Audit and Assurance Committee

Date: **5 June 2023**

Item: **TfL Statement of Accounts for the Year Ended 31 March 2023**

This paper will be considered in public

1 Summary

1.1 This paper presents the draft TfL Group Statement of Accounts, together with the Remuneration Report for the year ended 31 March 2023, to the Committee for consideration. The current drafts of the Statement of Accounts and Remuneration Report are attached to this paper and will be presented as a combined Annual Report and Statement of Accounts to the Board for approval on 26 July 2023.

2 Recommendations

2.1 The members of the Committee are asked to:

(a) note the draft Statement of Accounts and the Remuneration Report and the delegation to the Statutory Chief Finance Officer to make any adjustments arising from the ongoing audit work prior to submission to the Board. Any material adjustments arising will be reported to the next meeting of the Committee;

(b) recommend that the Board confirm its overall approval of the provision of an ongoing guarantee by Transport Trading Limited of all the outstanding liabilities of those of its subsidiary companies listed below, such guarantee enabling those subsidiaries to be exempt from the need to have their accounts audited.

(i) Woolwich Arsenal Rail Enterprises Limited;
(ii) City Airport Rail Enterprises Limited;
(iii) London Underground Limited;
(iv) LUL Nominee BCV Limited;
(v) LUL Nominee SSL Limited;
(vi) Docklands Light Railway Limited;
(vii) Tube Lines Limited;
(viii) Rail for London Limited;
(ix) Rail for London (Infrastructure) Limited
(x) Tramtrack Croydon Limited;
(xi) London Buses Limited;
(xii) London Bus Services Limited;
(xiii) London River Services Limited;
(xiv) Transport for London Finance Limited;
(xv) Victoria Coach Station Limited;

(c) note that:

(i) as a result of the application of IFRS 9 Financial Instruments, our auditors, Ernst & Young LLP, require that letters of financial support previously provided by Transport for London in respect of the liabilities of its subsidiaries be re-signed annually by TfL's Chief Finance Officer; and

(ii) Board approval for the issue of such letters was granted when the subsidiaries were first established or acquired [and the template for the letter to be signed is included in Appendix 2].

3 Background

3.1 The Statement of Accounts has been prepared in accordance with the provisions of the Local Audit and Accountability Act 2014 and the Accounts and Audit Regulations 2015 ("the Regulations"). The form, content and accounting policies followed in preparing the Statement of Accounts are as prescribed in the Regulations and by the Code of Practice on Local Authority Accounting which is developed and published by the CIPFA/LASAAC joint committee ("the Code"). The Code is based on International Financial Reporting Standards ("IFRS").

3.2 The Regulations require that the responsible financial officer, namely the Statutory Chief Finance Officer, sign and date the Statement of Accounts before the commencement of the period for the exercise of public rights and certify that it presents a true and fair view of the financial position of TfL at the end of the year to which it relates and of TfL's income and expenditure for that year.

3.3 The certified Statement of Accounts, which are at this stage unaudited, together with the Annual Governance Statement must be published on TfL's website, and an appropriate notice providing details of how public rights may be exercised is also required to be published. The period for exercise of public rights commences the next working day after all these conditions have been fulfilled and runs for a period of 30 working days.

3.4 After the conclusion of the 30 working day period, the Statutory Chief Finance Officer again certifies the Statement of Accounts, and following this re-certification the Statement of Accounts, with the addition of the Independent Auditor's Report, will be considered and approved by the Board.

3.5 The unaudited Statement of Accounts will be certified by the Statutory Chief Finance Officer and published on TfL's website together with the Annual Governance Statement. Appropriate notices have been placed on TfL's website. Following the conclusion of the period it is planned that the Board should consider the accounts at the Board meeting on 26 July 2023.

3.6 The period for exercise of public rights includes rights of objection and questioning as well as inspection. Should any questions or objections be raised, these will be reported to the Committee at its next meeting.

4 Results for the Year

4.1 Our 2023 Business Plan set out our strategy for rebuilding our finances following the pandemic. The results for 2022/23 show we are successfully delivering that strategy.

4.2 *Actively grow passenger demand, whilst creating new sources of revenue to reduce our reliance on fares income*: Fares income has increased by 34 per cent during the year. Passenger journey numbers are now at 85 per cent of pre-pandemic levels.

