall pay to the Secretary of State, at least annually, a fee in respect of the state financial indemnity.

3.5 In this condition:

- |                          |   |
|--------------------------|---|
| “fee”                    | means the amount equal to 0.8 per cent (on an annual basis) of the daily outstanding amount of financial indebtedness incurred by Network Rail Infrastructure Finance and which is supported by the state financial indemnity;  |
| “financial indebtedness” | <p>means the sum of:</p> <ul style="list-style-type: none"><li>(a) all financial liabilities arising from all transactions (including any forward sale or purchase agreement) which have the commercial effect of a borrowing;</li><li>(b) any counter-indemnity obligation in respect of any guarantee, indemnity, bond, letter of credit or any other instrument issued by a bank or financial institution; and</li><li>(c) any guarantee, indemnity or similar assurance against financial loss of any person in respect of any item referred to in paragraph (a);</li></ul> <p>less</p> |

- (d) cash and cash equivalents which are assets or investments that are held for the purpose of meeting short-term cash commitments or other investments with a maturity of twelve months or less for the purpose of pre-funding the repayment of financial indebtedness.

For the purposes of this condition:

(a) financial indebtedness excludes:

- (i) any financial indebtedness between the licence holder or any of the licence holder's subsidiaries and Network Rail Infrastructure Finance or any of Network Rail Infrastructure Finance's subsidiaries;
- (ii) any financial indebtedness between the licence holder and any of its subsidiaries;
- (iii) any financial indebtedness between any of the licence holder's subsidiaries;
- (iv) any financial indebtedness between Network Rail Infrastructure Finance and any of its subsidiaries; and
- (v) any financial indebtedness between any of Network Rail Infrastructure Finance's subsidiaries;

(b) financial indebtedness is:

- (i) calculated by reference to the principal amount outstanding of any such financial indebtedness (and no mark to market value will be used to calculate its amount); and
  - (ii) measured as specified in the regulatory accounting guidelines, issued in accordance with condition 11, in force at the applicable time;
- (c) where financial indebtedness denominated in a foreign currency is hedged by a foreign currency derivative transaction protecting against or benefiting from

fluctuations in foreign exchange rates, the principal amount outstanding shall be calculated by reference to the sterling amount payable under the relevant derivative;

“Network Rail  
Infrastructure Finance”

has the meaning given to it by condition 4.33;

“state financial  
indemnity”

means the financial indemnity provided by the Strategic Rail Authority on 29 October 2004 (and transferred to the Secretary of State on 26 June 2005), which is available until 2052; and

“Value of the RAB”

means the value of the licence holder’s assets calculated in accordance with the regulatory accounting guidelines, issued in accordance with condition 11, in force at the applicable time.

## **Schedule 2: Modifications to condition 11 of Network Rail's licence**

### **Condition 11: Regulatory accounts**

#### *Purpose*

- 11.1 The purpose of this condition 11 is to procure the provision of annual information on the financial performance and financial position of the licence holder, Network Rail Infrastructure Finance and any subsidiaries of Network Rail Infrastructure Finance which:
- (a) is relevant to ORR and other persons for the assessment and determination of the licence holder's access charges; and
  - (b) allows the financial performance and financial position of the licence holder to be monitored against the Determination Assumptions.

#### *General duty*

- 11.2 To achieve the purpose in condition 11.1, the licence holder shall prepare regulatory financial statements in relation to itself and, unless ORR otherwise consents, to Network Rail Infrastructure Finance in accordance with the following paragraphs of this condition 11 and any Regulatory Accounting Guidelines from time to time issued by ORR.
- 11.3 The licence holder shall, and shall procure that any affiliate or related undertaking of the licence holder and Network Rail Infrastructure Finance shall, maintain such accounting records, other records and reporting arrangements as are necessary to enable the licence holder to properly prepare the regulatory financial statements required by condition 11.2. The licence holder shall maintain all systems of control and other governance arrangements that ensure the information collected and reported to ORR is in all material respects accurate, complete and is fairly presented and that all control and other governance arrangements are kept under regular review by the directors of the licence holder so that they remain effective for this purpose.

