From: Linnett, Simon

Sent: 23 December 2015 11:19

To: Nicola Shaw

Cc: Shaw Secretariat; Douglas-Hamilton, James

Subject:Shaw Review

Dear Nicola

I have read your consultation document and met with Daniela on 22nd. We are pleased to offer our views in summary as follows:

1. Private sector capital can be attracted back into Network Rail if the form of regulation reverts to a predictable RAB-based model. This private sector capital could come from both the private markets (Pension, Sovereign Wealth or Infrastructure funds and Insurers) or public markets (listed equity). Many pension and sovereign wealth funds are happier to invest without a listing.

2. Such private capital would strengthen the company - it would ensure that capital is available when required rather than when available; it could add a different discipline to the organisation and it could (with other changes) take Network Rail and any independent debt off the government balance sheet. Private sector capital has consistently shown its ability to improve the quality performance of state-run assets – we showed you this in our presentation when you were new in the role (Q.20).

3. We favour RAB-based corporate private capital for the core asset over that which is structured under a PFI because it tends to offer greater flexibility and protection to both sides against legitimate over (or under) performance.

4. The sub-division of core Network Rail into sub-units has some attractions (comparability, "bite-sized chunks" for investors, different investor structures) but it also has other consequences (interfaces, units big enough to take on big ticket investment) – we believe Network Rail's current policy of giving greater autonomy and financial visibility to the zones should be encouraged as a first step. It is clearly essential to keep one signalling system operator.

5. Network Rail's balance sheet is currently too big to be efficient. It is too big when scaled against operational risk and also the economic (as against the social) returns the railway is capable of delivering. We argue rather that its size (and consequently its debt) should be shrunk to more affordable size and that the social investment in the railway should, in future, as for HS1, be paid "up front" rather than being borne by the railway. As/if private sector capital is introduced this becomes the more efficient use of the nation's balance sheet.

6. We do believe that there is merit in conducting separate ownership structures for non-core assets such as property, depots, stations and energy but these must not compromise safe and effective operation of the railway; to the extent that they confer a railway monopoly they should be regulated (but electrification could be regulated by Ofgem).

7. Network Rail has a range of different stakeholders (DfT as the railway sponsor, DfT as stakeholder and sponsor, ORR as economic regulator and Transport Focus, contributing the consumers' voice, and RDG representing the broader industry. The interaction between these

various roles, particularly to the two embedded in the DfT, may require further analysis, particularly as they relate to how the HLOS is specified and its economic return is established.

8. We would understand that the RDG is becoming an effective conduit for the railway to interact between its two essential components, infrastructure and service. We would think that it could be confusing to give franchisees excessive roles in Network Rail if private sector finance is to be secured.

As we said to [redacted: team member’s name], we are very happy to answer any questions or share with you any aspects of our earlier analysis which we shared with you at your first appointment.

Kind regards

Simon and James

Simon Linnett

Vice Chairman

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