TRANSPORT FOR THE NORTH

Transport for the North Board Meeting – Item 6

Subject:	Financial Position as at Quarter 4 & Outturn, Financial Year 2017/18
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Meeting Date:	Thursday 28 June 2018

1. Executive Summary:

1.1 This report provides an update on Transport for the North's financial position as at Quarter 4 and the outturn of financial year 2017/18.

1.2 The report highlights that at Quarter 4 Transport for the North underspent against its Revision 3 budget by £1.24m. This represents an underspend of 5% on the adjusted budget adopted in January by the former Transport for the North Commissioning Board, contributing to a £10.75m underspend against the original base budget.

1.3 The report further highlights that this Quarter 4 position was primarily driven by net underspends in Transport for the North's programme areas.

1.4 Reversing an in-year trend of slipped costs, the Northern Powerhouse Rail (NPR) programme saw future year activity accelerated into Quarter 4 to support the timely delivery of the strategic outline business case (SOBC), at a cost of £0.58m.

1.5 These additional costs were, however, more than offset by slippage of £1.67m in the Integrated & Smart Ticketing (IST) programme, as anticipated capital costs in support of the ITSO on Rail project moved into the new financial year following contracting difficulties.

1.6 At financial close, Transport for the North ended the year with £5.7m of uncommitted core cash reserves, set against the £5.5m target balance agreed as part of the budget setting process.

1.7 This report asks the Board to note the 'carry-forward' of resource into financial year 2018/19 relating to slipped 2017/18 activity. Carrying resource forward into the new budgetary period matches funding to activity costs, allowing activity that should have taken place in financial year 2017/18 to progress.

2. Recommendation:

2.1 This report provides an update on Transport for the North's financial position at the end of financial year 2017/18.

2.2 This position includes both the Quarter 4 position against the budget adopted at Revision 3, and the full-year position against the opening budget.

2.3 The report details financial performance in both the programme and operational areas, setting out information at both an activity and cost type level.

2.4 The report also provides an analysis of Transport for the North's cash and funding position as at the end of financial year 2017/18, noting the impact of slipped activity on the agreed 2018/19 budget.

3. Issues:

3.1 Transport for the North Board is asked to note the Quarter 4 outturn underspend of £1.24m against the Revision 3 budget.

3.2 Transport for the North Board is asked to note that this Quarter 4 position contributes to a full-year underspend of £10.75m against the opening 2017/18 base budget position.

3.3 Transport for the North Board is asked to note that the Quarter 4 position is principally driven by a net underspend due to activity and cost slippage.

3.4 Transport for the North Board is asked to note that this slippage impacts upon the amount of activity to be delivered in financial year 2018/19, and the resource required to deliver that activity.

3.5 Transport for the North Board is asked to note £2.29m of activity from 2017/18 that was not completed in the final quarter and which is being completed in 2018/19. This is funded using the resources that were earmarked to deliver it in 2017/18. This will be formally recognised in Budget Revision 1 that will be brought to the September board.

4. Discussion:

Financial Year 2017/18 Budget Summary

4.1 Transport for the North's budget for financial year 2017/18 was first agreed by Commissioning Board in February 2017. Over the course of the year the budget was amended at each quarter as part of the revision process, taking account of changes to assumptions and adjustments to delivery models and timescales.

4.2 Transport for the North's outturn expenditure of £25.53m placed it £1.24m (5%) under the final 'Revision 3' budget adopted in January 2018, but more significantly £10.75m (40%) behind the opening 'base' budget.

4.3 The following table highlights how the overall budget was consistently revised down over the course of the year:

Budget Stage	Total £m	Variance to Prior Budget £m	Variance to Prior Budget %	Variance to Base £m	Variance to Base %
Base	£36.28	-	-	-	-
Revision 1	£34.57	£1.71	5%	£1.71	5%
Revision 2	£29.35	£5.22	15%	£6.93	20%
Revision 3	£26.77	£2.58	9%	£9.51	32%
Outturn	**£25.53**	**£1.24**	**5%**	**£10.75**	**40%**

4.4 These downward revisions were principally driven by adjustments to activity and cost assumptions in the programme areas.

