

TRANSPORT FOR LONDON

AUDIT COMMITTEE

**SUBJECT: QUARTERLY PROGRESS UPDATE: THE INTERNATIONAL FINANCIAL REPORTING STANDARDS PROJECT**

**DATE: 2 MARCH 2011**

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**1 PURPOSE AND DECISION REQUIRED**

- 1.1 To provide the Committee with the quarterly progress update on the International Financial Reporting Standards (“IFRS”) project.

**2 BACKGROUND**

- 2.1 With effect from 1 April 2010, Local Authorities are required to prepare their own accounts following IFRS as interpreted by the CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2010/11 (the “Code”). The IFRS project has been established to coordinate the transition across the whole of TfL.

**3 INTERNATIONAL FINANCIAL REPORTING STANDARDS**

**Progress to date**

- 3.1 The IFRS project is now focussed on the following key aspects of work:
- (a) restated opening balance sheets for all entities as at 1 April 2009 are complete, subject to the consequential impact of the few outstanding technical items set out below;
  - (b) restated comparative financial statements with full disclosure notes;
  - (c) confirmation of approach to the transition and assumptions behind the interpretation and practical application of IFRS to TfL entities; and
  - (d) audit of the analysis work done, and the IFRS first adoption adjustments.
- 3.2 The proposed formats for the IFRS financial statements for the limited company subsidiaries are agreed, and are currently being populated. These draft IFRS financial statements will be reviewed by KPMG in advance of the year end to ensure that both the restatement and the disclosure are agreed. The proposed format for the TTL Group accounts has been prepared and is in the process of being populated.
- 3.3 The format for TfL itself is now in draft, following the publication of the CIPFA Guidance notes in December. The restated financial statements, including full disclosure notes, will be presented to KPMG for audit in March.
- 3.4 Extracts from the draft restated TfL accounts are attached as Appendix 1. The

Group Income and Expenditure Statement and Group Balance Sheet are still in draft, pending finalisation of the remaining technical issues (see 3.5 below). The 2011 financial statements will also include “transition statements”, reconciling from the 2010 UK GAAP position to the restated 2010 IFRS position. The draft transition statements are also attached. The transition statements will include narrative explanation of the major IFRS adjustments.

### 3.5 The remaining areas presenting the greatest challenges are:

- (a) The review of all property holdings and reclassification under the definitions used in IFRS. A practical definition of investment property has now been agreed with KPMG. There is some change in classification, where property that has previously been treated as infrastructure may now be treated as investment property, and vice versa. Valuations are currently being undertaken to ensure that the amounts reported in the 2011 financial statements are appropriate.
- (b) IFRS requires the capitalisation of interest on borrowings related to qualifying assets. Previously, TfL and the subsidiaries have adopted a UK GAAP-compliant policy of writing interest off to the income statement. For capitalisation to take place, a new process is required and this has now been designed and agreed in principle with KPMG. Work is underway on calculating the adjustments required, and it is anticipated that the adjustments will be audited by KPMG in March.
- (c) The first time adoption of IFRIC 4, Determining Whether an Arrangement Contains a Lease, has presented a number of challenges. It has now been agreed that, while the Heathrow T5 contract should be accounted for as a finance lease, the value of the finance lease creditor on that lease is nil. This is because the payments due under the contract are entirely contingent, and vary with the number of passengers using the service, and IFRS specifically requires that a nil value is assigned to contingent rentals when assessing a lease. The Northern Line Trains contract will come on balance sheet, and TfL is in the process of agreeing the calculation of the finance lease creditor with KPMG.
- (d) Deferred tax has presented significant challenges. This is only an issue for the subsidiary companies, and on consolidation in the Group accounts. The methodology for calculating the deferred tax asset or liability is different under IFRS and has required significant effort both at TfL and also from KPMG. The calculations are now complete, subject to any adjustments arising out of the other outstanding areas of work. Although this is subject to review and audit by KPMG, it is not currently anticipated that a net deferred tax liability will result.
- (e) The detailed disclosure in the TfL financial statements for related party transactions and segmental reporting requires further work. Segmental reporting in particular presents challenges. Under the Code, TfL is required to reconcile from what is presented to the Board (likely to be the Quarter 4 Operating and Financial Review) to what is presented in the financial statements, but the basis of preparation is quite different. A pragmatic solution, which does not confuse the reader of the accounts, is currently being drafted.

