Title: Proposals to devolve local major schemes for the next Spending Review	**Impact Assessment (IA)**
IA No:	**Date:** 31/01/2012
Lead department or agency: DfT	**Stage:** Consultation
Other departments or agencies:	**Source of intervention:** Domestic
	Type of measure: Other
	Contact for enquiries: Karl Murphy 020 7944 0079

Summary: Intervention and Options

RPC: RPC Opinion Status

Cost of Preferred (or more likely) Option				
Total Net Present Value	**Business Net Present Value**	**Net cost to business per year** (EANCB on 2009 prices)	**In scope of One-In, One-Out?**	**Measure qualifies as**
£48.3m	£0m	£0m	No	NA

What is the problem under consideration? Why is government intervention necessary?

The Government has delivered an affordable programme of Local Authority Major Schemes out to 2014/15, prioritising the best of the transport schemes left over from the previous Government's Regional Funding Allocation process. The Government now has the opportunity of putting in place a new system for the next Spending Review period, which will hand real control over decisions to local people, so that decisions can be more responsive to local economic conditions and needs. This is consistent with the Government's commitment to the devolution of power and greater financial autonomy to local government and community groups.

What are the policy objectives and the intended effects?

The main objective is designing a system which is more responsive to local economic conditions, delivers value to the tax-payer and enables local growth. Other policy objectives are also important including ensuring sustainable development, tackling carbon emissions and protecting the environment in bringing forward new transport schemes beyond 2014/15.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

It is assumed that the budget is allocated to around 20-25 local transport consortia (option 2), made up of adjoining Local Enterprise Partnerships. However, the consultation paper relates to forming local transport bodies at individual LEP scale. The Government wishes to encourage the scale of funding necessary for meaningful decisions whilst making decisions more responsive to local economic conditions and needs, and more transparent. There is little evidence on the impacts of devolving local major schemes, however, there is a strong case that it will place higher weight on local priorities. The 'do nothing' (option 1) is maintaining a central competition, with DfT scrutinising and assessing bids, and making final decisions. Alternative options are: allocating budgets and decisions to individual local transport authorities (option 3) and putting in place a central appraisal and approval process with sub-national bodies advising on priorities, similar to the previous Government's Regional Funding Allocation process (option 4).

Will the policy be reviewed? It will/will not be reviewed. **If applicable, set review date:** Month/Year

Does implementation go beyond minimum EU requirements?			N/A		
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.	**Micro** Yes/No	**< 20** Yes/No	**Small** Yes/No	**Medium** Yes/No	**Large** Yes/No
What is the CO_2 equivalent change in greenhouse gas emissions? (Million tonnes CO_2 equivalent)			**Traded:** N/A	**Non-traded:** N/A	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible SELECT SIGNATORY: .... Date: ....

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Summary: Analysis & Evidence

Policy Option 2

Description: Allocating budgets and handing decisions over to local transport consortia (preferred option)

FULL ECONOMIC ASSESSMENT

Price Base Year 2011	PV Base Year 2011	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: 23.6	**High:** 66.0	**Best Estimate:** 48.3

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	Optional		0.9	**7.8**
High	Optional		0.9	**7.8**
Best Estimate			0.9	**7.8**

Description and scale of key monetised costs by 'main affected groups'

£940,000 per annum cost for putting in place processes for assessing and prioritising transport schemes in each of the 25 consortia.

Other key non-monetised costs by 'main affected groups'

Non-monetised costs may arise because devolving decisions and funding on local major schemes may lead to different local authority major schemes being taken forward. There is currently very little evidence to make a reasonable prediction of what transport schemes would be funded under this option.

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	Optional		3.8	**31.4**
High	Optional		8.9	**73.8**
Best Estimate			6.7	**56.1**

Description and scale of key monetised benefits by 'main affected groups'

Local consortia administration costs: savings of £6.4m per annum (range of £3.5m to £8.6m) from undertaking less work to meet central requirements.

Central government administration costs: average annual saving of £306,000 per annum.

Other key non-monetised benefits by 'main affected groups'

Non-monetised benefits may arise because devolving decisions and funding on local major schemes may lead to different local authority major schemes being taken forward. There is currently very little evidence to make a reasonable prediction of what transport schemes would be funded under this option. This option will make decisions more accountable at the local level and responsive to local economic conditions and could potentially encourage increased third party funding.

Key assumptions/sensitivities/risks — **Discount rate (%)** 3.5

It is assumed that DfT has a reduced role in decisions, although this may vary across bodies and consortia, depending on what is right for them. The ability for consortia to fund large transport projects will depend on the number of consortia formed - on average, 25 consortia would have funding (including local and third party) over a four year period of £90m. If number increased to 37 this falls to £61m - the higher the number, the greater the risk that better value schemes are lost.

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:			**In scope of OIOO?**	**Measure qualifies as**
Costs: N/A	**Benefits:** N/A	**Net:** N/A	No	NA

Summary: Analysis & Evidence

Policy Option 3

Description: Allocating budgets and decisions to 87 individual local transport authorities

FULL ECONOMIC ASSESSMENT

Price Base Year 2011	**PV Base Year** 2011	**Time Period Years** 10	**Net Benefit (Present Value (PV)) (£m)**		
			Low: 34.9	**High:** 80.0	**Best Estimate:** 61.0

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	Optional		0	**0**
High	Optional		0	**0**
Best Estimate			0	**0**

Description and scale of key monetised costs by 'main affected groups'

It is assumed that this option would place no additional burdens on local authorities as they would use existing frameworks to assess schemes.

