Department
for Transport

From the Secretary of State
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TRANSPORT FOR LONDON FUNDING AGREEMENT

1. This letter sets out a funding agreement for Transport for London (TfL) for the years 2017/18-2020/21.

2. We continue to have a shared commitment to ensure delivery of the programme of tube upgrades, improvements to London's road network and delivery of Crossrail, all of which are essential not just to London, but to the national economy as a whole. The funding agreement set out in this letter supports essential investment in London's transport while encouraging TfL to deliver ambitious plans to further improve its efficiency, so that it can make an appropriate contribution towards necessary savings in public spending.

3. The Government is committed to supporting you in the delivery of TfL's cost reductions programme and commercial development income, particularly where legislative changes may be needed.

Basis of funding agreement and reviews

4. For the avoidance of doubt, any years quoted in this letter are financial years. This funding agreement replaces any other outstanding funding agreements reached for 2017/2018 onwards. It sets out my present intentions in relation to the Department for Transport's (DfT) funding of TfL for the years 2017/18-2020/21.

5. It also sets out the basis on which this funding is being provided. Except where otherwise expressly indicated, this letter sets out the totality of DfT grant and borrowing support for TfL for 2017/18-2020/21. Although it is my firm intention as Secretary of State to provide the support on the basis described, I cannot give a wholly binding commitment since I cannot fetter my ability, or that of a future Secretary of State, to determine final grant levels as I see fit in response to relevant considerations.

6. This settlement has been determined after consultation with you, as Mayor, and with TfL officials, and takes into account, amongst other things TfL's existing and anticipated spending commitments and potential revenue during this period.

7. It is our shared intention that TfL will manage the financing of the activities across its business and estate within the levels of borrowing and grant funding set out below, and taking into account its other sources of income, including income from fares and non-domestic rates retained by the Greater London Authority (GLA) under the Business Rates Retention (BRR) scheme. These activities include:

   - TfL's transport and corporate activities;
   - Pensions;
   - TfL's obligations toward third parties;
   - PFIs;
   - TfL's Crossrail contribution; and
   - The funding of the Independent Investment Programme Advisory Group.

8. To be assured that the financial support provided to TfL delivers value for money to the taxpayer and to provide independent assurance of TfL's Investment Programme, this settlement assumes your continued commitment to the Independent Investment Programme Advisory Group (IIPAG) whose terms of reference I understand that you are reviewing.

Business Rates

9. The Chancellor announced in the 2016 budget that, as part of the Government's devolution strategy, the Department for Transport would no longer pay any investment grant to the GLA from April 2017. Instead, the GLA will receive an equivalent amount through retention of a larger proportion of London's business rates. The high level principles of this agreement between the Government and the GLA are set out in annex C.

10. As a result of these changes, the existing Investment Grant (CDEL) will cease to be paid by the Department and will instead become part of your business rates income. From April 2017, the GLA will retain an additional amount in business rates that will be sufficient to cover the TfL investment grant as shown in annex C. We continue to expect this money to be used for transport and particularly infrastructure investment as set out in annex C.

11. This approach to investment funding is being piloted by the GLA in advance of the wider changes to the Business Rates Retention Scheme. The Government intends that the piloted approach should be without detriment to the resources that would have been available to the GLA for TfL.

Funding Settlements

12. My firm intention is that, subject to the final grant determination process and taking into account the matters raised below, my Department will provide funding to TfL over the period to 2020/21 as set out in table 1 below. A proposed payment schedule for 2017/2018 is at annex D.

13. This is a change to the previous settlement letter that was sent from the Department for Transport to the Mayor of London on 1 March 2016, to reflect the changes to the Business Rates Retention Scheme in London.

Table 1: summary of funding intentions (all figures in £m cash)

	2017/18	2018/19	2019/20	2020/21
Investment grant (CDEL)	0	0	0	0
General grant (RDEL)	228	0	0	0
LOROL grant	27	27	27	0

Other funding

Borrowing

14. TfL's borrowing to fund capital expenditure is to be contained within the profile in Table 2 below. TfL are able to defer borrowing from one year to the next until they need it, provided they inform the relevant HMT officials at least eight weeks ahead of the end of the financial year in question that they intend to delay borrowing from that year to the next.

15. TfL will also be allowed to borrow for short-term working capital in line with other local authorities as set out in the CIPFA Prudential Code. Otherwise borrowing is only to be used for capital investment. It remains my expectation that TfL will not undertake borrowing in advance of need.

16. In conjunction with these new flexibilities, TfL should continue to engage with the OBR on a six monthly basis and seek to share short-term projections to help enable more accurate forecasts of borrowing and expenditure.