### 3.6 KPMG has completed its audit work on the individual company transition

adjustments, although this is subject to any further amendments arising out of the outstanding areas above.

- 3.7 KPMG will shortly commence the audit of the restated consolidation for both TTL and TfL Groups.
- 3.8 It is anticipated that all remaining outstanding technical queries will be resolved in March 2011 and that the audit of the IFRS conversion, including restated Group accounts, will be completed before the end of March 2011.

#### **4 RECOMMENDATION**

- 4.1 The Committee is asked to NOTE the report.

#### **5 CONTACT**

- 5.1 Contact: Stephen Critchley, Chief Finance Officer  
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# Draft Group Balance Sheet

<i>At 31 March</i>	<i>Note</i>	<b>2011 £m</b>	2010 £m	2009 £m
<b>Long term assets</b>				
Intangible assets	10		120.9	37.4
Property, plant and equipment	11		21,967.8	19,940.5
Investment property	12		188.3	183.1
Other investments	13		-	-
Derivative financial instruments				
Long term debtors	14		-	-
			<u>22,277.0</u>	<u>20,161.0</u>
<b>Current assets</b>				
Inventories	15		18.3	20.2
Derivative financial instruments				
Short term debtors	14		648.9	470.9
Cash and cash equivalents	16		1,509.4	1,980.7
Short term investments			-	21.2
Assets classified as held for sale	17		6.5	6.5
			<u>2,183.1</u>	<u>2,499.5</u>
<b>Current liabilities</b>				
Short term creditors	18		(1,725.3)	(1,772.3)
Short term borrowings and overdrafts	19		-	-
Short term finance lease liabilities	20		(404.4)	(1,184.6)
Derivative financial instruments				
Short term provisions	21		(300.2)	(28.2)
			<u>(2,429.9)</u>	<u>(2,985.1)</u>
<b>Long term liabilities</b>				
Long term creditors			(35.2)	(45.7)
Long term borrowings	19		(4,117.8)	(3,017.6)
Long term finance lease liabilities	20		(3,196.8)	(2,328.2)
Derivative financial instruments				
Long term provisions	21		(265.2)	(125.1)
Retirement benefit obligation	22		(2,193.6)	(1,187.4)
			<u>(9,808.6)</u>	<u>(6,704.0)</u>
<b>Net assets</b>			<u>12,221.6</u>	<u>12,971.4</u>

# Group Balance Sheet

At 31 March

		2011 £m	2010 £m	2009 £m
<b>Reserves</b>				
Usable reserves			1,041.5	1,318.9
Unusable reserves	23		11,180.1	11,652.5
<b>Total Reserves</b>			<u>12,221.6</u>	<u>12,971.4</u>

The notes on pages XX to XX form part of these financial statements.

These financial statements were approved by the Board on xx June 2011 and signed on its behalf by:

**Boris Johnson**

Chair of TfL

# Group Income and Expenditure Statement

		2011	2011	2011	2010
	Note	Continuing operations	Acquisitions	Total	Continuing operations
		£m	£m	£m	£m
<b>Highways and Transport Services</b>					
Gross income	1,2				3,595.0
Gross expenditure	3				(6,108.5)
		<hr/>	<hr/>	<hr/>	<hr/>
<b>Net cost of services</b>					(2,513.5)
Other operating expenditure	5				(58.5)
Financing and investment income	6				246.1
Financing and investment expenditure	7				(759.3)
Surplus/ (deficit) on discontinued operations					-
Non specific grant income	8				3,337.7
Taxation expense					-
		<hr/>	<hr/>	<hr/>	<hr/>
<b>Surplus/ (deficit) on the provision of services</b>	2				252.5
		<hr/>	<hr/>	<hr/>	<hr/>

