

TRANSPORT FOR LONDON

AUDIT COMMITTEE

**SUBJECT: EXTERNAL AUDIT PLAN TfL, TTL AND SUBSIDIARIES – YEAR
ENDING 31 MARCH 2011**

DATE: 15 DECEMBER 2010

1 PURPOSE AND DECISION REQUIRED

- 1.1 To present to the Committee KPMG's Plan for the audit of the financial statements of Transport for London, Transport Trading Limited (TTL) and its subsidiaries for the year ending 31 March 2011.
- 1.2 The Committee is asked to note the Plan and make any comments as appropriate.

2 BACKGROUND

- 2.1 In previous years, the external audit plans for TfL and TTL have been presented by the Appointed Auditor, KPMG as separate documents. This year, recognising the fact that many of the key risk areas sit within TTL but then impact upon TfL on consolidation, KPMG is presenting one Plan that captures all risks.
- 2.2 The Plan has been developed by KPMG, and sets out the work that it proposes to undertake in the 2010/11 financial year. The Plan sets out the audit strategy and approach for the audit of the financial statements and also encompasses work relating to Value for Money.

3 RECOMMENDATION

- 3.1 The Committee is asked to NOTE the Plan.

4 CONTACT

- 4.1 Contact: Stephen Critchley, Chief Finance Officer
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TRANSPORT

Transport for London

Financial Statements Audit Plan

15 December 2010

INFRASTRUCTURE, GOVERNMENT AND HEALTHCARE

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This report is addressed to Transport for London and has been prepared for the sole use of the Transport for London Group (TfL) and the TTL Group (TTL). We take no responsibility to any member of staff acting in their individual capacities, or to third parties. The Audit Commission has issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies. This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. We draw your attention to this document.

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Wayne Southwood, who is the engagement Partner to TfL, telephone 0207 311 3232, email wayne.southwood@kpmg.co.uk who will try to resolve your complaint. If you are dissatisfied with your response please contact Trevor Rees on 0161 236 4000, email trevor.rees@kpmg.co.uk, who is the national contact partner for all of KPMG's work with the Audit Commission. After this, if you are still dissatisfied with how your complaint has been handled you can access the Audit Commission's complaints procedure. Put your complaint in writing to the Complaints Investigation Officer, Westward House, Lime Kiln Close, Stoke Gifford, Bristol, BS34 8SR or by e mail to: complaints@audit-commission.gov.uk. Their telephone number is 0844 798 3131, textphone (minicom) 020 7630 0421



Introduction

This document describes how we will deliver our audit work for the relevant entities for the year ending 31 March 2011.

- The TfL Group and Corporation audits are part of the Audit Commission’s framework contract. Our statutory responsibilities and powers are set out in the Audit Commission Act 1998, The Local Government Act 1999 and the Audit Commission’s Code of Audit Practice (the Code).
- Our work for 2010-11 will cover two key areas:
 - Financial statements (including the Annual Governance Statement): providing an opinion on your accounts; and
 - Value for money (VFM).
- We are also the auditors of the TTL Group companies, although this appointment falls outside of the Audit Commission. For these entities we will provide a statutory opinion on the Financial Statements.
- Set out below is a high level outline of our proposed work and outputs for these areas. Further detail is provided in later sections.

	Proposed work and output
Financial statements and Annual Governance Statement	<ul style="list-style-type: none"> • Our work will encompass: <ul style="list-style-type: none"> – A review of the controls over the completion of the accounts. We will rely on Internal Audit wherever possible to avoid unnecessary duplication. – A detailed audit of the financial statements, associated disclosure notes and the Annual Governance Statement. – For the TfL and TTL Group Accounts we will review your consolidation process and substantively test key consolidation adjustments. • The findings of this work support the audit opinion that we issue on your financial statements. • This is the first year that TfL is required to report under IFRS as modified by the Code and TTL under IFRS as approved by the EU. We will review the prior year restatement and opening balance sheet between November 2010 and January 2011 to ensure that the adjustments made are appropriate.
Value for Money	<ul style="list-style-type: none"> • Given the scale of the pressures facing public bodies in the current economic climate, the Commission has reviewed its work programme for 2010-11 and future years. As part of this exercise, the Commission discussed possible options for a new approach to value for money (VFM) audit work with key national stakeholders. From 2010-11 we will therefore apply a new, more targeted approach to our VFM audit work. This will be based on a reduced number of reporting criteria specified by the Commission, concentrating on: <ul style="list-style-type: none"> – Whether there are proper arrangements in place for securing financial resilience; and – Whether there are proper arrangements for challenging how it secures economy, efficiency and effectiveness. <p>We will no longer make annual scored judgements relating to our VFM audit work. Instead we will report the results of all the VFM audit work and the key messages for the audited body in our annual report to those charged with governance and in a clear and accessible annual audit letter.</p>

- The audit planning process and risk assessment is an on-going process and the assessment in this plan will be kept under review and updated if necessary. The remainder of this document provides details of our risk assessment, proposed work and fees for our work on the financial statements audit.

Audit overview

We undertake our work on your financial statements and Annual Governance Statement in four key stages.

Our work supports our audit opinion on your financial statements.

- We are required to satisfy ourselves that the accounts of the TfL and TTL Group comply with statutory requirements (including the Code for TfL) and that proper practices have been observed in compiling them. We are required to provide audit opinions on the consolidated accounts of TfL and TTL as well as on 16 subsidiary companies.
- We are also required to satisfy ourselves that your Annual Governance Statement (AGS) is consistent with our understanding of your operations. Our review of the work of internal audit and consideration of your risk management and governance arrangements are key to this opinion.
- In addition to TTL and TfL's financial statements, we are also required to audit and provide an opinion on TfL's Whole of Government Accounts.

Our Audit Process

- We have summarised the four key stages of our financial statements audit process for you below:

			Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul
1	Planning	<ul style="list-style-type: none"> • Determine risk assessment procedures and identify risks. • Determine audit strategy. • Determine planned audit approach. • Review internal audit findings and scope reliance. 	○ ○	○ ○ ○ ○								
2	Control Evaluation	<ul style="list-style-type: none"> • Understand accounting and reporting activities. • Evaluate design and implementation of selected controls. • Test operating effectiveness of selected controls. • Assess overall risk of material misstatement. 			○ ○ ○ ○				○ ○			
3	Substantive procedures	<ul style="list-style-type: none"> • Plan substantive procedures. • Perform substantive procedures. • Consider if audit evidence is sufficient and appropriate. • Perform work on consolidation. 				○	○	○	○ ○	○ ○	○ ○	
4	Finalisation	<ul style="list-style-type: none"> • Perform completion procedures. • Perform overall evaluation. • Form an audit opinion. • Audit Committee reporting. 									○	○ ○ ○

Audit overview

We work with your finance team and internal audit team to enhance the efficiency of the accounts audit.