Table 2: TfL prudential borrowing limits

£m (cash)	2017/18	2018/19	2019/20	2020/21
TfL borrowing	950[1]	500	500	600

17. No further borrowing should be undertaken without specific agreement from HM Treasury. Guidance on interpretation of borrowing limits and PFI accounting treatment is set out **at Annex A**.

Deliverables

18. This settlement has been drawn up on the basis that these funding and borrowing limits will allow TfL to take forward its investment programme and deliver **the agreed milestones listed at Annex B**.

[1] This reflects the fact that you have deferred £50m of borrowing from 2016/2017

Crossrail 2

19. The Government remains strongly supportive of the Crossrail 2 project and we have agreed to contribute a total of £80m from the Transport Development Fund to continue the development of the business case for it. TfL have agreed to match-fund this contribution. The profile of annual budgets and governance arrangements for agreeing spending on the scheme development going forward, including how the funds will be transferred, will be agreed in a side letter before the end of FY16/17. For clarity we have transferred £26m from the budget for FY16/17 of £36m.

20. No further commitment to the scheme has been made at this stage and the agreement of a fair, sustainable and deliverable funding settlement will be a prerequisite for the deposit of a hybrid bill.

21. The Department reserves the right to reconsider how the TDF funding is allocated depending on the decision taken on the SOBC by the SoS and central Government.

London Overground

22. In 2017/2018, we will pay the London Overground grant of £27,071m in four weekly instalments alongside the general grant. We will agree at a later date the payment schedule for the London Overground grant in 2018/2019 and 2019/2020.

23. As you know, these payments will cease altogether after 2019/2020 as set out in SR15.

Old Oak Common

24. I note your recent letter requesting amendments to the Memorandum of Understanding agreed between my Department and the Old Oak Common and Park Royal Development Corporation, including for government to fund the enabling works for development around the HS2 station in Old Oak Common. I will consider your request and respond in due course. Any discussion on direct or indirect funding from central government will require a clear rationale given the existing significant government commitments to London and the fact that benefits from development will accrue to London in taxes and jobs. I have asked my officials to work with the GLA to understand the detail of your proposition further.

Croxley Rail Link

25. This funding is also being provided on the assumption that you will continue to take forward the delivery of the Metropolitan Line Extension (otherwise known as the Croxley Rail Link), as agreed by your predecessor. Should you decide not to do this, or should there be significant further delay to the project, the Department would claw back funding that has already been provided to you for it, and adjust future borrowing limits downwards to reflect the fact that you will no longer need to borrow funding for this project.

Air Quality

26. I am grateful to your officials for their input into the update to the National Air Quality Plan for Nitrogen Dioxide, which is currently being developed. I know that we both recognise the importance of delivering compliance with legal obligations on air quality

and I will continue to look to you to take the lead on the measures for London which we agree are necessary as part of the new Plan.

Skills

27. I am grateful to your officials for their collaboration with the Department and infrastructure client bodies on transport infrastructure skills, and for the Commissioner's chairmanship of the Strategic Transport Apprenticeship Taskforce. I know that we both recognise the importance of developing a sustainable pipeline of skills and the role our significant investment can play in leveraging this development across the sector. I will look to you to ensure this collaboration continues.

Rail fares

28. The Government has made a commitment that rail fare increases nationally will be held at RPI inflation over this parliament. This settlement assumes that TfL's income from fares in London will rise broadly in line with your Business Plan assumptions, and the settlement will not be adjusted to take account of any future decisions you make on fares.

Other financial flexibilities

29. HMT will also continue to work closely with TfL and the Department to explore granting TfL some other financial flexibilities. My officials will discuss the detail of this with TfL. Separate discussions are continuing between our officials on the question of whether TfL might also be able to temporarily draw upon some of the Crossrail cash balances held in the Crossrail Sponsor Funding Account (SFA).

Future Reviews

30. As Secretary of State, I reserve the right to review this funding agreement if there is significant deviation from the commitments referred to above. The agreement may also be subject to review in the context of a further government Spending Review or other wider pressures on the Department's finances or those of the Government as a whole, or the emergence of external pressures beyond the control of TfL or GLA, on the TfL budget.

31. In any future review, the Government will take all relevant circumstances into account including:

   a) Delivery of the transport infrastructure milestones listed in Annex B;

   b) Adherence to the agreed borrowing limits in this letter;

   c) The extent to which TfL has managed its business and estate, including the use that TfL and the Mayor have made of their capacity to raise further income and reduce expenditure; and the extent to which any exceptional pressures on TfL's budget could have been, or can be, prevented or alleviated by them;

   d) DfT's public expenditure position and other pressures on the Department's budget and the finances of the Government generally;

   e) Whether TfL has met its existing funding commitments and obligations in relation to the Crossrail project;

f) Amounts available for the GLA to transfer to TfL under the BRR scheme; and

g) The proposed further devolution of business rates in London.

