

Statement by David Shipley

1. Introduction

I am David Shipley, a Harpenden resident affected by noise from London Luton Airport. I write in a personal capacity. I have experience in corporate governance.

I am currently Chairman of a Lloyd's of London managing agency and of the Equitas Group, which manages insurance liabilities arising out of Lloyd's policies issued before 1993, and I am on both companies' Audit Committees. Between 2003 and 2011 I was a member of Lloyd's governing Council and subsequently the Franchise Board, and also sat on Lloyd's Audit Committee.

2. Governance Issues and Force Majeure claim

I am concerned by governance issues arising from the relationship between Luton Borough Council (the LPA), London Luton Airport Limited (LLAL), which owns the airport, and London Luton Airport Operations Limited (the Applicant). The LPA owns and controls LLAL, which in turn contracts with the Applicant to operate the airport. All directors of LLAL are appointed by the LPA; they are all either elected Councillors or employees of the LPA, and until 2021 were all elected Councillors.

The current Chief Executive of the LPA, Mr Porter, was Chief Operating Officer of LLAL from 2012 until 2019, but was not a director of the company. His role at the LPA during that period was "Corporate Director – Customer and Commercial". Mr Olver was appointed Chief Executive Officer of LLAL in December 2020 but did not become a Director until August 2021.

None of the LLAL directors claims previous aviation experience. The Applicant is majority owned by Aena, which manages 62 airports and is the world's number one airport operator in terms of passenger traffic¹, and its Board includes highly experienced airport management professionals and investors from AMP Capital.

In January 2019 the Committee on Standards in Public Life ("CSPL") published a "Local Government Ethical Standards" report, which gave detailed guidance on best practice in local government in maintaining adherence to the Nolan Principles of selflessness, integrity, objectivity, accountability, openness, honesty and leadership. It referred specifically to councils with commercial subsidiaries, advising on appropriate governance arrangements.

In the Executive Summary of the report the CSPL states that *"Local authorities setting up separate bodies risk a governance 'illusion', and should take steps to prevent and manage potential conflicts of interest, particularly if councillors sit on these bodies. They should also ensure that these bodies are transparent and accountable to the council and to the public."*

LLAL makes very limited disclosure to the public. Board minutes are not published and LPA meetings discussing LLAL affairs are held in private.

¹ From "Airport Suppliers.com" website

There has been no disclosure of discussions resulting in LLAL's decision in November 2021, taken by councillors and council officers acting in their capacity as directors², to waive £45 million of concession fees, in effect public money (according to the LPA's website Luton Airport is owned on behalf of the people of Luton), to settle a "Force Majeure" claim brought by the Applicants. As the global law firm Norton Rose Fulbright observed in May 2020, successful claims for compensation under Force Majeure clauses are rare.³ In addition, the Concession agreement was extended from 31 March 2031 to 31 August 2032.

Without transparency, members of the public cannot assess whether the settlement was prudent or necessary, or a result of a contract unusually favourable to the Applicant, or a reflection of the imbalance of negotiating power and expertise between the two parties.

Further evidence of fundamental weaknesses in governance can be seen in the LLAL accounts for the year ending 31 March 2021, and the letter from Ernst & Young ("EY") to the LPA dated 6 September 2022. I also sense that this extends to an apparent weakness in planning control which led to the history of breaches of noise contour limits and subsequent non-enforcement.

3. LLAL accounts for the year ending 31 March 2021

Despite the limited commercial experience of its directors, LLAL has made very large capital investments in projects intended to support the airport operation, most recently the DART fast passenger transit system linking the airport to Luton Airport Parkway station.

LLAL's 2020-21 accounts report an impairment of £184.7 million in the valuation of DART even before it has opened, writing down the asset from £261.7 million costs previously capitalised in the course of construction to a value-in-use calculation of £77 million. The impairment alone represents just under 120% of the total Luton Borough Council income budget for the year, and is more than twice the total increase in revenue to LLAL generated by the rapid growth in passenger numbers from 2014 to 2019. The combined result for Luton over the

² The CSPL stated further that *"in general, we suggest that local authorities consider councillors or officers having observer, rather than director, status on a relevant board so as to minimise potential conflicts of interest. Thirdly, both the body and the local authority need to practice ongoing assurance, oversight, and transparency, and regularly review the governance procedures to ensure that they are still appropriate"*

³ In a May 2020 paper entitled "Q&A on COVID-19-related force majeure claims" they advised: *"In rarer cases, the contract will allow the affected party to claim financial compensation from the non-affected party for costs associated with the force majeure event. In those circumstances, carefully check the costs that the affected party is entitled to, how these should be calculated and what (if any) mitigation obligations apply. If you are the claiming party, do not assume that these costs will be easy to recover in the current economic climate."* This is in cases where one party is unaffected.

period is thus far worse than if there had been no growth and no DART, leaving aside the effects of the pandemic and the Force Majeure settlement.

