



Chief Finance Officer's Narrative Report for the Year ended 31 March 2016

1. Introduction

This Narrative Report (a new requirement for 2015/16, replacing the Explanatory Foreword) provides information about the North East Combined Authority, including the key issues affecting the Authority and its accounts. This report provides an explanatory narrative to key elements of the statements and sections in the accounts and also provides a summary of the Authority's financial performance for 2015/16 and its future financial prospects.

This report provides the reader with:

- A guide to the different financial statements within the Statement of Accounts.
- An overview of the activities and significant matters which occurred during the year.
- A summary of the Authority's financial performance during the year ended 31 March 2016 and its financial position at that date.
- A look ahead to 2016/17 and beyond.

The Statement of Accounts sets out the financial performance of the Authority for the year ended 31 March 2016 and its financial position at that date. They have been prepared in accordance with proper practices as set out in the Chartered Institute of Public Finance & Accountancy (CIPFA) Code of Practice on Local Authority Accounting in the United Kingdom (the Code). The Code requires that the accounts give a true and fair view of the financial position of the Authority. In line with the Code, suitable accounting policies have been applied and where necessary prudent judgements and estimates have been made.

The accounts feature four main financial statements:

- Movement in Reserves Statement.
- Comprehensive Income and Expenditure Statement.
- Balance Sheet.
- Cash Flow Statement.

The purpose of each of the above statements is described at the end of this report and the actual statements are contained within the accompanying Statement of Accounts document, which also includes detailed notes providing further backup relating to specific amounts and balances.

The main statements are supplemented by a further section which presents the Group Accounts, consolidating the figures of Nexus with those of the Authority. NECA is also the Accountable Body for the North East Local Enterprise Partnership (NELEP). Our accounts include all transactions relating to the NELEP and summary information is highlighted in this report.

These statements and accounts collectively provide a comprehensive view of the Authority's financial position during the period to which they relate.

The Authority seeks to make best possible use of resources available with regard to economy, efficiency and effectiveness. This is a responsibility shared by Members and officers of the Authority, with the Chief Finance Officer having a specific role in ensuring the adequacy of resources and proper financial administration. Our budget proposals for 2016-17, available on the NECA website (www.northeastca.gov.uk) set out how we will do this looking forward. The Statement of Accounts accompanying this report looks backwards at our performance over the past year. Reviewed together they provide the reader with a complete understanding of the financial position of the Authority.

2. What is the North East Combined Authority?

The North East Combined Authority (NECA) was established in April 2014 as a new legal body that brings together the seven councils which serve County Durham, Gateshead, Newcastle upon Tyne, North Tyneside, Northumberland, South Tyneside and Sunderland. Its ambition is to create the best possible conditions for growth in jobs, investment and living standards, making the North East an excellent location for business and enabling residents to develop high-level skills so they can benefit long into the future.

The authority was established in April 2014 in order to enable more effective collaboration on the key regeneration and transport issues which cut across council boundaries.

Work on a number of projects is already underway – most notably the first year of the Local Growth Fund programme – and there have already been a number of successes and achievements. Across the area 2015/16 has seen significant inward investment, leading to the creation of thousands of new jobs, and important steps forward in relation to transport improvements.

In addition NECA is spearheading a number of projects aimed at helping people into jobs and apprenticeships through improved training and better transport. There is an increasingly positive picture for the North East economy, with growth in employment and productivity being reported, and evidence of opportunities for further improvements.

NECA is working closely with the North East Local Enterprise Partnership and the wider business community to deliver the Strategic Economic Plan for the North East and capitalise on these opportunities. Ten new enterprise zone sites have been approved to start in April 2017 and NECA and the LEP is working jointly to secure a £120m North East extension to the JEREMIE access to finance for business fund, which is due to start in 2017. In the absence of a devolution deal for the North East, the authority will continue to seek external funding such as Local Growth funding; infrastructure funding for major transport projects; and will seek to maximise European funding and the replacement of Europe regional funding following Brexit for the North East.

3. Revenue Financial Summary 2015/16

Revenue expenditure covers the cost of the Authority's day to day operations and contributions to and from reserves.

A summary of NECA expenditure against budget is set out in the table overleaf. Expenditure totalling £118m was managed within the approved revenue budget and income, with an underspend of around £0.775m at the year end which means the requirement to fund activity from reserves is less than originally budgeted.

