

Date: 22 June 2022

Item: Funding Update on TTL Properties Limited

This paper will be considered in public

1 Summary

- 1.1 This paper updates the Committee on the assurance work undertaken since its meeting on 9 March 2022. This assurance work provides comfort that TTL Properties Limited (TTLP) can operate as a financially independent company within Transport for London (TfL) and secure the approvals necessary to enable TTLP to enter a committed, three-year, non-recourse revolving credit facility (RCF) for up to £200m.
- 1.2 As has previously been described to the Committee and agreed with HM Government, non-recourse debt is being proposed at the subsidiary TTLP level on the basis that TfL cannot afford to service any incremental borrowing from its core transport activities.
- 1.3 As a non-recourse facility TfL will have no obligation to support TTLP and the lenders will have no claim on TfL. TfL needs to be aware that the implication of this is that in extremis TfL would need to be prepared to let TTLP fail. This could mean the loss to the TfL Group of some or all of the assets vested in TTLP.
- 1.4 Affordability analysis has demonstrated that TTLP can operate without financial support from TfL. TTLP is a viable and sustainable business with mitigating options that will ensure it will not fail even under multiple stress scenarios.
- 1.5 In order to facilitate the non-recourse nature of the funding, a number of existing guarantees will need to be removed or not renewed.
- 1.6 The paper also seeks approval for a bespoke TTLP Treasury Management Strategy and Policy, which is a matter reserved to the Committee. The proposed policy sets out how TfL will continue to manage the funding, liquidity and cash arrangements for TTLP, as it does now, albeit with cash managed on a segregated basis and within revised authority limits and tighter liquidity requirements (a draft version was previously presented to the Committee at its meeting on 9 March 2022).
- 1.7 The paper also seeks approval for the proposed dividend policy: that 100 per cent of all operating profit will be returned to TfL as a dividend. Funds from any capital disposal and Joint Venture dividends will be recycled into the TTLP business.

- 1.8 Finally, the paper provides an update on governance, insofar as this relates to the debt funding. A fuller update will be given to the Land and Property Committee at its first meeting on 30 June 2022.
- 1.9 A paper is included on Part 2 of the agenda which contains supplemental information that is exempt from publication by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972, in that it contains information relating to the financial and business affairs of TfL. Any discussion of that exempt information must take place after the press and public have been excluded from this meeting.

2 Recommendations

2.1 The Chair, following consultation with the Committee, is asked to note the paper and the exempt supplementary paper on Part 2 of the agenda and:

- (a) approve the Treasury Management Strategy and Policy for TTLP, as attached in Appendix 1;**
- (b) endorse TTLP entering into the non-recourse revolving credit facility for up to £200m, as described in this paper, approval to be sought from the TfL Chief Finance Officer in accordance with the Treasury Management Strategy and Policy for TTLP (subject to its approval);**
- (c) approve the non-renewal and/or phasing out of the existing TfL and Transport Trading Limited guarantees in favour of TTLP and its subsidiaries over the next year, as described in this paper;**
- (d) approve the issuance of new guarantees, for the current financial year and subsequent years, and approve Land Authority for the provision by TTLP in respect of any of its subsidiaries (whether presently existing or to be formed) of:**
 - (i) letters of financial comfort to the relevant subsidiary's directors setting out that, while they remain a subsidiary, they will be put in funds to pay their debts as they fall due; and**
 - (ii) guarantees under section 479C of the Companies Act 2006; and**
- (e) approve the dividend policy for TTLP described in this paper.**

3 Background

- 3.1 On 9 March 2022, an update was provided to the Committee on how TTLP would achieve its target of building 20,000 homes and a growing net operating profit that is returned to TfL in the form of a dividend.
- 3.2 Since that meeting, further work has been undertaken on assurance of the TTLP Business Plan and the actions needed for TTLP to operate financially independently from TfL. In parallel, negotiations have progressed with funders.

- 3.3 The Land and Property Committee has now been established to oversee the effective operation of TfL's land and property activities, delivered through TTLP. The Land and Property Committee will meet for the first time on 30 June 2022.
- 3.4 The Land and Property Committee will approve annually the TTLP Business Plan and key performance indicators and Authorities in relation to opportunities for TTLP and its subsidiaries. All matters relating to the financing of TTLP remain within the remit of the Finance Committee and the Schemes of Authorities and Delegation within Standing Orders remain unchanged.
- 3.5 From 1 April 2022, TTLP began operating on the basis that no further funding would be provided by TfL and that TTLP would operate purely from its own financial resources. TTLP was separated from the TfL cash pooling arrangements and now runs independent banking arrangements.
- 3.6 It should be noted however that the Committee previously approved the establishment of an intercompany RCF of £25m from TfL to TTLP in its meeting on 25 November 2020. It is intended to implement this as a stand-by facility for working capital to facilitate the flow of monthly trading balances and/or short term credit between the two entities.

