Briefing Note on the Amendments to the LCRCA Single Entity Statement of Accounts 2018/19

1. Background

The draft Statement of Accounts were prepared and presented to the external auditors, Mazars, by the deadline date of 31st May 2019. The final audited set of accounts however was not available for publication by 31st July 2019. The delay was caused by the need to continue to conduct work to establish the appropriate accounting treatment on the two issues raised below. This work has now been completed and an appropriate accounting treatment has been agreed with Mazars. The Statement of Accounts has subsequently been amended to reflect these adjustments. Mazars are currently reviewing the revised Statement of Accounts.

2. Recognition of Capital Grant Payable to Merseytravel to Fund Rolling Stock Expenditure

The approved Rolling Stock programme was predicated on the basis that the procurement of the trains and associated works would be undertaken by Merseytravel. Per the business case, the scheme was to be funded by a mixture of use of reserves and external borrowing. Whilst the reserves for this scheme were split between the LCRCA and Merseytravel, the borrowing (circa £400m) was to be undertaken by the LCRCA and this was made clear in the resolution. This would require the CA to passport the funding to Merseytravel.

Over the last 3-4 years the LCRCA has been in receipt of significant grant receipts in respect of Local Growth Fund, Devolution Investment Funds and more latterly Transforming Cities funding which have significantly increased the cash balances of the LCRCA. To the extent that there has been surplus cash available, the LCRCA has been in a position to defer its need to borrow by funding capital expenditure through available grant and cash balances. The funding of this expenditure is accounted for as ‘internal borrowing’.

In the draft 2018/19 Financial Statements, the unfunded element of Rolling Stock capital expenditure amounted to £85.612m. This was reported in the Merseytravel draft Financial Statements, resulting in an increase of £85.612m in the Capital Financing Requirement.

The proposed revised accounting treatment is to recognise a capital grant payable from the LCRCA to Merseytravel to recognise the £85.612m funding provided by the LCRCA. The justification for this is that, in substance, the LCRCA has to grant or passport all income through to Merseytravel as the power to levy, receive grants and borrow all sit with the LCRCA.

3. LCRCA and Merseytravel Cash Balances

Historically Merseytravel and the LCRCA have shared joint bank accounts to make payments and receive income. The shared accounts avoid duplication of effort and additional costs.

The main bank account is held on a central Balance Sheet and the accounting treatment in the 2018-19 draft Financial Statements is to recognise Merseytravel and LCRCA calculated share of year-end bank balances on their individual Balance Sheets.

However, unlike the LCRCA, Merseytravel does not have the statutory power to invest surplus cash balances or to borrow. The LCRCA is defined as a Local Authority under the Localism Act 2011 which provides that a Local Authority has the power to do anything that individuals generally may do, known as the general power of competence. As individuals may borrow or invest, the LCRCA is able to borrow or invest. Furthermore, the Local Government Act 2003 section 1 provides a specific power to borrow. Merseytravel is not defined as a Local Authority and therefore does not have a general power of competence. As there are no other specific powers to borrow or invest in the Merseytravel Constitution this activity is not permissible.

In reality therefore, if Merseytravel operated a separate bank account, it would not hold any surplus year-end cash on its Balance Sheet as these balances would be transferred to and invested by the LCRCA. Similarly, should Merseytravel need to borrow externally, the loans would be raised by the LCRCA and report on the LCRCA Balance Sheet.

The proposed revised accounting policy is to recognise all year-end bank balances on the LCRCA Balance Sheet and to recognise an intercompany debtor and creditor on each Balance Sheet (dependent on the year-end position).

4. Impact upon the LCRCA Single Entity 2018-19 Draft Accounts – Primary Statements

Page 86 Movement in Reserves Statement

- Total Comprehensive Income and Expenditure deficit of £11.847m increases to £97.459m reflecting the payment of a capital grant of £85.612m to Merseytravel.
- Adjustments to Usable and Unusable Reserves (for the differences between accounting basis and funding basis under regulations) are amended by £85.612m reflecting a credit to the General Fund Balance and a debit to the Capital Adjustment Account to reverse the impact of the capital grant payment on the General Fund Balance.

Page 87 Comprehensive Income and Expenditure Statement

- Transport Gross Expenditure increases by £85.612m, from £216.684m to £302.296m, reflecting the capital grant payment to Merseytravel.

Page 88 Balance Sheet

- Cash and Cash Equivalents are reduced from £89.805m to £39.072m, an overall reduction of £50.733m. The cash balance is initially reduced for the £85.612m capital grant payment to Merseytravel. The Merseytravel Group draft financial statements show a bank overdraft of £50.734m which increases to a positive balance of £34.878m following the receipt of the capital grant.

This cash balance is now reported on the LCRCA Balance Sheet with an adjusting entry to an intercompany creditor (see below).

- Short-term creditors increase by £34.878m from £87.432m to £122.310m as detailed above.
- Unusable Reserves are reduced by £85.612m reflecting the charge to the Capital Adjustment Account for the capital grant payment.
- The Balance Sheet's as at 31st March 2017 and 31st March 2018 are restated to reflect the revised accounting policy in relation to the treatment of cash balances.

Page 89 Cashflow Statement

- Net deficit on provision of services is increased by £85.612m to reflect the capital grant payment.
- The adjustment to the net surplus on the provision of services for non-cash movements is restated by £37.349m. This adjustment represents the year on year movement in intercompany creditors resulting from the revised accounting policy in relation to cash balances. The intercompany creditor with Merseytravel as at 31st March 2018 is £34.878m as detailed above. The equivalent restated balance as at 31st March 2017 is £72.227m.
- The 2017-18 comparative Cashflow Statement is restated for the adjustments to intercompany creditors.