Other key non-monetised costs by 'main affected groups'

Non-monetised costs may arise because devolving decisions and funding on local major schemes may lead to different local authority major schemes being taken forward. There is currently very little evidence to make a reasonable prediction of what schemes would be funded under this option.

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	Optional		4.2	**34.9**
High	Optional		9.6	**80.0**
Best Estimate			7.3	**61.0**

Description and scale of key monetised benefits by 'main affected groups'

Local government administration cost: Appraisal costs of £7.0m per year across the programme (range of £3.9m to 9.3m) on the basis that local authorities prioritise and select schemes using existing frameworks. Central government administration cost: policy and economist support savings of £306,000 per annum.

Other key non-monetised benefits by 'main affected groups'

Non-monetised benefits may arise because devolving decisions and funding on local major schemes may lead to different local authority major schemes being taken forward. There is currently very little evidence to make a reasonable prediction of what schemes would be funded under this option. This option will make decisions more accountable at the local level and responsive to local economic conditions and could potentially encourage increased third party funding.

Key assumptions/sensitivities/risks — **Discount rate (%)** 3.5

Assume DfT has a reduced role in decisions. Promoters undertake appraisal and assessment in line with the Transport Business Case. The high number of authorities would mean that few would have sufficient funding to proceed with the most expensive schemes (which could make it impossible to deliver regionally strategic schemes). Allocating funding amongst 87 transport authorities also reduces the scope for (and benefits of) prioritising those schemes which most important schemes at a sub-national level.

BUSINESS ASSESSMENT (Option 2)

Direct impact on business (Equivalent Annual) £m:			**In scope of OIOO?**	**Measure qualifies as**
Costs: N/A	**Benefits:** N/A	**Net:** N/A	No	NA

Summary: Analysis & Evidence — Policy Option 4

Description: A centrally run appraisal and approval process with sub-national bodies advising on priorities. Rolling programme with schemes approved throughout each Spending Review period.

FULL ECONOMIC ASSESSMENT

Price Base Year 2011	PV Base Year 2011	Time Period Years 10	Net Benefit (Present Value (PV)) (£m)		
			Low: 16.3	**High:** 67.3	**Best Estimate:** 44.1

COSTS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Cost** (Present Value)
Low	Optional		0.3	**2.5**
High	Optional		0.3	**2.5**
Best Estimate			0.3	**2.5**

Description and scale of key monetised costs by 'main affected groups'

£300,000 per year cost for putting in place processes for assessing and prioritising transport schemes based on 8 sub-national bodies being in place.

Other key non-monetised costs by 'main affected groups'

Non-monetised costs may arise because devolving decisions and funding on local major schemes may lead to different local authority major schemes being taken forward. There is currently very little evidence to make a reasonable prediction of what transport schemes would be funded under this option.

BENEFITS (£m)	**Total Transition** (Constant Price)	Years	**Average Annual** (excl. Transition) (Constant Price)	**Total Benefit** (Present Value)
Low	Optional		2.3	**18.8**
High	Optional		8.4	**69.8**
Best Estimate			5.6	**46.6**

Description and scale of key monetised benefits by 'main affected groups'

Local government administration costs: savings of £5.6m per year (range of £2.2m to £8.4m) as a result of fewer schemes being developed to outline business case.

Central government administration costs: small reduction (£16,000 per annum) in costs resulting from fewer resources required to support an intensive bid system.

Other key non-monetised benefits by 'main affected groups'

Non-monetised benefits may arise because devolving decisions and funding on local major schemes may lead to different local authority major schemes being taken forward. There is currently very little evidence to make a reaonable prediction of what schemes would be funded under this option.

Key assumptions/sensitivities/risks — **Discount rate (%)** 3.5

It is assumed that early shortlisting reduces the incentive for local authorities and third parties to maximise their own contribution due to long timescales to approval and the fact they have already been allocated indicative budgets. Estimates of local authority and developer contributions based on previous RFA system.

BUSINESS ASSESSMENT (Option 3)

Direct impact on business (Equivalent Annual) £m:			In scope of OIOO?	Measure qualifies as
Costs: N/A	**Benefits:** N/A	**Net:** N/A	No	NA

Evidence Base (for summary sheets)

Initial background and rationale for the policy

Local major scheme funding is a key lever for enabling growth in local areas, and represents one of the Department's contributions to the decentralisation agenda.

The previous Government's Regional Funding Allocation process had a veneer of decentralisation, but little of the real substance. Initial decisions were taken by unelected and unaccountable regional bodies, and advised and influenced central government, leaving central government to make the final decisions.

The regional tier is in the process of being dismantled. The Localism Act has abolished regional strategies and the regional planning tier.

We now have the opportunity of designing a new system for beyond 2015, which shifts power from the centre into the hands of local communities and makes decisions more accountable at the local level and responsive to local economic conditions.

