Transport for the North Scrutiny Committee Meeting – Item 6

Subject:	Draft Funding Framework
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Sponsor:	Barry White, Chief Executive
Meeting Date:	Thursday 30 August 2018

1. Executive Summary:

1.1 A key element of the Final Strategic Transport Plan will be how the infrastructure proposed by TfN, as set out in the accompanying long term Investment Programme, will be funded over the period until 2050. TfN has therefore developed a Funding Framework that will allow its programmes to be delivered. The Draft TfN Funding Framework is attached as Appendix 1 and includes the following key features.

1.2 TfN's work, and the evidence contained within the National Infrastructure Assessment published by the National Infrastructure Commission, indicates that there is sufficient central funding available in the system to meet the investment requirement of around £60 - 70billion over 30 years for strategic transport interventions set out in the Draft Strategic Transport Plan. TfN's proposals are ambitious yet realistic but need to be funded by central government.

1.3 Investment by localities, including city regions within the North, are a key component of the work needed to deliver the transformational and inclusive economic growth that is TfN's objective. In particular, strategic transport investments will often mean consequential requirements for local investment. Some of the required interventions will be funded through current and future devolution deals and targeted funds such as the Transforming Cities Fund.

1.4 Where opportunities exist for localities to raise local revenues in relation to these complementary interventions, this money will be spent on infrastructure locally, rather than cross-subsidising strategic (i.e. national) investment. Locally raised money will be locally spent.

1.5 Governance is key – without the North, through the mechanism of TfN, having budgetary and decision-making control it is highly unlikely that the Strategic Transport Plan, nor the benefits that should flow from it, will be delivered. It is therefore proposed that TfN should move towards having responsibility for a long term devolved funding settlement for the North.

1.6 Further work is required to understand the detail of how the principles and proposals set out in the Funding Framework can be implemented, including discussions with the Department for Transport (DfT), HM Treasury (HMT) and other stakeholders.

2. Recommendation:

2.1 It is recommended that the Committee notes the Draft TfN Funding Framework and recommends its approval to the TfN Board.

3. Issues:

3.1 **Process to Date**

A key element of the Final Strategic Transport Plan will be how the infrastructure proposed by TfN, as set out in the long term Investment Programme, will be funded over the period until 2050. TfN has therefore developed a Funding Framework that will form the basis of the funding section that will be included in the Final Strategic Transport Plan and will also guide the business cases for Northern Powerhouse Rail and the interventions arising from the work on the seven Strategic Development Corridors.

3.2 The approach that TfN has adopted to the development of the Funding Framework has been grounded in the fundamental principles that were agreed by the Partnership Board in December 2016. KPMG was appointed in June 2017 to support TfN in this work.

3.3 At the same time TfN convened a Funding Steering Group, consisting of senior finance and strategy officers from Constituent Authorities and latterly a representative from the CBI. This Group has met four times and has provided invaluable assistance to TfN and its advisors. This has included facilitating the case studies that are included in the KPMG report, included at Appendix 2. In addition, the TfN Finance Director has briefed the Strategic Transport Plan Programme Board on two occasions with regard to progress on the funding work.

3.4 The TfN Finance and Strategy Directors have previously briefed and received feedback from the Partnership Board on the development of the Funding Framework, as well as undertaking individual member briefings to canvas views. DfT and HMT officials have also been kept informed with regard to the development of the Funding Framework.

3.5 **Key Elements of the Funding Framework**

The Draft TfN Funding Framework is attached as Appendix 1. It includes the following elements:

a) The Principles – which underpin a deliverable and appropriate funding arrangement
b) The Potential Funding Sources – demonstrating that TfN's funding requirement is reasonable
c) The Governance Arrangements that will enable funding allocated for strategic transport infrastructure in the North to be directed to TfN programmes
d) How Financial Risk is managed.

The Draft TfN Funding Framework also sets out the parameters within which the allocation and management of the financial resources required to deliver the objectives of the Strategic Transport Plan will be undertaken.

3.6 The key points to note within the Draft TfN Funding Framework are as follows:

a) The total funding envelope identified by TfN is deliverable within the context of a reasonable expectation of what funding might be made available. This is consistent with the National Infrastructure Commission's position as set out in the National Infrastructure Assessment. TfN is therefore not making unreasonable financial demands on central government – the decision to fund TfN is a choice that can be made by government within existing paradigms, based on robust business cases that will be presented through TfN's work programmes.
b) TfN does not have the power to capture value created by its promoted interventions – where these powers do not sit nationally, they sit locally with TfN's Constituent Authorities or other local authorities. These local authority powers have principally been granted to fund activity on a local rather than a regional basis. Where local plans are sufficiently developed, it is clear that those local powers will be fully utilised funding transport infrastructure within authorities and cannot be expected to fund strategic (i.e. national) infrastructure.
c) The TfN Funding Framework will be integrated with the pipeline of programmes and projects that is presented by TfN in the Strategic Transport Plan and the accompanying long term Investment Programme. Further work is required to understand the impact of the timing of those projects and the resultant profile of proposed funding through to 2050, although there has been some initial work done for the pre-2027 period.
d) The TfN Funding Framework also identifies where residual risks sit in relation to the funding of TfN promoted interventions and how this will be managed. Neither TfN nor its Constituent Authorities are in a position to back stop the risks associated with TfN's proposals and therefore as things stand this role will need to be taken on by central government. However, TfN could become the owner of programme risks, which would mirror some of the effects of financial risk taking.