Table 1: Summary of Revenue Expenditure Against Budget

	2015/16 Revised Budget	2015/16 Actual	Variance
	£000	£000	£000
Expenditure			
Transport Levy Budget			
- NECA retained (less contributions to other NECA activity)	2,447	2,310	(137)
- Grant to Durham	16,072	16,072	-
- Grant to Nexus	64,500	64,500	-
- Grant to Northumberland	5,896	5,896	-
Tyne Tunnels			
- Contract Payments	21,658	22,033	375
- NECA costs	237	303	66
- Financing Costs	6,419	6,404	(15)
Inward Investment	360	211	(149)
Corporate/Central Budget	300	456	156
Devolution Activity	500	250	(250)
Skills - Mental Health Trailblazer Project	-	48	48
Total Expenditure	118,389	118,483	94
Income			
External Grant Funding	-	(48)	(48)
Transport Levies	(89,177)	(89,177)	-
Tolls Income	(27,457)	(28,396)	(939)
Interest/Investment Income	(344)	(226)	118
Contributions from Constituent Authorities	(440)	(440)	-
Contributions from NELEP	(140)	(140)	-
Total Income	(117,558)	(118,427)	(869)
Net Revenue Expenditure to fund from Reserves	831	56	(775)

Within the accompanying Statement of Accounts document the **Comprehensive Income & Expenditure Statement** (CIES, page 12) sets out the Authority's financial position for the year before taking account of statutory adjustments required to be made to the accounts. The **Movement in Reserves Statement** (MIRS, page 11) reflects these statutory adjustments and shows how the financial performance for the year has impacted on the Authority's reserves. The figures presented in these statements are different from the budgeted revenue expenditure as they include accounting adjustments for costs such as Depreciation, and Revenue Expenditure Funded by Capital Under Statute and other grant-funded expenditure not included in the revenue budget.

The gross cost of services during the year including capital grants to third parties as well as revenue expenditure was £200.453m (£129.513m in 2014/15). This includes all areas of the NECA's activity. The significant increase is primarily due to Local Growth Fund activity during the year. This programme began from April 2015. A further increase in Highways and Transport Services expenditure is as a result of this being the first year of the seven-authority Transport Levy and corresponding grants paid to Durham and Northumberland County Councils for the delivery of highways and transport services.

Although Local Growth Fund grant is capital in nature, these payments are disclosed in the Cost of Services as 'Revenue Expenditure Funded by Capital Under Statute' – as they represent investment in capital assets owned by third parties, not by the Authority itself.

After deducting specific grants and income from fees and charges, the net cost of services was £75.610m (£59.966m in 2014/15). This was funded from a range of sources including the Transport Levy, other contributions from Constituent Authorities, Government Grants, Fees and Charges, and Enterprise Zones Business Rates Growth.

The CIES shows a net surplus for the year on the Provision of Services of £2.039m. This largely reflects grant income being credited to the CIES where conditions have been met but they have not yet been used to fund expenditure, and grant income released to the CIES which has been used to fund the issue of North East Investment Fund loans (which under accounting practice are not shown in the CIES as they are capital expenditure).

4. North East Local Enterprise Partnership

NECA is the Accountable Body for the North East Local Enterprise Partnership (NELEP) and, as such, these accounts include details of its income and expenditure during 2015/16, fully consolidated with the figures for NECA itself.

The NELEP brings together business leaders, universities and members of the NECA Leadership Board. It is the fourth largest LEP in the country and covers the seven local authority areas which also make up NECA. It is responsible for promoting and developing economic growth in the area and works together with NECA to ensure there is co-ordination across a range of activities. One of its major areas of activity is the North East Investment Fund (NEIF), a capital loans fund supporting projects that specifically encourage local economic growth and create jobs in the area.

Table 2: Summary of North East Investment Fund Activity 2015/16

	Grants Paid	Loans Advanced	Total Payments 2015/16	Interest Repayments 2015/16	Principal Repayments 2015/16	Total Repayments 2015/16
	£000	£000	£000	£000	£000	£000
Growing Places Fund	2,719	200	2,919	(658)	(3,603)	(4,261)
Regional Growth Fund	3,891	11,509	15,400	(78)	(885)	(963)
Contribution to JEREMIE 1 Extension	4,500	-	4,500	-	-	-
Total	11,110	11,709	22,819	(736)	(4,488)	(5,224)

The table below summarises the LEP's revenue expenditure in 2015/16.