Local partners have already successfully demonstrated that they are willing and able to pool resources and develop shared approaches to joint problems. They are best placed to make the tough trade-offs between schemes, not central government or its agencies. They need to be further empowered to make decisions which are right for their local areas and which deliver outcomes that are more transparent to local people.

The Department will spend around £1.5bn on major local transport schemes over this Spending Review period (a further enhancement of £170m was made as part of the Autumn Statement). The level of funding for the period post 2014/15 will be decided in due course.

Description of options considered (including do nothing);

Option 1 (do nothing option) – Local authorities bid to Department for Transport (DfT) for schemes based on the Transport Business Case. DfT scrutinises bids and awards funding to the best schemes assessed across all five cases.

DfT currently operate a bidding system to allocate funding for local major schemes. This was put in place as a transitional system in response to the abolition of the regional planning tier whilst decentralised options for allocating funding were developed. We have assumed, at this stage, this option would continue in the event that none of the other options are pursued.

Our experience is that competitions are usually over-subscribed, with more bids than there is funding for. Therefore, we have assumed that there is an initial pre-qualification stage in which the number of bidders is reduced so that there is a ratio of bids to available funding of 1.3 (i.e. £1.30 of bids for every £1 available). This is consistent with the approach that has been taken by DfT to prioritise the remaining funding available for local major schemes over the current Spending Review period (see: http://www2.dft.gov.uk/adobepdf/165237/706167/transportschemesupdate.pdf).

We have also assumed that the process of short listing, engagement and selection takes two years and is repeated at every Spending Review. Schemes are prioritised by DfT as a result of a competitive process assessed using the five case Transport Business Case model (see: http://assets.dft.gov.uk/publications/transport-business-case-tbc-/transportbusinesscase.pdf). Local Authorities have some discretion about what schemes to put forward but competitive pressure will inevitably place constraints on what can be funded.

Option 2 (preferred option) – Allocating budgets and decisions to 20-25 local transport consortia

The consultation paper includes options for how to put in place a system which encourages strategic investment decisions, and sets out the Government's preference to leave it to local discretion to create local transport consortia in order to deliver a handful of big schemes and create a scale of funding necessary for local major schemes to be delivered. The Government has assumed for the

purposes of this Impact Assessment that around 20-25 local transport consortia are formed, made up of several Local Enterprise Partnerships (or local transport bodies), and this is reflected as the leading policy option for which impacts are assessed.

Local Enterprise Partnerships are locally-owned partnerships between local authorities and businesses and play a central role in determining local economic priorities and undertaking activities to drive economic growth and create local jobs. They are also a key vehicle in delivering Government objectives for economic growth and decentralisation, whilst also providing a means for local authorities to work together with business. At the time of finalising the Impact Assessment, there are 39 Local Enterprise Partnerships in England, including one in London (London is not covered by these local major scheme proposals).

Local transport consortia will be formed by a process of collectively identifying functional economic areas along with realistic partnerships. Their primary role would be the same as a local transport body to decide and fund transport schemes across the consortia area. Consortia would need to put in place measures to ensure standards on governance, decision making and financial management are met.

For the purposes of this Impact Assessment we have assumed that 25 local transport consortia will be formed although the precise number and configuration will depend on responses to the consultation and the decisions of individual Local Enterprise Partnerships and local transport bodies, being wholly consistent with localism.

We have assumed that promoters will still need to undertake appraisal and assessment of options against the five cases in the Transport Business Case approach to meet statutory and planning requirements and to demonstrate value for money to auditors. However, final decisions on which schemes to prioritise will be made locally.

Under this option the formal role of the Department in the scrutiny of scheme appraisals is removed, although it is possible that this will be different for individual consortia, depending on the level of support which they might individually need on modelling, appraisal and evaluation.

Option 3 – Allocating budgets and decisions to 87 individual Local Transport Authorities

Under this option, funding and decisions would be devolved to Local Transport Authorities. County councils and unitary authorities are Local Transport Authorities and, as they have elected members, have democratic accountability. Metropolitan District Councils are the highway authority for their areas and likewise have democratic accountability. Like option 2, scheme promoters are required to develop a robust business case to support decisions locally and decisions will only be decentralised once appropriate governance structures are in place and following the Department's central assurance.

We have assumed that promoters will still need to undertake appraisal and assessment of options against the five cases in the Transport Business Case approach in order to meet statutory and planning requirements, demonstrate value for money to auditors and to make the case to their local partners. However, final decisions on which schemes to prioritise will be made locally rather than by Central Government.

We have assumed that the formal role of the Department in the scrutiny of scheme appraisals is reduced, although it is possible that this will be different for individual authorities, depending on the level of support which they might need on modelling, appraisal and evaluation. However, we have under this option assumed that schemes are prioritised by local areas with decisions informed by locally developed frameworks.

Option 4 – A centrally run appraisal and approval process with sub-national bodies advising on priorities. Rolling programme with schemes approved throughout each Spending Review.

This is the system most similar to the previous Government's Regional Funding Allocation (RFA) process. Schemes are shortlisted by sub-national bodies subject to an indicative funding envelope, and then scrutinised by DfT. Each scheme is assessed on its own merit using the Transport Business Case approach and approved only once DfT is satisfied that the business case is robust and the scheme is aligned with the Department's strategic objectives.