3.7 **Next Steps**

In the short term, the key elements of the TfN Funding Framework will be included in the Final Strategic Transport Plan and will also guide the business cases for Northern Powerhouse Rail and the interventions arising from the work on the seven Strategic Development Corridors.

3.8 In the longer term, the TfN Funding Framework will provide the basis for further detailed work that will include the following activity:

a) Engage with DfT, HMT and central government more widely to agree and define exactly what form the proposed budgetary decision-making control would take and demonstrate how it would enhance delivery of infrastructure in the North
b) Engage with Members and other stakeholders to further understand their ambition and consider any consequential impacts on TfN governance arrangements
c) Develop the detail of the proposed funding powers and associated risk management mechanisms and how these might be delivered
d) Consider how these powers and responsibilities would impact on TfN and its Constituent Authorities and in particular, any additional resources that might be required to discharge them
e) Consider how the proposed changes would impact on DfT, partner bodies (including delivery agencies), and identify how new processes could be adopted (including the transition to the proposed arrangements).

4. Options Considered:

4.1 Not applicable as there are no options to be considered.

5. Considerations:

5.1 Not applicable as there are no considerations.

6. Preferred Option:

6.1 Not applicable as there is no preferred option.

7. Appendices:

7.1 Appendix 1 – Draft TfN Funding Framework
7.2 Appendix 2 – Transport for the North Long Term Investment Programme Funding Framework Technical Report (KPMG, February 2018)

Required Considerations

Equalities:

Age	~~Yes~~	No
Disability	~~Yes~~	No
Gender Reassignment	~~Yes~~	No
Pregnancy and Maternity	~~Yes~~	No
Race	~~Yes~~	No
Religion or Belief	~~Yes~~	No
Sex	~~Yes~~	No
Sexual Orientation	~~Yes~~	No

Consideration	Comment	Responsible Officer	Director
Equalities	A full Impact assessment has not been carried out because it is not required for this report.	Iain Craven	Barry White

Environment and Sustainability

~~Yes~~	No

Consideration	Comment	Responsible Officer	Director
Sustainability/ Environment	A full Impact assessment has not been carried out because it is not required for this report.	Iain Craven	Barry White

Legal

~~Yes~~	No

Consideration	Comment	Responsible Officer	Director
Legal	TfN Legal Team has confirmed there are no financial implications.	Iain Craven	Barry White

Finance

~~Yes~~	No

Consideration	Comment	Responsible Officer	Director
Finance	TfN Finance Team has confirmed there are no financial implications.	Iain Craven	Barry White

Resource

~~Yes~~	No

Consideration	Comment	Responsible Officer	Director
Resource	TfN HR Team has confirmed there are no resource implications.	Iain Craven	Barry White

Risk

Yes	~~No~~

Consideration	Comment	Responsible Officer	Director
Risk	A risk assessment has been carried out and the key risks are included in the Corporate Risks Report.	Iain Craven	Barry White

Consultation

Yes	~~No~~

Consideration	Comment	Responsible Officer	Director
Consultation	A statutory consultation has been carried out on the Draft Strategic Transport Plan.	Iain Craven	Barry White

Appendix 1 – Draft TfN Funding Framework

Introduction

The Northern Powerhouse Independent Economic Review (NPIER) identified the scale of the productivity challenge facing the North, with a 1/3 improvement in GVA per capita over and above historic trends being necessary to bring the Northern Powerhouse into line with the national average (excluding London) by 2050.

This scale of progress will need genuinely transformational change, including very significant and sustained improvements across strategic and local transport networks.

Transport for the North is developing a Strategic Transport Plan (STP) that will be adopted during 2018/19. This will set out the case for strategic transport infrastructure investment through to 2050, incorporating new analysis and evidence from previous Rail North, stakeholder and partner strategies. Transport for the North's status as a statutory Sub-National Transport Body means that its STP will become a statutory document, allowing Transport for the North and its partners to take a leading role in developing the case for investment in the North.

Informed by the STP and the supporting work programmes, Transport for the North will produce an accompanying long term Investment Programme (LTIP) setting out connectivity priorities across the North that will help transform the economic performance of the region and materially narrow the productivity gap between the North and the country as a whole. Reflecting this need, the programme is wide-ranging, with an investment requirement that will be significant over the 30 period to 2050.

