Committees:	Dates:
Audit and Risk Management Committee **Finance Committee**	**4 November 2014** **18 November 2014**
Subject: **City's Cash Financial Statements 2013/14**	**Public**
Report of: **The Chamberlain**	**For Decision**

Summary

Attached at Annex 1, for approval, are the Annual Report and Financial Statements for City's Cash for the year ended 31 March 2014

Annex 2 sets out Moore Stephens LLP's Management Letter for consideration.

The key points are:

- inclusion for the first time of an estimated share of the net liability in the City of London Pension Scheme. The estimated City's Cash share is 49% which was £196.7m at 31 March 2014 (£167.5m at 31 March 2013) ***(these figures are shown in the Consolidated Balance Sheet on page 16 and analysed further in note 16 on pages 45-51)***;
- a change in the accounting treatment for 'non-property' investments following the transfer on 31 January 2014 of four of the six equity funds to pooled investment vehicles. As a consequence, from 1 February the incoming resources within the Income and Expenditure Account now include the gain or loss in fair value of all non-property investments rather than the dividend income. This has a part-year effect in 2013/14 but will have greater impact from 2014/15. Even relatively small movements in the markets from one year to the next will produce large values to be reported as operating gains or losses in the Income and Expenditure Account ***(paragraphs 9 – 11 of this report)***;
- the Consolidated Income and Expenditure Account indicates a net deficit of £6.1m for the year ***(page 15 of the financial statements)***;
- total City's Cash net assets of £1,860.3m, an increase of £199.9m (12%) since last year. This favourable movement comprises net gains on property investments of £196.1m and managed investments of £34.4m, partially offset by £24.5m

being the City's Cash share of the actuarial loss on the pension fund and the £6.1m net deficit on the income and expenditure account ***(the Consolidated Statement of Total Recognised Gains and Losses is on page 18)***;

- the potential contribution of £50m from City's Cash towards the Crossrail Project has been disclosed as a contingent liability in both the annual report ***(page 9)*** and the notes to the financial statements ***(page 58);***
- the outturn for the year was a worse than budget position of £1.9m, the main reasons for which are set out in paragraphs 13 to 17 of this report.

Recommendations

The Audit and Risk Management Committee is requested to:

- consider the contents of Moore Stephens LLP's Management Letter; and
- recommend approval of the City's Cash Financial Statements for the year ended 31 March 2014 to the Finance Committee.

The Finance Committee is requested to:

- consider the contents of Moore Stephens LLP's Management Letter;
- approve the City's Cash Financial Statements for the year ended 31 March 2014 taking account of any observations from the Audit and Risk Management Committee; and
- agree that the Financial Statements are signed by the Chairman and Deputy Chairman of the Finance Committee on behalf of the Court of Common Council.

Main Report

Introduction

1. The 2013/14 Financial Statements for City's Cash are attached at Annex 1. The statements are prepared in accordance with United Kingdom Generally Accepted Accounting Practice (UKGAAP).

2. The external auditor, Moore Stephens LLP intends to give an unqualified opinion on the City's Cash Financial Statements and has issued the management letter set out in Annex 2. The management letter will be distributed to all Members of the Court of Common Council for information. Representatives from Moore Stephens LLP will be in

attendance at the Audit and Risk Management Committee to present their report and to clarify any points or issues.

3. The Audit Review Panel of the Chamberlain's and Bridgemasters' Accounts met on 6 October 2014 to review the processes adopted by Moore Stephens LLP and the Panel intends to certify that those processes were in accordance with the prescribed auditing standards.

City of London Pension Scheme

4. City of London staff excluding police officers, teachers and judges, are eligible to join the Local Government Pension Scheme – a statutory scheme administered in accordance with Government regulations.

5. Previously the City's Cash share of the estimated net deficit on the City of London Pension Scheme had not been included in the balance sheet. This exclusion arose because the estimated net deficit is the responsibility of the City of London as a whole, as one employer, rather than the specific responsibility of any of its three funds. Thus City's Cash does not have an exclusive relationship with the City of London Pension Fund and the proportion of the Pension Fund relating to City of London employee members engaged on City's Cash activities is not separately identifiable. Consequently, in accordance with FRS17, the pension arrangements had been treated as a defined contribution scheme in the City's Cash accounts. This meant that only the employer's contributions to the scheme had previously been included in the accounts.

6. However, although the Pension Fund net deficit cannot be attributed precisely between the City Fund, City's Cash and Bridge House Estates, it is now considered that an apportionment of that deficit and inclusion in the respective balance sheets presents a fairer view of the funds' financial positions than if the deficit were to continue to be excluded. Accordingly an apportionment has been made which is based on employer's annual contributions to the fund.