Table 3: North East LEP Revenue Expenditure

	LEP Core Activity	NE Growth Hub	National Careers Pilot	NEIF Coordination	Total
	£000	£000	£000	£000	£000
Expenditure					
Employees	946	67	67	-	1,080
Premises	88	-	-	-	88
Support Services	420	-	-	25	445
Other Operational Costs	393	290	24	144	851
Contribution to other NECA activity	105	-	-	69	174
Gross Expenditure	1,952	357	91	238	2,638
Income					
LA Contributions	(250)	-	-	-	(250)
Government Grant	(1,568)	(500)	(165)	(169)	(2,402)
Other Contributions	(3)	-	-	-	(3)
Brought forward balances	(93)	-	-	-	(93)
Interest	(224)	-	-	(69)	(293)
Miscellaneous	(10)	(2)	-	-	(12)
Gross Income	(2,148)	(502)	(165)	(238)	(3,053)
Net (Surplus)/Deficit	(196)	(145)	(74)	-	(415)

Further details of the activities of the NELEP are available at www.nelep.co.uk.

5. Capital Investment

Capital investment during the year totalled £127m (£89m in 2014/15). This consisted of capital expenditure on the Authority's own assets, capital expenditure via capital grants to third parties and long-term capital loans to third parties. An analysis of capital investment by programme and by thematic area are shown in the following charts:

Chart 1: Capital Investment by Programme

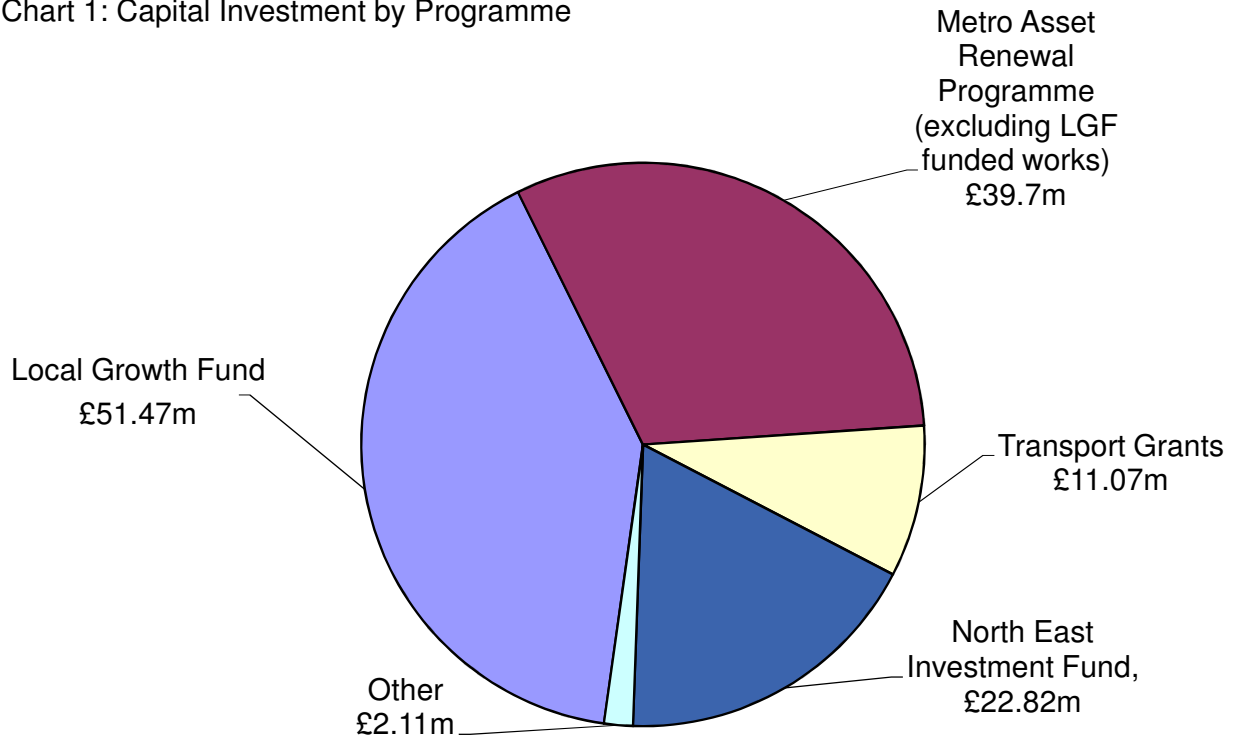
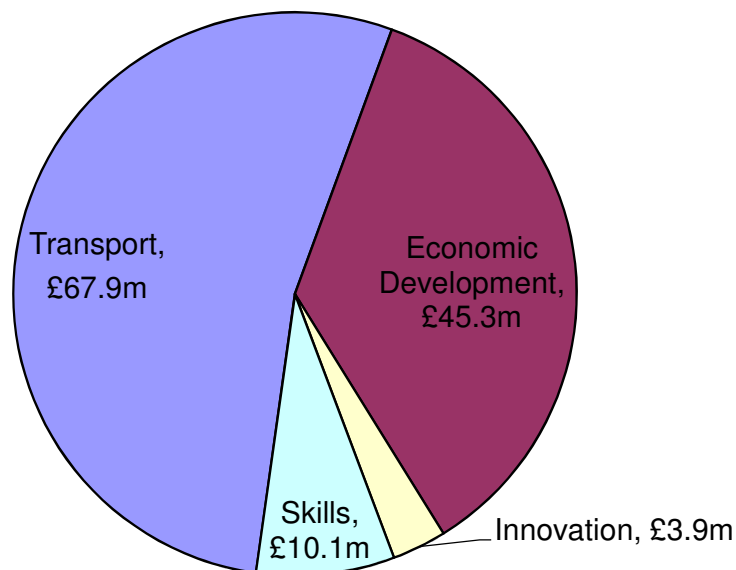