The Draft STP identifies a funding requirement for strategic transport of around £60 - 70 billion during the period to 2050. Assuming the current levels of committed strategic transport funding are continued from 2020 through to 2050, this could equate to around £39 - 43 billion, meaning that additional expenditure of £21 - 27 billion would be required over the period for Transport for the North to achieve improvements to the transport system that will allow it to facilitate transformational economic growth.

Based on current estimates therefore, an average of £2.0 - 2.3 billion will need to be spent on strategic road and rail infrastructure in the North per annum to deliver the STP and the economic benefits that will flow from it.

Context

Although Transport for the North's strategic interventions and programmes will account for the largest projects with the longest lead-times, they represent only part of the funding challenge faced by the North. Meeting the ambitions of economic growth and rebalancing will also depend on a significant investment in critical local transport infrastructure and services. This will require further material additional investment, both in absolute terms and as a portion of the core capital funding requirement for the programme.

The 2017 Budget made clear that the ratio of gross economic infrastructure spend to GDP in the UK is expected to rise to 1% of GDP by the end of this Parliament – compared to a long term fiscal remit of 1% to 1.2% provided to the National Infrastructure Commission (NIC). At current GDP levels, the maximum remaining headroom (0.2% of GDP a year) translates into less than £3.5 billion per annum across England as a whole.

Transport for the North will need to consider the timing of its programme of projects within these parameters. However, even at the upper end of the range of the required investment, the increase of £900 million per annum in transport infrastructure expenditure in the North is achievable within these constraints. Moreover, the NIC's National Infrastructure Assessment, published in July 2018, indicates that the strategic transport requirements as set out in the STP and LTIP are deliverable within the NIC's fiscal remit for infrastructure investment.

Transport for the North does not have any fundraising powers of its own – consistent with the national position, the vast bulk of the tax and other revenue levied in North flows to and is directed by central government, the balance being held by local and combined authorities to address local priorities. Around 94% of all revenues raised in the UK are raised and spent by central government, and although technological change (such as electrification of the road fleet) is likely to significantly impact on mechanisms that central government uses to raise revenue, there is no reason to assume that these proportions will change in the near to mid-term future.

The principal financial challenge in respect of delivering the LTIP relates to funding, rather than financing. The scale and diversity of Transport for the North's programme mean that there will be a need to consider the most appropriate delivery models for the delivery of specific projects. However, the most efficient and value for money approach to managing cash flow and risk can only be properly addressed once the question of how the infrastructure necessary to deliver on the North's economic potential is ultimately paid for over time has been resolved.

Purpose of the Funding Framework

This Funding Framework sets out the parameters within which the allocation and management of the financial resources required to deliver the objectives of the STP will be undertaken.

As previously noted, Transport for the North has no revenue raising powers, and in addition is unable to borrow. The adoption of the elements that make up this framework will therefore need to be agreed with the Department for Transport (DfT) and HM Treasury (HMT), as well as with its Constituent Authorities.