Combined with the onerous interest payments to the LPA, and the Force Majeure settlement, this impairment has left LLAL in a precarious financial situation, with borrowings now over £500 million up from £350 million as reported in the 2020-21 accounts. Yet the valuation of the airport asset was reassessed by LLAL's directors in the 2020-21 accounts, resulting in an upward restatement of the previous two years' assets by £887 million before tax provisions.

4. Audit opinion: PricewaterhouseCoopers ("PWC") in respect of LLAL

External auditors do shine some independent light on what has happened under the veil of corporate secrecy. PWC, a leading accountancy firm, issued a qualification of LLAL's accounts in respect of the airport valuation, stating:

"We have independently developed a reasonable range for the estimate of the valuation, based on assumptions which we considered to be appropriate, of between £835m and £1,300m. The directors' valuation of £1,488m falls outside what we consider to be a reasonable range."

The LLAL directors' valuation exceeds the midpoint of the PWC range by £420 million, and would have to be reduced by £188 million even to reach PWC's most optimistic reasonable assessment.

PWC also noted a material uncertainty related to going concern, arising out of the need for further financial support from the owner, the LPA. Until the DART is operational, the only material source of funds to support interest payments to the LPA is from concession fees, and under the Force Majeure settlement the concession fees have been reduced by £45 million over 6 years.

PWC subsequently resigned as auditors to LLAL. In my experience, this is an extremely serious signal of "no confidence" in the board.

5. Audit letter from Ernst and Young ("EY") in respect of Luton Borough Council

Leading auditors EY have been unable to agree the LPA's accounts for 2018/19 or any subsequent year. They are now nearly three years overdue and the auditors stated in a letter dated 1 September 2022 that:

"Following our review of the revised unaudited financial statements, we are unable to conclude our audit of Luton Borough Council ('the Council') for the year ended 31 March 2019. We have been unable to obtain sufficient and appropriate evidence on which to base our audit opinion and our concerns relate to five areas of the Council's financial statements. We consider that the effects on the financial statements from these areas and any associated undetected misstatements could be both material and pervasive to the financial statements as a whole."

The areas of significant concern are listed as:

- 1. Valuation of Luton Airport
- 2. Accounting for the costs incurred on the LLAL Development Consent Order for further Airport expansion.
- 3. Accounting for Infrastructure Assets.
- 4. Prior period restatement in the group accounts for the net pensions liability
- 5. Adequacy of accounting adjustments and disclosures in the revised 2018/2019 financial statement

Regarding Airport valuation, they share the view of PWC and state *“we are unable to conclude whether or not the revised valuation of the Airport as at 31st March 2019 and for the prior periods is within an acceptable range of estimation and uncertainty and has been reliably measured.”* This is not a definitive opinion, as further valuations have been commissioned, so it is possible that this item may eventually become an “emphasis of matter” because of *“very significant material estimation uncertainty implicit in the Airport valuation assumptions”*.

For both PWC and EY the estimated range of uncertainty is of the order of three times the LPA’s annual revenues, or eight times LLAL’s revenues before the pandemic.

Regarding the DCO costs, EY say that: *“We have not been able to obtain sufficient and appropriate evidence from the Council that the costs incurred to date on the DCO application are all, or in part, eligible to attributable to phase 1 of the proposed expansion”* and as such cannot be capitalised as assets.

Under adequacy, EY list seven different areas in which they still have significant concerns, including that *“Note 4 (assumptions made about the future and other major sources of estimation uncertainty) does not make any disclosure about the Airport valuation”*. In other words the LPA did not see any need to discuss this source of uncertainty in their Notes.

In conclusion EY refer to their obligations under the Local Audit and Accountability Act 2014.

