Transport for London

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Tom Scholar
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Dear Tom

COVID-19 TfL Emergency Budget & Immediate Funding Request

I am writing to make you aware of the urgent need to resolve emergency grant funding for Transport for London.

As you are aware, we are continuing to provide transport services to enable essential journeys in London, particularly by NHS staff. But the impact of the COVID-19 crisis on TfL's finances has been, and continues to be, catastrophic; and this is now putting those services at significant risk.

We are engaging in constructive discussions on funding support with the Department for Transport and whilst on 12 April we received a helpful initial letter from the Permanent Secretary committing to work with us, no quantified funding support is yet in place. This is now an urgent and critical issue that will have devastating economic and other consequences unless resolved.

TfL is a relevant authority for the purposes of Part VIII of the Local Government Finance Act 1988 and is obliged to produce a balanced annual budget. Without confirmation of grant support within the next few days, we will have no prospect of being able to balance our budget this year and will have to take action under Section 114 of the Local Government Finance Act 2008 and issue a report that will necessarily outline the requirement to impose immediate spending restrictions and bring services down to the statutory minimum.

Since the loss of Government grant some years ago, approximately 80% of TfL's £6bn revenue per annum comes from passenger fares income, driven by demand; advertising revenues, driven by footfall across our estate; and congestion charge income and property rentals, both of which have been temporarily suspended during the crisis.

We are actively encouraging our passengers not to travel unless absolutely necessary, to support the Government's position, in accordance with Public Health England advice. Since the beginning of the crisis, TfL's passenger numbers have fallen significantly - tube travel is down by 95% and bus travel down by 85%. You will be familiar with this from the daily COBR charts. Our modelling, informed by the Government commissioned work by Imperial College, shows that in a central scenario (assuming some easing of lockdown measures over the next six months), TfL could lose up to £4bn in income over a the course of the next year alone, with further impacts persisting in the medium term. Other scenarios show worse effects - the length of the shutdown is very uncertain, as is the trajectory of how these revenues may recover.

We are doing, and will continue to do, what we can to reduce our costs to mitigate this loss of revenue. But public transport is a classic example of a high fixed cost base, and while the system is open, the ability to reduce costs is small. Notwithstanding this, we have placed over 7,000 staff on furlough across the organisation, including over 4,000 in London Underground, and have identified over £400 million in gross operating cost savings and £500 million in capital expenditure that can be deferred.

We need grant support, for a temporary period only, to rebuild our operating account, remain a going concern and meet our statutory obligations in relation to a balanced budget. Last week, we presented the Department for Transport with an Emergency Budget that sets out the need for approximately £2bn of grant funding until the end of September, after taking into account the cost mitigations outlined above and ensuring that sufficient services can be run, where practicable, so that we can maximise our ability to manage any social distancing that might be required. This will be a significant challenge on our network and my team is working closely with the Department for Transport to examine how this might be achieved.

Outside London, Train Operating Companies, light rail and bus operators and local authorities have all recently been given very clear financial assurances about grant funding in recognition that public transport services are needed to enable critical workers such as NHS, emergency services and food supply chain to function effectively at this time of national crisis.

It is extraordinary that TfL, whose integrated public transport system is classed as part of the UK's critical national infrastructure, is in a position where it does not have a clear unequivocal statement of Government support or any assurance that Government will not stand by and do nothing whilst this immense loss of revenue is being sustained.

Before the crisis, we had a prudent level of cash reserves of around £2.2bn based upon the risks we faced at that time, including the likely impacts of Brexit, pressures on Crossrail and general softening of demand and slowing of the economy. At that time, our credit rating agencies viewed this as only "adequate" and despite access to the PWLB, have highlighted TfL's liquidity as an ongoing risk. The loss of revenue we are now suffering means these cash reserves are being exhausted quickly – it costs us £600m every four weeks to run the network.

In the last week alone, our cash reserves have fallen below the level deemed prudent for an organisation of our size and structure to deal with strategic risks. Within the next week, we will have used over £1bn of our cash and our reserves will have fallen to £1.2bn, equivalent to 60 days operating expenditure, the minimum required by the credit rating agencies. What this really covers is our debt service costs and enough for only one month's payroll costs. If we go below this, our credit rating will be downgraded (potentially quite severely) which will lead to issues and inevitable costs around debt default and the risk of action by the Pension's Regulator. By June, we will run out of cash completely.

It is important to remember that TfL is not a private business – it does not have shareholders from which it can raise additional funding. Borrowing is also not an option. By law, we are not allowed to borrow for operating purposes (i.e. to replenish lost revenues). Even before the crisis, TfL had significant debts of over £11bn and an extremely limited flexibility to take on more borrowing. With no passenger fares income or certainty in long term forecasts, and no underlying support, we simply cannot borrow - there is no way for us to deem additional borrowing either prudent or affordable in the medium to long term.

