



# **Network Rail Management Incentive Plan Statement**

**Effective from 1 April 2011**

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# Introduction and pay philosophy

Our pay philosophy is to reward outstanding performance, both organisational and individual. Our incentive arrangements are a key part of delivering on that philosophy and, as a result, form a significant element of the compensation package for Network Rail Executive Directors and Executive Committee Members.

This Management Incentive Plan ('the Plan') has been significantly revised to take better account of the particular requirements of Control Period 4. The Plan is closely aligned to the Network Rail Delivery Plan and Network Rail's Key Performance Indicators and 'Scorecard'.

The Plan is designed to reward outstanding performance, not just in the short-term but also in the medium and longer-term. It is designed to work from three different perspectives:

- To incentivise performance this year;
- To support the medium term delivery of objectives to the end of the current control period in March 2014; and
- To lay the foundations for sustainable, improving performance in the longer term (i.e. CP5 and beyond).

As a result the Plan consists of both annual and longer-term elements and significant rewards can only be achieved if the longer-term elements of the Plan are also satisfied.

In creating this Plan, Network Rail's Remuneration Committee<sup>1</sup> has sought to align the objectives of Network Rail with those of our customers and funders. The Plan is designed to enable the members of Network Rail's Executive Committee to be able to clearly identify and establish how they can influence the performance of the organisation and as a result their potential awards.

This Statement summarises the principal terms of both the Annual Incentive Plan for 2011-12 and the Longer-Term Gainshare Plan (which runs to the end of CP4) and has been prepared so that it complies with Condition 16 of Network Rail's network licence, and is in accordance with the Incentive Principles contained within the Incentive Policy, referred to in the Articles of Association of Network Rail.

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<sup>1</sup> The Remuneration Committee determines all matters concerning Executive Directors' and other senior executives' remuneration and incentives. This includes making decisions about the framework of remuneration and associated costs, and determining, on behalf of the Board, specific remuneration packages for each Executive Director or Senior Executive. The Remuneration Committee also decides the form and content of the Management Incentive Plan ('the Plan') for each financial year (within the terms of the Incentive Policy). It then decides on the awards to be made under each year's Plan, including the discretionary elements of the Plan. The Remuneration Committee is made up of Non-Executive Directors of Network Rail.

## Participants

This Management Incentive Plan, which has both an annual and longer-term element, applies to Network Rail's Executive Directors as follows:

Role	Name
Chief Executive	David Higgins
Group Finance Director	Patrick Butcher
Group Infrastructure Director	Peter Henderson
Director, Investment Projects	Simon Kirby
Director, Operations and Customer Services	Robin Gisby
Director, Planning and Development	Paul Plummer

In addition, the Plan also applies to the following Executive Committee Members:

Role	Name
Director, Communications	TBC
Director, Corporate Development	Catherine Doran
Group Company Secretary	Hazel Walker
Human Resources Director	Peter Bennett

The key principles of the Plan will also be cascaded to other senior managers with a significant level of responsibility in terms of shaping the future success of the company.

The details of the Annual Incentive Plan and the longer-term Gainshare Plan are described below.

## The Annual Incentive Plan

Payments made under the Annual Incentive Plan (AIP) are only earned by delivering specified outcomes. For the 2011-12 AIP the outcomes are more closely aligned than ever before to both the objectives as set out in Network Rail's Delivery Plan and the company's Key Performance Indicators (KPIs).

To achieve these specified outcomes will require high levels of commitment, innovation and ingenuity of all participants. In addition the AIP is designed to encourage the members of Network Rail's Executive Committee to work together as a team and foster increased collaboration across the organisation to encourage the devolution of responsibility.

## Potential awards under the AIP

The maximum potential award for the participants in the AIP is shown below:

Role	Maximum annual bonus award (expressed as a percentage of base salary)
Executive Director	60%
Executive Committee Member	60%

It should be noted that the maximum bonus that can be achieved by Executive Directors under the AIP has been reduced to 60% of salary in 2011-12 (from 100% of salary in previous years).

It is intended that the key elements of the AIP are cascaded to other Network Rail senior managers. Different performance criteria and levels of potential bonus will apply for different groups of senior managers and performance criteria will cascade through the organisation from the target and performance criteria set for the Executive Directors and Executive Committee Members so that other senior managers are measured against performance criteria that are appropriate and relevant to their role.