32. I acknowledge that in order to achieve some of the milestones efficiently, TfL will need to enter into contractual commitments that extend beyond 2020/21. The Government will take account of these when considering levels of grant and borrowing headroom in future Spending Reviews.

ANNEX A: GUIDANCE ON INTERPRETATION OF BORROWING LIMITS AND PFI ACCOUNTING TREATMENT

The borrowing limits set out in this letter relate to net additions to borrowing, or other on-balance sheet liabilities, across the TfL Group. Within these overall limits, TfL should manage its liabilities as it sees fit; this may include swapping finance leases (as measured for National Accounts purposes) with borrowing undertaken at the TfL level, subject to there being no overall increase in liabilities across the TfL Group.

Following the adoption of IFRS from 2009/10, HM Treasury has prepared guidance for central Government Departments regarding the budgetary treatment of PFIs. In determining whether PFI transactions undertaken by TfL or its subsidiaries score within the borrowing limits, TfL should take account of the impact of those transactions on the National Accounts rather than the accounting treatment under IFRS. To determine whether a particular transaction should be treated as on or off balance-sheet for National Accounts purposes, TfL should follow the guidance on HM Treasury website: "Consolidated Budgeting Guidance" which is updated each year. TfL should consult with the Department if there is any uncertainty over the interpretation of this guidance. Contracts signed before 2009 will continue to be treated as they were under UK GAAP (as a proxy for the National Accounts framework of the time) for budgeting purposes unless there is a material change to the relevant PFI contract, at which point the PFI contract should be reassessed against the latest framework (currently ESA10) and following the guidance on HM Treasury website "Consolidated Budgeting Guidance".

The Department is aware that changes to the treatment of leases under IFRS are under consideration. No decisions have yet been taken on how such changes, if they were to come about, would affect budgets and borrowing limits in the public sector.

ANNEX B: INDICATIVE INFRASTRUCTURE AND SCHEME DELIVERY MILESTONES

ITEM	MILESTONE	DATE
Part one: short term milestones		
1.	Completion of Phase 1 of Structures and Tunnels Investment Programme which involves major renewal and replacement works on the Capital's most important bridges and tunnels including Highbury corner, Ardleigh Green Bridge, Power Road, Upper Holloway and Fore Street Tunnel	2017
2.	Victoria Station Upgrade – Northern ticket hall complete, including step-free access to all platforms via lifts.	2017
3.	Bond Street station upgrade complete, including a new station entrance and step-free access to all platforms.	2017
4.	Victoria Line Upgrade to 36 trains per hour	2017
5.	Archway Gyratory Better Junctions, construction complete (excluding Despard Road Loading Bay)	2017
6.	London Underground Track renewals: drainage (2,500 metres), track renewal and re-ballast (7,000 metres) and Deep Tube track (2,500 metres)	2018
7.	Elizabeth Line fully open and extends to Reading	2019
Part two: longer term priorities		
8.	Progress the Road Reliability Programme to ensure road assets are fit for the future, including major highways enhancements and phase 2 of the Structures and Tunnels Investment Programme to improve reliability of the road network and reduce congestion.	
9.	Progress investment in healthy streets to improve public spaces and increase walking and cycling (eg cycle network improvements, vision zero, liveable neighbourhoods and Oxford Street Pedestrianisation)	
10.	Progress investment to deliver improvements in London's air quality and carbon footprint, through new infrastructure to enable and incentivise cleaner vehicles (eg ULEZ, Greenwich power station upgrade, Hybrid buses)	
11.	Progress river crossings programme (eg Rotherhithe)	
12.	Progress the delivery of additional capacity on the existing Rail & Underground network through line upgrades and additional capacity programmes (e.g Four Lines Modernisation Programme and Deep Tube Upgrade Programme).	
13.	Progress a number of key line extensions to add new capacity to the Rail & Underground network (e.g. Crossrail 2, Bakerloo Line Extension, Sutton Tramlink Extension, Croydon Tramlink Dingwall Road Loop, Metropolitan Line Extension, Barking Riverside)	
14.	Deliver a programme of Rail & Underground core asset renewals which focuses on the provision of safe and reliable services for customers.	
15.	Progress programme to improve accessibility at tube stations including schemes to deliver 40% fully step-free station access by 2021/22	

Annex C – Business Rates Retention

PILOTING THE APPROACH TO 100% BUSINESS RATES RETENTION IN THE GREATER LONDON AUTHORITY FROM 2017/18

This note sets out the high level principles agreed between the Government and the Greater London Authority (GLA) regarding the Budget 2016 announcement that the GLA will receive an increase in the share of business rates retained from 2017/18 onwards in exchange for the reduction of TfL capital grant.