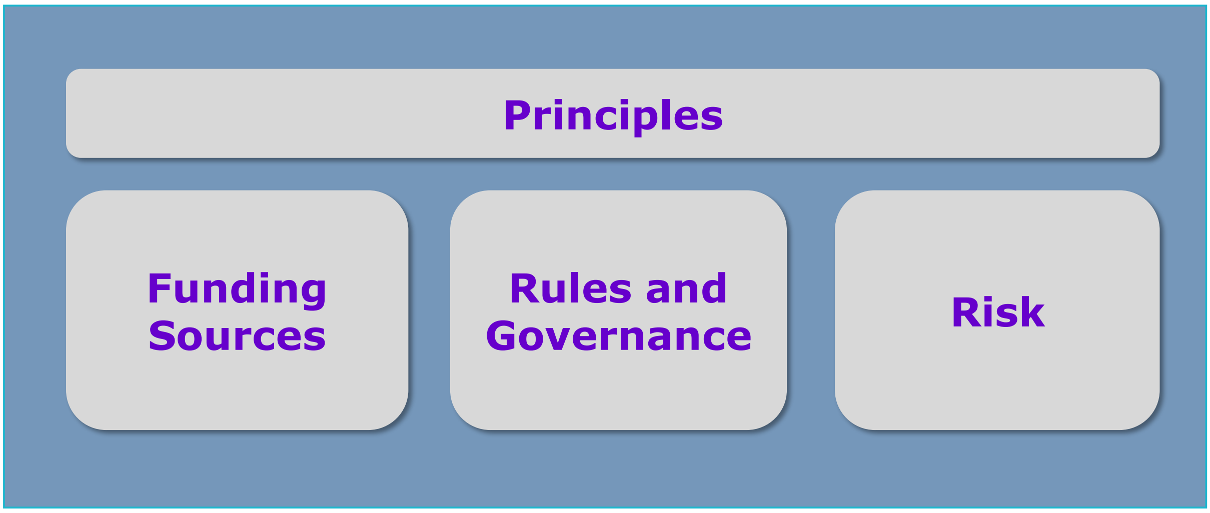
TRANSPORT FOR THE NORTH

Elements of the Funding Framework

Transport for the North's funding arrangements will be shaped by the complex and diverse landscape within the North for the delivery of its projects. In addition, it can be anticipated that specific funding sources, industry processes and priorities will change over time. This indicates a need for Transport for the North's Funding Framework to be underpinned by a set of fundamental principles which can be used by Transport for the North, its Constituent Authorities and central government to deal with changing circumstances over time, as well as the means by which funding will be allocated and managed.

The Transport for the North Funding Framework therefore consists of four building blocks:

1. The **Principles** – which underpin a deliverable and appropriate funding arrangement;
2. The potential **Funding Sources** – from which revenues could ultimately flow;
3. The **Governance Arrangements** that will enable funding allocated for strategic transport infrastructure in the North to be directed to Transport for the North programmes; and
4. How **Financial Risk** is managed.



1. Funding Framework Principles

The success of the UK in the global marketplace and the Government's industrial strategy depends upon transforming the economy of the North of England. The NPIER identified that achieving transformational economic growth will require investment and improved performance in a number of critical areas, including transport.

At the core of Transport for the North's mission is therefore the need to facilitate sustainable economic growth. Transport for the North has therefore identified a series of principles that will guide its approach over time to funding the delivery of the LTIP in response to current and changing future circumstances.

i) **Evidence based decision making** – Transport for the North's overarching objective is the delivery of transformational and inclusive economic growth. The STP and LTIP will prioritise schemes that demonstrably contribute to the overarching goal of facilitating this growth in a sustainable way across the North. The criteria upon which investment decisions are made will therefore need to be reflective of a broad range of measures that include the economic and social benefits that projects will deliver.

ii) **Strategic consistency** – The means by which identified programmes and projects are funded should be consistent with the overarching goal of facilitating economic growth. For example, mechanisms that directly or indirectly increase the general tax burden for individuals or businesses in some or all of the North in relation to other regions will dampen activity and impact negatively on inward investment decisions.

iii) **Locally raised funding should be spent locally** – Delivering transformational, inclusive economic growth will require investment at a local as well as a regional level – as recognised in Chapter 4 of the National Infrastructure Assessment – to ensure that a "whole journey" approach to improving transport is followed. In some cases, Transport for the North-led investments will result in financial benefit to developers, businesses or individuals that can be captured locally. At the same time, Transport for the North's proposals will have implications for local expenditure, principally through the need for new or enhanced local infrastructure. Localities will seek to maximise the extent to which such benefits can be captured, but the funding raised by localities, for example through commercial revenue, user charges or local taxation mechanisms will be spent in those localities on local schemes, rather than being used to subsidise strategic (i.e. national) infrastructure.

iv) **Multi-modal solutions** – Planning is currently done at a national level on a modal basis. Transport for the North is engaged in genuinely multi-modal planning in relation to its Strategic Development Corridor studies and such an approach offers clear potential for cost and efficiency benefits where the targeted outcome is to enable economic activity rather than deliver improvements to specific modes. The Funding Framework should allow investment to be focused where the evidence indicates that it will have the greatest impact.

2. Funding Sources

Transport for the North's mission is essentially economic – to use transport to facilitate transformational and inclusive economic growth and help to rebalance the UK economy. Whilst Transport for the North and its Constituent Authorities are committed to exploring project-level value capture opportunities to deliver consequentially required local enhancements, the evidence indicates that the LTIP will need to be underpinned by public funding commitments that meet a very high proportion of the overall expenditure requirement.

Transport for the North itself does not have any fundraising powers of its own through the regulations under which it was established. Consistent with the national position, the vast bulk of the tax and other revenue levied in North flows to and is spent by central government, the balance being held by local and combined authorities to address local priorities. Around 94% of all revenues raised in the UK are raised and spent by central government, and although technological change (such as electrification of the road fleet) is likely to significantly impact on mechanisms that central government uses to raise revenue, there is no reason to assume that these proportions will change in the near to mid-term future.

Transport for the North has <u>not</u> sought to identify specific central government revenue streams that can be hypothecated to it and used to fund its proposals. Instead it has identified the quantum of transport related revenue flows that could be earmarked for transport and compared this to what it plans to spend. This indicates that the STP is deliverable within the context of a reasonable expectation of what funding might be made available.