7. Amounts included for 2012/13 have also been restated from those published last year to include City's Cash estimated proportion of the net Pension Fund deficit. The total net deficit in the City of London Pension Fund was £402m at 31 March 2014 (2012/13: £342m). The estimated proportion of this deficit is £196.7m or 49% (2012/13: £167.5m or 49%). These deficits reduce total reserves at 31 March 2013 and 31 March 2014 as set out in the following table.

	31-Mar-14	31-Mar-13
	£m	£m
Total reserves **prior** to change in accounting treatment	2,057.0	1,827.9
Less City's Cash estimated proportion (49%) of the Net Pension Fund Deficit	196.7	167.5
Total reserves **after** change in accounting treatment	1,860.3	1,660.4

8. Pension fund deficits (or surpluses) are relatively sensitive to movements in the underlying assumptions. The main reasons for the increase in the City of London Pension Fund deficit are a reduction in the discount rate used for calculating the present day value of future payments from the fund – with a decrease in the rate resulting in higher liabilities and vice-versa – together with an increase in longevity; partly offset by an increase in the fund's assets.

Non-Property Investments – Change in Accounting Treatment

9. On 31 January 2014, four of the six equity funds transferred to pooled investment vehicles. Consequently, income generated by these funds remains within those funds to be reinvested, with City's Cash drawing down income as required. As a consequence, from the date of transfer, the Income and Expenditure Account now includes the gain or loss in fair value of all non-property investments rather than the dividend income.

10. In 2013/14 this change has a part year effect. Dividend income is £14.9m for the period from 1 April 2013 to 31 January 2014 and the gain in fair value from 31 January to 31 March is £1.5m. Both of these figures are included in the Income and Expenditure Account. The net gain on managed investments of £34.4m within the Consolidated Statement of Total Recognised Gains and Losses relates only to the period from 1 April to 31 January.

11. In subsequent years, the full effect of this change has the potential to dominate the net operating position. Even relatively small movements in the markets from one year to the next will produce large values to be reported as operating gains or losses in the Income and Expenditure Account.

Consolidated Income and Expenditure Account

Comparison with Previous Year

12. The Consolidated Income and Expenditure Account for the year ending 31 March 2014 shows a net deficit of £6.1m. This compares to a net deficit of £0.3m in the previous year. The main variations are as follows:

- a reduction of £4.4m in net investment income, from £51.5m in 2012/13 to £47.1m in 2013/14. This was due to the change in investment management arrangements outlined above whereby income generated since the transition date is reinvested within the funds and also to a reduction in property rental income. The latter relates to a number of building leases coming to an end and properties being redeveloped or refurbished during the year.
- net expenditure on education has increased by £2.2m to £12.1m. Of this increase, £1.7m relates to the Guildhall School of Music and Drama largely due to temporary additional resources which were agreed to further develop its teaching and learning infrastructure to enable it to take full advantage of the new facilities at Milton Court. The balance of £0.5m is additional net expenditure by the three independent schools.
- net expenditure on markets has reduced from £4.3m in 2012/13 to £0.5m in 2013/14 due to a combination of service charge income following the commencement of new leases at Smithfields and the one-off costs in 2012/13 of establishing new working arrangements at Billingsgate.
- a net increase from £3.5m to £4.1m on other activities including expenditure on grants, and on repairs and maintenance to the City Magistrates Court.
- a one-off VAT refund of £5.4m in 2012/13.
- the sale of fixed assets generated a profit of £7m in 2013/14 compared to £4m in 2012/13.

Comparison with Budget

13. The financial statements and the budget are not directly comparable due to differences in the way in which the two documents are constructed. However, with the exception of investment income, the table below compares the budget and outturn on a comparable basis and indicates a worse than budgeted position of £1.9m.

	City's Cash Outturn 2013/14			
		Budget	Outturn	Variation (Better)/ Worse
		£m	£m	£m
1	Net expenditure on services	70.0	68.5	(1.5)
2	Supplementary revenue projects	3.8	1.9	(1.9)
3	Estate rent income	(41.8)	(42.4)	(0.6)
4	Investment income	(20.5)	(16.5)	4.0
5	Interest on balances	(0.3)	(0.4)	(0.1)
6	**Operating Deficit**	**11.2**	**11.1**	**(0.1)**
7	Profit on asset sales	(9.0)	(7.0)	2.0
8	**Deficit after Profit on Asset Sales**	**2.2**	**4.1**	**1.9**

14. However, the position in the table is skewed by the change in investment management arrangements which is the main reason for the reduction of £4m shown for investment incomes. Adjusting for this change, the underlying position would be a favourable movement of £2.1m.