Our Audit Process (cont.)

- As part of our audit process, we will work closely with the finance team to understand and continually improve the accounts production process. We will issue a 'prepared by client' list for each material mode, which will include a detailed schedule of information requests, tailored to you, to support the financial statements.

Fraud awareness and prevention

- Our audit procedures also include an assessment of your arrangements to deliver your responsibilities to prevent and detect fraud. The auditing standard for fraud, ISA240 (revised), responds to the increased sensitivity to fraud and the importance given to auditors' work on fraud. TfL has a dedicated anti-fraud team, who utilise techniques such as this, and we meet them twice annually to receive an update on activities.
- TfL also participates in the National Fraud Initiative, which is the Audit Commission's computerised data matching exercise designed to detect fraud perpetrated against public bodies. During our audit we will review TfL's progress and actions in following up the matches identified.
- We utilise KPMG forensic specialists to perform data analytics on journals posted across the group. This identifies trends and highlights any unusual transactions for further investigation. In 2010-11 we will extend this analysis to payroll transactions and will share the findings with management.
- The responsibilities of management and the arrangements with regard to fraud prevention and detection is set out in more detail in Appendix 7.

Liaising with Internal Audit

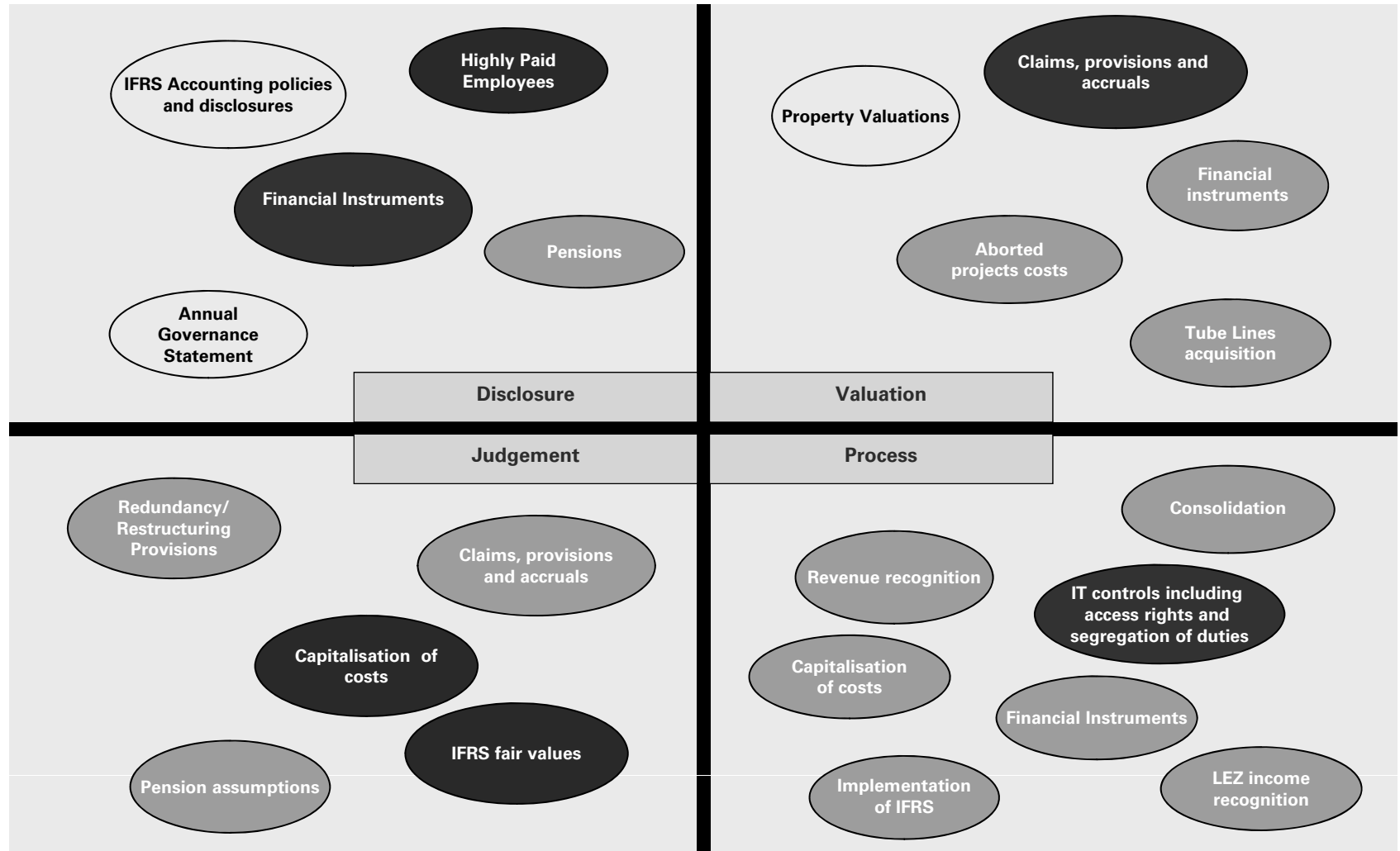
- We have a strong working relationship with Internal Audit and we will continue to work closely with them to maximise the effectiveness of their work on core financial systems and governance at TfL. We receive the annual Internal Audit plan and review this to ascertain where specific reviews can assist us in our controls work. In addition we also use these reports to inform our understanding of the entity and its wider control environment. Specifically, the Internal Audit function's work on anti-fraud informs our own fraud assessments. For the 2010-11 plan we intend to refer to the following reviews:
 - Asset Sales
 - SAP Audits (programme governance; security and use of existing landscapes; security authorisations team and effectiveness; testing for password sharing, CRM application controls)
 - Declarations of Interest
 - Ongoing Delivery of the IM Security Strategy
 - Fraud Risk Management
 - TfL Board Effectiveness
 - Congestion Charging Contract – We have agreed a scope of work with Internal Audit
 - Ticket refunds
 - Leavers' processes
 - Crossrail Audits (management of claims; effectiveness of the new financial and procurement management system; business continuity, resilience and disaster recovery; IT strategy and management of Fujitsu; management of land and property acquisitions).

Whole of Government Accounts (WGA)

- We are required to review and report on your WGA consolidation pack in accordance with the approach agreed with HM Treasury and the National Audit Office. The 2010-11 WGA consolidated pack will need to be produced in compliance with International Financial Reporting Standards (IFRS).