As under the previous RFA system, we have assumed that there is a rolling programme with schemes approved throughout each Spending Review period. DfT acts as a gateway to ensure value for money and wider appraisal requirements are met. We have assumed this option gives local authorities greater freedom to put forward schemes they would like, although they are limited by requirements to meet minimum standards, for example on value for money and the constraints/objectives of the sub-national decision making processes.

Monetised and non-monetised costs and benefits of each option (including administrative burden);

In considering the cost and benefits of the options, we have focused on the potential administrative efficiencies which can be achieved from a more decentralised approach. The analysis does not attempt to analyse the impact on the overall scale of the programme – which is a matter for the Spending Review and individual local authorities. Neither does this analysis seek to assess the impact of local authorities/transport consortia taking different decisions than central government about which major schemes to prioritise. This is discussed further in the “risks and assumptions” section below.

The following bullet points describe the main administrative costs and savings associated with each option. These have been assessed and valued as changes on option 1 and are summarised in table 1.

- ***Direct costs incurred by local transport consortia and local authorities when prioritising schemes*** – Under options 2 to 4, sub-national bodies will be expected to take a greater role in the prioritisation of Local Major Schemes. Under option 2 it is assumed Local consortia will need to put in place processes for assessing and prioritising schemes. It is assumed that the preparation of business cases will still be the responsibility of relevant local authorities. Assuming 25 consortia at £150,000 every four years (this is the amount based on support to regions in RFA1) suggests an average cost of £940,000 per annum. It is assumed that option 3 imposes no new costs on local authorities on the basis that they will prioritise and select schemes using existing local frameworks (although this is subject to a high level of uncertainty). Under option 4 it is assumed that sub-national bodies will need to put in place processes for assessing and prioritising schemes. Assuming 8 sub-national bodies at £150,000 every four years (this is the amount based on support to regions in RFA1) suggests costs of £300,000 per annum.

- ***Administration costs to central government*** – Under the do nothing scenario (option 1) we estimate the cost of administering the programme at £364,000 per annum. Our analysis suggests that this would remain broadly the same if the Department were to move back toward a RFA type model (option 4). Administration costs reduce significantly under options 2 and 3 as central government no longer has to scrutinise and approve individual business cases. Whilst we anticipate some residual activities to support the programme (e.g. briefings for ministers, evaluation, technical support where applicable), our best estimate is that these two options deliver savings of around £300,000. The scale of these savings may vary depending on decisions about the level of central support to be provided and the role of DfT in evaluation and monitoring.

- ***Administration costs on local transport authorities and local transport consortia*** – We have estimated that appraisal costs (modelling, data collection, appraisal and surveys for environmental impact assessments) under the status quo are in the region of £20m per annum (range of £13m to £28m) across whole programme. The greatest saving of appraisal costs is likely to occur under option 3 where individual transport authorities are undertaking their own assessments. We estimate appraisal cost savings of £7.0m (range of £3.9m to £9.3m) on the basis that local authorities prioritise and select schemes using existing local frameworks. Appraisal costs under the preferred option represent savings of £6.4m per annum (range of £3.5 to £8.6m per annum). These savings result from local authorities having to undertake less work to meet specific DfT requirements. A small allowance (0.1% of total scheme costs) is retained for undertaking work to meet specific local transport consortia requirements.

Table 1. Summary of annual administration costs/savings from options (options 2-4 shown as change on option 1)

	Direct costs	Central Government Administration Costs	Local Administration Costs
Option 1	*N/A*	*£364,000*	*£20,345,000*
Option 2	+£940,000	-£306,000	-£6,437,000

Option 3	NIL	-£306,000	-£7,024,000
Option 4	+£300,000	-£16,000	-£5,592,000

There are a number of non-monetised impacts that have informed the overall assessment of options:

- The more centralised the processes are, the longer the delays to bringing schemes forward would appear to be e.g. as DfT request additional information or for new analysis to be undertaken. There are currently unquantified benefits (in relation to options 2 and 3) of starting schemes earlier, which could be significant. This implies that existing problems remain unresolved for longer while there is greater potential for costs to escalate. Delaying a maintenance project for example can significantly increase the costs of repair.
- Options 2 and 4 increase the opportunities for local authorities and LEPs to consider and manage the interdependencies and trade-offs between different infrastructure projects (including non-transport infrastructure) and other policies which affect the sub-regional economy. Better co-ordination of these decisions can help reduce costs (e.g. by sharing inputs), increase the value of investment (e.g. by maximising synergies between projects) and improve future flexibility (e.g. leave open options for future upgrades or new technologies).
- The formation of local transport consortia (option 2) could encourage local authorities to share best practice and resources e.g. by rolling out shared service models for delivery of transport planning advice. This could provide further efficiency savings and increase transport expertise across local authorities.

Risks and assumptions;

The risks and assumptions are considered in two parts. In the first sub-section we consider the risks and opportunities associated with the second-round effects, particularly in relation to the impact a new system could have on which schemes are implemented. These are given explicit consideration here as they have informed our selection of a preferred option. In the second sub-section we consider the risks and assumptions underpinning the analysis of administration costs described above.