## The structure of the AIP

The 2011-12 AIP will have of a number of specific components known as 'hurdles', 'business goals' and 'modifiers'. These are described more fully below.

### Hurdles

The hurdles are two specific measures that must be achieved before any bonus is usually payable as follows:

- The Public Performance Target (PPT) which measures the percentage of trains arriving on time (both passenger and freight); and
- The Asset Stewardship Indicator (ASI) which measures the quality of Network Rail's asset stewardship based on asset condition, reliability and performance across Network Rail's key asset categories.

The performance measures for these hurdles will be set in accordance with the targets that were set in the 2009 Delivery Plan which are planned to achieve the outputs as specified by the Office of Rail Regulation (ORR) in its CP4 Final Determination.

For the avoidance of doubt it should be noted that the 2009 Delivery Plan (and subsequent updates) does not include a specific reference to PPT. PPT incorporates the Public Performance Measure (PPM) target for passenger journeys (as set out in the 2009 Delivery Plan) and an equivalent target for freight journeys, with weightings which reflect the relative volume of passenger and freight trains. PPT therefore creates a single measure which combines both passenger and freight performance to produce a single performance measure.

The 2011/12 hurdle targets are as follows:

#### Public Performance Target (per cent annual average)

	2009/10	2010/11	2011/12	2012/13	2013/14
<b>PPT</b>	89.0	89.6	<b>90.0</b>	90.4	90.8

#### Asset Stewardship Indicator (at a network level)

	2009/10	2010/11	2011/12	2012/13	2013/14
<b>Asset Stewardship Indicator</b>	<b>0.026</b>	<b>0.039</b>	<b>0.051</b>	<b>0.063</b>	<b>0.075</b>

For any bonus to be paid, ORR will have to confirm that the PPT and ASI levels as outlined above have been met.

Failure to achieve either of these two hurdles will normally result in no payment being awarded under the AIP, although the Remuneration Committee may exercise its judgement if the hurdles are missed for reasons beyond Network Rail's reasonable control.

## Business goals

Assuming that the hurdles as outlined above are passed, the potential bonus entitlement under the AIP will be calculated by reference to the achievement against six business goals. These business goals are essential precursors to the outperformance of the CP4 Delivery Plan and for the purposes of the 2011-12 AIP relate to organisational and cultural change objectives. For 2011-12 the indicative business goals are:

Measure	How performance will be assessed
Devolution	Implementation of stages 1&2 Audit Control Accounting
VfM outcomes	Train Operator Alliancing IIP submission HLOS input SBP preparation
Projects	Launch April 2012 Governance Skill / Capacity Business Plan
Asset Management	Maturity Assurance with devolution Project Delivery
Occupational Health, Safety and Environment	Cultural Change
People	Performance appraisal Customer focus

The potential bonus payout will be determined by performance against each of these business goals on an equal basis (i.e. 10 per cent of salary per measure). If the individual goal is met, then the maximum bonus for that goal becomes payable.

In assessing Network Rail's performance against each of these goals the Remuneration Committee will have regard to ORR's assessment of Network Rail's performance.

## Modifiers

The Remuneration Committee will also apply structured discretion to adjust potential bonus payments (both upwards and downwards) based on the following 'modifiers':

- Safety;
- Passenger Satisfaction;
- Customer Satisfaction; and
- Supplier engagement.

## Remuneration committee judgement (AIP)

By reference to the modifiers as set out above, and having had particular regard to the achievement of the three high-level objectives as specified by ORR (see below), the Remuneration Committee will decide whether to exercise its judgement to adjust the potential bonus entitlement. The normal modifier range will be +/- 20 per cent of the potential bonus but in the event of significant safety issues this may be extended to -40 per cent. It should be noted that any bonus cannot exceed the maximum percentage as detailed in the 'Potential Awards under the AIP' section above.

In deciding whether to exercise its judgement the Remuneration Committee will consider longer-term trends in performance and Network Rail's compliance with its regulatory and contractual obligations (including, but not limited to, the obligations placed on Network Rail through its network licence).

Any adjustment will be made 'in the round' taking into account all relevant circumstances. The Remuneration Committee will publish the reasons for its decisions.