Key financial statement audit risks

Through discussions with officers and our existing TfL and sector knowledge we have identified a number of key financial statement risks.



■ High ■ Medium □ Low

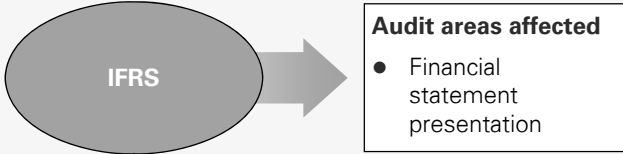
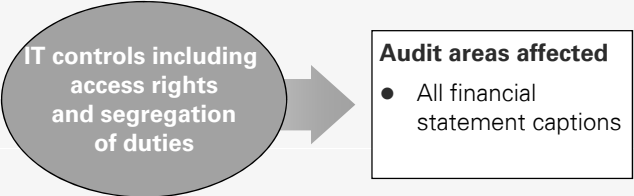
The high and medium risk issues are discussed overleaf

NB: The size of each bubble is not representative of the scale of the risk

Key financial statement audit risks (cont.)

For each key risk we have outlined the impact on our audit plan.

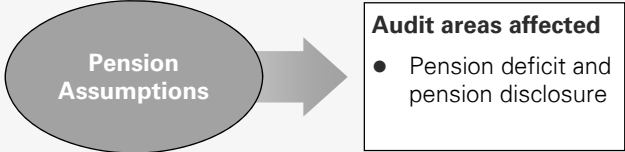
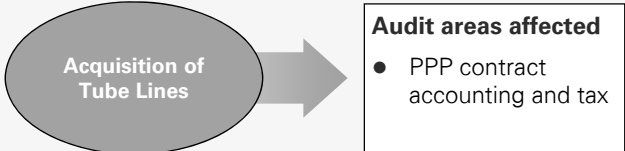
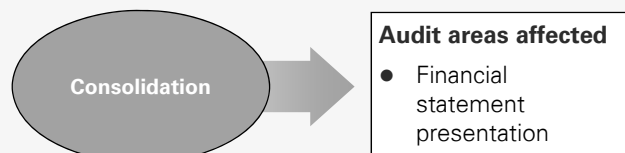
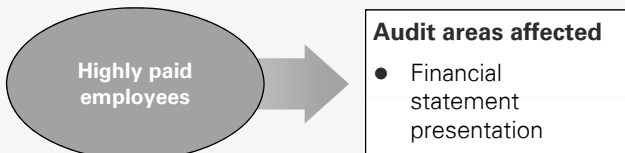
We will provide an update to the Audit Committee on these risks at the June Audit Committee meeting.

KEY audit risks	Impact on audit plan
 <p>Audit areas affected</p> <ul style="list-style-type: none"> Financial statement presentation 	<ul style="list-style-type: none"> The adoption of International Financial Reporting Standards (IFRS) is required by local government bodies for 2010-11. This will require the opening balance sheet as at 1 April 2009 and the financial statements for 2009-10 to be converted to IFRS for comparative purposes. TfL have opted for all subsidiary companies to adopt IFRS in full. As such TfL will need to introduce new accounting policies for the Group. The adoption of IFRS will have an impact on many areas including: <ul style="list-style-type: none"> Processes Accounts coding and mapping Disclosure requirements Ensuring IT systems are able to cope with the added complexities. TfL have a dedicated team with responsibility for overseeing the conversion process and have identified work streams and have allocated work to modes. We are working closely with the IFRS team to understand processes for adopting IFRS and to walkthrough key controls and processes for identifying and computing differences. We will audit the opening balances and comparators, gaining an understanding of all material adjustments.
 <p>Audit areas affected</p> <ul style="list-style-type: none"> All financial statement captions 	<ul style="list-style-type: none"> Our work in previous years identified a significant number of users with access to a wide range of SAP transactions. This gave rise to a number of potential segregation of duties issues. We identified a number of users with access rights who could theoretically process invoices (enter invoices into SAP), approve payments (by issuing a Goods Received Note) and/or amend vendor master data, although executing all three processes would require these users to access non routine functionality within SAP. We will use our IT specialists to carry out a review of SAP access rights and segregation of duties ahead of our final audit in April.

Key financial statement audit risks (cont.)

For each key risk we have outlined the impact on our audit plan.

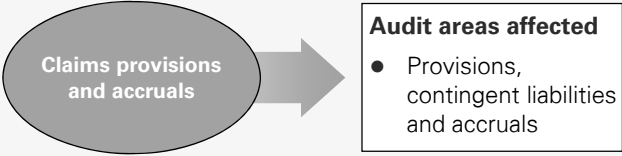
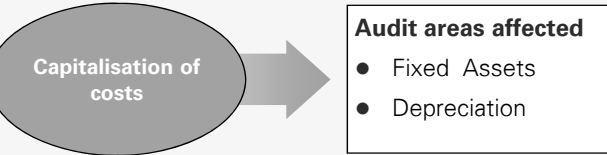
We will provide an update to the Audit Committee on these risk issues.

KEY audit risks	Impact on audit plan
 <p>Pension Assumptions</p> <p>Audit areas affected</p> <ul style="list-style-type: none"> ● Pension deficit and pension disclosure 	<ul style="list-style-type: none"> ● The majority of TfL's employees are members of the public sector section of the TfL Pension Fund. Given current market conditions, assumptions used may cause the pension deficit to change significantly. A triennial valuation of the fund as at 31 March 2009 was completed last year. ● We will audit the data and balances as well as use our pensions specialists to challenge the assumptions and to review the disclosure required by IAS 19.
 <p>Acquisition of Tube Lines</p> <p>Audit areas affected</p> <ul style="list-style-type: none"> ● PPP contract accounting and tax 	<ul style="list-style-type: none"> ● On 7 May 2010 TfL finalised the agreement to acquire the equity shares in Tube Lines from Bechtel and Amey (Ferrovial) for £310m. The acquisition completed on 27 June 2010. ● Acquisition accounting under IFRS will be applied at the Group level with the fair value of acquired assets and liabilities determined together with an assessment of the carrying value of any residual goodwill (including valuation of the pre-existing relationships). ● We have performed an audit of the TLL statutory accounts as at 27 June 2010.
 <p>Consolidation</p> <p>Audit areas affected</p> <ul style="list-style-type: none"> ● Financial statement presentation 	<ul style="list-style-type: none"> ● The consolidation is currently driven by a series of excel spreadsheets. The Group size increases the risk of 'manual error'. ● We understand that you are implementing Clarity, however this may not be fully operational for the year ending 31 March 2011. ● We will continue to test your consolidation spreadsheet, agreeing all source data to audited packs and consolidation adjustments to underlying data.
 <p>Highly paid employees</p> <p>Audit areas affected</p> <ul style="list-style-type: none"> ● Financial statement presentation 	<ul style="list-style-type: none"> ● TfL is required under the LG Code to publish details of all highly paid employees. ● Given TfL's high profile this information is very sensitive and consequently it is essential that the information is accurate and complete. ● We will review the process by which this disclosure is generated and will test a sample of employees by agreeing back to P60s.