4.5 As the following table shows, £10.53m (98%) of the £10.75m underspend against the base budget arose in the programme activity associated with NPR, IST, and the Strategic Development Corridors:

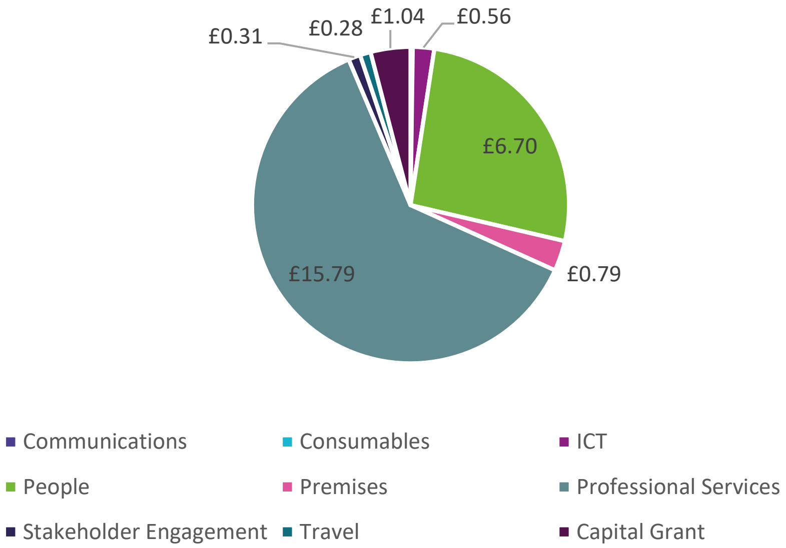
	Base £m	Outturn £m	Variance £m	Variance %
Programme areas	£27.09	£16.56	£10.53	39%
Operations areas	£9.19	£8.97	£0.22	2%
Total Budget	**£36.28**	**£25.53**	**£10.75**	

4.6 This is set in context against the relatively immaterial underspend of 2% against the base budget in the 'operations' areas, covering the back, middle, and front office teams of Transport for the North.

4.7 These underspends reflect the complexity of running major programmes, and their sensitivity to both internal and external factors whilst in their developmental stage.

4.8 They also underscore the importance of differentiating between major programme financial performance, and that of the organisation's operations areas. Without such a differentiation, the relative scale of the programme areas makes it difficult to view the smaller - but no less important - movements within the wider running of Transport for the North's organisational infrastructure.

4.9 At outturn, the distribution of expenditure around cost types reflects the nature of Transport for the North's business model as a commissioning organisation. Costs are heavily centred around professional service contracts, and people costs such as salaried officers and agency and contractor support:



4.10 This report will analyse Transport for the North's financial performance at the programme and operations level. Outturn performance will be measured against the Revision 3 budget as the last iteration of the 2017/18 budget and the opening base budget for overall reference.

Programme Performance

4.11 The programme areas consist of the following workstreams:

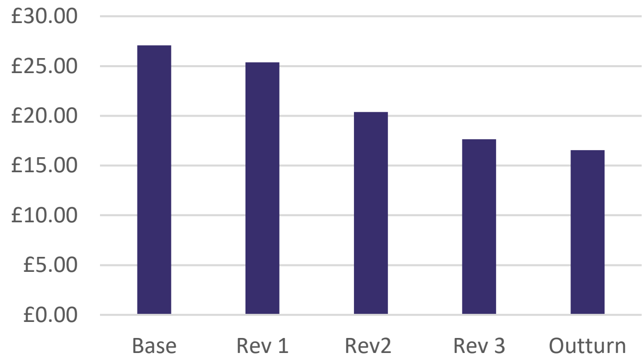
a) Major Roads;
b) Northern Powerhouse Rail (NPR); and,
c) Integrated and Smart Ticketing (IST)

4.12 These programme areas made up the significant bulk of the Transport for the North financial budget in 2017/18, and movements within the areas consequently had a significant impact on the overall budget.

4.13 The 2017/18 base budget saw the programme areas account for £27.09m (75%) of the overall Transport for the North budget:

2017/18 Programme Areas	Base £m
Major Roads	£0.61
Northern Powerhouse Rail	£12.94
Integrated & Smart Ticketing	£13.54
	£27.09

4.14 Over the course of the year however, the forecast expenditure levels for the programme areas was consistently revised down to the final outturn position of £16.56m, as the following graphic shows:



4.15 There were three principal factors that have affected this net downward trend over the course of the year.

4.16 These factors include savings made from delivering activity below budget; slippage from delayed activity that will now fall into future periods; and, additional activity and associated costs which offset some of the underspend. These factors include:

a) The addition of three Strategic Development Corridor studies in April 2017, which increased the Major Roads budget by £1.6m;

b) The successful completion of elements of the NPR Sequence 3 Phase 2 rail studies under budget, and the delays to the remitting of other work packages; and,