Chart 2: Capital Investment by Thematic Area



The largest area of capital expenditure is in relation to Transport, reflecting the NECA's responsibilities as Transport Authority, which it inherited from the former Tyne and Wear Integrated Transport Authority. Activity on Economic Development continues to grow, building on strong performance in 2014/15, and includes the North East Investment Fund. Skills and Innovation are new areas of activity for NECA in 2015/16.

A selection of the significant by value capital projects / programmes under each thematic area are set out below (figures in brackets represent capital investment in the year funded by NECA sources).

Economic Development

- North East Investment Fund – Loans and grants including the region's round 1 Enterprise Zone sites, Centre for Innovation and Growth at Durham University, Vantec's second warehouse development, SME Office Accommodation in Jesmond (£18.3m)
- Extension of the NE Jeremie Fund (£4.5m)
- LGF – Infrastructure for Forrest Park (£6.2m)
- LGF – Commissioners Quay, Blyth (£1.9m)
- LGF – North East Rural Growth Network (£1.6m)

Innovation

- LGF – Sunderland Enterprise and Innovation Hub (£2.2m)
- LGF – Centre for Innovation in Formulation (£0.8m)
- LGF – Newcastle Laboratory and Life Science Incubation Hub (£0.6m)

Transport

- Metro Asset Renewal Programme (£39.8m)
- LGF – Northern Access Corridor Phase 2 (£3.6m)
- LGF – Local Sustainable Transport Fund Package (£2.7m)
- LGF – Central Metro Station Refurbishment (£2.5m)
- Tyne Tunnels Capital Programme (£1.9m)

Skills

- LGF – Rural Skills Development, East Durham College (£7.5m)
- LGF – Tyne Met College STEM and Innovation Centre (£1m)
- LGF – Facilities for Marine and Offshore Engineering (£1.2m)

A summary of how this capital investment was financed is shown in the following table:

Table 4: Capital Funding 2015/16

	2015/16	2015/16
	£000	%
Local Growth Fund Grant	(51,472)	40.5%
Local Transport Plan Grant	(13,603)	10.7%
Metro Capital Grant	(32,601)	25.6%
Regional Growth Fund	(15,401)	12.1%
Growing Places Fund	(2,919)	2.3%
Other Capital Grants	(108)	0.1%
Capital Receipts	(4,500)	3.5%
Revenue/Reserves	(6,616)	5.2%
Total Funding	(127,220)	100.0%

6. Enterprise Zones

The North East Low Carbon Enterprise Zone is located across four local authority areas: Newcastle upon Tyne, North Tyneside, Northumberland and Sunderland. Business rates growth generated on these designated sites accrues to the benefit of the North East LEP for a 25 year period. 2015/16 was the third year of the zone's life.