Key financial statement audit risks (cont.)

For each key risk we have outlined the impact on our audit plan.

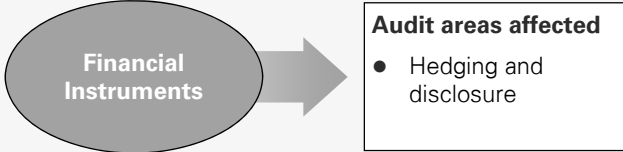
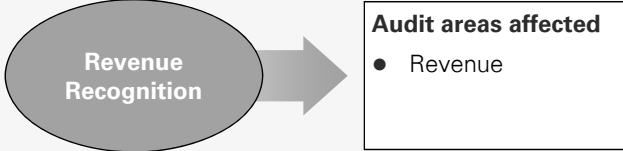
We will provide an update to the Audit Committee on these risk issues.

KEY audit risks	Impact on audit plan
 <p>Claims provisions and accruals</p> <p>Audit areas affected</p> <ul style="list-style-type: none"> • Provisions, contingent liabilities and accruals 	<ul style="list-style-type: none"> • TfL is subject to significant claims from contractors in respect of projects and contracts, as well as disputes in the ordinary course of business (for example, on compulsory purchases). The assessment of the amount to be provided in respect of such claims is a highly subjective matter. • Where we are aware of claims we will meet with management to discuss and fully understand the nature of the claims and how any provision has been calculated, including reviewing the assumptions underpinning this judgement as well as the review of any supporting documentation. • We will also meet with the Head of Legal to determine whether any other claims have been received and review the treatment of these claims.
 <p>Capitalisation of costs</p> <p>Audit areas affected</p> <ul style="list-style-type: none"> • Fixed Assets • Depreciation 	<ul style="list-style-type: none"> • On the majority of projects undertaken within TfL and TTL a judgement needs to be made concerning the split of costs between capital and operating expenditure. In many cases, projects will involve a mixture of repairs and maintenance (operating expenditure) and replacement (capital expenditure). • Given the current economic environment there is an increased risk of projects being terminated or suspended, which increases the risk of potential write-offs of assets under construction. The treatment of costs associated with such projects will need to be carefully considered. • We will review the split of capital and revenue for new additions. We will also discuss any aborted projects with management and determine how any associated costs have been accounted for.

Key financial statement audit risks (cont.)

For each key risk we have outlined the impact on our audit plan.

We will provide an update to the Audit Committee on these risk issues.

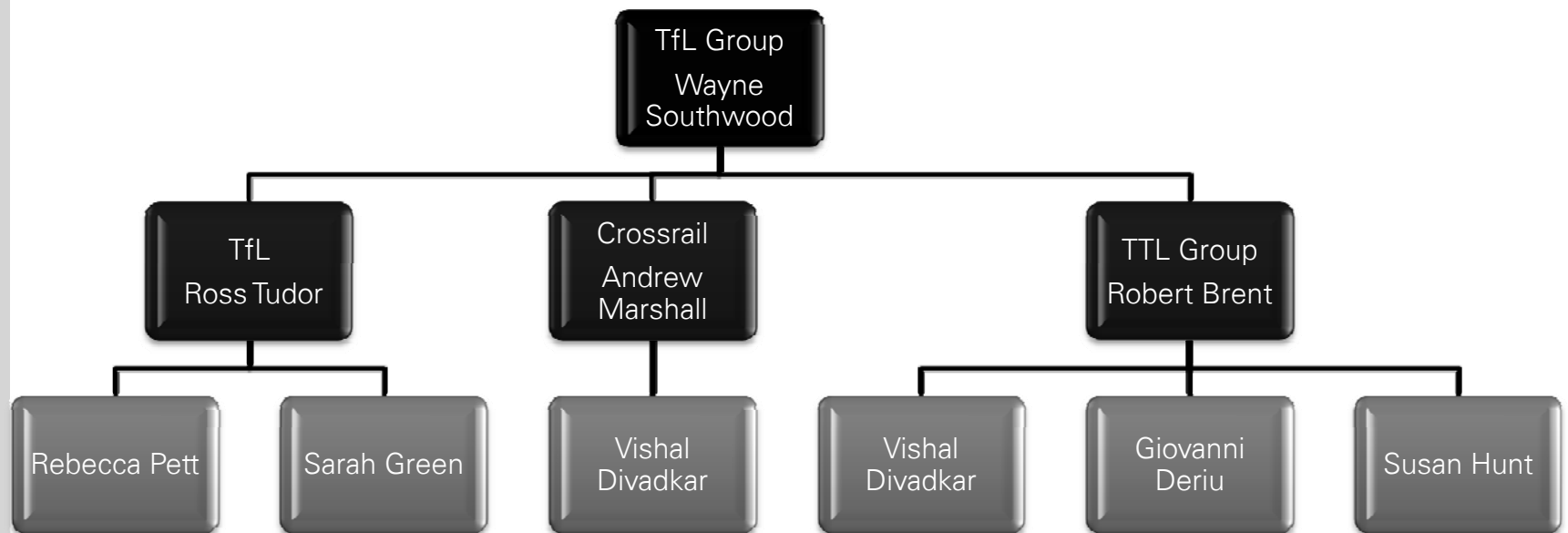
KEY audit risks	Impact on audit plan
 <p>Financial Instruments</p> <p>Audit areas affected</p> <ul style="list-style-type: none"> Hedging and disclosure 	<ul style="list-style-type: none"> We understand that TfL is in the process of entering into a series of forward starting swaps with a nominal value of circa £700m, in order to forward fix the interest rate exposure on highly probable future debt issuance. Our treasury specialist has reviewed the processes being followed and is working with management to agree the accounting treatment and disclosure requirements of these arrangements.
 <p>Revenue Recognition</p> <p>Audit areas affected</p> <ul style="list-style-type: none"> Revenue 	<ul style="list-style-type: none"> A significant proportion of revenue is collected through Underground stations. The majority of the balance is collected through newsagents and managed by an outsourced provider, Oyster Sales Service. TfL relies on data supplied by this third party for recording such revenue in its accounts. Revenue is then allocated between the various modes based on survey data (Travelcards) and real time travel data (Pay As You Go). In the absence of robust reconciliations, there is a risk of manipulation of revenue; this is significantly mitigated by close monitoring of sales returns and bankings, and by the work of Internal Audit's fraud prevention team. Income from Congestion Charging (CC) and Low Emission Zone (LEZ) is also collected and administered through a service provider, IBM. We will review the controls and processes in place at TfL to ensure that there is appropriate oversight of the contracts as well as perform logic checks on the revenue received from these areas. We will also review cash reconciliations and use our IT colleagues to review the ticketing system.