4.3 *Continue to deliver recurring cost savings to remain affordable for customers and taxpayers:* The introduction of new services, including the Elizabeth line and the full-year impact of the expansion of the ULEZ in 2021, and high levels of inflation meant our gross expenditure increased by £658m. However, our continual delivery of savings meant that like-for-like costs of operations decreased by 4.4 per cent in real teams.

4.4 *Create and grow an operating surplus based on our own sources of income:* There are significant differences in the basis of preparation of the Group Comprehensive Income Statement compared with management reports (see section 11 below). The Income Statement shows a surplus in the provision of services after tax of £109m, down from a surplus of £504m in 2021/22.

4.5 However, our growing income and effective cost control meant a reduced provision of extraordinary grant funding from the Government. The level of extraordinary grant support reduced to £920m, down from £1,717m in 2021/22.

4.6 *Fully fund our capital programme with a long-term Government settlement and an affordable level of debt*: In August 2022 we agreed a long-term funding settlement with Government to March 2024. Whilst not the genuine long-term capital funding settlement we need, this has supported our capital programme during 2022/23.

4.7 Careful management of our debt has meant that the nominal value of debt has decreased to £12.910bn at 31 March 2023. A reduction of £56m from the prior year of £12.966bn. A bond buy back transaction was undertaken during the year, which reduce the level of debt and a repayment of £35m was made relating to the DfT Crossrail loan facility.

4.8 Right-of-use lease liabilities have decreased by £221m to £2,216m at 31 March 2023. This was driven by the £277m purchase of Class 378 rolling stock and termination of the related lease liabilities of £102m. The reason for the difference in values is the lease liabilities only represented the existing lease contract, which was not for the full life of the assets. Higher interest rates meant that purchasing the rolling stock will result in a significant cost saving to TfL over the life of the assets.

4.9 *Maintain cash reserves to make payments and protect against shocks:* Our liquidity policy requires that we aim to maintain cash reserves equivalent to at least 60 days' worth of forecast annual operating expenditure, on average £1.2bn for 2022/23. This enables TfL to deal with economic and other travel demand shocks. During the year our cash reserves remained on average around this level. This is also in line with the Government settlement, which requires that usable cash reserves are maintained at no more than £1.2bn on average.

4.10 As at 31 March 2023, the Group had usable reserves of £399m, down from £681m at 31 March 2022.

4.11 The General Fund balance of £269m represents sufficient cash-backed reserves held by the Group to cover risks that may arise. The Group has a target General Fund balance of £500m, which was increased from £150m at the start of the pandemic in March 2020. The primary reason for falling below the benchmark was a transaction in March 2023 to purchase leased Class 378 rolling stock for £277m. The saving in lease financing over the life of the asset will further support TfL as it rebuilds its usable reserves.

4.12 In the most recent Budget the General Fund is forecast to be £334m by the end of 2023/24 and after adjusting the December Business Plan, back to the target level of £500m in 2024/25.

4.13 The Capital Grants Unapplied Account of £102m represents capital grants received for Project Oval, Elephant & Castle and DLR rolling stock where costs have not yet been incurred.

5 Funding

5.1 TfL has a funding agreement until the end of March 2024, to support the running of our day-to-day operating costs and protecting our growing passenger income following the dramatic fall in our fares. The DfT contributed revenue grant funding totalling £920m to TfL in 2022/23 (2021/22 £1,717m) under a number of Extraordinary Funding and Financing Agreements. Without providing details of the quantum of future funding, DfT have acknowledgement that, over the longer term, TfL cannot be expected to cover the cost of major capital enhancements from its own operating incomes. It is on the basis of these assurances that the Statement of Accounts for 2022/23 continue to be prepared on a going concern basis. Preparation of going concern disclosures and the audit of those disclosures is still in progress.

5.2 The Auditor's Report for 2021/22 contained a paragraph on material uncertainty relating to the ability to operate current planned operational services within available sources of funding. Discussions regarding levels of future funding are ongoing with the Department for Transport and the impact on our accounts and disclosures of any developments between the date of this report and the date of final approval by the TfL Board of the Statement of Accounts in July will be kept under review.

6 Accounting Policies

6.1 There have been no changes to the Code for 2022/23 that have had an impact on the financial statements.

6.2 During the year CIPFA introduced a temporary solution for accounting for infrastructure assets, focusing on the reporting of the derecognition provisions where there is replacement expenditure and particularly for highways assets. TfL has chosen not to adopt this temporary solution, but instead conducted a detailed review of the fixed asset register resulting in material adjustments to gross cost and gross accumulated depreciation on assets with nil net book value. This is detailed further in Section 9.

