Finance Committee

Date: **11 October 2023**

Item: **Prudential Indicators – Outturn for the year ending 31 March 2023**

This paper will be considered in public

1 Summary

1.1 On 23 March 2022, the Board approved prudential indicators and debt limits for TfL for the 2022/23 financial year, as required and defined in the Chartered Institute of Public Finance and Accountancy Prudential Code (the Code). The limits and indicators were based on figures in TfL's Budget, as approved by the Board on 23 March 2022, adjusted for known significant changes in assumptions relating to revenue, cost and funding where relevant, and subject to assumptions on future government funding at the time these limits and indicators were approved.

1.2 The purpose of this paper is to report on TfL's performance against the indicators for the financial year 2022/23. In line with Code requirements, TfL's 2022/23 Statement of Accounts has been used to calculate the outturn which has been compared against the Board approved indicators.

2 Recommendation

2.1 **The Committee is asked to note the paper.**

3 Background

3.1 The Code plays a key role in capital finance for local authorities. The Code 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 The framework 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 outturn indicators based on the Statement of Accounts at each financial year end. Indicators relate to capital expenditure, external debt and treasury management.

3.3 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.

3.4 The Code states that when an authority prepares group accounts, in setting indicators, the authority must include all items where a residual interest remains with the authority. Thus, TfL prepares prudential indicators at both the TfL Corporation (Corporation) and TfL Group (Group) level. The Corporation is made up of our road network operations, Taxi and Private Hire licensing and compliance and the TfL corporate centre which, for legal and accounting purposes, constitutes TfL – a local authority. The Group comprises the Corporation and its subsidiaries, in which the remainder of our operations are carried out.

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 were deferred, as permitted by the revised Code until 2023/24. However, the general ongoing principles of the revised Prudential Code were applied with immediate effect.

3.6 There are no penalties applied to a local authority for breaching individual indicators, with the exception of the Authorised Limit for External Debt (the Authorised Limit). The other indicators, if breached, act as an early warning that financial plans may require review and amendment.

4 Outturn

Operational Boundary

4.1 The Operational Boundary is the sum of all the borrowings, and long-term capital liabilities, including finance lease creditors and provisions as shown in the TfL Budget and Business Plan.

Operational Boundary for External Debt (£m)	Approved	Outturn
TfL Corporation		
Borrowing	13,069.0	12,937.1
Long-term liabilities	535.3	506.7
Total Operational Boundary for External Debt	**13,604.3**	**13,443.8**
TfL Group		
Borrowing	13,069.0	12,937.1
Long-term liabilities	2,675.2	2,476.1
Total Operational Boundary for External Debt	**15,744.2**	**15,413.2**

4.2 The Operational Boundary for direct borrowing for the Group and Corporation was set at £13,069m, with the outturn coming £132m under this level. This was driven by the impact of repurchasing and refinancing some of our outstanding bonds and a decrease in our outstanding Commercial Paper balance.

4.3 The Operational Boundary for long-term liabilities at 31 March 2023 was set at £2,675m for the Group and £535m for the Corporation. The outturn for indirect borrowing was £26m below the boundary for the Corporation and £199m below for the Group.

4.4 The main driver of the variance for the Group was the purchase of Class 378 rolling stock, used on the London Overground, for £277m and termination of 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.

4.5 Other drivers of the variance predominately relate to a rephasing, and earlier settlement, of long-term capital provisions when compared with the expected profile at the time prudential indicators were set.

Authorised limit

4.6 The most important prudential indicator is the Authorised Limit, which sets the maximum legal limit for direct and indirect (e.g. long-term creditors, provisions) debt for the organisation. Both the Corporation and the Group were within their Authorised Limits for the year ended 31 March 2023.

4.7 The Authorised Limit is derived by adding an element of headroom to the Operational Boundary for External Debt (the Operational Boundary), to allow for unexpected cashflow fluctuations. This provides a mechanism to raise further debt in a limited number of circumstances, without breaching TfL's maximum legal debt limit, at any point during the financial year – albeit these are an unbudgeted set of circumstance.

Authorised Limit for External Debt (£m)	**Approved**	**Outturn**
TfL Corporation		
Borrowing	13,769.0	12,937.1
Long-term liabilities	785.3	506.7
Total Authorised Limit for External Debt	**14,554.3**	**13,443.8**
TfL Group		
Borrowing	14,568.8	12,937.1
Long-term liabilities	3,175.4	2,476.1
Total Authorised Limit for External Debt	**17,744.2**	**15,413.2**

4.8 The Authorised Limit for direct borrowings for the Group was set at £14,569m, which included £1,500m of headroom items as at 31 March 2023. They are to mitigate against financial shocks and allow for short-term refinancing activities. For the Group they include:

(a) an existing overdraft facility of £100m and a money market facility of £100m;

(b) an allowance of £500m to avail of favourable market conditions in relation to short-term refinancing activities;

(c) the Places for London revolving credit facility (RCF) of £200m; and

(d) an allowance of £600m for refinancing of assets and assets under construction, which may have resulted in additional liabilities on the balance sheet.

