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Dear John

## **Licence Condition**

As you are aware Network Rail has been undergoing changes to the composition of its Board over the period of the last twelve months involving the retirement and the appointment of a number of Non-Executive Directors.

As part of this process a careful review was undertaken of the requisite skills and experience that would best serve Network Rail in the future. Details of the resulting profiles identified have been shared with the ORR at the time.

As you are also aware our Network Licence includes a condition which stipulates that Network Rail 'shall ensure that at all times the board of directors...contains a majority of non-executive directors who shall be persons of standing and of which at least two shall each have satisfied the Office of Rail Regulation that he or she has substantial relevant experience of working in the railway industry'. I also note that Part II, paragraph 5 of the Network Licence provides the flexibility for you to extend dates specified in the licence by a reasonable period.

At the time of the Network Licence last being reviewed we requested that this requirement be removed since its need related to the circumstances existing in 2002 with Network Rail's acquisition of Railtrack and the issues facing the new Board at that time. We expressed the view at the last licence review that the knowledge and skill base of the Board needed now no longer demands this level of rail expertise of Non-Executive Directors is written into the licence. Moreover the role of Members has developed significantly since 2002 which also reduces the need for the condition. In writing to you now, however, we are not asking you to modify the licence at this stage.

It is our continuing intention to secure compliance with the licence and we have been taking steps to achieve this. As such as part of the search for the new Non-Executive Directors we have been seeking a suitable candidate to meet this criteria. To this end the appointment of Graham Eccles earlier this year thus meant that upon Chris Green's retirement from the Board this July we continue to fulfil the Licence condition at present.

Unfortunately David Bailey is due to retire from the Board shortly and we are presented with the challenge again of finding one more Non-Executive Director with railway experience. We have carried out extensive searches for this position using our own contacts as well as the knowledge base of others including search consultants. Disappointingly the results have produced very limited



options usually due to an inability to meet the criteria both within our Articles of Association on Director eligibility and/or the issue of conflicts of interests.

Again as you will be aware, recently we thought that we had found a suitable candidate but during the last stage of investigation emerging conflict of interest issues arose which have resulted in that no longer being an appropriate appointment.

This latest event is immensely disappointing to us but we are still keen to continue to search for a suitable person for this position. What is key, however, in our view is that the choice must be driven first and foremost by the right skill sets. In holding responsibility for the primary governance of Network Rail, the Board must comprise of the right people with the right skill sets. Moreover the skills that we had previously identified also need to be reviewed now that we have identified the future CEO. We would generally wish to have two such directors but we do not believe there is such a pressing need for this in the immediate term and the priority should be to select the right person. In the mean time, we continue to have the benefit of one extremely experienced and respected Non-Executive Director meeting the Condition criteria.

We do not believe it would be appropriate, nor practically possible, to make an interim external appointment pending identification of the right long term appointee. Moreover, the appointment of an experienced railway operator from within Network Rail would not be regarded as "independent" both at a practical level and under the definition of independent under the Listing Rules Governance Code.

We are taking steps to remedy the situation but it will not be possible to complete this process within the period of one month specified in the licence. We therefore ask that you specify an alternative date by which the requirement must be met to secure compliance with the licence. We propose that this date should be 31 March 2011.

We will keep you informed of progress and if it appears that we will be unable to make a suitable appointment by the beginning of the next financial year I will write to you again to explain what further steps we are taking to remedy the matter. If the matter has not been resolved by the time of our AGM at the latest I am sure that this will be a matter which our members will wish to understand regardless of any licence condition.

I am copying this letter to Juliet Lazarus.

Yours sincerely

A handwritten signature in blue ink, appearing to read "Paul Plummer".

**pp** Paul Plummer  
**Director, Planning and Development**