## The CP4 Gainshare plan

The Gainshare Plan (GSP) is designed to complement the AIP by focussing on longer-term sustainable performance over CP4. The plan builds on the existing and previous long-term incentive plans although the approach taken in the GSP is deliberately different in that the performance focus of the GSP is purely on Financial Value Added (FVA) with all other performance elements being measured and rewarded under the AIP.

The FVA is intended to reflect all sources of financial outperformance to the company compared to the original assumptions as set out in the 2009 Delivery Plan (which was itself intended to deliver ORR's final determination from the periodic review). FVA will be reinforced as the commonly accepted sustainable outperformance measure for CP4.

A positive FVA means that Network Rail has been able to deliver sustainably the outputs as required by ORR's Final Determination with less money than was made available to the company at the start of the Control Period. A positive FVA therefore reflects direct savings to the tax-payer. The higher the FVA the greater the savings that have been made.

To aid transparency, at the end of CP4, ORR will validate the level of FVA achieved by Network Rail before any GSP payments are made to Network Rail Executive Directors and Executive Committee Members.

It is expected that a similar plan to this GSP will operate during CP5 subject to decisions by ORR and the Remuneration Committee.

## How the GSP is different to previous long-term incentive plans?

The GSP differs from previous long-term incentive plans provided by Network Rail in a number of ways. The key differences are summarised below:

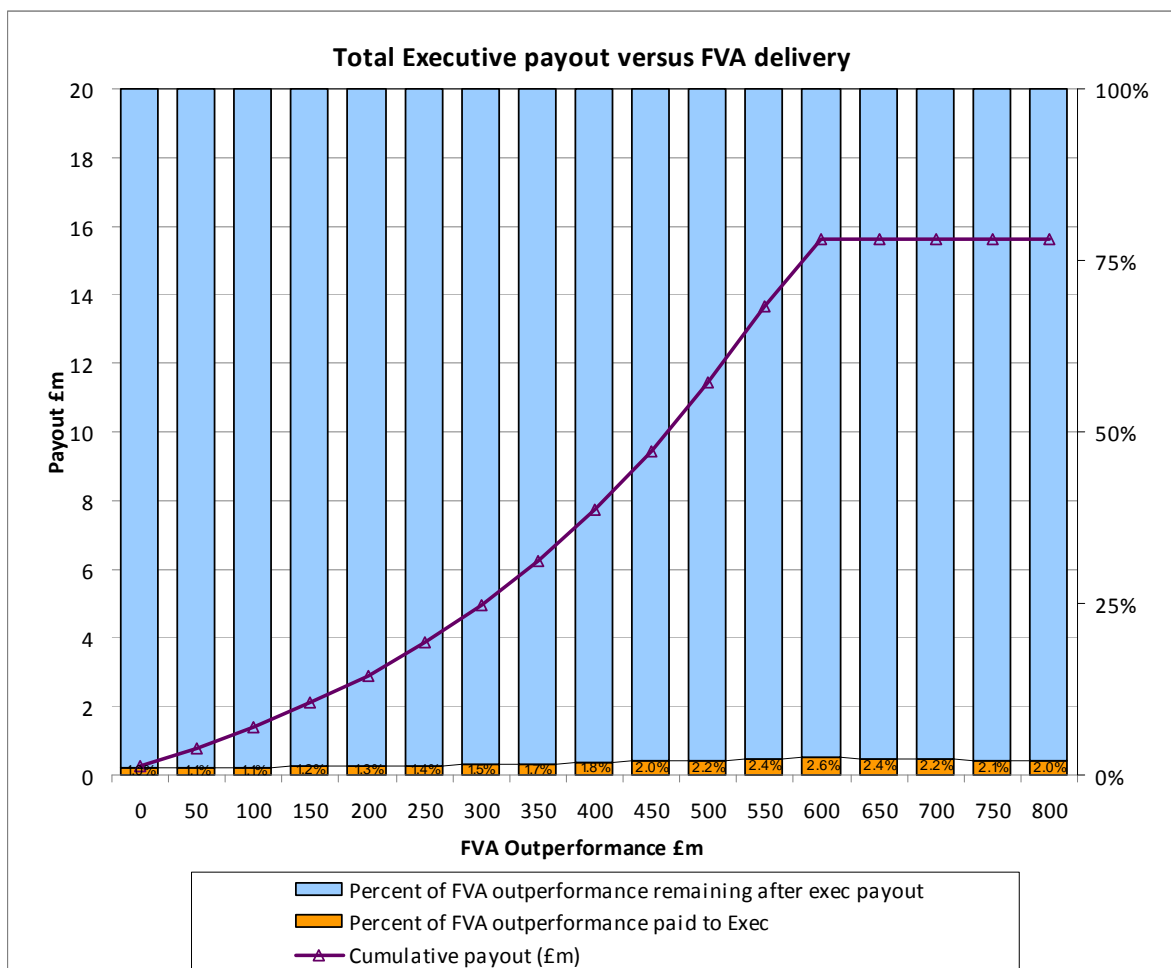
- It no longer focuses on performance over a three-year rolling period but now focuses on performance over the course of CP4. As a result, the GSP Performance Period will close at the end of the 2014 financial year.