15. The budget and outturn can also be analysed on a Committee basis as follows:

	City's Cash Net Expenditure (Income) by Committee 2013/14					
	Committee	**Budget**	**Outturn**	**Variation (Better)/Worse**		
				Total	**Local Risk**	**Central Risk/ Support Services**
		£'m	**£'m**	**£'m**	**£'m**	**£'m**
1	Culture, Heritage and Libraries	0.0	0.0	0.0	0.0	0.0
2	Finance	(10.3)	(5.5)	4.8	(0.2)	5.0
3	General Purposes Committee of Aldermen	3.3	3.0	(0.3)	(0.2)	(0.1)
4	Guildhall School of Music and Drama	9.1	9.1	0.0	(0.2)	0.2
5	Markets	1.0	0.2	(0.8)	(0.5)	(0.3)
6	Open Spaces Directorate	0.0	0.0	0.0	0.0	0.0
7	Epping Forest and Commons	6.5	6.7	0.2	0.2	0.0
8	Hampstead Heath, Queen's Park & Highgate Wood	6.6	6.4	(0.2)	(0.2)	0.0
9	Bunhill Fields	0.3	0.3	0.0	0.0	0.0
10	West Ham Park	1.0	1.0	0.0	0.1	(0.1)
11	Planning and Transportation	0.1	0.1	0.0	0.0	0.0
12	Policy and Resources	11.3	10.3	(1.0)	0.0	(1.0)
13	Port Health and Environmental Services	0.2	0.2	0.0	0.0	0.0
14	Property Investment Board	(32.5)	(32.8)	(0.3)	(0.1)	(0.2)
15	City of London School	1.6	1.5	(0.1)	(0.1)	0.0
16	City of London Freemen's School	2.8	2.5	(0.3)	(0.3)	0.0
17	City of London School for Girls	1.2	1.1	(0.1)	(0.1)	0.0
18	**Total City Fund Requirement**	**2.2**	**4.1**	**1.9**	**(1.6)**	**3.5**

16. The main variations were:

- Finance Committee, £4.8m worse:
    - £4m reduction in investment income due to the change in investment management arrangements;
    - £2m reduction in profits from the sale of assets. The shortfall relates to two asset disposals that were deferred to 2014/15. Both have now been completed and the profit from the sales was £2.3m.
    - £0.7m City's Cash share of fees payable to the City's procurement partner to facilitate an earlier conclusion to the partnership including the bringing forward of payments that would otherwise have been paid later in the contract for ongoing savings already achieved;

      partly offset by
    - £1.9m slippage/rephasing of supplementary revenue projects mainly relating to Guildhall School and Investment Property schemes.
- Markets Committee, £0.8m better - Savings on employees, energy and billing costs; lower expenditure on repairs and maintenance; and additional income from rents, parking and dilapidations.
- Policy and Resources Committee, £1m better – Primarily relates to the uncommitted balances in the Policy Initiatives Fund and Contingency which have been carried forward to 2014/15.

17. In accordance with the City's budget management arrangements, requests for the carry forward of City's Cash resources totalling £2.1m have been agreed by the Chamberlain in consultation with the Chairman and Deputy Chairman of the Resource Allocation Sub-Committee. This increases the call on City's Cash reserves in 2014/15. In addition, £1.9m of projects and works programmes have slipped and/or been rephased to 2014/15.

Consolidated Statement of Total Recognised Gains and losses

18. As set out in the table below, the recognised gains for the year total £199.9m (31/3/13 – gains of £121.2m).

	31/03/2014 £m	31/03/2013 £m
Deficit for the financial year	(6.1)	(0.3)
Unrealised gains		
Gain on revaluation of investment properties	196.1	56.7
Gain on revaluation of non-property investments (April to January)	34.4	55.5
Actuarial gain (loss) on defined benefit pension scheme	(24.5)	9.3
Total gains recognised for the year	199.9	121.2

Consolidated Balance Sheet

19. City's Cash net assets total £1,860.3m at 31 March 2014 compared to £1,660.4m a year earlier reflecting the £199.9m total gains recognised for the year as set out above.

Contribution to Crossrail

20. The potential contribution of £50m from City's Cash towards the Crossrail Project has been disclosed as a contingent liability in both the annual report and the notes to the financial statements. The reasons for this treatment, rather than the inclusion of a long term liability, are that although the report to the Policy and Resources Committee last December indicated the contributions could be made in two instalments of £25m in 2018 and 2019, this was subject to further discussions and completion of the works. Consequently, at this stage, the payments are contingent on further Member approval and the fulfilment of any conditions that may be required.

Signing of the Financial Statements

21. The Chairman and Deputy Chairman of the Finance Committee will be requested to sign the financial statements.

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