Analysis of the business rates generated to date is shown in the table below. This funding is available to support future NELEP activity; primarily additional Enterprise Zone site development works to future enhance this income stream in the coming years.

Table 5: NE Enterprise Zone Business Rates Growth

	2013/14	2014/15	2015/16	Total
	£000	£000	£000	£000
Local Authority Area				
Newcastle upon Tyne	(312)	(330)	(262)	(904)
North Tyneside	(14)	(55)	(100)	(169)
Northumberland	(12)	(28)	(96)	(136)
Sunderland	(696)	(653)	(745)	(2,094)
Gross Expenditure	(1,034)	(1,066)	(1,203)	(3,303)
NEIF Repayment	-	-	542	542
Financing Costs	-	-	424	424
EZ Costs	-	9	9	18
Interest	-	(3)	(7)	(10)
Total Surplus	(1,034)	(1,060)	(235)	(2,329)

During the year, NECA and NELEP received confirmation of a second Enterprise Zone covering 10 areas and 175 hectares, with a start date of April 2017.

7. Treasury Management

The Balance Sheet on page 13 of the accounts shows external borrowing of £171.690m at the end of the year, which is split between short term borrowing (£3.356m) and long term borrowing (£168.333m). This compares to £198.824 for 2014/15. The decrease is due to the early repayment of some Public Works Loans Board (PWLB) loans and the regular principal repayments made on Equal Instalment of Principal (EIP) loans. The average rate of interest on external borrowing for the year was 4.28% which is comparable with the previous year.

The Balance Sheet also shows short term external investments of £89m at the end of the year compared to £28m at the end of the previous year, consisting of £51m NECA's own investments and £38m of investments held on behalf of Nexus. The increase in NECA investments in 2015/16 compared to the previous year is primarily due to receipt of grant income in advance of payments being made to projects and the need to achieve better investment returns leading to deposits being placed for longer time periods where it is considered safe to do so.

8. Debtors

The Balance Sheet on page 13 shows short term debtors of £9.965m at the end of the year compared to £11.243m at the end of the previous year. These balances are analysed in more detail in Note 13 on page 39. The main reasons for the movement during the year are:

- An increase in the level of central government debtors as a payment of Local Sustainable Transport Fund grant was outstanding from DfT at 31 March 2016;
- A decrease in amounts owed by Other Local Authorities due to the repayment of North East Investment Fund loans in the year.
- An increase in amounts owed by Other Entities due to additional North East Investment Fund loans being made during the year.

9. Creditors

The Balance Sheet on page 13 shows short term creditors of £113.252m at the end of the year compared to £43.697m at the end of the previous year. These balances are analysed in more detail in Note 15 on page 39. The main reasons for the movement during the year are:

- A significant increase in amounts owed to Other Local Authorities due to a creditor of £43m with Newcastle City Council. NECA's banking arrangements have changed during the year so that it receives income into its own account, but payments are still made from Newcastle's account due to NECA using its financial systems. The balance outstanding was reconciled following the year end and settled during April
- Further amounts were owed to Other Local Authorities and Other Entities for accrual claims on the Local Growth Fund, for which there was no equivalent in the prior year.
- An increase in amounts owed to Nexus due to an increase from £28m to £38m in investments NECA places on its behalf. A creditor is shown to recognise the fact that these investments must be repaid to Nexus on request.

10. Pensions Costs

The Authority is an employer in the Tyne and Wear Pension Fund (the pension fund), which is part of the Local Government Pension Scheme, which provides defined benefits based on members' final pensionable salary and years of service. In accordance with IAS19, the Authority is required to value all pension liabilities that have accumulated at the end of the year consisting of:

- Pension benefits that are being paid out to former employees who have retired.
- Pension benefits earned to date by current employees but not yet paid out.