#### *Specific obligations*

11.4 The financial statements referred to in condition 11.2:

- (a) shall be prepared in respect of the financial year ended 31 March 2002 and (save as otherwise provided in this condition 11 or the Regulatory Accounting Guidelines) on a consistent basis in respect of each financial year;
- (b) shall be prepared such that, so far as is reasonably practicable, the definition of items in primary statements; the valuation of assets and liabilities; the treatment of income and expenditure as capital or revenue; adjustments in respect of the provision, utilisation, depreciation and amortisation of assets and liabilities; and any other relevant accounting policies shall be consistent with:
  - (i) ORR's valuation of the Regulatory Asset Base for the purpose of determining access charges for the access review periods specified in the Regulatory Accounting Guidelines; and
  - (ii) the Determination Assumptions for the access review periods specified in the Regulatory Accounting Guidelines;(and so that where the presentation of an item in the primary statements departs from the basis for the Regulatory Asset Base or the Determination Assumptions, a reconciliation shall be included by way of a note);
- (c) shall include, as a primary statement, a statement of regulatory financial performance comparing income and expenditure, for the access review periods specified in the Regulatory Accounting Guidelines with the Determination Assumptions;
- (d) shall include all details reasonably necessary to reconcile items included in the primary statements with any corresponding items in annual statutory accounts for the access review periods specified in the Regulatory Accounting Guidelines; and
- (e) shall include narrative explaining the material variances from the previous year and from the Determination Assumptions.

*Sufficiency of resources*



11.5 The licence holder shall make a statement, which shall be approved by a resolution of the board of directors of the licence holder and signed by a director of the licence holder pursuant to that resolution, certifying the adequacy (or otherwise) of the management and financial resources, personnel, fixed and moveable assets, rights, licences, consents and facilities of the licence holder for the period of 12 months commencing on the date of the statement.

11.6 The statement made under condition 11.5 shall be in one of the following forms:

either:

(a) “After making enquiries, and subject to the outcome of any access charges review which is due to be concluded within the 12 month period referred to in this statement, the directors of the licence holder have a reasonable expectation that the licence holder will have available to it, after taking into account in particular, but without limitation:

(i) any dividend or other distribution, loan repayments or other sums due which might reasonably be expected to be declared or paid by the licence holder;

(ii) any mortgage, charge, pledge, lien or other form of security or other encumbrance; and

(iii) any indebtedness or guarantee;

sufficient resources, including (without limitation) management and financial resources, personnel, fixed and moveable assets, rights, licences, consents, and facilities, on such terms and with all such rights, to enable the licence holder to: (a) properly and efficiently carry on the Permitted Business; and (b) comply in all respects with its obligations under the Act and under its network licence, for the period of 12 months referred to in this statement.”

or:

(b) “After making enquiries, and subject to the outcome of any access charges review which is due to be concluded within the

12 month period referred to in this statement, the directors of the licence holder have a reasonable expectation, subject to the factors set out below, that the licence holder will have available to it, after taking into account in particular, but without limitation:

- (i) any dividend or other distribution, loan repayments or other sums due which might reasonably be expected to be declared or paid by the licence holder;
- (ii) any mortgage, charge, pledge, lien, or other form of security or other encumbrance; and
- (iii) any indebtedness or guarantee,

sufficient resources, including (without limitation) management and financial resources, personnel, fixed and moveable assets, rights, licences, consents, and facilities, on such terms and with all such rights, to enable the licence holder to: (a) properly and efficiently carry on the Permitted Business; and (b) comply in all respects with its obligations under the Act and under its network licence, for the period of 12 months referred to in this statement. However, they would like to draw attention to the following factors which may cast doubt on the ability of the licence holder to do this.”

or:

- (c) “In the opinion of the directors of the licence holder, the licence holder will not have available to it sufficient resources, including (without limitation) management and financial resources, personnel, fixed and moveable assets, rights, licences, consents, and facilities, on such terms and with all such rights, to enable the licence holder to: (a) properly and efficiently carry on the Permitted Business; and (b) comply in all respects with its obligations under the Act and under its network licence, for the period of 12 months referred to in this statement.”

11.7 The licence holder shall submit to ORR details of the main factors which the directors of the licence holder have taken into account in making the statement under condition 11.5 and the information specified in the Regulatory Accounting Guidelines. In the case of a

statement of the kind contemplated by condition 11.6(b) the licence holder shall also submit with the statement a description of the factors which may cast doubt on the ability of the licence holder to carry on the activities authorised by this licence.

11.8 The licence holder shall -

- (a) notify ORR in writing immediately if its directors become aware of any circumstance that causes them no longer to have the reasonable expectation expressed in the most recent statement made under condition 11.5 in the forms set out in condition 11.6; and
- (b) subject to complying, as if it were a company whose ordinary shares are for the time being admitted to the Official List of the UK Listing Authority, with the listing rules of the Financial Services Authority acting in its capacity as a competent authority for the purposes of Part VI of the Financial Services and Markets Act 2000, publish its notification to ORR in such form and manner as ORR may direct. This notification will include the information specified in the Regulatory Accounting Guidelines in relation to the operation of the re-opener provisions.