Impact of options on scheme selection and third party/local authority funding

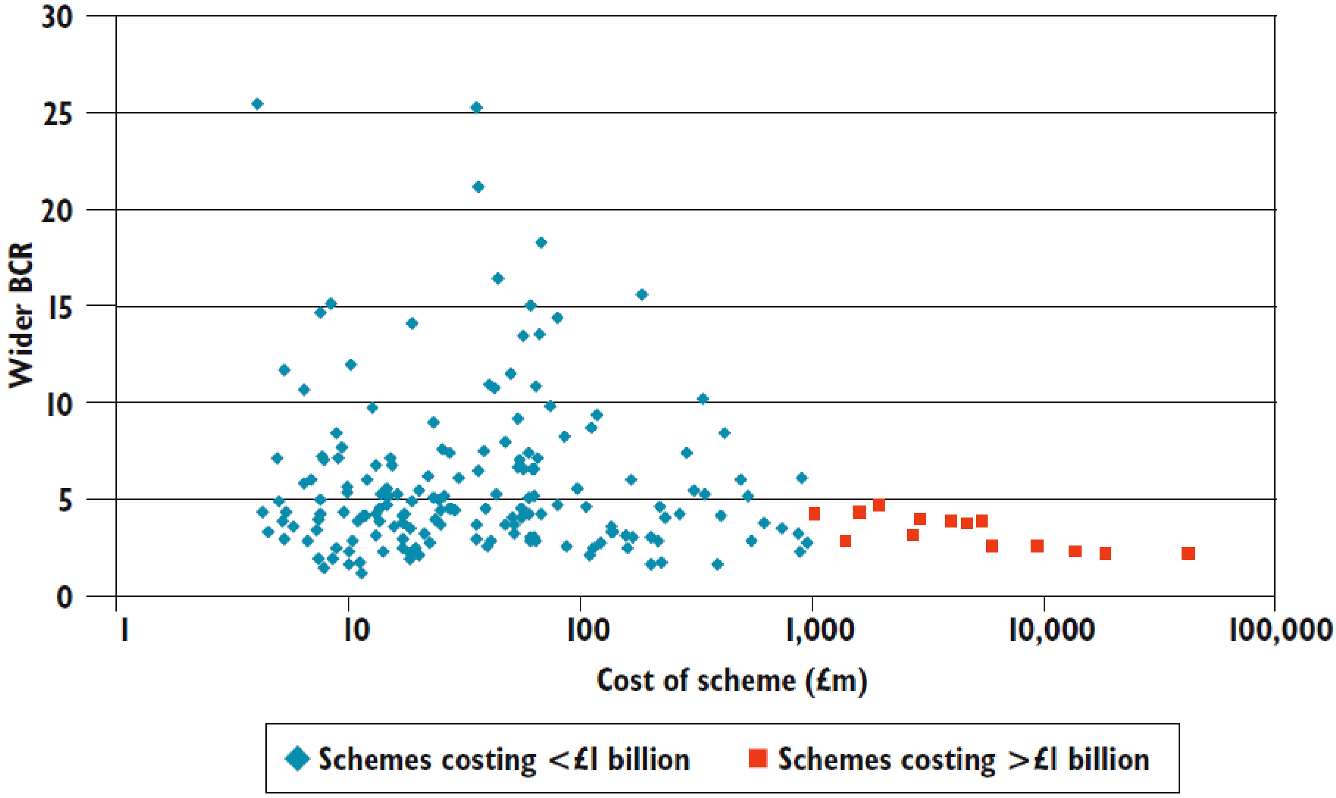
Overall there is a lack of evidence about how local communities (including local authorities and Local Enterprise Partnerships) will respond to the increased freedoms associated with the decentralisation of local major scheme funding. In refining the options under consideration and selecting the preferred option we have considered the following factors:

- ***A new approach leads to different decisions about which schemes are prioritised –*** Decentralising decision making is likely to place higher weight on local priorities, making decisions more effective at addressing local needs. It is possible that schemes implemented under these new arrangements would not have been funded under the do nothing option (and vice versa). This is dependent on the decisions made by local authorities/local transport consortia and there is very little evidence with which to make a reasonable prediction. To help ensure that value for money continues to be secured in the options under consideration, DfT propose seeking assurance on systems and institutions being in place to ensure benefits and costs are properly assessed before decentralising funding.
- ***A new approach may encourage third parties to provide additional funding towards the funding of major schemes –*** increased local control over decisions may help local authorities raise additional funding locally as there is greater certainty about the scheme progressing (e.g. from developers, retention of business rates and so on). We have assumed under the do nothing scenario that third parties will fund an amount equivalent to 12% of DfT central funding: £46m per annum on average (source: internal DfT analysis of interim returns for the Development Pool). Based on the programme of local major schemes delivering an average BCR of 4, a doubling of third party funding (compared to the do nothing scenario) would provide additional net benefits of £138m (over a 60 year period) per annum. Our estimate is that this is most likely to occur under options 2 and 3. Based on our experience of the RFA process, our best view is that third party contributions would fall under option 4. Our view is that early short listing may reduce the scope to get third party funding due to the long timescales to approval and limited incentive to contribute

once a scheme is short-listed as funding has already been provisionally allocated to take the scheme ahead.