## 35 Explanation of transition to Adopted IFRSs

### a) Explanation of transition to Adopted IFRS - Group

#### Reconciliation of equity as at 1 April 2009 (date of transition to IFRS)

<i>Note</i>	UK GAAP £m	Reclassified £m	IFRS Transition Effect £m	Adopted IFRS £m
<b>Non-current assets</b>				
Intangible assets	-	-	37.4	37.4
Property, plant and equipment (Fixed Assets)	a 19,456.0	-	484.5	19,940.5
Investment property	-	-	183.1	183.1
Other Investments	-	-	-	-
Long term debtors (Trade and other receivables)	-	-	-	-
	<u>19,456.0</u>	<u>-</u>	<u>705.0</u>	<u>20,161.0</u>
<b>Current assets</b>				
Inventories (Stock)	20.2			20.2
Short term debtors (Trade and other receivables)	488.4	(8.1)	(9.4)	470.9
Cash and cash equivalents (Cash & Bank)	34.1	1,946.6	-	1,980.7
Short term investments	1,967.8	(1,946.6)	-	21.2
Assets classified as held for sale	-	-	6.5	6.5
	<u>2,510.5</u>	<u>(8.1)</u>	<u>(2.9)</u>	<u>2,499.5</u>
<b>Current liabilities</b>				
Short term creditors (Trade and other payables)	(2,079.2)	385.3	(78.4)	(1,772.3)
Short term Borrowings and overdrafts	-	-	-	-
Short term Finance lease liabilities	-	(368.7)	(815.9)	(1,184.6)
Short term Provisions	-	(28.2)	-	(28.2)
	<u>(2,079.2)</u>	<u>(11.6)</u>	<u>(894.3)</u>	<u>(2,985.1)</u>
<b>Non-current liabilities</b>				
Long term creditors	(2,519.5)	2,479.6	(5.8)	(45.7)
Long term borrowings	(3,017.6)	-	-	(3,017.6)
Long term finance lease liabilities	-	(2,488.7)	160.5	(2,328.2)
Long term provisions	(193.8)	68.7	-	(125.1)
Deferred grants	(8,216.2)	-	8,216.2	-
Retirement benefit obligation	(1,147.5)	(39.9)	-	(1,187.4)
	<u>(15,094.6)</u>	<u>19.7</u>	<u>8,370.9</u>	<u>(6,704.0)</u>
<b>Net assets</b>	<u>4,792.7</u>	<u>-</u>	<u>8,178.7</u>	<u>12,971.4</u>
<b>Reserves</b>				
Usable reserves (General fund and Earmarked reserves)	1,308.0	12.5	(1.6)	1,318.9
Unusable reserves (Other reserves)	3,484.7	(12.5)	8,180.3	11,652.5
<b>Total reserves</b>	<u>4,792.7</u>	<u>-</u>	<u>8,178.7</u>	<u>12,971.4</u>

Descriptions in brackets are UK GAAP headings that were used in the 2009/10 Statement of Accounts

## 35 Explanation of transition to Adopted IFRSs

### a) Explanation of transition to Adopted IFRS - Group

#### Reconciliation of equity as at 31 March 2010 (last date of UK GAAP financial statements)

<i>Note</i>	UK GAAP £m	Reclassified £m	IFRS Transition Effect £m	Adopted IFRS £m
<b>Non-current assets</b>				
Intangible assets	-	-	120.9	<b>120.9</b>
Property, plant and equipment (Fixed Assets)	a 21,629.1	-	338.7	<b>21,967.8</b>
Investment property	-	-	188.3	<b>188.3</b>
Other investments	-	-	-	-
Long term debtors (Trade and other receivables)	-	-	-	-
	<u>21,629.1</u>	<u>-</u>	<u>647.9</u>	<u><b>22,277.0</b></u>
<b>Current assets</b>				
Inventories (Stock)	18.3	-	-	<b>18.3</b>
Short term debtors (Trade and other receivables)	698.6	1.3	(51.0)	<b>648.9</b>
Cash and cash equivalents (Cash & Bank)	36.9	1,472.5	-	<b>1,509.4</b>
Short term investments	1,472.5	(1,472.5)	-	-
Assets classified as held for sale	-	-	6.5	<b>6.5</b>
	<u>2,226.3</u>	<u>1.3</u>	<u>(44.5)</u>	<u><b>2,183.1</b></u>
<b>Current liabilities</b>				
Short term creditors (Trade and other payables)	(2,067.1)	384.5	(42.7)	<b>(1,725.3)</b>
Short term financial liabilities	-	(389.0)	(15.4)	<b>(404.4)</b>
Short term borrowings and overdrafts	-	-	-	-
Short term finance lease liabilities	-	-	-	-
Short term provisions	-	(300.2)	-	<b>(300.2)</b>
	<u>(2,067.1)</u>	<u>(304.7)</u>	<u>(58.1)</u>	<u><b>(2,429.9)</b></u>
<b>Non-current liabilities</b>				
Long term creditors	(2,581.2)	2,552.4	(6.4)	<b>(35.2)</b>
Long term borrowings	(4,117.8)	-	-	<b>(4,117.8)</b>
Long term finance lease liabilities	-	(2,550.0)	(646.8)	<b>(3,196.8)</b>
Long term provisions	(617.2)	352.0	-	<b>(265.2)</b>
Deferred grants	(9,710.5)	-	9,710.5	-
Retirement benefit obligation	(2,142.6)	(51.0)	-	<b>(2,193.6)</b>
	<u>(19,169.3)</u>	<u>303.4</u>	<u>9,057.3</u>	<u><b>(9,808.6)</b></u>
<b>Net assets</b>	<u>2,619.0</u>	<u>-</u>	<u>9,602.6</u>	<u><b>12,221.6</b></u>
<b>Reserves</b>				
Usable reserves (General fund and Earmarked reserves)	1,031.8	11.1	(1.4)	<b>1,041.5</b>
Unusable reserves (Other reserves)	1,587.2	(11.1)	9,604.0	<b>11,180.1</b>
<b>Total reserves</b>	<u>2,619.0</u>	<u>-</u>	<u>9,602.6</u>	<u><b>12,221.6</b></u>