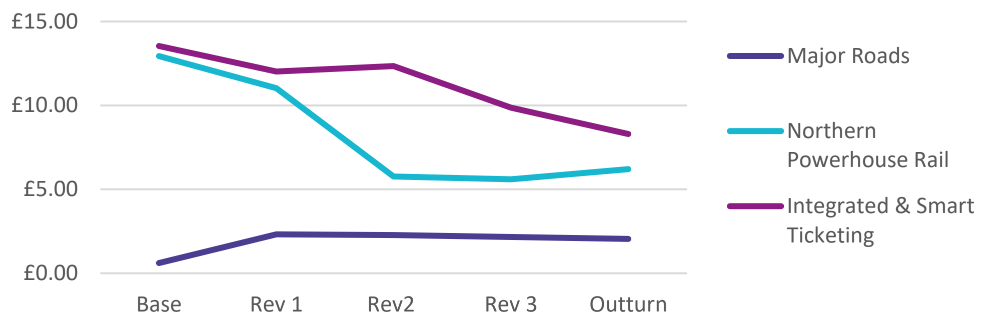
c) Delays to the passage of the IST tranches through the government gateway approval processes, and notable delays in the agreement of franchise side agreements with train operating companies for the Tranche 1 ITSO on Rail project.

4.17 By the end of the financial year, programme area expenditure had fallen £1.08m behind the latest budget adopted at Revision 3, and £10.53m behind the opening base budget.

4.18 Though the variance to the base budget remains significant (at 40%), the following graphic usefully highlights that the Revision 2 budget adopted at the mid-year mark largely arrested variations in the Major

Roads and NPR areas, with material uncertainty persisting in the IST area:

4.19



4.20 At Quarter 4, the programme areas underspent against the adopted Revision 3 budget by £1.08m, and £10.53m against the opening position.

4.21 The Quarter 4 position represents a net number. That is, some areas had costs above budget, offset by others below budget. The following table highlights this point:

2017/18 Programme Outturn Variances	Outturn £m	Revision 3 £m	Variance £m	Variance %
Northern Powerhouse Rail	£6.20	£5.60	-£0.60	-11%
Highways	£2.06	£2.17	£0.11	5%
Integrated & Smart Ticketing	£8.30	£9.86	£1.57	16%
Total	**£16.56**	**£17.64**	**£1.08**	**6%**

4.22 This net underspend position consists of a number of movements set out below:

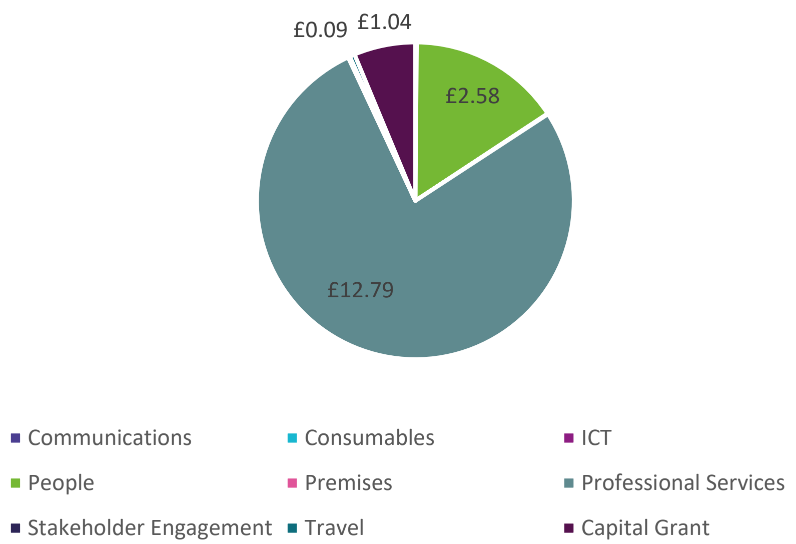
Programme Variance Analysis	Slippage £m	Savings £m	Accelerations £m	Total £m
Northern Powerhouse Rail	-	£0.04	-£0.63	-£0.59
Integrated & Smart Ticketing	£1.67	-	-£0.11	£1.56
Highways	£0.11	-	£0.00	£0.11
Total	**£1.78**	**£0.04**	**-£0.74**	**£1.08**

4.23 Slippage represents planned activity that was delayed, and will now fall into financial year 2018/19. Savings have principally arisen from staffing underspends, the resource for which is now available for redeployment. Accelerations represent planned future work that has been brought forward for operational reasons.

4.24 The following table usefully highlights that the principal variance on programme expenditure is around the forecasts for IST capital grant expenditure (for payments made to the TOCs), offset by an increase in professional service costs associated with the NPR programme delivery:

Programmes Outturn - Cost Types	Outturn £m	Revision 3 £m	Variance £m	Variance %
Communications	-	-	-	50%
Consumables	-	-	-	26%
ICT	£0.02	£0.02	£0.01	23%
People	£2.58	£2.57	-£0.01	0%
Premises	£0.01	£0.01	-	-67%
Professional Services	£12.79	£12.23	-£0.55	-5%
Stakeholder Engagement	£0.03	-	-£0.03	-614%
Travel	£0.09	£0.09	-	-
Capital Grant	£1.04	£2.71	£1.67	62%
Total	**£16.56**	**£17.64**	**£1.08**	

4.25 At outturn, the cost distribution principally reflects the nature of the programme areas where studies and development support are provided to Transport for the North by partner organisations (such as the Network Rail contract) and external professional providers:



4.26 This report now provides narrative for each of the programme areas in more detail.

Major Roads

4.27 The Major Roads programme area’s opening budget stood at £0.6m before £1.6m was added to resource the completion of three Strategic Development Corridor Studies.