4 Affordability Analysis and Stress Testing

- 4.1 The TTLP Business Plan has been tested by TfL Corporate Finance for a number of specific and combined downside stress scenarios which include economic downturn, delayed market sales, extended inflation and interest rate rises, cost increases, delayed build, and lower income.
- 4.2 These scenarios have been set against both mitigating actions that could be reasonably deployed in any stressed scenario and the loan covenants that have now been negotiated into the draft term sheet (loan to value, net tangible worth and interest cover). The testing horizon was over five years.
- 4.3 The analysis concludes that in all stressed scenarios the loan covenants were either not breached or capable of being fully mitigated and there was no call on TfL for further funding
- 4.4 The work also identified recommendations for controls and processes that will be taken forward in order to support ongoing affordability and debt management.
- 4.5 The Affordability Report produced by TfL Corporate Finance has been included in the related paper on Part 2 of the agenda.

5 CIPFA Prudential Code

- 5.1 Further assurance has been sought on the ability of TTLP to borrow, given recent changes to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code, which TfL is legally obliged to have due regard to.
- 5.2 The Prudential Code (updated in December 2021) now states that Local Authorities "must not borrow to invest primarily for financial return". Finance Committee had previously asked we confirm compliance to the code.

- 5.3 We believe that TTLP is not borrowing purely for financial return for reasons that include: i) it is investing in affordable housing delivery; ii) its delivery is in line with the Mayor's Transport Strategy; iii) development of TfL's estate is specifically permitted under legislation – the GLA Act 1999 states that "Transport for London may develop its land in such a manner as it thinks fit."
- 5.4 This assessment has been tested with counsel who confirmed it is reliable.

6 Non-recourse Implications for Guarantees

- 6.1 The non-recourse nature of the proposed RCF has implications for the current TfL parent company guarantee structure and for the directors of TTLP, in that if the debt is truly non-recourse then all guaranteed support from TfL should be released.
- 6.2 Currently, as with other subsidiaries, TfL provides a letter to TTLP's directors providing comfort that the company will be funded to pay its debts as they fall due.
- 6.3 TTL also provides a parent company guarantee to TTLP under s479C of the Companies Act 2006, registered at Companies House, whose purpose is primarily to avoid the need for TTLP's accounts to be audited. These arrangements are replicated for TTLP's subsidiaries.
- 6.4 It is proposed that this parent support for TTLP and its subsidiaries is removed. In the case of TTLP's subsidiaries, that support will be replaced by a guarantee in substantially the same terms by TTLP.
- 6.5 In preparation, TTLP is already producing audited accounts for 2021/22.
- 6.6 Separately, there are a number of guarantees from TTL to joint venture partners in respect of ongoing development projects. These guarantee the equity investment in the project. For several projects, the contractually committed equity investment has already been made so those guarantees will not be called upon. Of the remaining projects, some may be subject to contractual variations so opportunities may exist to substitute in TTLP as guarantor. On the rest, there are still contributions to be made so the guarantees still apply, and we are intending to leave these guarantees in place and allow them to fall away over time. For any new projects, TTLP will be offered as guarantor so there will be no further call on TfL.

7 Non-recourse Implications for Directors

- 7.1 In the absence of recourse to TfL and in addition to the affordability analysis described above, TTLP's directors will need to be satisfied on an ongoing basis that the company remains solvent.
- 7.2 TTLP's directors have been engaged and assurance will be provided to them through quarterly briefings and regular updates of the following documents:
- (a) business performance;
 - (b) cash flow and liquidity forecast and headroom;
 - (c) affordability, stress testing and mitigation updates;

- (d) strategic risk register;
- (e) future reporting;
- (f) assurance matters – audits, directors’ disclosures and controls;
- (g) TTLP Business Plan; and
- (h) financial accounts.

7.3 Based on the affordability and stress testing scenarios, we are confident in the financial viability of TTLP. A plan to mature the business processes, controls and assurance is in place and has been agreed by senior TfL Finance teams.

8 Treasury Management Strategy and Policy

8.1 As a result of the change in funding arrangements and TTLP’s financial independence, a new Treasury Management Strategy and Policy have been drafted for TTLP. These were presented to the Committee on 9 March 2022, in draft, where the Committee was requested to note the documents.

8.2 They set out how TfL will continue to manage the funding, liquidity and cash arrangements for TTLP. Cash will be managed on a segregated basis within policy limits, required changes to authority limits and the need for tighter liquidity requirements.

8.3 The Liquidity Policy will require that there is sufficient undrawn borrowing commitment and cash in bank to meet financial commitments over the next 18 months and that a cash reserve of £10m is maintained.