- ***The size of decision making bodies may constrain the selection of schemes –*** The higher the number of the consortia, the more difficult it will become to fund larger, more expensive schemes. Based on existing levels of expenditure on local authority major schemes, local transport consortia (option 2) would receive on average total funding of £90m over a four year period. This assumes that there are 25 consortia. If the number of consortia increased to 37 the amount of available funding falls to £61m (not accounting for how the funding may be distributed, for example by formula). Under option 3, the 87 local authorities would receive on average total funding of £26m over a four year period. Whilst reduced funding may limit the ability of local authorities/transport consortia to address large scale strategic problems on their networks it is not immediately apparent that this would reduce the overall benefits delivered by the local major scheme programme. The Department's analysis as part of the Eddington Report on the value of smaller schemes demonstrates that they can deliver very high returns as indicated below.

Figure 1.8: Economic returns of smaller schemes relative to larger schemes (those costing more than £1 billion)[a]



[a]Costs are in a log scale.
Source: DfT.

(Eddington Main Report, Volume 3 Figure 1.8 on page 132) - http://news.bbc.co.uk/1/shared/bsp/hi/pdfs/01_12_06eddingtonvol3.pdf

The Report sets out that the "reasons for the high returns are likely to vary according to the particular intervention. It may be that because lower-cost schemes tend to be smaller scale, they are more likely to be targeted on particular problems and pinch points that provide significant benefits for many travellers. In absolute terms, where a small and a large intervention offer the same wider BCR, the contribution of larger schemes is of a much higher magnitude for a much higher cost. However, small schemes may not be of sufficient scale to tackle the magnitude of future challenges. In some cases, the highest return option in the longer term for a given problem may be a large-scale and high-cost intervention."

- ***The more decision making bodies there are, the more difficult it is to ensure funding is allocated to areas that can deliver the best schemes*** – Under the decentralisation options (options 2 and 3), funding would be allocated to individual local authorities or on behalf of individual LEP areas, and then schemes would be prioritised and selected within the authority/consortia. This leaves open the possibility that the best scheme in one consortium has a weaker business case than a rejected scheme in another consortium. Whereas under the current system it is possible to trade-off schemes from across England and target resources on schemes which deliver the strongest business case. Given that it is not possible to calculate benefits from not trading-off schemes, we have included a stylised example below (on page 13) to illustrate the potential impacts. We have indicatively estimated the maximum loss in benefits from this implicit restriction as £200m per annum under option 2 and £560m per annum under option 3. These losses in benefits should be considered illustrative (for example, these estimates make the crude assumption that you prioritise those schemes with the highest BCR). Whilst the uncertainties associated with this analysis suggest that we shouldn't place too much emphasis on the absolute values reported above, the relative difference between options 2 and 3 suggest that any potential efficiency loss significantly increases if funding were devolved to local authorities (option 3).

Risks and assumptions underpinning analysis of administration costs

- Net administrative savings may not be as high. Some of the additional costs associated with the re-submission or addressing questions may be picked up during the planning process and/or local consultation. These estimates make no allowance for increases in benefits and reductions in costs associated with the scrutiny role (e.g. cost savings achieved as a result of central scrutiny).
- The analysis assumes that the same number of schemes are developed under the new arrangements prior to shortlisting. The number of schemes developed in the future will depend on the specification of new prioritisation processes but lowering the cost of appraisal may increase the number of authorities willing to take the risk of developing a business case.
- Often DfT will liaise directly with consultants working on the promoter's behalf on the development of modelling and appraisal. This may act as a form of Quality Assurance on the modelling/appraisal which would no longer be available to local authorities who would need to perform this function themselves. This may reduce the savings available to local authorities.
- The analysis assumes that local consortia generally follow the principles of the Transport Business Case approach and do not introduce any additional requirements of their own. It is worth noting that there may be a loss in benefits from the lower quality of the appraisal, i.e. diminishing returns from appraisal effort as appraisal can often lead to an improvement in the design of the scheme. However, the wider spreading of business cases to a larger number of decision-makers by itself lowers the average benefits, and it can be argued that authorities are reducing their effort and that this reduces the average benefits to society.
- There is a degree of uncertainty about the extent of involvement of a central process, where some consortia may request further central support than others. This will be taken forward on an individual basis depending on the particular needs and asks of individual consortia, and in the context of a central assurance and governance framework.
- It is assumed that all areas in England outside London are covered by the new arrangements. It is feasible that some local transport bodies and Local Enterprise Partnerships decide not to form local transport consortia with other Local Enterprise Partnerships. There is a risk with this that some local areas will decide not to deliver a local major scheme, but instead will bring forward very local, small-scale infrastructure. This infrastructure, however, might never have been possible under the previous system and may also be good value for money.
- Administration costs are held constant in real terms.