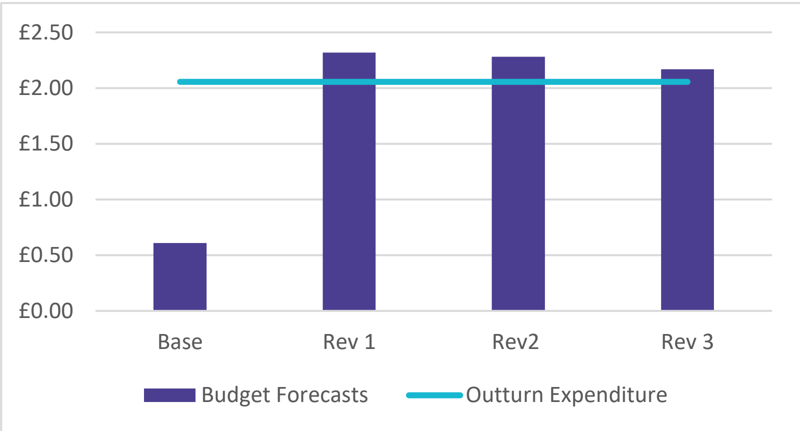
4.28 This activity was the principal driver of expenditure within the area over the course of 2017/18, supported by a number of complementary modelling and appraisal studies.

4.29 Between Quarter 1 and Quarter 3, revised profiling of activity and costs within the studies led to a £0.11m year-to-date underspend.

4.30 In Quarter 4, the drivers of this underspend were largely mitigated with the majority of activity and costs catching up with forecast. However, a £0.08m modelling commission scheduled to commence in Quarter 4 slipped entirely out of the financial year.

4.31 This activity now falls into Quarter 1 financial year 2018/19, attracting irrecoverable VAT costs at 20%.

4.32 The following graphic shows the budget forecasts for the area over the course of the year, set against the outturn position:



Northern Powerhouse Rail

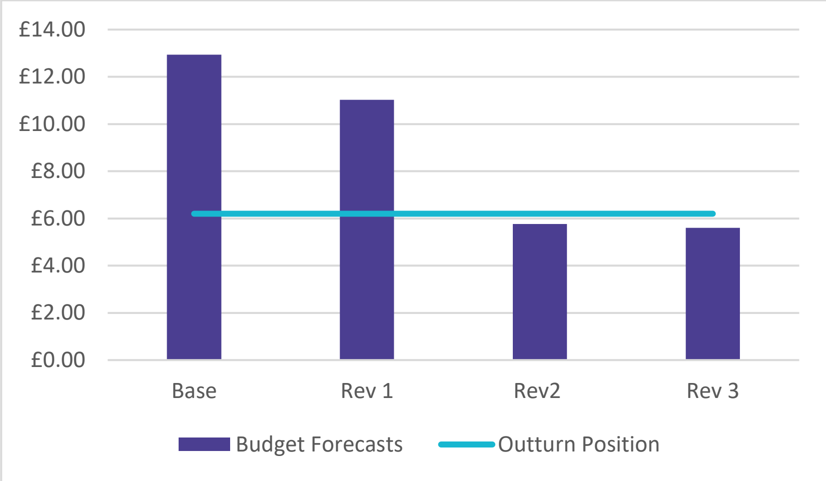
4.33 In 2017/18 the costs of the NPR programme were principally driven by a contract with Network Rail for the delivery of rail studies in support of the NPR SOBC.

4.34 Over the year, this work was centred on Sequence 3 Phase 2 activity.

4.35 Network Rail are remitted to deliver studies through co-clienting arrangements between Transport for the North and the Department.

4.36 The complex nature of the studies, and the challenges of the formative remitting governance arrangements, meant that it was particularly difficult for Network Rail to forecast both the overall cost of activity and when costs will fall.