7 Remuneration Disclosures

7.1 The requirements for producing the various elements of remuneration disclosure are unchanged from earlier years. To aid understanding, the required disclosures are made in an extended Remuneration Report, presented outside the financial statements. Audited sections have been clearly identified and are cross-referenced in the notes to the financial statements.

8 Disclosure of IAS 19 Pension Fund Surplus and IFRIC 14

8.1 The Group Balance Sheet includes the surplus on the Public Sector section of the TfL Pension Fund, TfL's share of the deficit on the Local Government Pension Scheme, the surplus on the Crossrail Shared Cost Section of the Railways Pension Scheme (RPS), and the liability in respect of unfunded pension obligations, all calculated in accordance with IAS 19 Employment Benefits.

8.2 The IAS 19 basis of valuation is different to that used by the Fund Actuary in the triennial valuations which determine the level of contributions that TfL is required to make to the TfL Pension Fund. The last such valuation was at 31 March 2021 and revealed a surplus of £179m for the Public Sector section. Employer's contributions for 2022/23 for the Public Sector section were 27.3 per cent of pensionable pay, with a 5 per cent contribution rate for members.

8.3 The net surplus on TfL's defined benefit pension schemes and unfunded liabilities, calculated in accordance with IAS 19, has increased from a net deficit of £3.1bn at 31 March 2022 to a net surplus of £1.5bn at 31 March 2023. The main reason for the net surplus are the change in the financial assumptions adopted. The rise in discount rate and decrease in expected inflation, resulting in a significant decrease on the liabilities over the accounting period.

8.4 The draft Statement of Accounts recognise the full surplus of the TfL Pension Fund and the Crossrail Shared Cost Section of the RPS on the Balance Sheet. However, IAS 19 limits the measurement of the defined benefit assets to the 'present value of economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan'. IFRIC 14 provides further interpretation on this point. TfL have shared a draft opinion and accounting paper with EY, which is now under review by their specialist pension team. More work may be required by our actuary, which may change the level of surplus recognised on the Balance Sheet. This has no impact on TfL's contributions to the fund or the fund valuation.

8.5 A difference exists between the funding valuation and the IAS 19 valuation due to the different rules applying to the two valuation bases, particularly the different discount rate. The discount rate for the IAS 19 valuation is required to be based on AA corporate bond yields, but the discount rate for the funding valuation is based on expected returns on the Scheme's assets. There are also differences in the other assumptions. The pension fund Trustees are required to adopt "prudent" assumptions whereas IAS 19 requires "best estimate".

8.6 The Code requires that IAS 19 does not impact on Council Tax rates. The income and expenditure account therefore includes an appropriation from or to the Pensions Reserve. The result of these entries is that the pension deficit is not charged to the General Fund, and is instead charged to a separate reserve, and only the actual contributions paid to the pension funds impact on the General Fund.

9 Infrastructure Assets and Prior Period Misstatements

9.1 As part of an industry wide focus on accounting for infrastructure assets, which was a risk identified by EY during the planning phase of their audit, TfL undertook an extensive review of the fixed asset register. This identified £4.4bn of fully depreciated pooled infrastructure assets (£nil net book value) that should have been derecognised in prior years in line with our accounting policy. This has been adjusted in gross cost and gross accumulated depreciation in the property, plant and equipment disclosure. There is no impact on the Balance Sheet or Income Statement.

9.2 Management also identified non-pooled lifts and escalator assets where renewals work had taken place but the replaced portion of the assets, with a net book value of £28.8m, had not been written off. This has been recognised in the current year on the grounds of materiality. Management are implementing enhanced controls in the 2023/24 financial year to ensure that where renewals works take place on this class of assets, there is a process involving asset management teams to determine the value of write off required.

10 Property Valuations

10.1 In 2019/20, the majority of TfL's investment properties were consolidated into a commercial property portfolio created as a vehicle to support delivery of homes under the Mayor's Transport Strategy and grow a sustainable income stream. In the last two financial years there have been further minor phases of other properties transferred.

10.2 For the TfL Group, there was a net fair value loss of £155m (2021/22 gain of £93m) in relation to our investment property portfolio (including those classified as "held for sale").

10.3 All valuations were undertaken by external professionally qualified valuers in accordance with the appropriate sections of the Red Book, RICS Valuation – Global Standards published by the Royal Institute of Chartered Surveyors and are compliant with International Valuation Standards.