Rationale and evidence that justify the level of analysis used in the IA (proportionality approach);

<u>Administration Costs</u>

(a) Cost to local authorities of developing a major scheme business case

60 scheme promoters submitted information on the costs of producing appraisals for major schemes at the time of the NATA refresh (circa 2008/2009). The main details of the survey was as follows:

- Appraisal activities that were included in the survey included data collection, modelling analysis, environmental assessment and appraisal.
- The survey responses varies significantly in terms of quality, accuracy and completeness hence results should be treated with caution.
- It found that on average appraisal accounts for 2.7% of forecast scheme outturn costs.
- There was significant variation in appraisal costs with a reported range of 0% to 12%. However, in around 75% of cases appraisal costs represented less than 4% of total costs.
- The evidence presented suggests that the relative proportion spent on appraisal varied significantly for small major schemes, and that the cost reduced (in proportionate terms) for more expensive schemes. However, there was insignificant evidence to confirm the significance of this trend.

Many of the costs incurred preparing an appraisal would still need to be incurred even if DfT held no formal scrutiny role e.g. to meet local scrutiny and for statutory purposes (e.g. in relation to planning and environmental protection). For the purposes of this Impact Assessment we need to consider the costs imposed by DfT over and above what would incurred anyway, that is in two ways:

- DfT can specifically ask for work to be undertaken on a business case that has been submitted (e.g. clarification questions).
- Promoters may undertake work in anticipation of queries from DfT even though they might not have done this work themselves if they did not need to seek DfT approval and the analysis does not form part of statutory/planning requirements.

There is some limited information in the results of the survey undertaken in 2008/09 on the costs associated with DfT requests:

- Appraisal costs increased by 0.7% of total scheme outturn costs between pre-submission and award of Programme Entry and a further 0.4% by full approval (although the significance of this is unclear as this result is based on a cross-sectional analysis of schemes rather than a panel dataset).
- The promoters of one scheme reported preparation costs of £380,000 of which 35% related to re-submission and DfT questions (£133,000). The costs of resubmission and DfT questions were equivalent to 0.6% of total scheme costs.
- Another partnership reported that it cost a local authority £50,000 on answering DfT questions. This is 0.1% of the estimated outturn cost of £50.9m reported at Programme Entry.

One authority has suggested that they might save roughly in the order of £400,000 as a result of not having to seek DfT approval. This is a high level estimate and makes no distinction between the activities that the promoter undertook in anticipation and response to DfT questions. Given that one of the authority's schemes is expected to cost around £80m this is equivalent to around 0.5% of outturn costs.

Based on the figures above we have assumed that under the old RFA system 2.7% of the costs of a local major scheme are incurred in preparing the business case. To reflect uncertainty around this assumption we have assumed that this varies by +/-1% in the high and low scenarios. Within this we have assumed that 0.5% of costs were incurred meeting specific DfT requirements (range of 0.1% to 0.7%). Under options 2 and 3 it is assumed that the costs of meeting DfT requirements are no longer incurred. Under option 1 it is assumed that only half these costs are incurred as the deadlines associated with the competitive process limit the amount of additional analysis that can be requested by DfT.

The other assumptions applied to generate estimates of administration cost savings in the central case for each option:

- Percentage of costs incurred prior to shortlisting:
  - Option 1: 1% (source: DfT estimate)
  - Option 2: 0.25% (source: DfT estimate)
  - Option 3: 0.1% (source: DfT estimate)
  - Option 4: 0.5% (source: DfT estimate)
- Ratio of bids to available funding prior to shortlisting: 175% for all options (source: DfT estimate)
- Ratio of bids to available funding post-shortlisting: 105% for options 2-4 (source: DfT estimate), 130% for option 1 (source: DfT analysis of interim returns for Development Pool).
- Funding available: £560m for options 1-3 (source: DfT analysis of interim returns for Development Pool – funding from local authorities and third parties is equivalent to 45% of available central government grant. Average funding for local authority majors over SR10 period is £386m). £464m for option 4 (source: DfT analysis of interim returns for development pool –the funding arrangements for the same schemes under the old RFA system would have seen local authorities and third parties only contribute 20% to costs).

The application of these assumptions to generate costs is summarised below.

	Option 1	**Option 2**	**Option 3**	**Option 4**
% of costs incurred prior to shortlisting	1%	0.25%	0.1%	0.5%
Ratio of schemes to available funding	175%	175%	175%	175%
Available funding (per annum)	£560m	£560m	£560m	£464m
Total costs incurred prior to shortlisting (1)	**£9.8m**	**£2.4m**	**£1.0m**	**£4.1m**
% of costs incurred post shortlisting	1.5%	2.0%	2.1%	2.2%
Ratio of schemes to available funding	130%	105%	105%	105%
Available funding	£560m	£560m	£560m	£560m
Total costs incurred post-shortlisting (2)	**£10.6m**	**£11.5m**	**£12.3m**	**£10.7m**
TOTAL COSTS pa (1) + (2)	**£20.4m**	**£13.9m**	**£13.3m**	**£14.8m**
Change on option 1 (per annum)		*-£6.4m*	*-£7.0m*	*-£5.6m*

b) Administration costs to DfT

Analysis of internal management information systems found that the modelling/appraisal of major schemes required staff time of 62 days per month in 2009/10. This was under the old RFA system (e.g. similar to option 4). This was broken down as follows:

- PB4 = 0.5 FTE (50% of time) = 10 days per month
- PB6 = 2.1 FTE split across three people (70% of time) = 42 days per month
- PB7 = 0.5 FTE (50% of time) = 10 days per month

Based on the mid-point of salary ranges for each grade and an allowance for on-costs of 21% this equates to annual costs of £191,000.