8.4 These documents are attached as Appendix 1 and approval is now sought [there have been no changes to the documents presented to the Committee on 9 March 2022].

9 The Revolving Credit Facility

9.1 Discussions have progressed with selected lenders in relation to the £200m non-recourse RCF. The proposed terms have been considered with each lender on a bilateral basis and a coordinator was selected from the lender group to progress negotiations with TTLP.

9.2 A detailed term sheet has now been agreed and prospective lenders are currently seeking credit approval. Alongside this, work is progressing with the coordinator to agree a draft of the full facility agreement. Supplementary information on the RCF is included in the related paper on Part 2 of the agenda.

9.3 An update on progress will be provided at the Committee. Subject to the Committee’s approval, it is expected to have the facility in place by the end of June 2022.

10 Dividend Policy

10.1 The dividend policy forms an integral part of TTLP’s overall corporate strategy by supporting TTLP’s objectives of growing net operating profit that is returned to TfL whilst also building 20,000 new homes. To support these aims, it is proposed that the dividend is equal to profit after tax attributable to recurring

income. Profit after tax attributable to non-recurring income, such as dividends from 'for sale' joint ventures and profits on disposal proceeds, will be recycled into the TTLP Business Plan to support further investment.

- 10.2 It is proposed that dividends will be declared and paid out annually, post confirmation of the year-end position as a single 12-month trailing dividend payment.

11 Governance and Assurance

- 11.1 Established by the Board on 23 March, the Land and Property Committee will set the strategic direction of TTLP and will oversee and provide assurance on behalf of the Board of delivery against TTLP's Business Plan. The Land and Property Committee is expected to meet at least four times a year and the first meeting will be held on 30 June 2022.
- 11.2 As set out in the Terms of Reference for the Land and Property Committee, consideration and approval of matters relating to the financing of TTLP (including the RCF referred to in this paper) will remain within the remit of the Finance Committee.
- 11.3 With TTLP operating as a financially separate entity, the role of TTLP as a corporate entity becomes more important. The appointment of TTLP directors is a matter for TfL as the shareholder. The current TTLP directors comprise the Chief Customer and Strategy Officer (Chair), the Director Commercial Development and the Property Development Director. Additional directors will be appointed once the new TTLP Executive structure is finalised.
- 11.4 The TTLP directors will receive periodic performance updates and a formal briefing will be provided at a TTLP company meeting on a quarterly basis. The decisions that TTLP will ordinarily be expected to make as a company include:
- (a) endorsement of the TTLP Business Plan and Investment Strategy before submission to the Land and Property Committee;
 - (b) approval of letters of comfort to directors of TTLP's subsidiaries;
 - (c) approval of accounts and auditor letter of representation annually; and
 - (d) approval of a guarantee of its subsidiaries under s479C of the Companies Act 2006.
- 11.5 On assurance, it is proposed to put in place a formal three lines of defence assurance model. TTLP will have its own Integrated Assurance Plan and Enterprise Risk Framework, both modelled on TfL's current arrangements. This will include a TTLP Independent Investment Programme Advisory Group (IIPAG) sub-group, with a chair and two members to cover TTLP's functions. The new roles will operate to a plan set by the Audit and Assurance Committee and the Land and Property Committee. The assurance will be reported to TTLP management and to both the Audit and Assurance and Land and Property Committees.
- 11.6 Working arrangements are being put in place to articulate the interface between TfL and TTLP. This considers similar models currently in use, including for the London Transport Museum, and will set out the principles for engagement.

11.7 With the new governance arrangements in place, it is not considered necessary to continue with the Commercial Development Advisory Group (CDAG) and it is therefore proposed to close that Group. TfL and TTLP remain grateful for the significant contribution that CDAG members have made in helping TfL develop its property portfolio and setting up TTLP as a commercial property company.

12 Conclusion

- 12.1 A financially independent commercial property vehicle in TfL was envisaged in 2019 when the Committee agreed to the consolidation of TfL's property assets to create a new balance sheet that could be used to attract new streams of funding and create focus for improved management and financial returns.
- 12.2 As a direct result, TfL was able to respond quickly to the financial challenges brought about by the coronavirus pandemic and accelerate plans to attract new funding streams.
- 12.3 With commercial funding in place, TTLP will be able to build dozens of medium-density, high-amenity, high-accessibility, low-carbon developments across the capital. TTLP will be delivering tens of thousands of new homes and millions of square feet of new sustainable commercial space where Londoners most want to live and work.
- 12.4 TTLP will also generate a growing dividend of tens of millions of pounds a year to TfL, and manage an asset base whose value will double to £4bn in a decade. TTLP will do so while taking no funding from TfL and assuming no direct grant funding from Government.

List of appendices to this report:

Appendix 1: TTLP Treasury Management Strategy and Policy

List of Background Papers:

None

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