This view is supported by the NIC's National Infrastructure Assessment – based on any reasonable allocation methodology across regions, in particular when the separate funding line for NPR is taken into account, Transport for the North's expenditure proposals are consistent with the overall levels of funding identified by the NIC through to 2050. In the NIC's own words, *"While the Commission's recommendations comprise an ambitious programme of investment, this is not an unaffordable wish list"* (National Infrastructure Assessment, page 14).

Transport for the North is therefore not making undue financial demands on central government – the proposals included within the Draft STP are ambitious yet realistic. The decision to fund Transport for the North is a choice that can be made by government within existing paradigms, based on the overall objective of rebalancing the economy through transformational and inclusive growth, and robust business cases that will be presented through Transport for the North's work programmes.

Requirements

As noted, Transport for the North's estimated funding requirement through to 2050 is consistent with the NIC's overall fiscal remit. To provide further, more detailed support for this position, TfN has considered the sources of transport related revenue that might support its programme. This work has included:

- the current funding regime for strategic transport infrastructure;
- the range of the overall funding requirement that would be needed to deliver the required strategic infrastructure, and
- the opportunity for capturing incremental value created by the strategic investments in the LTIP.

The LTIP will consist primarily of major road and rail enhancements. Transport for the North has identified an indicative programme of rail and road interventions, with an estimated cost of £60 - 70 billion (in current prices) over 30 years. Local transport infrastructure investment will continue to be the responsibility of the relevant combined authorities and local authorities and Transport for the North cannot be funded at the expense of these programmes if the overarching economic objectives of Transport for the North are to be achieved.

Existing Funding Arrangements

There is an ongoing programme of transport infrastructure works in the North of England, funded through existing industry processes or specific major projects.

- Highways – the taxes and duties levied on road users significantly exceed highway expenditure. In 2017, fuel duty alone raised over £27 billion, while VED accounted for a further £6 billion. Recently it has been announced that from 2020 onwards, VED revenues will be hypothecated towards expenditure on the Strategic Road Network (SRN) and the Major Road Network (MRN).
- Rail – around 60% of rail expenditure is raised directly from passengers, and another third from consolidated government budgets funded through a combination of taxes and duties.

More recently project-level contributions have been sought for specific investments where beneficiaries are anticipated to gain from transport investment. However, such an approach has not yet been successfully used to fund strategic infrastructure in the North and indeed these incremental forms of funding have been raised predominately through additional local taxes for local transport projects (albeit on a large scale in London), rather than SRN/MRN or strategic rail investment programmes.

Whilst Transport for the North is a new statutory body, expenditure on strategic infrastructure in the North, and the allocation of the associated funding is a continuing requirement. Work performed by KPMG on behalf of Transport for the North indicates that if the current level of expenditure on strategic transport infrastructure in the North were maintained during the period through to 2050 it would receive £39 - 43 billion. This represents between 55 and 70% of the funding requirement identified in the Draft STP.

Whilst this is insufficient to fund the investment that is currently estimated to be required to facilitate transformational and inclusive economic growth, it does provide a baseline that demonstrates the extent to which Transport for the North proposals represent an incremental increase on current arrangements – an ambitious but achievable programme – rather than requiring a step change in the funding allocated to the North.

Future Funding Sources

1) Approach to centrally-derived rail and road funding

As noted above, the UK's centralised funding regime means that the funding for the LTIP will need to come from central sources.

This is consistent with the approach to transport funding today, where allocations that pay for national infrastructure are made to delivery bodies (Network Rail, Highways England) and strategic programmes (such as HS2) from centrally collected taxation, supplemented on the railways by user revenues.

On this basis, the exact source of each pound expended on strategic transport infrastructure in the North does not matter – that is not how government currently manages its finances. What is important is that the quantum of expenditure identified by Transport for the North is manageable within a reasonably assumed future funding environment. The work done by KPMG, consistent with the macro approach adopted by the NIC, indicates that this is the case.

The table below sets out the elements that might fund Transport for the North's proposals based on current revenue raising mechanisms. Whilst it is likely that the balance of the funds that can be raised from these mechanisms over time will vary (for instance due to technological changes) the assumption would be that central government would over time take steps to address any revenue erosion that might result from this to maintain its financial position.