The Government and the GLA agree that:

1. The TfL Investment Grant (see funding definition in Table 1 below) will cease to be paid to the GLA from April 2017. The GLA will retain an additional amount in business rates from April 2017 that will be sufficient to cover the TfL Investment Grant amounts set out in Table 1 through an increase in the percentage of London's business rates to be retained by the GLA. The GLA will in return take on full responsibility for funding TfL's capital projects (excluding Crossrail 2 which will be subject to a separate funding discussion and any similar strategic or regional transport investment projects the Government may decide to part finance in the future).

Table 1:

£m	2017/18	2018/19	2019/20	2020/21
TfL Investment Grant	960	976	993	1010

2. The sum of retained taxes equivalent to the foregone TfL Investment Grant 2017/18 up to and including 2020/21 is expected to be earmarked for capital projects. The Government expects that this level of funding will continue to be spent on transport capital projects for the years covered by the existing Spending Review letter, and that the Mayor will use the funding to deliver the agreed programme of transport infrastructure investment and other commitments set out in that letter, including the "annex B milestones". Any income in excess of those annual amounts is to be spent at the discretion of the GLA.

3. DCLG, HMT and GLA will work together to ensure appropriate accounting and accountability arrangements for the increase in the share of business rates retained by the GLA.

4. The precise details of the approaches to be piloted are to be worked up between the GLA and the Government over the coming months and will include the development of mechanisms to manage risk and reward under 100% rates retention. In developing pilot approaches to 100% rates retention, Government will work with the GLA and London Boroughs to deal with the financial impacts for London of an increased business rates percentage, including the impact on the GLA's resources of appeal risk, provisions and prior year adjustments. While the GLA accepts the risks and rewards of this increased devolution, the Government intends the piloted approaches to be without detriment to the resources that would have been available to the GLA under the current local government finance regime, meaning that during the course of the pilot the Mayor will have sufficient resources to cover capital investment broadly in line with current levels.

5. The GLA will work with the Government to explore with the 32 London boroughs and the Corporation of London the options for implementing a full 100% retention pilot in London ahead of the implementation of the national reforms, including options for dealing with any potential increase in appeal risk and provisions.

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6. The GLA will support DCLG and the Department for Transport in achieving the necessary legislative changes to the GLA Act 1999, the Local Government Finance Act 1988 and the Local Government Finance Act 2012 and other applicable legislation, and in creating new statutory instruments as necessary.

7. This is an opportunity to pilot approaches to 100% business rate retention and for the GLA to receive some of the benefits of 100% retention ahead of full roll out, but these arrangements do not prejudice the final scheme design for the 100% business rate retention.

Stuart Hoggan

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Department for Communities and Local Government

D. Gallie

David Gallie
Assistant Director, Finance
Greater London Authority

Annex D – Schedule of payments for 2017/2018

Payment no	Period	Amount (£)	LOROL (£)	Date to arrive in GLA bank
1	1 Apr – 30 Apr	17,538,461.50	2,082,385	Mon 6 Apr 2017
2	1 May – 28 May	17,538,461.50	2,082,385	Tue 2 May 2017
3	29 May – 25 June	17,538,461.50	2,082,385	Tues 30 May 2017
4	26 June – 23 July	17,538,461.50	2,082,385	Mon 26 Jun 2017
5	24 July – 20 Aug	17,538,461.50	2,082,385	Mon 24 Jul 2017
6	21 Aug – 17 Sept	17,538,461.50	2,082,385	Mon 21 Aug 2017
7	18 Sept – 15 Oct	17,538,461.50	2,082,385	Mon 18 Sept 2017
8	16 Oct – 12 Nov	17,538,461.50	2,082,385	Mon 16 Oct 2017
9	13 Nov – 10 Dec	17,538,461.50	2,082,385	Mon 13 Nov 2017
10	11 Dec – 7 Jan	17,538,461.50	2,082,385	Mon 11 Dec 2017
11	8 Jan – 4 Feb	17,538,461.50	2,082,385	Mon 8 Jan 2018
12	5 Feb – 4 March	17,538,461.50	2,082,385	Mon 5 Feb 2018
13	5 Mar – 30 Mar	17,538,461.50	2,082,380	Mon 5 Mar 2018
		228,000,000	27,071,000	

With best wishes

Rt Hon Chris Grayling MP

SECRETARY OF STATE FOR TRANSPORT