11 Reconciliation between the Quarterly Performance Report and Group Comprehensive Income and Expenditure Statement

11.1 The net cost of operations as reported in the Quarterly Performance Report for 2020/21 was £416m. The surplus on provision of services after tax in the Group Comprehensive Income and Expenditure Statement was £504m. A difference of £877m. Some of the differences relate to items not included in the Quarterly Performance Report but which are required to be included in the Income and Expenditure Statement. Some differences relate to items not included in the Income and Expenditure Statement, but included in the Quarterly Performance Report. Other differences arise from differing treatment of items explained below and summarised in the table in 13.4.

11.2 Items not included in net cost of operations in the Quarterly Performance Report but included in the Income and Expenditure Statement comprise:

(a) depreciation, amortisation and impairment charges;

(b) defined benefit pension service costs;

(c) gains and losses on the disposal of fixed assets and investment property;

(d) valuation gains and losses on the revaluation of investment property;

(e) net interest on the defined benefit pension obligation;

(f) interest payable on lease and PFI liabilities;

(g) capitalised interest;

(h) share of gains or losses from associated undertakings and joint ventures;

(i) premium receivable on settlements; and

(j) taxation.

Items not included in the Income and Expenditure Statement but included in the net cost of operations in the Quarterly Performance Report comprise:

(k) cash payments under PFI and lease arrangements;

(l) pension payments charged to operating costs; and

(m) capital renewals.

11.3 The net cost of operations as reported in the Quarterly Performance Report for Items where the treatment is different comprise:

(n) grant income adjustments primarily related to grants received other than Business Rate Retention.

11.4 A reconciliation from the management reports Income Statement as included in the Quarterly Performance Report to the Comprehensive Income and Expenditure Statement as included in the financial statements is set out below.

	£m
Operating surplus as reported in the management reports Income Statement of the Quarterly Performance Report	**621**
Depreciation, amortisation and impairments	(1,533)
Difference between defined benefit pension service costs under IAS19 and pension payments charged to the operating account	(263)
Taxation	(1)
Net interest on the defined benefit pension obligation	(79)
Interest and contingent rentals payable on lease and PFI liabilities	(93)
Share of net loss from joint ventures and associates	(31)
Premium receivable on settlements	46
Gains and losses on the disposal of fixed assets, investment property and termination of right-of-use assets	(62)
Valuation losses on the revaluation of investment property	(155)
Capitalisation of interest	32
Cash payments under PFI and lease arrangements	392
Capital renewals	624
Different treatment of specific capital grants	602
Other	9
Surplus on provision of services after tax in the Accounts	**109**

12 Audit Opinion

12.1 Under the Local Audit and Accountability Act 2014, TfL's auditors, Ernst & Young LLP are required to opine on the following:

(a) whether the financial statements, in their opinion, give a true and fair view of the financial position of the Transport for London Corporation and Group as at 31 March 2023 and of its expenditure and income for the year then ended

(b) whether the financial statements have been prepared properly in accordance with the CIPFA/LASAAC Code of Practice on Local Authority Accounting the United Kingdom 2022/23; and

(c) whether they are satisfied that, in all significant respects, Transport for London has put in place proper arrangement to secure economy, efficiency and effectiveness in its use of resources for the year ended 31 March 2023 .

12.2 Ernst & Young's update in respect of audit progress in relation to the above is not covered by this paper but is addressed in the EY Report to those charged with governance included elsewhere in the Audit and Assurance Committee agenda.

13 Subsidiary Companies Audit Exemption

13.1 For the year ended 31 March 2014, the Group took advantage of changes under section 479A of the Companies Act 2006 that enable certain UK subsidiary companies to claim exemption from audit of their accounts.

13.2 The exemption is conditional on a parent undertaking giving a guarantee to its subsidiary in respect of all liabilities of that subsidiary outstanding at the balance sheet date, and on 5 June 2014, under authority delegated by the Board on 26 March 2014, the then Finance and Policy Committee agreed that, for the year ended 31 March 2014 and for future years until withdrawn, the holding company for TfL's trading subsidiaries, Transport Trading Limited, will offer the guarantee to a majority of its subsidiaries.

13.3 For the year ended 31 March 2023, the majority of TTL's subsidiaries, except for TTL Properties Limited, will again claim exemption from audit.

List of appendices to this report:

Appendix 1: Draft TfL Financial Statements
Appendix 2: Template for annual letter of support from TfL to its subsidiary companies
Appendix 3: Remuneration Report

List of Background Papers:

None

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