The table below sets out what has been assumed about modelling/appraisal support under options 1, 2 and 3.

	Option 1	Option 2	Option 3

PB4	1.25 (2 years out of every 4)	0.25	0.25
PB6	1.75 (2 years out of every 4)	0.75	0.75
PB7	0.5 (2 years out of every 4)	0	0
Average annual cost	£99,000	£57,000	£57,000
Activities assumed	Engagement/support to bidder in year prior to bids and scheme scrutiny	Limited technical support and evaluation	Limited technical support and evaluation

We have also estimated the policy support costs based on the number of employees and the costs associated with their grades for the different options. Under the do nothing option, this is assumed to be £264,000 per annum. Under option 4, this is assumed to be £157k per annum, which is a saving of £107,000 per annum in comparison to the do nothing. We have assumed that for the preferred option (option 2) and option 3 that the policy support costs will be zero. However, in all likelihood, there will be a small level of policy support needed to progress issues and advise Ministers.

The total administration cost savings (per annum) for each option are as follows:

- Option 2: £306,000 (£42,000 savings in modelling/appraisal support and £264,000 savings in administration).
- Option 3: £306,000 (£42,000 savings in modelling/appraisal support and £264,000 savings in administration).
- Option 4: £16,000 (£92,000 increase in modelling/appraisal support and £107,000 savings in administration).

Stylised example setting out the background to the risk that: 'the more decision making bodies there are, the more difficult it is to ensure funding is allocated to areas that can deliver the best schemes overall."

It is not possible to calculate the loss in benefits from the possibility that the best scheme in one consortium has a weaker business case than a rejected scheme in another consortium. There is simply no evidence base to properly assess this risk and we cannot predict the basis on which local transport consortia will select schemes. These estimates, therefore, were not included in the estimates of monetised benefits and costs. However, the below explanation illustrates the potential issues associated with increasing the number of decision making bodies.

The indicative estimate of the potential loss in benefits from not having a funding formula aligned to need, i.e. the risk that funding is not allocated to places which offer the greatest returns, was produced by randomly assigning a distribution of 44 scheme BCRs (drawn from interim submissions made by local authorities bidding for development pool funding) into 22 pairs. This simulated in a crude way the choices faced by 22 Local Transport Consortia faced with a decision between two schemes. The loss in benefits reported (£200m) is based on a comparison of the average BCR obtained when each consortia chooses the scheme with the highest BCR, with the average BCR you would get if you selected the 22 schemes with the highest BCRs nationally.

The potential loss in benefits for option 3 was estimated by comparing the average BCR across all 44 schemes against the average BCR you would get is you selected the 22 schemes with the highest BCR nationally. The principle behind this analysis can be illustrated in the following example. Assume that there are four schemes to select from each costing £10m and that there is £20 million available. The Benefit Cost Ratios for each scheme are as follows:

- Scheme A: 5 (benefit = 50, cost = 10)
- Scheme B: 4 (benefit = 40, cost = 10)
- Scheme C: 3 (benefit = 30, cost = 10)
- Scheme D: 2 (benefit = 20, cost = 10)

It is assumed that by running a competition, central government can select from amongst all schemes and get a maximum benefit of £90m (by selecting schemes A and B). If the £20m budget for schemes is allocated to two transport consortia each with two schemes to select from the maximum benefit that can be achieved could be lower even if the same schemes are on offer:

- If transport consortia 1 has to select between scheme A and B the maximum benefit they can get is £50m
- If transport consortia 2 has to select between scheme C and D the maximum benefit they can get is £30m

Therefore by splitting funding between two transport consortia you have potentially lost out on £10m of benefits.

Summary and preferred option with description of implementation plan

The Government is promoting discussion on a new system for funding and deciding local major schemes for the next Spending Review. A system which gives local areas the greatest freedom and flexibility but ensures value for money, economic growth and sustainable development is delivered.

The Government wishes to encourage a system which enables strategic investment delivery from the bottom-up, and meaningful decisions on priorities at the same time.

Therefore, the Impact Assessment has assumed that the Government will allocate funding to between 20-25 local transport consortia. However, the consultation paper sets out the options for encouraging strategic investment delivery, and proposes that there is no central encouragement or requirement to help promote their delivery. Individual Local Enterprise Partnership areas would get a budget to prioritise whatever schemes were agreed locally, and the Government would stand ready and willing to help facilitate effective partnership working.

Whilst option 3 delivers the greatest administration cost savings, this has been rejected in favour of option 2 (allocate funding and decisions to 20-25 local transport consortia) in order to achieve the scale needed to make meaningful decisions on investment priorities.

But, the design of the new system is the basis of the consultation paper. The consultation paper only sets out what the Government is minded to do, and the Government welcomes comments from local authorities, Local Enterprise Partnerships and others on the questions raised in the consultation paper, together with the assessment in this Impact Assessment.