The Mayor retains a share of business rates under devolution arrangements and passes those on to TfL as a grant. He will continue to do that, to the extent he is able, backed by the support the Government is giving to local authorities. But he has only very limited flexibility to find additional money for TfL. In 2020-21 we expect funding of £1.88 billion in total, which is 78% of the total rates retention income budgeted to be allocated by the Mayor for the Greater London Authority (GLA) group. There is also a small payment, £6 million, out of the Mayor's council tax precept. The GLA is protected from the business rate reliefs which the Government has offered to the retail and hospitality sectors, as these are matched by payments of grant. But the GLA is exposed, through the London pool, to changes in the overall levels of business rates paid. Detailed modelling work is being undertaken by the GLA, London Councils and the London Boroughs on the impact on London's collective business rates pool but initial estimates are that the loss of business rates to the GLA in 2020-21 could be around 10% of the total budgeted income, which pro-rata could reduce TfL's income from business rates by over £170 million.

The GLA's other income from business rates and council tax is overwhelmingly allocated to the Metropolitan Police Service and given their critical importance during this crisis and the well documented pressures on these services, it is not feasible to make any material reallocations of funding to TfL. In these circumstances, it would be unrealistic to assume that the GLA can contribute additional funding to help resolve TfL's revenue deficit, as it will be facing significant challenges just trying to meet its existing commitments to TfL and also maintain its revenue support to the Metropolitan Police and London Fire Brigade, particularly if there is a reduction in council tax revenues.

Fares increases in the short term do not produce sufficient revenue to offset the loss of revenue suffered as a result of the crisis, even if demand levels return to normal. It is also that case that fares increases now, whilst travel restrictions are in place, would only penalise those groups of people who are still using our services including key workers and other vulnerable groups. Fares increases would clearly deter, not attract, passengers back to our services and would, therefore, act against using public transport to help support an economic recovery.

It is also the case that TfL cannot provide any certainty to its supply chain absent government support. A continuation of the current position is likely to begin to cause irreparable damage to critical suppliers, which will impact TfL's ability to continue to provide services and support a recovery. In the best of times, like Government, TfL's procurement challenges are some of the most extraordinary and diverse in the UK. TfL depends upon the capabilities of specialist systems manufacturers, service providers and suppliers capable of delivering critical services and the most complex civil engineering programmes. If such critical suppliers fail, TfL will not only lose continuity of supply, but risks losing important proprietary capabilities and IP: products/services, processes, technologies/systems.

Our supply chain is already beginning to collapse. For example, our Bus Operators are already facing significant pressures and have issued stark warnings to us, that absent our ability to make commitments to them, they will imminently be forced to begin to reduce services. These companies have already utilised furlough, where they can, but it is not enough to ensure their ongoing viability and there are impending risks around potential financial failure. Yet we can do nothing to support these companies absent certainty over funding. These are very real and immediate issues that underline the need for funding support now.

As mentioned above, without immediate Government support, a Section 114 Report will need to be issued to our Board very shortly. We are briefing our Finance Committee on Friday of this week to discuss this and the critical issue of our ability to continue as a going concern. After a Section 114 Report is issued, absent Government support, we will be forced to reduce services to a statutory minimum (i.e. only operating the Woolwich ferry, taxi and private hire licensing activities, Dial-a-Ride and some school bus services). There would be no Tube, no Rail or Dockland Light Railway services. Minimal bus services may be possible for a short period only.

We would be forced to cancel our entire capital programme and our operating contracts, leading to significant contractor claims (estimated at around £1bn) and considerable financial viability issues in our supply chain. Given that the majority of services would need to be shut-down with no foreseeable route to restarting, there would be significant redundancy, which would have associated payments. We would have a rapidly diminishing workforce of trained personnel and a significant loss of skilled resources. This would inevitably create significant Industrial Relations issues.

There is a risk that a Section 75 liability could be triggered in relation to the Pension Fund (especially if TfL are technically insolvent) resulting in liability of over c.£12bn. [redacted]

As mentioned above, a credit rating downgrade would be inevitable absent the provision of government support. This is likely to be a deep downgrade of between 1-3 notches reflecting the severing of the link to Government upon which our rating currently relies. [redacted]

We have been and of course wish to provide the transport services London needs now for essential journeys, and as lockdown restrictions are eased do our part to support economic recovery in the city and wider region. However, we continue to do so, on the basis and expectation of Government support being forthcoming, as has previously been indicated would be the case.

To reiterate, our discussions with DfT colleagues have been constructive, but the situation is now extremely urgent; we now need explicit agreement to providing the £2 billion grant funding needed to keep our services going until 30th September in the first instance, and a commitment to providing support thereafter, based upon further discussions with Government over the next few months.

Otherwise, I cannot, in good faith, see how we will avoid a shutdown of London's transport network and the vital services it provides.

Yours sincerely

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Mike Brown MVO

Copy to: Bernadette Kelly
Attachments: Responses to DfT questions, Emergency Budget presentation