Key Audit Team

Wayne Southwood joins the audit team as your Audit Partner, replacing June Awty.

Andrew Marshall will continue as Partner on Crossrail Ltd but all other responsibilities for the TTL Group have been assumed by Robert Brent.

Contact details are shown on the contents page.



Independence Confirmation

Our independence and objectivity responsibilities under the Code are summarised in Appendix 3.

We confirm our audit team's independence and objectivity is not impaired.

Independence and objectivity confirmation

- Professional standards require auditors to communicate to those charged with governance, at least annually, all relationships that may bear on the firm's independence and the objectivity of the audit Engagement Partner and audit staff. The standards also place requirements on auditors in relation to integrity, objectivity and independence.
- The ISA defines 'those charged with governance' as 'those persons entrusted with the supervision, control and direction of an entity'. In your case this is the Audit Committee.
- KPMG LLP is committed to being and being seen to be independent. APB Ethical Standard 1 Integrity, Objectivity and Independence requires us to communicate to you in writing all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place, that in our professional judgement, may reasonably be thought to bear on KPMG LLP's independence and the objectivity of the Engagement Lead and the audit team.

Confirmation statement

- We confirm that as of the date of this report in our professional judgement, KPMG LLP is independent within the meaning of regulatory and professional requirements and the objectivity of the Appointed Auditor and the audit team is not impaired.

Our Audit Fees

We set out here our proposed audit fees for the financial statements audits of the Group entities, the Value for Money assessment, IFRS work and the Whole of Government Accounts opinion.

We have targeted efficiencies across all entities in order to offset the increased costs arising from inflation and also the increased audit work that accompanies IFRS's additional disclosure and fair values.

- Our fee is calculated with reference to a number of factors including your turnover and our assessment of audit risk and control environment.

Element of the audit	2010-11 (£)	2009-10 (£)
Corporation/Group Financial Statement Audit	311,010	288,000
Value for Money*	[TBC]	90,000
Whole of Government Accounts	5,500	5,500
Total for TfL Corporation and Group	316,510	383,500
TTL excluding Tube Lines	1,004,020	1,044,355
Total for TTL	1,320,530	1,427,855
Tube Lines – new for 2010/2011	190,000	-
Total for TfL	1,510,530	1,427,855

*The Audit Commission has not fully scoped the work to be undertaken in relation to reaching a Value for Money conclusion. The assessment will now focus on two thematic areas i) securing financial resilience and ii) prioritising resources in a financially strained economy. The Audit Commission have indicated that they anticipate a reduction in work compared with the previous year. There is currently a lack of clarity from the Audit Commission on the work required for 2010/11 and it is therefore not possible to propose a fee at this time.

The above fee excludes a rebate from the Audit Commission in relation to the 'one off' cost of IFRS.

TTL Fee

	2010 Fee (£)	Inflation (3%) (£)	IFRS increment (5%) (£)	Revised 2010 base with inflation (£)	Efficiencies targeted (£)	2011 Proposed (£)
TTL fee agreed	969,355	29,080	48,467	1,046,902	(117,882)	929,020
Crossrail	75,000	2,250	3,750	81,000	(6,000)	75,000
TTL Group	1,044,355	31,330	52,217	1,127,902	(123,882)	1,004,020
Tube Lines for 2009 (Deloitte fee)	[280,000]	8,400	0	288,400	(98,400)	190,000
Total Base fee for TTL	1,324,355	39,730	52,217	1,416,302	(222,282)	1,194,020

IFRS – audit of opening balance sheet and comparatives

- The above fees do not include the fee for auditing the conversion of the opening balance sheet and prior period statements. We have made an estimate of the hours and fees for our audit of the IFRS conversion, which is being discussed with management.

Audit Fees (cont.)

Our audit fee is indicative and based on you meeting our expectations of your support as outlined in Appendix 1.

Meeting these expectations will help the delivery of our audit within the proposed audit fee.

Audit fee assumptions

- The audit fee is indicative and is based on you meeting our agreed expectations as outlined in Appendix 1. In setting the fee, we have assumed:
 - The overall level of risk in relation to the audit of the financial statements is not significantly different from that identified for 2009-10;
 - You will inform us of any significant developments impacting on our audit;
 - Internal audit continues to meet the appropriate professional standards;
 - Internal audit undertakes appropriate work on all areas as agreed with KPMG, eg congestion charging;
 - You will identify and implement within your 2010-11 financial statements any changes required under the CIPFA IFRS-based Code of Practice on Local Authority Accounting;
 - Your financial statements will be made available for audit in line with the timetable we agree with you;
 - Good quality working papers and records will be provided to support the financial statements by the date we agree with you;
 - Requested information will be provided within agreed timescales;
 - Prompt responses will be provided to draft reports; and
 - Additional work will not be required to address questions or objections raised by local government electors or for special investigations such as those arising from disclosures under the Public Interest Disclosure Act 1998.
- Meeting these expectations will help ensure the delivery of our audit within the agreed audit fee.

Changes to the audit plan

- Changes to this plan and the audit fee may be necessary if:
 - New significant audit risks emerge;
 - Additional work is required of us by the Audit Commission or other regulators; and
 - Additional work is required as a result of changes in legislation, professional standards or financial reporting requirements.
- If changes to this plan and the audit fee are required, we will discuss and agree these initially with the Head of Group Financial Accounting and Chief Finance Officer.

