**Board**

**Date:** **23 March 2022**

**Item:** **TfL Prudential Indicators 2022/23 to 2024/25**

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**This paper will be considered in public**

**As provided for under section 100B(4)(b) of the Local Government Act 1972, the Chair is of the opinion that this item should be considered as a late item. The reason for urgency is that Members need to consider the Budget update and the Prudential Indicators that draw on information in the Budget and not all information was available at the time the Board papers were published.**

## 1 Summary


1.1 This paper sets out the proposed TfL borrowing limits and other Prudential Indicators under the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code (the Code), which are consistent with the Treasury Management Strategy for 2022/23 and the principles underpinning the long-term TfL Capital Strategy. These limits and indicators are based on figures in the TfL's Budget that is submitted for approval by the Board elsewhere on the agenda.

1.2 Under the Prudential Code, TfL is required to adopt Prudential Indicators which support decision making on planned capital expenditure, borrowing and treasury management activities. The proposed Prudential Indicators for 2022/23 and the following two years are attached to this paper as Appendix 1. In line with guidance from CIPFA, Treasury Management Indicators are shown separately in Appendix 2.

1.3 Under Capital Finance regulations, local authorities are also required each year to set aside some of their revenues as provision for debt. TfL has a statutory duty to make an annual statement as to its policy for the calculation of this provision. This paper, therefore, sets out and asks the Board to approve the TfL Policy Statement on Minimum Revenue Provision, as set out in section 7.

1.4 Capital structure options are being explored in relation to TfL's commercial development subsidiary, including the potential to raise commercial funding for future investment in housing. The borrowing limits set out in this paper make an allowance for potential future debt arising from this activity.

1.5 TfL operates a structure of parent company guarantees across most companies within the Group, with the guarantees being registered at Companies House. This has the benefit of allowing the accounts of guaranteed companies an exemption from audit. However, to allow for the proposed capital structuring outlined in 1.4 above to be undertaken, and for any debt drawn down within subsidiary companies to be non-recourse to TfL, it is proposed that, for the financial year 2022/23, the

guarantees of TTL Properties Limited and, possibly, its subsidiaries which enter into development-specific joint ventures should not have their guarantees from Transport Trading Limited renewed.

1.6 TfL’s Extraordinary Funding and Financing Agreement with the Department for Transport (DfT), dated 25 February 2022, extends only until 24 June 2022. TfL’s Budget has therefore been prepared using assumptions in respect of levels of future government support that may not, in the event, prove accurate. Any future financing agreement from the DfT could, in addition, contain conditions attached to further funding which may impact more widely on TfL’s operations and capital investment activities.

1.7 In the event that a new funding agreement is put in place during 2022/23 that materially impacts on the assumptions underlying TfL’s approved Budget, a revised Budget will be required. Amendments to the prudential indicators will be submitted for approval accordingly.

## 2 Recommendations

2.1 **The Board is asked to note the paper and approve:**

**(a) the TfL Prudential Indicators as set out in Appendix 1;**

**(b) the Treasury Management Indicators as set out in Appendix 2 for 2022/23 and the following two years; and**

**(c) the Annual TfL Policy Statement on Minimum Revenue Provision set out in section 7 of the paper.**

## 3 Background on the Prudential Code

3.1 The Code plays a key role in capital finance in local authorities. It was developed as a professional code of practice to support local authorities in their decision-making processes for capital expenditure and its financing.

3.2 Local authorities are required by regulation to have regard to the Code when carrying out their duties under Part 1 of the Local Government Act 2003 (the Act).

3.3 The framework of Prudential Indicators established by the Code aims to ensure that an authority’s capital investment plans are affordable, prudent and sustainable. As part of the strategic planning process, authorities are required, on a rolling basis, to calculate a range of indicators for the forthcoming budget year and two subsequent years. Authorities are also required to monitor performance against indicators within the year as well as preparing indicators based on the Statement of Accounts at each year end. Indicators relate to capital expenditure, external debt and treasury management.

3.4 As required by the Code, TfL prepares Prudential Indicators at both the Corporation and TfL Group level.

3.5 A revised Code was published in December 2021, setting out changes to the requirements for the capital strategy, prudential indicators and investment reporting, as well as a requirement that an authority must not borrow to invest primarily for financial return. Application of the revised reporting requirements has been deferred, as permitted by the revised Code until 2023/24. However, the general ongoing principles of the revised Code have been applied with immediate effect.