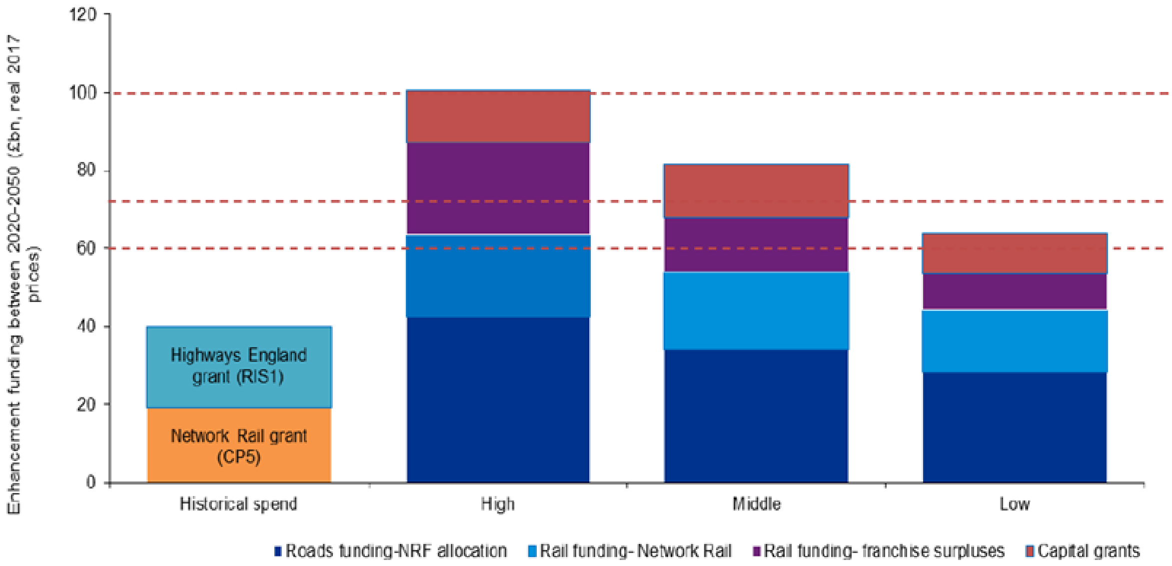
These elements are therefore presented in order to demonstrate that the order of magnitude of the funding required is manageable in relation to the funding that is potentially available, rather than identify pots of resource that Transport for the North would seek to "commandeer".

Source	Description	Potential Quantum (real in 2017 prices)
VED revenues - National Roads Fund	To date, investment in the SRN is funded by an allocation made by the Government to Highways England, as well as capital grant programmes for specific projects and schemes. The recent Transport Investment Strategy suggested a shift in this structure, with the Government confirming its commitment to direct VED revenues to pay for improvements to the roads network through the new National Roads Fund (NRF) from 2020 onwards.	Preliminary analysis suggests that the allocation of VED revenues on a regional basis could contribute £28-43bn to the programme over 30 years, compared to around £19bn under 'business as usual' projections.

	Although the details are still under development, given the linkage now being made at the national level between VED revenue and Highways England investment, the allocation of at least a proportion of VED on a regional basis may be an appropriate component of the Transport for the North Funding Framework.	
Rail capital enhancement programmes	Capital grants are an important source of funding for major rail upgrades and enhancements, funded via the Network Rail regulatory process or specifically to major projects such as HS2 or Crossrail.	Historical funding for rail enhancements in the North has been around £700m per annum (equivalent to around £21bn over 30 years).
NPR major project grant	Arguably, there has been an historical underspend in the funding allocated for enhancements in the North. Therefore, in addition to allocations for Network Rail consistent with historical trends, it is anticipated that a form of capital grant for Northern Powerhouse Rail (NPR), the largest rail scheme in the LTIP, will be available.	Assuming grant funding is received equivalent to the capital cost of the Manchester to Leeds new line component of NPR, this could represent a further £9-13bn.
Hypothecation of rail franchise surpluses	A potential additional source of funding for the LTIP could be derived from the hypothecation of future surpluses generated by the Northern and TPE franchises. This would be supported and incentivised through the optimisation of demand management, investment in the railway, and potentially reforming the fares structure to align to future needs of the network.	Preliminary analysis suggests that future surpluses could contribute £9-23bn over 30 years. Much of these surpluses would be back-ended, which would reduce their capital 'buying power' as a funding stream. Equally, the higher-end scenarios implicitly require extra capacity investment not currently assumed within the emerging Transport for the North investment programme.

Source: KPMG – "Transport for the North Long Term Investment Programme Funding Framework Technical Report"

High level modelling has been undertaken to derive an indicative range of funding that these elements might contribute over time. The results of this analysis are set out in the bar chart overleaf.



Source: KPMG – "Transport for the North Long Term Investment Programme Funding Framework Technical Report"

This suggests that even at the low end of the range of potential outcomes, with the necessary reform to funding flows and allocation arrangements, central funding for the LTIP can support the investment levels identified in the Draft STP. This is consistent with the fiscal remit analysis included at page 112 of the National Infrastructure Assessment, and the levels of strategic transport investment set out in the Draft STP are around 0.8% of the North's (current) GDP.

Transport for the North recognises that the estimated level of funding identified in the Draft STP, whilst reasonable, indicates a higher level of funding than would be provided under 'business as usual'. However, this simply reflects the scale of the challenge that Transport for the North has been established to address.