- The GSP will effectively share part of the FVA achieved by Network Rail (up to a cap of £600m) with Executive Directors and Executive Committee Members, meaning that the greater the FVA, the greater the individual rewards.
- Whilst the design and structure of the GSP is different from the long-term incentive plan which it replaces, the potential value delivered to Participants could be broadly equivalent in value had the previous long-term scheme continued into the future.
- Subject to a six month employment eligibility period, new joiners will be eligible for payments under the GSP at the same time as other Participants, back-dated and pro-rated to their date of starting in that role.

## Potential awards under the GSP

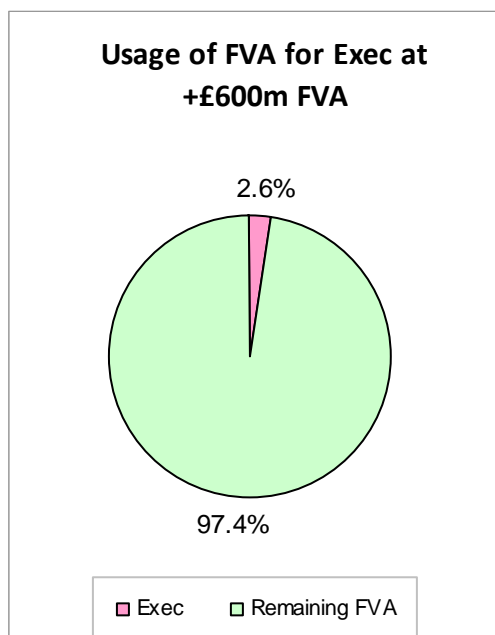
Executive Directors and Executive Committee Members will be entitled to a share of the outperformance against the regulatory determination measured by FVA. The degree of FVA achieved will directly determine the size of the potential award that is available to participants. They will be eligible to share in this outperformance on an increasing scale. FVA outperformance is capped at a maximum of £600m at which the percentage available to participants will be 2.6 per cent of FVA. This would represent a very significant achievement against ORR's CP4 Final Determination.

The link between FVA and potential bonus payments that can be earned by participants can be seen from the graph below:





So, as can be seen from the chart below if a total of £600m FVA was achieved to the end of the control period, 2.6 per cent of that FVA would be shared between Network Rail's Executive Committee.



## Remuneration committee judgement (GSP)

The Remuneration Committee will also retain the discretion to adjust potential GSP payments (downwards only) based on a number of 'modifiers' drawn from the CP4 regulatory targets, such as:

- Passenger safety indicator;
- Workforce fatalities and weighted injuries;
- Achievement of the PPM, CaSL and delay minutes target;
- Capacity including delivery of the enhancement programme;
- The requirement to maintain capability at the April 2009 baseline;
- Network availability targets for passenger and freight services;
- Station condition measure;
- Asset serviceability and reliability measures including depot condition;
- Environmental sustainability measures;
- Excellence in health and safety culture and risk control;
- Excellence in asset management;
- Efficiency assumptions; and
- Customer and passenger satisfaction scores.

The Remuneration Committee will take account of appropriate evidence to assess performance against these modifiers 'in the round' but will individually consider whether each has been fully delivered, partially delivered or has not been delivered.