IAS19 also requires the Authority to value all investments held by the pension fund at market value at the end of the year.

When assets and liabilities at year-end are compared this results in surplus or deficit.

At the end of the year there was a pension fund deficit of £0.890m and this is disclosed on the Balance Sheet on page 13. This compares with a deficit of £1.020m at the end of the previous year. The main reason for the decrease is due to the assumptions made by the pension fund actuary, particularly a higher discount rate used to revalue liabilities which are based upon reference to market yields on high quality corporate bonds or market yields on government bonds. An increase in the discount rate reduces the current value of the liability outstanding.

Further disclosures related to the pension fund are included in Note 18 from pages 41-46 of the Statement of Accounts.

11. Net Assets

The Authority's total net assets have increased from £149m at 31 March 2015 to £151m at 31 March 2016. This is primarily due to an increase in short term assets in terms of external investments, and a decrease in external borrowing.

12. Group Results

The Group Accounts included as part of the Statement of Accounts fully incorporate the results of Nexus, the Tyne and Wear Passenger Transport Executive. Details of the relationship can be found in Note G1 on page 89 of the Statement of Accounts.

The Group results show a surplus for the year of £23.046m (surplus of £3.125m in 2014/15). This increase is largely a result of a movement in Nexus accounts with regard to the re-measurement of the Pensions defined benefit liability, and a decrease in depreciation costs. The net assets of the Group stood at £599.718m at 31st March 2016 (£570.389m in at 31st March 2015). The increase mainly results from an increase in Long Term Assets owned by Nexus, and a significant increase in short term investments, and a decrease in the pension liability resulting from a change to the discount rate applied by the actuary.

13. Accounting Developments

The main changes in the current year which have affected the accounts for NECA are as follows:

- **IFRS 13 – Fair Value measurement:** clarification of the term 'fair value' as a valuation approach. The fair value of surplus assets is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.
- **Accounts and Audit Regulations 2015 – Narrative Report:** there is now a requirement to produce a separate Narrative Report to the Statement of Accounts, replacing the former Foreword within the Annual Report and Statement of accounts. This must include a commentary by the Authority on its financial performance and economy, efficiency and effectiveness in its use of resources.
- **Accounts and Audit Regulations 2015 – Inspection Period:** the public inspection period is increased from 20 to 30 working days and must include the first 10 working days of July. The audit of the Statement of Accounts cannot be completed until this inspection period has closed.

Additional accounting developments have been reviewed and determined to have no significant impact on the Authority, see Note 26 (page 55) within the Statement of Accounts.

14. Looking Ahead

In the absence of a devolution deal, NECA will continue to provide transport services and will work with the North East LEP to help deliver an updated Strategic Economic Plan. This will include the establishment of a JEREMIE 2 North East access to Finance fund.

The constituent councils of the Authority face significant government funding reductions in the coming years. This means there is likely to be pressure for budget reductions and further savings to be delivered by NECA.

15. The Statement of Accounts

The Statement of Accounts is set out in the accompanying document, they consist of the following statements that are required to be prepared under the Code of Practice:

Movement in Reserves Statement (Statement of Accounts page 11)

This statement shows the movement in the year on the different reserves held by the Authority, analysed into Usable Reserves (i.e. those which can be applied to fund expenditure) and Unusable Reserves (which cannot). The surplus or deficit on the provision of services line shows the economic cost in accounting terms of providing NECA's services, more details of which are shown in the Comprehensive Income and Expenditure Statement. These are different from the statutory amounts required to be charged to the General Fund Balance for the purposes of setting the levy. The net increase or decrease before transfers to earmarked reserves line shows the statutory General Fund Balance before any discretionary transfers to or from earmarked reserves undertaken by the Authority.

Comprehensive Income and Expenditure Statement (Statement of Accounts page 12)

The Comprehensive Income and Expenditure Statement shows the accounting cost in year of providing services in accordance with generally accepted accounting practice, rather than the amount to be funded from the levy and other sources of income which is set out in the MiRS, as described above.

Balance Sheet (Statement of Accounts page 13)

The Balance Sheet summarises the Authority's financial position at 31 March each year. The net assets of the Authority (total assets less total liabilities) are matched by the reserves held by the Authority. Reserves are reported in two categories, Usable and Unusable as described above. Unusable Reserves include those which hold unrealised gains and losses (e.g. the Revaluation Reserve) where amounts only become available to provide services if the assets are sold; and reserves that hold timing differences shown in the MiRS line "adjustments between accounting basis and funding basis under regulations".