It is important to remember that the ability to be able to address an overall funding requirement is only the first step towards being able to deliver the LTIP. This analysis does not address the timing of funds flows, modal allocations or the risks associated with funding a programme of this size. These will be explored further as the Final STP is developed, but some initial work has already been undertaken for the pre-2027 period.

2) Incremental local or project/location specific funding opportunities

The revenue raising mechanisms for capturing local/project level revenue do not sit with Transport for the North. Transport for the North does not have revenue raising powers of its own. Neither, in many cases, do they sit with Transport for the North's Constituent Authorities, but rather with the individual local authorities which serve the North. Those local powers were not granted in order to fund strategic/national infrastructure. The current funding environment is extremely challenging for local authorities in general and local transport funding in particular, meaning that these mechanisms cannot be used to raise direct contributions for the interventions within the LTIP.

In addition, whilst Transport for the North is focused on pan-Northern transport interventions, there is an equally important job to be done at local level to enhance mobility within local functional economic geographies, particularly within the city regions, and ensure that the value of major regional schemes is not diluted through failure to invest locally. This has been explicitly recognised in the National Infrastructure Assessment (Chapter 4).

Whilst the NIC's proposals for Devolved Cities and Non-Urban local transport would go some way to closing the current gap between the need for local transport investment and the money that is available to pay for it, local schemes will need to have the 'first call' on any local funds that can be incrementally raised from investment in transport infrastructure. Locally raised revenue needs to be locally spent.

Of course, there will be instances where Transport for the North investments will result in financial benefit to developers, businesses or individuals that can be captured locally.

At the same time, Transport for the North's proposals will have implications for local expenditure, principally through the need for new or enhanced local infrastructure. Localities will therefore seek to maximise the extent to which such benefits can be captured, but the funding raised by localities, for example through commercial revenue, user charges or local taxation mechanisms will be spent in those localities on local schemes, rather than being used to subsidise strategic (i.e. national) infrastructure.

Transport for the North has sought to identify and quantify the likely extent of this funding opportunity – being those funding sources that are project-related and/or derived at the local level for specific schemes and interventions, reflecting the benefit they will provide to local areas and meeting local needs. The principal ones are set out in the table below.

Category	Funding Source
Targeted grant funding	• Specific grants (beyond transport)
Redirection of project-generated revenues	• Incremental commercial revenues and income • Long term savings and efficiencies unlocked by projects and additionally aligned programmes
New charges and levies	• Land Value Capture (LVC) • Project or programme-based user charges

Recognising that London has demonstrated that it is able to fund substantial elements of its proposals from locally derived benefits, Transport for the North has sought to test the extent to which the approaches set out in the table above could generate significant revenues for its local partners that could be spent on local infrastructure to support its overall objectives. Transport for the North identified a number of case studies, based on projects that were likely to form part of the LTIP.

Transport for the North then worked with relevant partners to understand both the opportunity for additional, project based, revenues to be raised as well as the level of incremental costs that would arise locally from either the need to accommodate the project within the existing local transport network, or from the additional housing or commerce (and therefore population) that might be the result of certain value capture mechanisms.

Transport for the North's work has highlighted the sizeable challenges faced by the North in generating significant revenue streams from individual projects, particularly in comparison to London:

- Base levels of productivity, wages and land values are significantly lower than other parts of the country, as well as there being significant differences within the North itself. Fundamentally, transport projects in London seek to relieve the effects of economic demand whereas Transport for the North is seeking to help stimulate demand. The context for the generation of local value is therefore entirely different.
- Transport for the North infrastructure is broadly national in nature, although its focus on improvement is mainly east-west movements rather than north-south, and the benefits that are generated are much more diffuse over a broader area. Most of the projects proposed by Transport for the North intersect with the local economy less frequently than is the case within a city or conurbation and therefore the geographical footprint that is directly impacted is much smaller. For example, Crossrail 1 is 73 miles long and connects 41 stations – meaning an intersection with the local economy every 1.82 miles. The proposed NPR Manchester to Leeds new line will likely have three stations on a route of around 50 miles – a station every 25 miles.

Based on this preliminary analysis, the role of local funding sources is assessed as being relatively limited in the context of Transport for the North-led investment and the overall quantum of funding required for its core programme and consequential investments required of local partners. The ability to raise local funding is obviously greatest in absolute terms when considering the links between the North's major economic centres although paradoxically the scale of the costs involved in delivering the associated projects means that, where opportunities do exist, in proportional terms the value to be derived from smaller individual road and rail schemes is larger.

3. Governance

As important to the delivery of Transport for the North programmes as the availability of funds within the system is the ability to direct the funding that is available for strategic transport infrastructure to support the delivery of the STP, and by extension the economic objectives of Transport for the North. If Transport for the North is not able to exert more control over strategic transport investment in the North, and the system that currently delivers infrastructure continues in its current form, it is highly unlikely that the STP, or the benefits that will flow from it, will be delivered.