4.37 As the following graphic shows, early expectations on full-year expenditure were significantly higher than that achieved at outturn:

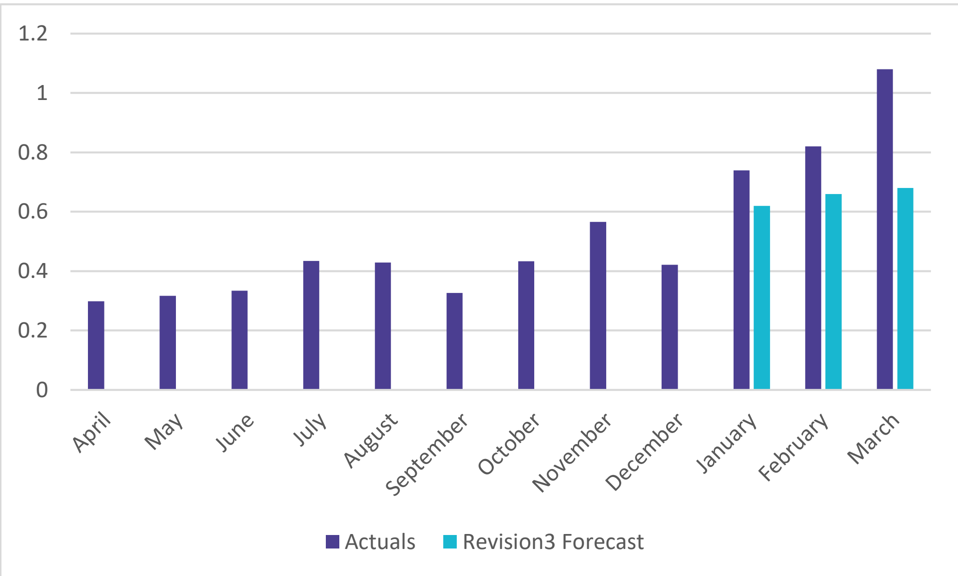


4.38 The graphic shows that the full year expenditure forecast adopted in the opening budget of £12.94m was optimistic, being corrected at Revision 2 to what was felt to be a more prudent assumption of £5.76m.

4.39 The write-down in total forecast expenditure reflected two key points:

a) Efficiencies in the delivery of some elements of the activity, meaning that Network Rail was able to complete the works without the expected need for support from sub-contractors; and,
b) Delays to the commencement of activity planned for the latter half of the year, and in particular the commissioning of Mott McDonald to take forward much of the activity.

4.40 The Revision 3 budget adopted in January planned for a modest increase in Network Rail costs associated with the increase in tempo once remitting issues had been resolved. However, in Quarter 4, activity and costs accelerated beyond the budget forecast:



4.41 This variance reflects that Network Rail and the co-clients adopted an Integrated Delivery Plan (IDP) for the residual Sequence 3 Phase 2 works after the Revision 3 budget had been agreed.

4.42 The IDP allowed for a greater level of activity to be delivered than had been originally forecast, delivering a commensurate increase in costs. This increase in costs does not represent an overspend, but an acceleration of activity and costs from future accounting periods.

4.43 As the work is required to deliver the NPR SOBC in a timely manner, Transport for the North and the co-clients adopted the IDP.

Integrated & Smart Ticketing

4.45 IST budget assumptions fluctuated throughout the year 2017/18 due to two principal issues:

a) How quickly Phase 3 could pass government's OBC gateway; and
b) How quickly Phase 1 ITSO on Rail activity could be operationalised through the conclusion of Franchise Side Agreements with the train operating companies (TOCs).

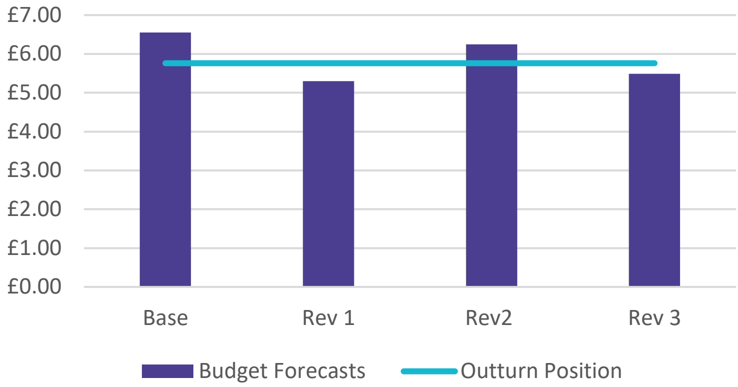
4.46 In particular, revenue cost forecasts have varied as officers tried to understand the implications of delays to Tranche 3 achieving OBC approval. Delays to OBC approval affected both the cost mix of the programme, and how those costs could be funded.

4.47 Simply, post OBC, different types of support will be required by the programme team than before, and to a different scale. Equally, post OBC costs fall to be capitalised, as there is a sufficient reason to believe that the activity and associated costs will lead to future economic benefit from the creation of an asset.

4.48 This issue persisted throughout the year. At Revision 3, it was assumed that Phase 3 would achieve OBC sign-off by March 2018, however by the year-end this assumption had been re-set to May 2018.