3.6 TfL's Budget submitted for approval by the TfL Board elsewhere on the agenda has been used to calculate the proposed indicators (see Appendix 1).

3.7 The Capital Expenditure and External Debt Indicators relevant to TfL are the:

(a) Authorised Limit;

(b) Operational Boundary;

(c) Capital Financing Requirement;

(d) Capital Expenditure; and

(e) Ratio of Financing costs to Net Revenue Stream.

Definitions for each of these are included in Appendix 3.

## 4 Treatment of PFI Liabilities in the Calculation of External Debt Limits for 2021/22

4.1 In setting the direct borrowings element of the authorised limit for 2021/22 an allowance was made for the Corporation to refinance certain PFI transactions held as long-term liabilities in subsidiary entities as and when it becomes commercially advantageous to do so. The long-term liabilities element of the authorised limit for the Group was adjusted down by the same amount to ensure that there was no overall increase in the total authorised limit for the Group.

4.2 The Budget for 2021/22 assumed that only the portion of PFI liabilities outstanding at the start of any particular year that was scheduled to be repaid within that year would be refinanced; and the Operational Boundary was calculated to reflect this.

4.3 For the Group indicator, so long as total debt remains within the overall authorised limit, movement may be made between direct borrowings and other long-term liabilities without penalty. These debt reclassifications are accordingly not considered to be a matter for concern as they have no net effect on the overall total limit for external debt.

4.4 No new PFI liabilities have been recognised for a number of years, and the remaining liability balances in relation to PFI contracts have significantly reduced as contractual payments have been made. Accordingly, this refinancing allowance is no longer considered necessary and has not been made in the proposed indicators for 2022/23 or later years.

## 5 Changes to Prudential Indicators for 2022/23 to 2023/24

5.1 **Changes to Borrowing Limits for Future Years**

Prudential Indicators for the years 2021/22 to 2023/24 were approved by the Board in March 2021. For 2022/23 and 2023/24 changes are proposed as set out in the paragraphs below:

(a) the Operational Boundary for long-term liabilities (and the total Authorised Limit for External Debt) in both the Corporation and Group have been amended to reflect the revised settlement profile for long term capital provisions;

(b) the phasing of the Crossrail funding package agreed with the Department for Transport in December 2018 has been updated. Within this package, TfL made drawdowns under a £750m loan facility provided by the DfT. TfL's debt limits have been amended to reflect the latest assumptions in respect of the repayment profile of this facility;

(c) in the Group, the reduction to the authorised limit for long-term liabilities for the possible refinancing of PFI liabilities has been removed as this is no longer considered necessary;

(d) the allowance within the Authorised Limit to avail of favourable market conditions in relation to the refinancing of existing tranches of debt has been uplifted for future years to provide adequate coverage in the years where we have greater debt maturities occurring;

(e) certain contracts TfL enters into in the ordinary course of business may result in the recognition of lease liabilities where prior to IFRS 16 these contracts were not so classified. Classification is highly technical and dependent on the specifics of each contract which may not be known in advance of that contract being entered into. An increase in the Authorised Limit has been deemed necessary, to provide headroom against the risk that items included in the Budget may have been incorrectly classified;

(f) the Operational Boundary and Authorised Limits have been increased to reflect a planned revolving credit facility of £200m limit in 2022/23 ringfenced to finance investment by TTL Properties Limited as set out in 1.4. The Group Operating Boundary includes budgeted drawdowns under this facility, while the Authorised Limit includes the undrawn balances; and

(g) TfL is currently reviewing options to refinance some of its asset and assets under construction. The accounting solution for some of these options might potentially result in a liability on the balance sheet, which has been included as headroom in the Authorised Limit.

**Reconciliation of Changes in External Debt Limits for the Corporation for 2022/23 to 2024/25**

| | Paragraph reference | 2021/22 (no change from previously approved limits) | 2022/23 | 2023/24 | 2024/25 |
|---|---|---|---|---|---|
| | | £m | £m | £m | £m |
| **Corporation:** | | | | | |
| **Previous Operational Boundary for Gross External Debt** | | **13,733.3** | **13,656.4** | **13,576.0** | n/a |
| Re-phasing of provisions and liabilities | 5.1 (a) | - | (52.1) | (49.5) | n/a |
| Department for Transport Crossrail loan facility[4] | 5.1(b) | - | - | 35.0 | n/a |
| **Proposed Operational Boundary for Gross External Debt** | | **13,733.3** | **13,604.3** | **13,561.5** | **13,485.2** |
| Overdraft facility [1] | | 200.0 | 200.0 | 200.0 | 200.0 |
| Refinancing of PFIs [2] | 5.1 (c) | 132.3 | - | - | - |
| Refinancing of short-term borrowings [3] | 5.1 (d) | 1,000.0 | 500.0 | 500.0 | 500.0 |
| Leases [5] | 5.1 (e) | 250.0 | 250.0 | 250.0 | 250.0 |
| **Proposed Authorised Limit** | | **15,315.6** | **14,554.3** | **14,511.5** | **14,435.2** |