Audit timeline and deliverables

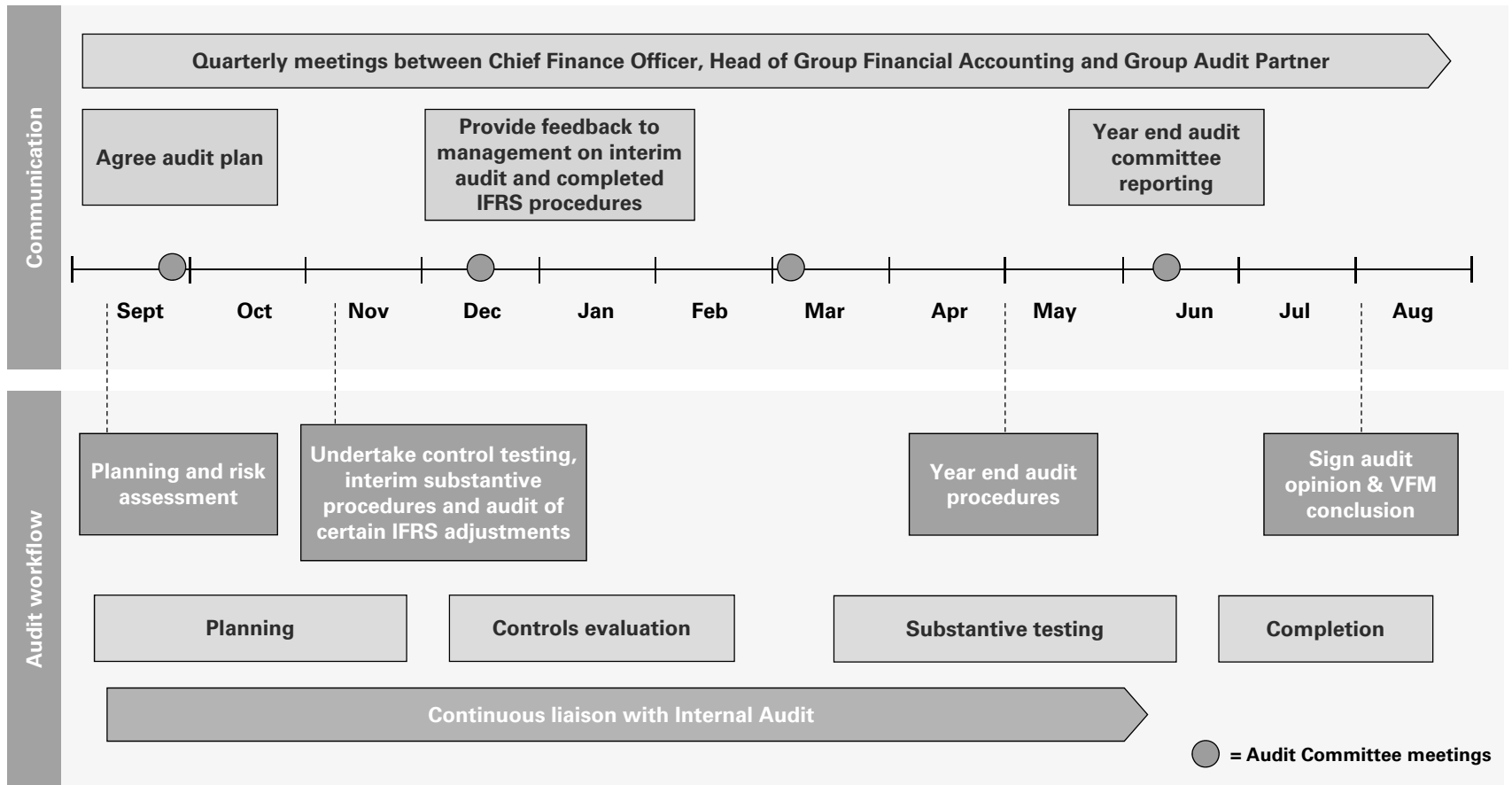
Our key deliverables will be delivered to a high standard and on time.

We will discuss and agree each report with management prior to publication.

Deliverable	Purpose	Timing
Planning		
Audit plan	<ul style="list-style-type: none"> ● Outline audit approach. ● Identify areas of audit focus and planned procedures. ● Confirm plan with Audit Committee. 	December 2010
IFRS		
IFRS sign off to management	<ul style="list-style-type: none"> ● Opening balances and prior year comparatives 	February 2011
Final Audit		
Report to those charged with governance (ISA 260)	<ul style="list-style-type: none"> ● Auditor's report on financial statements. ● Auditor's report on TfL's value for money. ● Detail the resolution of key audit issues. ● Communication of adjusted and unadjusted audit differences. ● Performance improvement recommendations identified during our audit. 	June 2011
Opinion on financial statements	<ul style="list-style-type: none"> ● Financial Statement opinion. 	July 2011
Value for Money		
Opinion on economy, efficiency and effectiveness	<ul style="list-style-type: none"> ● Value for Money conclusion. 	July 2011

Audit timeline and deliverables (cont.)

We will be in continuous dialogue with you throughout the audit.



Meeting your expectations

We have summarised how we plan to meet your expectations.

How we will conduct ourselves

Communications

- We will be proactive in developing relationships with your staff where our audit work requires their input.
- We will ensure that telephone calls, letters and emails are answered within a reasonable timeframe.
- We will ensure that all recommendations, and in particular those relating to our performance management work, are included within our Annual Audit Letter only after having been agreed with relevant Officers.
- Wayne Southwood, Robert Brent and Ross Tudor will attend all Audit Committee meetings and ensure that other relevant KPMG staff are invited as appropriate.

Working together

- We will ensure that the Chief Finance Officer, Head of Group Financial Accounting and other key members of staff are kept informed of the progress of our audit work throughout the year.
- We will liaise with staff at all levels of the Group to ensure that our work is appropriately planned and completed and where recommendations are made these are agreed with the responsible officer.

Cooperating with TfL

- We will continue to coordinate our work with that of internal audit and ensure that we provide appropriate proactive commentary to the finance function on issues that affect TfL's accounts.
- We will respond promptly to requests for comment on aspects of the TfL's operations, where appropriate.

Our expectations of your support

Audit Plan

- Brief our staff on key issues affecting TfL.
- Review and agree the draft plan.

Interim Audit

- Ensure that key officers are available for the duration of our audit.
- Respond to and agree our draft reports in good time.

Accounts Audit

- Ensure that a full draft of the account packs are available on the agreed start date of our audit, and that only agreed adjustments are put into the accounts following receipt of this draft.
- Produce the documents listed within our prepared by client request by the agreed start date of our audit.
- Ensure that the mandatory content of the Annual Report is available at the agreed time of our final account audit.