Descriptions in brackets are UK GAAP headings that were used in the 2009/10 Statement of Accounts



## 35 Explanation of transition to Adopted IFRSs

### a) Explanation of transition to Adopted IFRS - Group

#### Reconciliation of the Income and Expenditure statement for the year ended 31 March 2010

	Note	UK GAAP £m	Reclassified £m	Effect of transition to Adopted IFRSs £m	Adopted IFRSs £m
<b>Gross income (Revenue)</b>		3,594.3	-	0.7	<b>3,595.0</b>
Gross expenditure (Expenditure including depreciation of fixed assets and amortisation of deferred capital grants)	a	(5,676.5)	-	(432.0)	<b>(6,108.5)</b>
<b>Net cost of services</b>		<u>(2,082.2)</u>	<u>-</u>	<u>(431.3)</u>	<b><u>(2,513.5)</u></b>
Other operating expenditure (Loss on disposal of assets)		(14.5)	-	(44.0)	<b>(58.5)</b>
Financing and investment income (Finance income)		13.9	241.1	(8.9)	<b>246.1</b>
Financing and investment expenditure (Finance costs)		(390.7)	(339.8)	(28.8)	<b>(759.3)</b>
(Pensions interest cost and expected return on pension assets)		(98.7)	98.7	-	-
Non specific grant income (Revenue grants and precept)		1,367.6	-	1,970.1	<b>3,337.7</b>
Taxation expense		-	-	-	-
<b>Surplus/(deficit) on the provision of services (Deficit/(surplus) for the year)</b>		<u>(1,204.6)</u>	<u>-</u>	<u>1,457.1</u>	<b><u>252.5</u></b>

Descriptions in brackets are UK GAAP headings that were used in the 2009/10 Statement of Accounts

## 35 Explanation of transition to Adopted IFRSs (continued)

### a) Explanation of transition to Adopted IFRS - Group (continued)

#### Reconciliation of the Comprehensive Income and Expenditure Statement for the year ended 31 March 2010

	<i>Note</i>	UK GAAP £m	Reclassified £m	Effect of transition to Adopted IFRSs £m	Adopted IFRSs £m
Surplus/(deficit) on the provision of services (Deficit/(surplus) for the year)		(1,204.6)	-	1,457.1	<b>252.5</b>
Surplus/(deficit) on revaluation of property, plant and equipment (revaluation of fixed assets)		32.8	-	(33.2)	<b>(0.4)</b>
Actuarial losses on defined benefit pension schemes (actuarial losses on pension assets and liabilities)		(1,001.9)	-	-	<b>(1,001.9)</b>
		<hr/>	<hr/>	<hr/>	<hr/>
		(2,173.7)	-	1,423.9	<b>(749.8)</b>
Net change in fair value of cash flow hedges reclassified to profit or loss		-	-	-	-
Other comprehensive income and expenditure		-	-	-	-
Tax on other comprehensive income and expenditure		-	-	-	-
(Prior year adjustments)		377.1	-	8,178.7	<b>8,555.8</b>
<b>Total comprehensive income and expenditure (Total recognised gains and losses recognised since last annual report)</b>		<hr/>	<hr/>	<hr/>	<hr/>
		(1,796.6)	-	9,602.6	<b>7,806.0</b>

Descriptions in brackets are UK GAAP headings that were used in the 2009/10 Statement of Accounts