**Reconciliation of Changes in External Debt Limits for the Group for 2022/23 to 2024/25**

| | **Paragraph reference** | **2021/22 (no change from previously approved limits)** | **2022/23** | **2023/24** | **2024/25** |
|---|---|---|---|---|---|
| | | **£m** | **£m** | **£m** | **£m** |
| **Group** | | | | | |
| **Previous Operational Boundary for Gross External Debt** | | **15,923.5** | **15,798.5** | **15,669.8** | **n/a** |
| Re-phasing of provisions and liabilities | 5.1 (a) | - | (54.3) | (82.8) | n/a |
| Re-phasing of Department for Transport loan facility [4] | 5.1 (b) | - | - | 35.0 | n/a |
| TTL Properties RCF facility | 5.1 (f) | - | - | 21.5 | n/a |
| **Proposed Operational Boundary for Gross External Debt** | | **15,923.5** | **15,744.2** | **15,643.5** | **15,586.7** |
| Overdraft facility [1] | | 200.0 | 200.0 | 200.0 | 200.0 |
| Refinancing of PFIs [2] | 5.1 (c) | 27.0 | - | - | - |
| Refinancing of short term borrowings [3] | 5.1 (d) | 1,000.0 | 500.0 | 500.0 | 500.0 |
| Leases | 5.1 (e) | 500.0 | 500.0 | 500.0 | 500.0 |
| Commercial property undrawn RCF facility [5] | 5.1 (f) | - | 200.0 | 178.5 | 83.7 |
| Asset refinancing provision | 5.1 (g) | - | 600.0 | 600.0 | 600.0 |
| **Proposed Authorised Limit** | | **17,650.5** | **17,744.2** | **17,622.0** | **17,470.4** |

**Notes**

1 An overdraft facility is in place to mitigate short term adverse cash flow variances and this is included in the authorised limit.

2 In setting the Prudential indicators in March 2012, the Board approved an increase in the authorised limit to allow for the refinancing of certain PFI contracts (as permitted in annex C of TfL's SR2013 settlement letter) as and when commercial opportunities arise and value for money can be demonstrated.

3 In setting the Prudential indicators in March 2012, the Board also approved an increase in the authorised limit to provide flexibility in refinancing of borrowings, to ensure that the most advantageous rates can be secured.

4 Facility made available as part of the funding package to deliver Crossrail agreed with the Department of Transport in December 2018, draw down is subject to conditions precedent.

5 The Authorised Limit has been uplifted to capture the planned revolving credit facility for investment by TTL Properties Limited.

5.2 **Changes to Other Prudential Indicators for Future Years**

Further amendments to reflect TfL's Budget have been applied to the other Prudential Indicators for 2022/23 and 2023/24 for the Corporation and Group. Indicators have been set for the first time for 2024/25. The tables in Appendix 1 set out the revised indicators.

## 6 Treasury Management Indicators

6.1 In addition to the Prudential Indicators, there are a number of treasury indicators that outlined in CIPFA's Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (the TM Code), published in December 2017. Local authorities are required to have regard to these Treasury Management Indicators.

6.2 The TM Code recommends that local authorities should adopt the following Treasury Management Indicators:

(a) upper and lower limits on the maturity structure of borrowing, including variable as well as fixed rate debt; and

(b) the period for upper limits to the total of principal sums invested longer than one year.

6.3 While there is not a specific recommended indicator in respect of interest rate exposures, the TM Code suggests that authorities should explain the strategy for managing their interest rate risk as part of the investment and/or capital strategies. We cover our targets for fixed and floating rate debt, as well as general approach to interest rate risk, in our Treasury Management Strategy.

6.4 The proposed Treasury Management Indicators are detailed in Appendix 2.

6.5 A revised TM Code was published on 20 December 2021 requiring the adoption, from 2023/24 of a broader range of Treasury Management Indicators, including a new debt liability benchmark indicator to support the risk management of the capital financing requirement. These new requirements have not been reflected in the indicators presented here for the 2022/23 financial year.