Annual Audit Letter

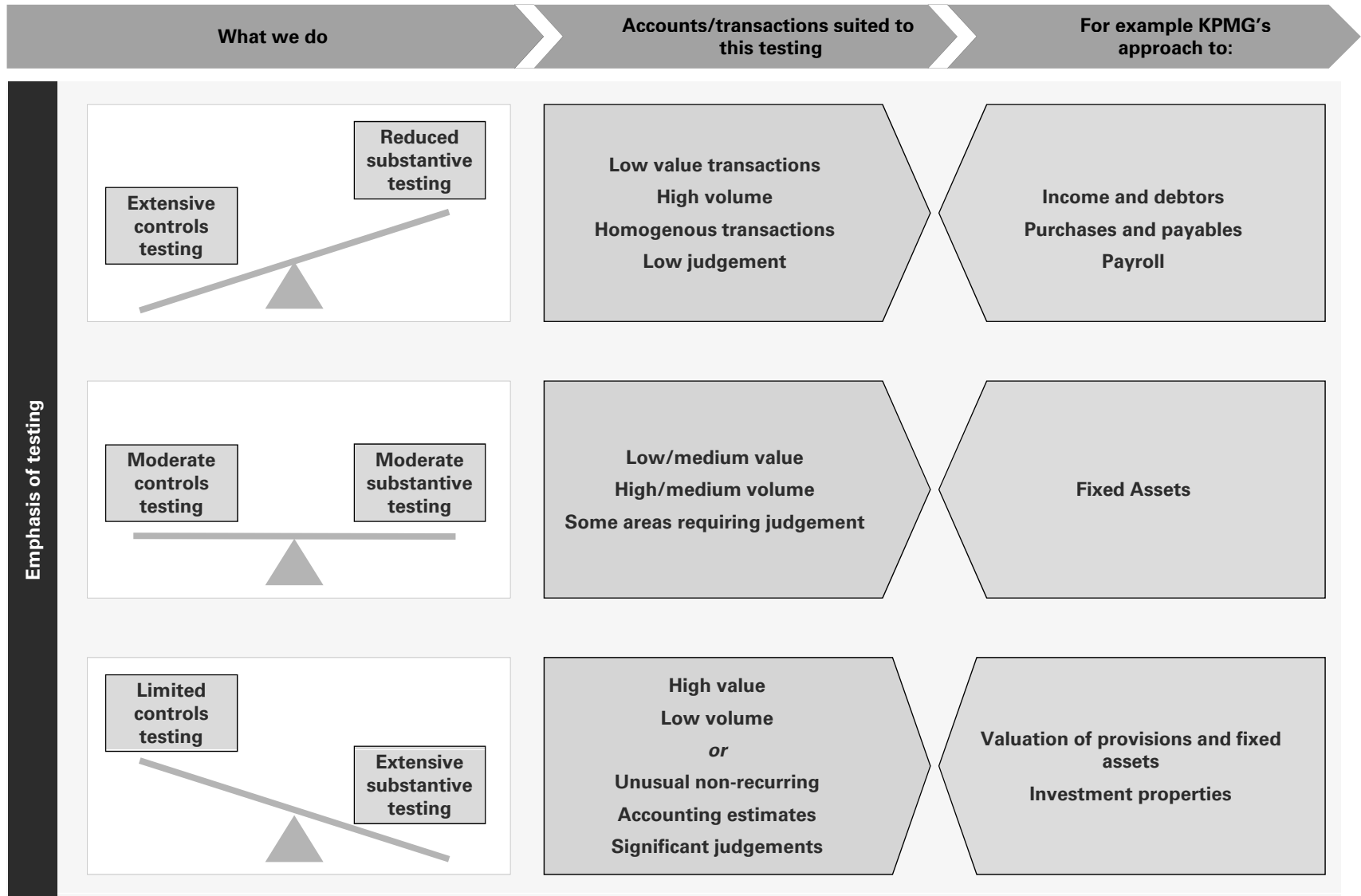
- Discuss and agree our draft Annual Audit Letter in good time for the Audit Committee.
- Ensure that all action plans are agreed and followed up in due course.

Other work

- Agree a key contact as a focal point for the study or work.
- Discuss and review our findings so that action plans can be fully completed and implemented.

Balance of internal controls and substantive testing

This appendix illustrates how we determine the most effective balance of internal controls and substantive audit testing.



Note: Assuming controls are found to operate as designed

Independence and objectivity requirements

This appendix summarises the auditor's responsibilities regarding independence and objectivity.

Independence and objectivity

- Auditors are required by the Code to:
 - Carry out their work with independence and objectivity;
 - Exercise their professional judgement and act independently of both the Commission and the audited body;
 - Maintain an objective attitude at all times and not act in any way that might give rise to, or be perceived to give rise to, a conflict of interest; and
 - Resist any improper attempt to influence their judgement in the conduct of the audit.
- In addition, the Code specifies that auditors should not carry out work for an audited body that does not relate directly to the discharge of the auditors' functions under the Code unless approved by the Audit Committee and the Audit Commission.
- The Code also states that the Commission issues guidance under its powers to appoint auditors and to determine their terms of appointment. The Standing Guidance for Auditors includes several references to arrangements designed to support and reinforce the requirements relating to independence, which auditors must comply with. These are as follows:
 - Any staff involved on Commission work who wish to engage in political activity should obtain prior approval from the Partner;
 - Audit staff are expected not to accept appointments as lay school inspectors;
 - Firms are expected not to risk damaging working relationships by bidding for work within an audited body's area in direct competition with the body's own staff without having discussed and agreed a local protocol with the body concerned;
 - Auditors are expected to comply with the Commission's statements on firms not providing personal financial or tax advice to certain senior individuals at their audited bodies, auditors' conflicts of interest in relation to PFI procurement at audited bodies, and disposal of consultancy practices and auditors' independence;
 - Auditors appointed by the Commission should not accept engagements which involve commenting on the performance of other Commission auditors on Commission work without first consulting the Commission;
 - Auditors are expected to comply with the Commission's policy for the Engagement Lead to be changed on each audit at least once every five years (subject to agreed transitional arrangements). Audit suppliers are required to obtain the Commission's written approval prior to changing any Engagement Lead in respect of each audited body;
 - Audit suppliers are required to obtain the Commission's written approval prior to changing any Engagement Lead in respect of each audited body; and
 - The Commission must be notified of any change of second in command within one month of making the change. Where a new Engagement Lead or second in command has not previously undertaken audits under the Audit Commission Act 1998 or has not previously worked for the audit supplier, the audit supplier is required to provide brief details of the individual's relevant qualifications, skills and experience.

Appendix 4

Sustainability

This appendix summarises the auditor's commitment to sustainability.