4.9 With the exception of the Places for London (formerly TTL Properties Limited) RCF, the headroom items in the Authorised Limit do not represent additional borrowings that TfL can utilise to support further planned investment.

4.10 Total actual borrowings at 31 March 2023 were below this limit at £12,937m. The variance was driven by the variance against the Operational Boundary (explained above) and these headroom items not being utilised.

4.11 The Authorised Limit for direct borrowings for the Corporation was set at £13,769m, which included £700m of headroom items. The headroom items do not represent additional borrowings that TfL can undertake to fund its activities. For the Corporation, they include:

(a) an existing overdraft facility of £100m and a money market facility of £100m; and

(b) an allowance of £500m to avail of favourable market conditions in relation to short-term refinancing activities.

4.12 Total actual borrowings at 31 March 2023 were below this limit at £12,937m. The variance was driven by the variance against the Operational Boundary (explained above) and these headroom items not being utilised.

4.13 Long-term liabilities for the Group as at 31 March 2023 were £2,476m, compared to the Authorised Limit for indirect borrowing limit of £3,175m (£700m lower than the limit set). Aligned with the principle explained in 4.5, the Authorised Limit for indirect debt included an uplift to the Operational Boundary of £500m to capture the potential for new commercial contracts to be entered into that are classified as long-term leases under IFRS 16.

4.14 Similarly, for the Corporation, long-term liabilities as at 31 March 2023 totalled £507m, compared to an indirect borrowing limit of £785m, resulting in an outturn of £278m lower than the limit set. The Authorised Limit for indirect debt included an uplift to the Operational Boundary of £250m to capture the potential for new commercial contracts to be entered into that are classified as long-term leases under IFRS 16.

Capital expenditure

Capital Expenditure (£'m)	Approved	Outturn
TfL Corporation	1,571.6	1,983.2
TfL Group	2,445.1	2,484.9

4.15 The 2022/23 Budget for capital expenditure was set in March 2022 before the agreement of the 30 August 2022 funding settlement with Government, which provided additional funding to TfL.

4.16 Consistent with paragraphs 4.8 and 4.11, the capital expenditure estimate included a £500m for the Group and £250m for the Corporation to capture the potential for new commercial contracts to be entered into that are classified as long-term leases and consequently, capital spend/right of use assets under IFRS 16.

4.17 The Code acknowledges the capital expenditure indicator is an estimate and subject to fluctuation in the ordinary courses of business. The Corporation exceeded the budgeted assumption by £412m primarily due to the March 2022 budget assuming a lower level of funding from Government and the Corporation funding the purchase of Class 378 rolling stock for £277m explained in paragraph 4.4 which was not included in the budget.

Ratio of financing costs to net revenue stream

Ratio of financing costs to net revenue stream (%)	Approved	Outturn
TfL Corporation	15.4%	18.4%
TfL Group	17.1%	21.6%

4.18 The Code acknowledges the ratio of financing costs to net revenue stream is an estimate and subject to fluctuations in the ordinary course of business. There are numerous variables within the calculation and no predominant driver has been noted when compared with the indicators set. The outturn for the Corporation and Group is above the approved indicator. This does not represent an increase in the underlying interest charge and cash cost of direct and indirect debt and is largely driven by the portion of grant income allocated to capital being higher than assumed in the March 2022 budget, which reduces the net revenue stream. For the Group and Corporation, the outturn is considered within a reasonable range of the estimates set.

Gross Debt to Capital Financing Requirement

Gross debt to Capital Financing Requirement (£m)	Gross debt 31 March 2023	Capital Financing Requirement 31 March 2025
TfL Corporation	13,446.5	13,928.4
TfL Group	15,413.2	16,969.9

4.19 The final indicator set is the comparison of Gross Debt to Capital Financing Requirement and in line with expectations, the level of Gross Debt as at 31 March 2023 does not exceed the anticipated level of Capital Financing Requirement for the current and next two financial years as at 31 March 2025.

5 Conclusion

5.1 The outturn for the financial year 2022/2023 is satisfactory upon comparison to the Prudential Indicators approved.

List of appendices to this report:
None

List of Background Papers:
None

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