4.49 This had multiple effects. Principally, it meant that Phase 3 costs that were scheduled to be capitalised in March fell to be funded by revenue resource. It also meant that there was an on-going need for external professional services to continue the development work in support of the OBC submission.

4.50 The following table shows the budget forecasts for IST revenue expenditure over the course of the year, set against the outturn position, highlighting that though revenue expenditure was below the opening budget value it was above the forecasts of the adopted Revision 3 budget:

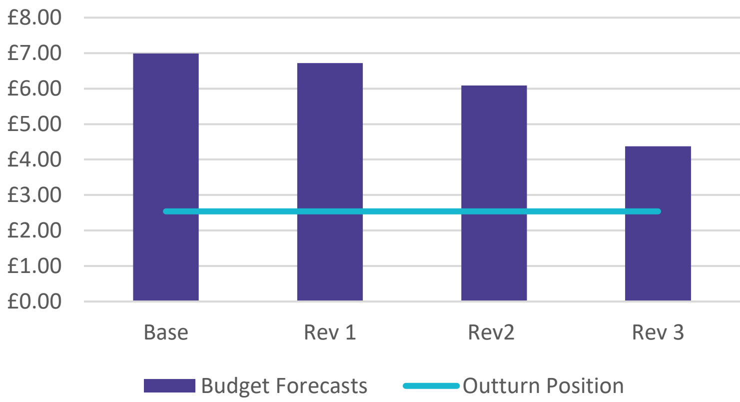


4.51 IST revenue expenditure was funded in year by £3.2m of revenue programme grants, with the balance coming from 'core' grant allocations.

4.52 Similarly, the budgets adopted throughout 2017/18 forecast significant Quarter 4 capital expenditure, as Transport for the North was forecast to advance the TOCs capital grant to support the ITSO on Rail Phase 1 delivery.

4.53 However, difficulties in contracting for the FSAs impacted on procurement and delivery timescales, pushing activity and costs into financial year 2018/19.

4.54 The following graphic shows how significantly capital cost assumptions have changed over the course of the year:



4.55 The graphic highlights that it wasn't before the Revision 3 budget was adopted in January that material adjustments began to be made to the forecast total capital expenditure. This reflected that by January, the ITSO on Rail project was already behind schedule in agreeing FSAs with the TOCs. However, there was still an assumption that time could be made up.

4.56 By the February of Quarter 4, an agreement was reached for Rail North Ltd to sign FSAs with Transpennine Express and Arriva Northern, and for West Yorkshire Combined Authority to sign a memorandum of understanding with Merseytravel.

4.57 Although the completion of these documents allowed for activity to commence, the delays accrued impacted upon procurement processes, pushing activity and expenditure into financial year 2018/19.

4.58 By the year-end total capital expenditure of £2.54m was accrued against the initial budget estimation of £6.99m, representing an adverse variance of £4.54m (64%).

Operations Performance

4.59 The operations area cover the front, middle, and back office teams and functions of Transport for the North. These areas areas represent the functions familiar to any organisation, which facilitate the delivery of the major programmes.

4.60 At outturn the programme areas underspent against the Revision 3 budget by £0.16m (2%), and £0.22m against the opening budget position (2%).

	Operations £m	Variance to Prior Budget £m	Variance to Prior Budget %	Variance to Base £m	Variance to Base %
Base	£9.19				
R3	£9.13	£0.06	1%	£0.06	1%
Outturn	£8.97	£0.16	2%	£0.22	2%

4.61 These relatively immaterial variances have arisen on a net basis, with underspends in some teams offsetting cost accelerations in other areas:

Operations Variances	Outturn £m	Revision 3 £m	Variance £m	Variance %
Finance	£2.50	£2.35	-£0.15	-6%
Business Capabilities	£2.56	£2.61	£0.05	2%
Programme Management Office	£0.47	£0.46	-	-1%
Leadership	£0.22	£0.22	-	-2%
Rail North	£0.32	£0.42	£0.10	23%
Analysis, Modelling & Economics	£1.92	£2.06	£0.15	7%
Strategy & Policy	£0.99	£1.01	£0.03	3%
Total	**£8.97**	**£9.13**	**£0.16**	**2%**

4.62 The following table further highlights the net movements that occurred, with total costs being impacted by slippage of activity and costs being brought forward from future periods:

Variance Analysis	Operations £m
Slippage	£0.24
Savings	£0.27
Accelerations	-£0.34
Total	**£0.16**

4.63 Costs were accelerated in a number of areas to assist with operational delivery. This includes the implementation of the back-office ERP system (£0.25m), the delivery of additional processing capacity to enable the modelling teams to run timely iterations of their data models in support of the NPR SOBC (£0.04m), and investment in Skype telephony to save on more expensive landline systems (£0.04m).