Cash Flow Statement (Statement of Accounts page 14)

The Cash Flow Statement shows the changes in cash and cash equivalents of the Authority during the reporting period. The statement shows how the Authority generates and uses cash and cash equivalents by classifying cash flows from operating, investing and financing activities. Investing activities represent the extent to which cash outflows have been made for resources which are intended to contribute to the Authority's future service delivery. Cash flows arising from financing activities are useful in predicting claims on future cash flows by providers of capital (i.e. borrowing) to the Authority.

Group Financial Statements and Notes (Statement of Accounts pages 83-109)

Reports the financial picture of all activities conducted by the Authority, including those delivered through partnership and separate undertakings controlled by the Authority.

16. Annual Governance Statement

To accompany the Narrative Report and Statement of Accounts, the leadership of the Authority prepares an Annual Governance Statement that sets out the principal arrangements that operate to ensure proper governance of the Authority's affairs and the stewardship of resources at its disposal. It also outlines the principal arrangements that are in place to ensure that a sound system of internal control is maintained.

17. Non-Financial Performance

The Statement of Accounts is focused on the Financial Performance of the Authority. NECA also monitors and reports its non-financial Performance, particularly in the following areas:

NECA Structure

Still a relatively new organisation, NECA continues to adapt and grow to meet the requirements of the region, while keeping costs to a minimum. Movement in employee numbers, which mainly relates to staff supporting the North East LEP, is set out in table below:

	Employees at the year end
2015/16	15
2014/15	2

Tyne Tunnels

NECA owns the Tyne Tunnels, which link the A19 under the River Tyne between Howdon and Jarrow. There are two tolled vehicle tunnels, and tunnels for both pedestrians and cyclists. The Tunnels are entirely self-financing from the tolls, i.e. there is no call on the Authority's budget or local tax payers to support them, and assets and liabilities associated with the tunnels are ringfenced to the Tyne and Wear constituent councils within the Authority.

The Tunnels are operated under a contract to a concessionaire company, TT2 Ltd.

Traffic Indicators:

	Class 1	Class 2	Class 3	Exempt	Total
2015/16	204,751	16,218,493	989,451	581,377	17,994,072
2014/15	195,798	15,265,379	873,270	508,444	16,842,891
2013/14	185,471	13,970,360	804,147	464,529	15,424,507
2012/13	160,889	13,066,933	775,757	396,412	14,399,991

Tyne and Wear Passenger Transport Executive – Nexus

NECA sets public transport policy for the region, which in Tyne and Wear is delivered operationally by Nexus. The following indicators describe the general performance of public transport in Tyne and Wear during 2015/16.

- The number of passenger journeys across Tyne and Wear was estimated at 170 million; a reduction when compared to 173 million in the previous year.
- We estimate that patronage declined on Bus, with the number of journeys falling by 3.2% in 2015/16 to 128 million.
- Metro patronage increased by over 2 million in 2015/16 to 40 million journeys.
- The Ferry carried 442,000 passengers in 2015/16, down slightly from 469,000 the year before.
- Rail passengers in Tyne and Wear made more than 1.4 million journeys on local services, in line with the previous year.
- Metro reliability (operated mileage) was 98.0% during 2015/16, a small decrease on the 98.2% achieved in the previous year.
- Metro Charter punctuality was 80.2% during 2015/16, a marginal reduction when compared to the 80.4% achieved in the previous year.

18. Further Information Available

Access to this report, the accounts and the Annual Governance Statement will be made available to the general public via the Authority's website. If this information is needed in another format or language please use the contact below.

If you have any problems understanding this publication, any general enquiries on the accounts or have any suggestions on how it may be improved, please contact:

Eleanor Goodman
Principal Accountant
Civic Centre
Barras Bridge
Newcastle upon Tyne
NE1 8QH

Tel: (0191) 277 7518
Fax: (0191) 211 4901
e-mail: eleanor.goodman@northeastca.gov.uk

Paul Woods
Chief Finance Officer, North East Combined Authority