*“Given the matters set out in this update, we have serious concerns over the Council’s ability to produce revised 2018/19 and subsequent years accounts that properly reflect the applicable financial reporting framework, professional accounting standards and provide sufficient and appropriate information and explanations to substantiate critical accounting judgements, estimation risks and uncertainties, **particularly those relating to the Council’s ownership and exposure to London Luton Airport Limited.***

*In the event of a disclaimer of our audit opinion, urgent steps will need to be taken by management to address our concerns and remove **the limitations which are preventing us or any other external auditor being able to form the basis of an opinion on the Council’s financial statements.** We are considering writing to the Secretary of State of Department for Levelling Up, Housing and Communities (DLUHC) under our statutory powers within the Local Audit and Accountability Act 2014 setting out our audit position and concerns, and our view of **the improvements that the Council needs to make urgently to their financial reporting arrangements.**”*

6. The Chartered Institute of Public Finance and Accountancy (“CIPFA”) review

In June 2021, as a condition of emergency COVID funding, the Department for Levelling up, Housing and Communities commissioned CIPFA to review the LPA’s financial arrangements. Its report states:

“LBC’s auditors have not yet issued their opinion on the Authority’s 2018/19 and 2019/20 accounts. They require additional assurances on ‘going concern’ and post-balance sheet events in regard to the level of exposure the Council expects to take on through its airport subsidiary stabilisation package, the recoverability of the debenture loans issued by the Council, whether aspects of spend on airport access and other improvements can be treated as adding capital value and the scale of borrowing relative to the overall value of ownership of the airport to the Council. The Authority is still in the process of providing information to their auditors. It will be important that Luton follow proper accounting practice and make appropriate provisions should any doubts emerge in these areas.”

The EY letter indicates that the LPA is not yet in compliance with this requirement.

7. Noise breaches and non-enforcement

It is a matter of record that the Airport was in breach of its noise contour planning conditions in each of the years 2017-2019; based on forecasts provided to the LPA it would have breached them again in 2020 if not for the COVID pandemic. At no stage has enforcement action been taken by the LPA despite the repeated and worsening nature of the breaches.

8. Significance for current planning application

In summary I would suggest that this planning application is quite different from a carefully prepared, properly contextualised, process of local planning development. The extended period of inadequate and increasingly impenetrable documentation, multiple consultations leading to “consultation fatigue” and a change of approach between 2019 and 2021 smacks of something born of commercial necessity rather than something in keeping with a properly curated Local Plan. The adoption of a hastily revised Masterplan a week before the planning meeting is just one example. The governance and audit reviews I have cited provide other reasons why this should be looked at as a special case:

- According to the CSPL on the one hand and two leading audit firms on the other, there are considerable weaknesses in the LPA’s and LLAL’s governance, financial and reporting arrangements.
- The LPA has made loans of three times its annual income to LLAL and is dependent in the longer term on revenue from LLAL to enable it to deliver public services.
- LLAL’s balance sheet rests entirely on assumptions of the future value of the airport after the termination of the current Concession Agreement, as the present value of concession fees discounted at 8% does not cover the debt to the LPA even if the maximum passenger numbers are achieved in every year from 2023 onwards.

- The LPA has allowed serious, repeated breaches, despite advance warning through the forecasting mechanism, suggesting that it prioritises commercial gain over planning protection. LLAL's self-inflicted financial situation creates an even more stark and still-unresolved conflict of interest for the LPA, which now has a pressing need to support it and the Applicant in maximising revenues through increased passenger throughput regardless of noise so that the huge debt to the LPA can be serviced..
- It therefore comes as no surprise that the LPA granted the Applicant permission to increase the noise contours by around 13-15% before the application was Called-In.
- Under the direction of the LPA through its nominated board members, LLAL has spent some £60 million on plans to increase capacity at the airport from the current 18 million passengers per annum to 32 million, showing the LPA's ambition for aggressive growth at the airport. The LPA has not reached agreement with its auditors about the proper accounting treatment of this expenditure. The cost involved in preparing these plans, which if approved would cause very significant environmental harms, would clearly have been better spent bringing governance and financial management and reporting capabilities up to acceptable standards.
- As a result of the last few years, Luton is already worse off. While, like everyone, it has suffered the effects of the pandemic, most of the losses have been self-inflicted as a result of decisions taken in secret by councillors acting in their capacity as directors of LLAL. Had the Airport operation followed the path charted in 2013 of expansion over 15 years to 18 million passengers per annum, with sound financial disciplines and properly informed decision making, the people of Luton would have been far better off financially. Recent history gives no support to an assumption that further expansion of the Airport will deliver benefits either to the LPA's finances or to the community as a whole.
- The socio-economic arguments being presented here are in my view born of self-inflicted folly, not reasonable necessity.