## 7 TfL Policy Statement on Minimum Revenue Provision

7.1 Local authorities are required each year to set aside some of their revenues as provision for debt. TfL has a statutory duty to determine for the current financial year an amount of minimum revenue provision which it considers to be 'prudent' in relation to debt service obligations.

7.2 While statutory guidance suggests four potential methods for calculating Minimum Revenue Provision (MRP) it also allows for other methods and approaches to be used. Since 2016/17 TfL has applied the principles inherent in the statutory guidance on MRP, to make an annual provision in the Transport for London (the Corporation), that aims to build up a reserve on the Balance Sheet over the average useful economic life of the assets funded by borrowings in the Corporation, such that, at the end of that useful economic life, that reserve may be employed to either repay borrowings or to finance replacement capex for those assets that have reached the end of their lives. An MRP is effectively already made for borrowings passed down to the subsidiaries through TfL's existing processes for funding those entities.

7.3 Given current levels of debt (including finance leases) retained within the Corporation the MRP is anticipated to be approximately £56m per annum throughout the business plan period and will result in an annual transfer of this amount from usable reserves (i.e. the General Fund) to unusable reserves (namely the Capital Adjustment Account).

**List of appendices to this report:**

Appendix 1: For Approval: TfL Prudential Indicators for 2022/23 to 2024/25
Appendix 2: Treasury Management Indicators
Appendix 3: Definitions for Prudential Indicators

**List of Background Papers:**

Treasury Management Strategy for 2022/23
Draft Budget
Draft long-term TfL Capital Strategy.

Contact: Patrick Doig, Group Finance Director
Email: patrick.doig@tfl.gov.uk

# Appendix 1

**FOR APPROVAL: PRUDENTIAL INDICATORS FOR 2021/22 TO 2024/25**
**TRANSPORT for LONDON**

| | Paragraph reference | Approved Indicators 2021 - 22 £millions | Proposed Revised Indicator 2022 - 23 £millions | Proposed Indicator 2023 - 24 £millions | Proposed Indicator 2024 - 25 £millions |
|---|---|---|---|---|---|
| **Operational Boundary for External Debt*** | | | | | |
| **TfL Corporation** | | | | | |
| Borrowing | | 13,162.5 | 13,069.0 | 13,068.7 | 13,033.5 |
| PFI and long-term liabilities | | 570.8 | 535.3 | 492.8 | 451.7 |
| **Total Operational Boundary for External Debt in TfL Corporation** | 5.1 | **13,733.3** | **13,604.3** | **13,561.5** | **13,485.2** |
| **TfL Group** | | | | | |
| Borrowing | | 13,162.5 | 13,069.0 | 13,089.9 | 13,149.3 |
| PFI and long-term liabilities | | 2,761.0 | 2,675.2 | 2,553.6 | 2,437.4 |
| **Total Operational Boundary for External Debt TfL Group** | 5.1 | **15,923.5** | **15,744.2** | **15,643.5** | **15,586.7** |
| **Authorised Limit for External Debt**** | | | | | |
| **TfL Corporation** | | | | | |
| Borrowing | | 14,494.8 | 13,769.0 | 13,768.7 | 13,733.5 |
| PFI and long-term liabilities | | 820.8 | 785.3 | 742.8 | 701.7 |
| **Total Authorised Limit in for External Debt in TfL Corporation** | 5.1 | **15,315.6** | **14,554.3** | **14,511.5** | **14,435.2** |
| **TfL Group** | | | | | |
| Borrowing | | 14,494.8 | 14,568.8 | 14,568.4 | 14,533.0 |
| PFI and long-term liabilities | 5.1 | 3,155.7 | 3,175.4 | 3,053.6 | 2,937.4 |
| **Total Authorised Limit for External Debt in TfL Group** | | **17,650.5** | **17,744.2** | **17,622.0** | **17,470.4** |
| **Estimates of Capital Expenditure (Annual)** | | | | | |
| **TfL Corporation** | 5.2 | **2,671.2** | **1,571.6** | **1,131.1** | **1,671.2** |
| **TfL Group** | 5.2 | **3,634.9** | **2,445.1** | **2,641.8** | **2,508.9** |
| **Estimates of Capital Financing Requirement (Cumulative)***** | | | | | |
| **TfL Corporation** | 5.2 | **14,740.5** | **14,046.0** | **13,986.2** | **13,928.4** |
| **Total TfL Group** | 5.2 | **18,941.3** | **17,773.6** | **17,406.9** | **16,969.9** |

* The Operational Boundary is a calculation based upon the cash flows in the TfL Budget. If breached, it is a warning that financial plans may require review and amendment.

