

Date: 18 July 2013

Item 8: Exchange Rate and Interest Rate Derivative Programmes

This paper will be considered in public

1 Summary

- 1.1 The purpose of the paper is to seek approval for derivative programmes proposed to mitigate TfL's exposure to exchange rate risk when that risk is encountered in the ordinary course of business and to interest rate risk on future borrowings.
- 1.2 A paper is included on Part 2 of the agenda, which contains exempt supplemental information on exchange rate risk and interest rate risk. The information is exempt by virtue of paragraph 3 of Schedule 12A of the Local Government Act 1972 in that it contains information relating to the financial affairs of TfL. Any discussion of that exempt information must take place after the press and public have been excluded from this meeting.

2 Recommendations

2.1 That the Committee:

- (a) note this paper;
- (b) approve, pursuant to Section 49 of the Transport for London Act 2008 (the Act) and the TfL Group Policy Relating to the Use of Derivative Investments for 2013/14, Transport for London Finance Limited (as a qualifying TfL subsidiary for the purposes of the Act) entering into derivative investment(s) in relation to:
- (i) mitigating exchange rate risk related to specific currency exposures arising from the procurement of goods or services by any member of the TfL Group in the ordinary course of business as soon as practicable once the quantum of exchange rate risk to any member of the TfL group is established, such approval to be effective until 31 March 2014; and
 - (ii) mitigating interest rate risk related to any imminent TfL borrowing, once the borrowing has become certain and authorised according to relevant Treasury Management Strategy 2013/14 provisions, such approval to be effective until 31 March 2014; and
 - (iii) mitigating interest rate risk related to any other planned future TfL borrowing in accordance with Transport for London's Treasury Management Strategy and the TfL Group Policy on the Use of Derivatives Investments for 2013/14, once a strategy for

planned future borrowing has been discussed with the Committee, such approval to be effective up to the next meeting of the Committee, provided that Managing Director Finance or the Group Treasurer consult with as many Members of the Committee that are available, on the terms of the derivative investment in advance;

for the purposes of the prudent management of the financial affairs of TfL and its subsidiaries and limiting the extent to which one or more TfL bodies will be affected by changes in exchange rates or interest rates as applicable;

- (c) delegate authority to any of the Commissioner, Managing Director Finance, General Counsel, Chief Finance Officer, and Group Treasurer to agree and execute any documentation (including without limitation all agreements, deeds, guarantees, announcements, notices, contracts, certificates, letters or other documents) to be entered into in connection with the derivative investments referred to in paragraph 2.1 (b).**

3 Background

- 3.1 TfL's Risk Management Strategy 2013/14 (RMS) was approved by the Board on 27 March 2013, as part of the 2013/14 Treasury Management Strategy (TMS). The RMS provides for measures to address identifiable financial risks, including interest rate risk and exchange rate risk.
- 3.2 The high level principles established by the RMS are to:
- (a) achieve greater value for money through reducing costs or protecting revenues;
 - (b) reduce volatility/increase certainty relating to the impact of financial risks upon the Business Plan; and
 - (c) holistically manage financial risk across the whole of TfL.
- 3.3 Under the TfL Group Policy relating to the use of Derivative Investments, the Committee has delegated authority to approve derivative transactions.

4 Governance and Reporting

- 4.1 Under section 49 of the Transport for London Act 2008 (TfL Act), TfL has the power to enter into certain financial derivatives investments (derivative instruments) through a qualifying TfL subsidiary. Transport for London Finance Limited (TfLFL) has been set up to act as the main qualifying TfL subsidiary for this purpose. These powers may only be used to manage the financial risks set out in section 49 of the TfL Act, for example exposure to exchange rate risk.
- 4.2 On 27 March 2013, the Board approved the Derivatives Policy, which delegates to the Committee the authority to give consent on behalf of TfL to enter into certain derivative instruments.

- 4.3 The high level principles adopted as part of the RMS include the management of specific, identified financial risk, including:
- (a) interest rate risk related to TfL's planned future borrowing requirements; and
 - (b) exchange rate risk related to specific currency exposures arising from the procurement of goods or services by the TfL Group; and from receipts of European Union subsidies or other grants/revenues payable other than in Sterling.
- 4.4 In accordance with the Derivatives Policy and practices, the following reporting and governance arrangements apply:
- (a) approval from Managing Director Finance and Chief Finance Officer will be obtained before any derivative instrument or series of derivative instruments is entered into;
 - (b) daily monitoring by Group Treasury of derivative and counterparty credit risk exposures;
 - (c) weekly collateral monitoring and settlement with counterparties;
 - (d) weekly Group Treasury Flash Reports to the Treasury Group, comprising the Managing Director Finance, the Chief Finance Officer and the Group Treasurer;
 - (e) biannual reports to the Committee on the status of the hedges in place, on the strategy to be pursued in the coming months, on the effects of decisions taken and the derivatives transactions executed over the review period, and on any non-compliance with this policy and practices described; and
 - (f) an annual report to the Board on the strategy to be pursued in the coming year.
- 4.5 The derivatives proposed in this paper fall within the scope of section 49 of the TfL Act.
- 4.6 The proposal is made for the purposes of the prudent financial management of the financial affairs of TfL and its subsidiaries.

List of appendices to this report:

Exempt supplemental information is included in a paper on Part 2 of the agenda.

List of Background Papers:

None

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