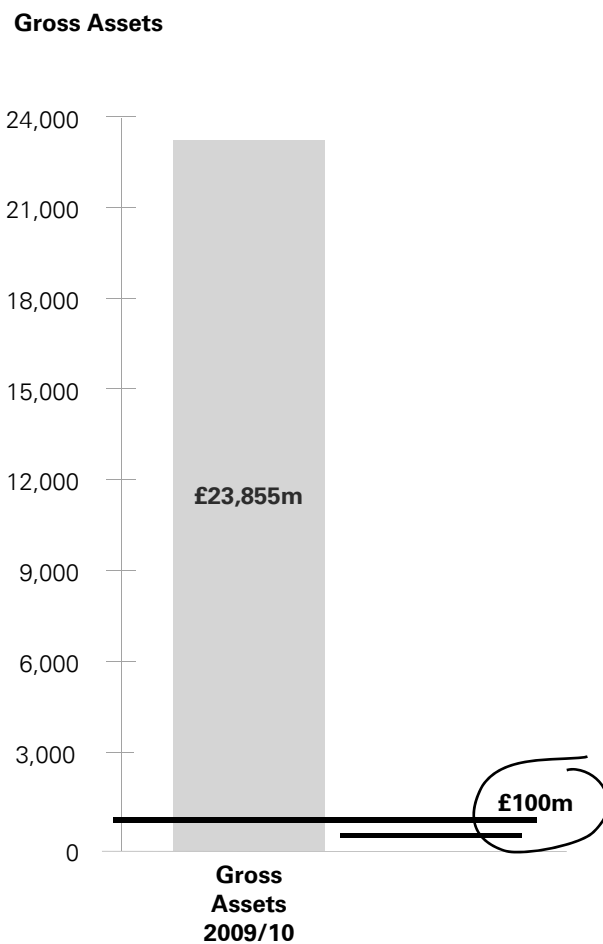
Sustainability

- The Audit Commission is committed to promoting sustainability in working practices and we will actively consider opportunities to reduce our impact on the environment. This will include:
 - Reducing paper flow by encouraging you to submit documentation and working papers electronically;
 - Use of video and telephone conferencing for meetings as appropriate;
 - Reducing travel; and
 - Other initiatives.
- KPMG are also taking steps to improve our environmental performance. Achievements to date include:
 - All offices certified ISO14001, the leading international standard for environmental management systems;
 - Our Responsible Consumption programme enables our people to actively contribute to the firm being environmentally responsible;
 - More than 40 percent of paper purchased is recycled paper;
 - Over 90 percent of the electricity used in buildings is now from renewable sources; and
 - Some 1.8 million travel miles have been saved through car sharing schemes and 1.5 million miles have been saved through audio and video conferencing.

Appendix 5

Materiality (TfL Group)

Our audit work is planned to detect errors that are material to the accounts as a whole.



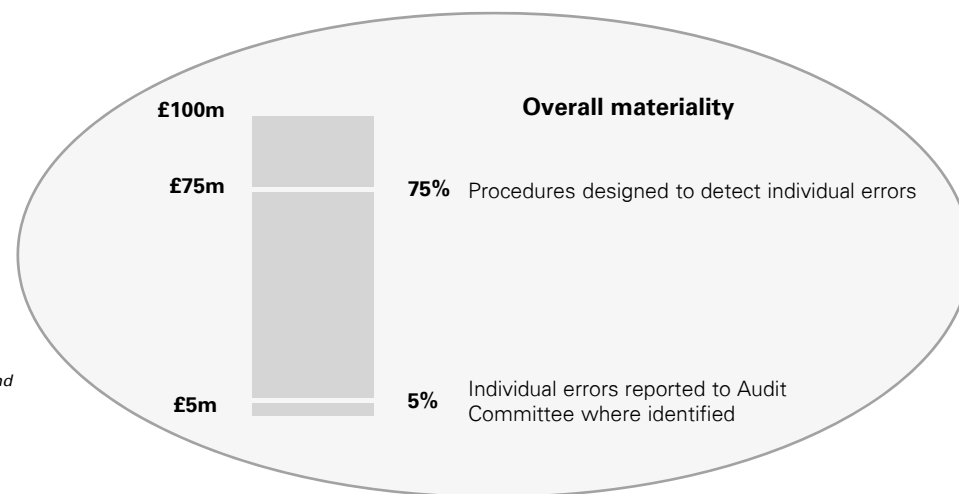
Note: Materiality may be updated on receipt on the draft financial statements and will be less for individual entities
 Source: 2009-10 financial statements

Determining materiality

- We consider quantitative and qualitative factors in setting materiality and in designing our audit procedures.
- Materiality has been set at £100m for all balances which is 0.4% of gross assets.
- We design our procedures to detect errors at a lower level of precision, i.e. £75m; we have some flexibility to adjust this level downwards.

Reporting to Audit Committee

- To comply with auditing standards, the following three types of audit differences will be presented to the Audit Committee:
 - summary of adjusted audit differences
 - summary of unadjusted audit differences
 - summary of disclosure differences (adjusted and unadjusted)



Appendix 6

eAudit

This appendix summarises the changes to KPMG's audit management processes.

eAudit

- For the year ending 31 March 2011 we will be using our new eAudit tool to manage your audit.

We believe the use of eAudit will benefit you as follows:

- **Consistency** – All audit teams involved in the audit of your group will use the same application and methodology. Applying a consistent approach globally promotes efficiency, regardless of the location where the audit is performed.
- **Industry knowledge** – Access to industry knowledge facilitates our audit professionals' ability to focus on what's important to your business. Our global knowledge base allows us to provide you feedback on how your processes and controls compare with industry leaders.
- **Project management tools** – Embedded project management tools help our team stay focused on meeting your deadlines and performing the audit as efficiently as possible.
- **Summary of significant matters** – The eAudit tracker summarises all significant matters as they are identified during the audit and allows us to provide you with regular updates throughout the audit so that there are no surprises.

Consideration of fraud

This appendix summarises our consideration of fraud and the respective responsibilities of management, those charged with Governance and audit

Consideration of fraud

- Auditing standards require that we consider the possibility of fraud (in the context of pervasive and specific risks) at all stages of the audit process
- Our approach to fraud risks in 2010 will include: one-on-one discussions with senior management, those charged with Governance, internal audit and your Head of Fraud; and
- Consideration of TfL's process for confirming and reporting instances of fraud.

Respective Responsibilities

- It is the responsibility of management to establish a control environment and maintain policies and procedures to assist in achieving the objective of ensuring, as far as possible, the orderly and efficient conduct of the entity's business.
- It is the responsibility of those charged with governance to ensure, through oversight of management, the integrity of an entity's accounting and financial reporting systems and that appropriate controls are in place, including those for monitoring risk, financial control and compliance with the law.
- An audit is designed to provide reasonable assurance that the financial statements, taken as a whole, are free from material misstatement, whether caused by fraud or error. The fact that an audit is carried out may act as a deterrent, but the auditor is not and cannot be held responsible for the prevention of fraud and error under the Auditing Standards.