** The Authorised Limit is the maximum amount that TfL may borrow legally.

*** The Capital Financing Requirement is the amount of capital expenditure to be financed by means other than grant or asset sales proceeds.

**Prudential Indicators for Prudence and Affordability**

| **Estimates of ratio of financing costs to net revenue stream** | **Paragraph reference** | **Approved Indicator 2021 - 22** | **Proposed Revised Indicator Budget 2022 - 23** | **Proposed Revised Indicator Budget 2023 - 24** | **Proposed Indicator Budget 2024 - 25** |
|---|---|---|---|---|---|
| **TfL Corporation** | 5.2 | **11.0%** | **15.4%** | **23.0%** | **26.3%** |
| **TfL Group** | 5.2 | **16.6%** | **17.1%** | **18.2%** | **18.7%** |

| **Gross Debt and the Capital Financing Requirement*** | **TfL Group* £millions** | **Corporation £millions** |
|---|---|---|
| Authorised Limit for total debt at 31 March 2023 | 17,744.2 | 14,554.3 |
| Less headroom for refinancing of short-term debt | (1,000) | (1,000) |
| Adjusted Gross Debt at 31 March 2023 | **16,744.2** | **13,554.3** |
| Capital Financing Requirement at 31 March 2025 | **16,969.9** | **13,928.4** |

* The Prudential Code stipulates that Gross Debt at 31 March 2023 should not generally exceed the Capital Financing Requirement at 31 March 2025 Headroom included in the calculation of the Authorised Limit for External Debt has been stripped out for the purposes of this comparison, as this represents a uplift of debt limits solely to allow flexibility in the timings of drawdown of debt such that TfL is able to obtain the most favourable rates on its borrowings. It does not represent debt that could be used to fund the capital activities of the Group.

# Appendix 2

**For Approval: Treasury Management Indicators**

| **Maturity Structure of Borrowing** | **Budget 31 Mar 2022** | |
|---|---|---|
| | Upper | Lower |
| < 1year | 35% | 0% |
| 1 year to < 2 years | 35% | 0% |
| 2 years to <5 years | 50% | 0% |
| 5 years to <10 years | 75% | 0% |
| 10 years and above | 100% | 20% |

This indicator represents limits of the percentage of borrowing maturing in the future periods above as a total of fixed rate borrowing outstanding.

Actual amounts will depend on the projects financed and which ones have been converted into long-term obligations

| **Maximum Outstanding Principal sum Invested for more than 365 days** | **Budget**<br><br>**31 Mar 2023**<br>£millions | **Budget**<br><br>**31 Mar 2024**<br>£millions | **Budget**<br><br>**31 Mar 2025**<br>£millions |
|---|---|---|---|
| **Forward Financial Year 1** | **0** | **0** | **0** |
| **Forward Financial Year 2** | **0** | **0** | **0** |

## Appendix 3

**Definitions for Prudential Indicators used by TfL**

1. **External Debt - Operational Boundary**
   The Operational Boundary is a sum of external borrowings and long-term capital liabilities, including finance lease creditors and provisions, as shown in the Budget and Plan. If breached, it is a warning that financial plans may require review and amendment.

2. **External Debt - Authorised Limit**
   The authorised limit is the maximum amount that TfL may borrow legally.
   It is comprised of the Operational Boundary plus an element of headroom to allow for unexpected cashflow fluctuations.

3. **Capital Expenditure**
   For the Group this is the total of fixed asset additions for the given period.
   For the Corporation this is the Corporation's own fixed asset additions plus any loans or capital grants passed to the subsidiaries for the given period.

4. **Capital Financing Requirement**
   The Capital Financing Requirement (CFR) is the amount of capital expenditure to be financed by means other than grant or asset sales proceeds. It is calculated from the balance sheet of the Group and Corporation by deducting deferred grant, and capital reserve balances from the total fixed asset balance.

   There is a requirement in the Code to ensure that the estimate for the CFR at the end of 2025 is not exceeded by gross debt budgeted at the end of 2023. This requirement seeks to ensure that over the medium term, debt will only be for a capital purpose.

5. **Ratio of financing costs to net revenue streams**
   Indicator expresses the interest costs, net of interest income as a percentage of TfL's Revenue Grant and fares income plus or minus transfers to reserves.