4.64 Cost accelerations have been made possible due to genuine savings (£0.27m) which release available budget, and the slippage of activity and associated costs which makes cash available in-year (£0.24m).

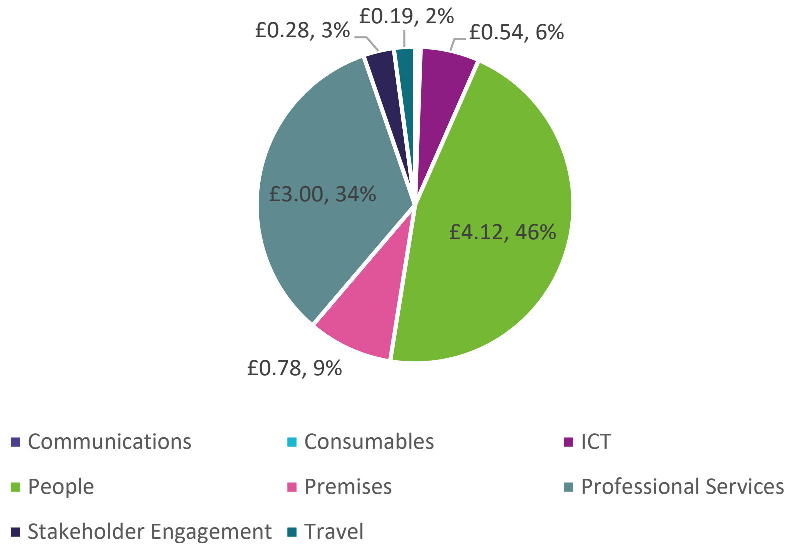
4.65 It is important to note that accelerated costs do not represent overspends. An overspend has a lasting budget impact, reducing available resource. A cost acceleration is simply a reallocation of an existing budgeted cost from one accounting period to another.

4.66 Accordingly, accelerating costs into future periods frees up future year budgets to deal with emerging priorities and cost pressures.

4.67 In year savings were generated principally from vacancy control and lower than forecast need for professional services over the final quarter of the year.

4.68 Slippage on professional services commissions have arisen in a number of areas, but principally centre on the Modelling and Economic Appraisal function (£0.16m) and the Rail North team (£0.07m). This slipped activity will now fall to be completed in financial year 2018/19, and attract irrecoverable VAT costs.

4.69 Costs in the operational area differ from those in the programme areas in that they have a higher concentration of people costs and a much lower level of professional services. People costs include salaried officers, and agency and contractor roles. The following chart shows the distribution of costs as at outturn:



Cash & Funding

Cash & Funding Background

4.70 Transport for the North's resource in 2017/18 came entirely from DfT grant.

4.71 Grant itself came in different forms and can be differentiated by:

a) Whether it was discrete funding for specific activity, or general resource over which Transport for the North has discretion; and,
b) Whether it was grant for capital or revenue expenditure.

4.72 Because Transport for the North's separate grants come with differing conditions, Transport for the North is required to operate distinct funds and be able to evidence how it has drawn down upon them to meet expenditure.

4.73 Transport for the North is permitted to carry-forward unused grant resource from one year to the next, with the consent of the Department.

4.74 As part of the budget setting process for 2018/19 the Department agreed that Transport for the North would aim to outturn at the end of financial year 2017/18 with 'core' grant reserves of not less than £5.5m.

4.75 This balance has accrued over the last two years, reflecting misalignment between the availability of core grant and the profiling of its costs during the mobilisation and establishing of Transport for the North as an STB.

4.76 That balance of reserves would then, in part, be drawn upon over the coming two years to support a managed reduction of the need for 'core' funding, until the budget stabilised at a level that could be resourced from the annual core allocation of £10m.

4.78 Central to Transport for the North's agreed prudent reserve-strategy, £2m of the reserve would then be retained as a cash buffer to both guard against financial shock and provide a balance of resource to meet un-budgeted opportunities that may arise.

Outturn Position

4.79 Transport for the North can present its outturn position on both a cash and funding position. The difference between the two represents commitments that are made on cash that has yet to be used to settle obligations.

4.80 On a cash basis, Transport for the North retained £15.41m at outturn. This position reflects a balance of cash brought forward of £20.98m and cash expenditure of £22.94m:

Outturn Position Cash Basis	Core £m	TDF* Rail £m	TDF Roads £m	IST – Rev. £m	IST - T1 Cap. £m	IST – OBC† Cap. £m	Total £m
Balance b/f	16.60	1.89	0.64	0.00	0.00	1.85	20.98
Cash Expenditure in Year	-17.80	-5.60	-0.64	-3.20	-0.47	-0.81	-28.51
Cash Receipts in Year	10.00	5.74	0.00	3.20	4.00	0.00	22.94
Balance c/d	**8.80**	**2.04**	**0.00**	**0.00**	**3.53**	**1.04**	**15.41**

**Transport Development Fund*
†Outline Business Case

4.81 The cash basis does not reflect the need for cash to settle accrued expenditure. That is, costs that have been incurred but not yet paid for.