## Payments under the GSP

At the end of the Performance Period, provided that the objectives set out under CP4 have been met, the FVA will be calculated and corresponding payments will be made to Participants subject to the maximum award size.

Payments at the end of the Performance Period will be made in three tranches and subject to continued employment and the absence of any exceptional circumstances. The first tranche will be made in July 2014 and taken together with payments under previous long-term incentive plans will total 50 per cent of the amount payable. The remainder will be distributed in two equal payments, one in January 2015 and one in July 2015.

Participants who leave before the end of the Performance Period will not be eligible for any further payments, unless they are deemed to be a good leaver. In the case, the Remuneration Committee has discretion to pro-rata any payments based on expected FVA performance to the date of leaving.

## ORR objectives

For the purposes of this Plan, the Remuneration Committee has agreed with ORR its three high-level objectives (1) a delivery objective (2) an outperformance objective and (3) an accountability and transparency objective. These objectives are described more fully below.

### **Delivery objective**

ORR has specified that the primary focus of Network Rail's Management Incentive Plan arrangements should be to incentivise proven long-term sustainable delivery of all Network Rail's performance and output obligations coupled with a requirement to give full weight to the improvement trajectories agreed between Network Rail and ORR to ensure progress on efficiency, service culture, excellence in health and safety culture / risk control and asset management excellence.

### **Out-performance objective**

ORR has specified that the rewards within Network Rail's Management Incentive Plan framework should be so proportioned that they strongly incentivise significant out-performance of the efficiency assumptions established at the 2008 periodic review.

### **Accountability and transparency objective**

ORR has stipulated that Network Rail's Remuneration Committee shall seek the views of Network Rail's principal funders and members and do so openly and transparently:

- Initially on the full rationale and justification for the overall remuneration framework as set out within this plan and its potential implications for the remuneration of Network Rail Executive's (in aggregate terms); and
- Annually on the data and information used by the Remuneration Committee to make decisions under the Management Incentive Plan year by year (again in aggregate terms).

In both cases the Remuneration Committee is required to have regard in its final published decisions to the views expressed. The decisions of the Remuneration Committee will need to include a full explanation of the Remuneration Committee's reasons and how it has dealt with the views expressed.

Network Rail's performance against each of these objectives will be discussed with ORR and the Remuneration Committee will take account of ORR's views when reaching its remuneration decisions.

# Compliance with objectives referred to in Condition 16 of the network licence

Network Rail has a licence granted under Section 8 of the Railways Act 1993 (as amended) to operate the rail network. ORR has primary responsibility for enforcing the conditions under this licence.

In accordance with the requirements of Condition 16 of Network Rail's network licence, Network Rail is required to have a Management Incentive Plan. Once a year the Remuneration Committee will publish a statement which summarises the criteria which have been applied in determining the level of remuneration of the executive directors and such other persons as ORR have specified.

It should be noted that both the Annual Incentive Plan and the Gainshare Plan are discretionary and do not form an entitlement under any contract of employment. Payments are not guaranteed and Network Rail reserves the right to withdraw this or any other Management Incentive Plan at any time.

Subject to the above, participants will be entitled to receive payments under this Plan in accordance with the following general rules:

- All payments will be subject to the deduction of income tax and national insurance contributions;
- Payments made under this Plan are not pensionable;
- No payments will be made to participants who are the subject of disciplinary measures or personal performance improvement measures; and
- New joiners and those working part-time hours will qualify for a pro-rata payment.

## **Termination of employment**

As this is a discretionary plan designed to encourage performance and aid retention, participants are only entitled to payment under this Plan if they are employed by Network Rail at the time of payments.

## **Good Leavers**

In exceptional circumstances the Remuneration Committee (or Human Resources Director for individuals outside the remit of the Remuneration Committee) has the discretion to measure performance over a short period and make payments where this is considered to be appropriate.

## **Other Leavers**

No payment will be made to Other Leavers under this Plan.

## **Remuneration Committee Discretion**

In the event of any disputes in relation to payments under this Plan, the Remuneration Committee shall have the right to final determination.

For the avoidance of doubt, at the end of the Performance Period the Remuneration Committee will publish a statement summarising the criteria which have been applied in determining the levels of award made under this Plan.