*Regulatory Accounting Guidelines*

11.9 ORR may from time to time issue Regulatory Accounting Guidelines, which may:

- (a) further specify the accounting policies, format and content of the financial statements and the matters to be shown or reported in them;
- (b) provide for appropriate segmental analysis and/or further breakdown of any items contained in the financial statements;
- (c) provide for specification or description of any transactions or arrangements between the licence holder and any affiliate or related undertaking (including, without limitation, so as to enable ORR to monitor compliance with the conditions of this licence);

- (d) further include provision requiring the licence holder to prepare and publish information in respect of proposed enhancements which the licence holder shall log up as enhancement expenditure, and annually, information on those enhancements actually made; and
- (e) specify the provision and/or publication of such other information as ORR may reasonably require in order to monitor the licence holder's financial performance and financial position or assist in the determination of the licence holder's access charges.

#### *Auditors*

11.10 The licence holder shall procure a report by the Auditors addressed to ORR:

- (a) stating whether, in their opinion, the regulatory financial statements (other than those referred to in condition 11.10(c)) and information on proposed enhancements have been prepared in accordance with this condition, including Regulatory Accounting Guidelines;
- (b) stating whether, in their opinion, the regulatory financial statements present fairly the financial performance and financial position of the licence holder and (to the extent that they relate to Network Rail Infrastructure Finance) of Network Rail Infrastructure Finance in accordance with this condition and any Regulatory Accounting Guidelines; and
- (c) stating whether the information on enhancement expenditure produced in accordance with condition 11.9(d) has been prepared in accordance with the Regulatory Accounting Guidelines and is consistent with such expenditure presented in the primary financial statements.

11.11 Each statement made under condition 11.5 shall be accompanied by a report prepared by the Auditors and addressed to ORR, stating whether the Auditors are aware of any inconsistencies between that statement and any supporting statements and either the financial

statements referred to in condition 11.2 or any information which the Auditors obtained in the course of their audit work for the licence holder and, if so, the report of the auditors should state what the inconsistencies are.

- 11.12 The licence holder shall enter into a contract of appointment with the Auditors which shall include a term that the Auditors will provide such further explanation or clarification of their reports and such further financial information in respect of the matters which are the subject of their reports as ORR may reasonably require for the exercise of its functions, including, in relation to monitoring, compliance by the licence holder with the conditions of this licence.

*Publication and provision of information*

- 11.13 The licence holder shall deliver to ORR a copy of the financial statements together with any information provided for in the Regulatory Accounting Guidelines, the Auditors' report referred to in condition 11.10 and the statement referred to in condition 11.5 as soon as reasonably practicable and in any event not later than 1 July following the end of the financial year to which they relate (or a later date approved by ORR). The financial statements, information, the Auditors' report referred to in condition 11.10 and the statement referred to in condition 11.5, subject to any modifications approved by ORR, (including the deletion of any information the publication of which ORR is satisfied would or might seriously and prejudicially affect the interests of the licence holder or any other person), shall be published within one calendar month of delivery to ORR and then made available to any member of the public on request.

- 11.14 With a view to enabling the licence holder to comply with its obligations under condition 11.2, the licence holder shall, unless ORR otherwise consents, procure from Network Rail Infrastructure Finance a legally enforceable undertaking or undertakings in favour of the licence holder which shall require Network Rail Infrastructure Finance to prepare and give to the licence holder financial statements in relation to Network Rail Infrastructure Finance and its subsidiaries in such a form and covering such periods as may be specified in any Regulatory Accounting Guidelines from time to time issued by ORR.

11.15 The licence holder shall:

- (a) deliver to ORR evidence (including a copy of all such undertakings) that the licence holder has complied with the obligation to procure any undertaking pursuant to condition 11.14;
- (b) inform ORR immediately in writing if the directors of the licence holder become aware that any undertaking procured pursuant to condition 11.14 has ceased to be legally enforceable or that its terms have been breached; and
- (c) comply with any direction from ORR to enforce any of the undertakings procured pursuant to condition 11.14.

11.16 In this condition:

“Auditors”	means the person appointed by the licence holder for the purpose of reporting on the regulatory financial statements referred to in this condition 11;
“Determination Assumptions”	means any assumptions (including their definitions and bases of measurement) from time to time notified to the licence holder by ORR as assumptions that have been used for determining access charges;
“Network Rail Infrastructure Finance”	has the meaning given to it by condition 4.33;
“Regulatory Accounting Guidelines ”	means any guidelines issued by ORR from time to time in accordance with condition 11.9;
“Regulatory Asset Base”	means the <del>asset values as from time to time notified to</del> <u>value of</u> the licence holder <del>by ORR as being asset values that have been or are to be used for determining access charges</del> <u>for regulatory purposes</u> .

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