4.82 At outturn, Transport for the North accrued for expenditure totalling £6.31m. Adjusting for this reduces Transport for the North's uncommitted resource to £9.10m:

Outturn Position - Accruals Basis	Category £m	Bal b/f £m	Receipts £m	Expend. £m	Bal c/d £m
Core Funding	Revenue	£9.25	£10.00	-£13.08	£6.17
Transport Development Funding - NPR	Revenue	£0.33	£5.74	-£6.44	-£0.37
Transport Development Funding - Roads	Revenue	£0.26	-	-£0.26	-

IST - Development	Revenue	-	£3.20	-£3.20	-
Total Revenue		**£9.84**	**£18.94**	**-£22.99**	**£5.79**
IST - OBC Development	Capital	£1.85	-	-£0.93	£0.92
IST - ITSO on Rail	Capital	£0.00	£4.00	-£1.61	£2.39
Total Capital		**£1.85**	**£4.00**	**-£2.54**	**£3.31**
Total Funding		**£11.69**	**£22.94**	**-£25.53**	**£9.10**

4.83 The above table usefully highlights that Transport for the North is overdrawn on its TDF NPR funding. This reflects the acceleration of the Network Rail Sequence 3 Phase 2 activity beyond the Revision 3 budget forecast.

4.84 The Department has agreed to fund this activity, and Transport for the North will draw down upon cash from grant to resource the expenditure as it is required.

4.85 The accruals basis reflects Transport for the North's true resourcing position, as it takes account obligations Transport for the North must settle.

4.86 However, it is also useful to consider the impact of slippage on the funding position. Slipped activity will generally still need to be carried out, albeit in the new financial year. Accordingly, the year-end cash and funding position is effectively over-stated by the resource that would have otherwise been used had activity proceeded to plan.

4.87 Adjusting for slippage shows that Transport for the North's uncommitted resource is lower still, at £6.35m:

Cash & Commitment	**Core**	**TDF Rail**	**IST - T1 Capital**	**IST - OBC Capital**	**Total**
	£m	**£m**	**£m**	**£m**	**£m**
Outturn Cash Position	£8.80	£2.04	£3.53	£1.04	£15.41
Accrued Expenditure	-£2.64	-£2.41	-£1.14	-£0.11	-£6.31
Cash less Accruals	**£6.16**	**-£0.37**	**£2.39**	**£0.93**	**£9.10**
Slippage from Revision 3	-£0.23	-£0.12	-£1.67	-	-£2.02

Slippage between Revision 3 & Budget	-£0.13	-£0.14	£0.00	-	-£0.27
Total Slippage	-£0.36	-£0.26	-£1.67	-	-£2.29
VAT on Slippage	-£0.07	-£0.05	-£0.33	-	-£0.46
Balance c/d	**£5.73**	**-£0.69**	**£0.38**	**£0.93**	**£6.35**

4.88 Whilst the resources exist to manage the slipped activity and costs, it is unbudgeted. That is, the 2018/19 budget does not take account of the need for the activity, as it envisaged the activity being undertaken in the prior year.

4.89 To deal with this, this paper notes that at the September Transport for the North Board a recommendation will be brought to approve an extension to the existing 2018/19 budget ceiling for 'carry-forwards' of the un-used resource and activity. This will allow the activity to be undertaken in 2018/19, with resource being allocated to fund it.

4. Options Considered:

4.1 This is a monitoring report and no recommendations for action are presented.

5. Considerations:

5.1 This is a monitoring report and no recommendations for action are presented.

6. Preferred Option:

6.1 This is a monitoring report and no recommendations for action are presented.

Appendices:

None.

List of Background Documents

Required Considerations

Please confirm using the yes/no options whether or not the following considerations are of relevance to this report.

Equalities:

Age	~~Yes~~	No
Disability	~~Yes~~	No
Gender Reassignment	~~Yes~~	No
Pregnancy and Maternity	~~Yes~~	No
Race	~~Yes~~	No
Religion or Belief	~~Yes~~	No
Sex	~~Yes~~	No
Sexual Orientation	~~Yes~~	No

Environment and Sustainability

~~Yes~~	~~No~~

Legal	~~Yes~~	No
Financial	Yes	~~No~~
Resource	~~Yes~~	No
Risk	~~Yes~~	No
Consultation	~~Yes~~	No