In the short term, Transport for the North will need to work with the mechanisms that are currently in place. This will include working closely with DfT, Highways England and Network Rail to achieve the following:

- delivery of "quick wins" where possible on an opportunistic basis;
- inclusion of projects in the LTIP for 2020-25 in industry processes; and
- ensuring that these projects are then delivered at the necessary time by the national agencies.

This would very much be 'business as usual' based on current powers and operating paradigms to influence central decision making, but limited to a largely advisory capacity (albeit in the context of a statutory body).

There is some opportunity to take a different approach to the delivery of the pre-2027 schemes across the North on the MRN, but this will depend on how the DfT responds to its recent consultation on the MRN when the final proposals are published later in 2018.

In the longer term, how Transport for the North develops and the role that it plays in the planning, promotion and delivery of strategic transport infrastructure needs to be addressed. This would need to cover Transport for the North's role in strategic and business planning and budgetary processes as well as decision making and accountability.

Transport for the North has considered a range of options as to how this could be achieved, ranging from a purely strategic role for Transport for the North (with no funding resource or remit) but with a sponsorship and 'score keeping' role to a much more autonomous role as a budget holder, able to shape future investment and incentivised to deliver greater reforms.

These potential approaches are illustrated overleaf and described in the following paragraphs.

Continue / influence existing arrangements

Separate modal regulatory settlements for the North

Combined regulatory settlement for the North

Budget Holder

Option 1: Continue / influence of existing arrangements. If existing funding arrangements for rail and road – delivered primarily via the respective five-year regulatory processes – were to continue, Transport for the North's role would likely be limited to an advisory role and strategic planning, providing input into national process such as Network Rail's and Highways England's business planning, and keeping score in terms of baselines and comparisons between places and regions in expenditure on Transport for the North-led interventions. This option would require minimal changes to funding arrangements and governance structures.

Option 2: Separate modal regulatory settlements for the North. Alongside the multi-year funding settlements for Network Rail and Highways England, HS2, London etc., the North would have a separate baseline plan for its rail and road enhancements – like a Northern HLOS and RIS, similar to the current Scottish HLOS. A separate baseline funding envelope for the North would provide greater certainty of funding, with options for establishing the size of the envelope on a formula basis, for example using a percentage of GVA as recommended by the NIC, potentially reflecting the implications of rebalancing objectives for these ratios in different parts of the country. This option would still see separate envelopes for different modes, but by providing baselines for each, it would provide the kind of clarity around additionality and consistency between places and regions without which it will be difficult to make a case for discretionary additional local or regional funding. It would require the development of an agreement between Transport for the North and its Constituent Authorities on rules to ensure a fair allocation of funding across regions and a long term pathway to maximising value generation to support funding future projects.

Option 3: Combined regulatory settlement for the North. This version would involve a single pooled funding envelope for transport enhancements (across all strategic modes) in the North, aligned with Transport for the North's multi-modal LTIP. This unique funding envelope for the North would give greater autonomy and discretion to Transport for the North on the allocation and prioritisation sequencing of investments between modes. It would otherwise be similar to Option 2 in terms of the incentives provided to address what could be achieved through additional local/regional contributions over time.

Option 4: Budget Holder. In the most radical vision of the future, revenue from all funding sources for strategic investment would be directed to a devolved Transport for the North budget, set against a long-term baseline and with 'Barnet style' or match funding rules aligned to the achievement of rebalancing objectives. Such arrangements would necessitate mechanisms to ensure that central government (and, where relevant, locally-derived) funding is spent on value for money projects and would require both mechanisms to manage risks, and enhanced governance arrangement for Transport for the North to support democratic accountability at the regional/local level given that Transport for the North's remit would extend into the delivery as well as design of its programmes.

It is clear that in order for TfN to be able to ensure the delivery of its programme it needs to have control over budgets and decision making – otherwise the North will remain vulnerable to schemes being cancelled or delayed based through remote decision making. This is not a theoretical risk – many of the current issues on the northern road and rail systems are a consequence of just such decisions

TfN is therefore of the view that it needs to target a position where it agrees and controls a long term funding settlement for strategic transport infrastructure in the North. On the basis that TfN and its Constituent Authorities are best placed to identify the balance of need between road and rail it makes sense for this to be done on a pan-modal basis, rather than on the basis of a modal allocation that would fix road and rail expenditure envelopes potentially without reference to regional need.

TfN therefore wishes to move to the position set out in Option 3, where it becomes responsible for a combined regulatory settlement in the North. Dependent on the success of this arrangement in delivering much needed strategic infrastructure in the North, it may then be appropriate to move to a position where TfN takes on the full 'Budget Holder' role as set out in Option 4. Such an approach will require discussion and agreement with central government, and in particular DfT and HMT. In addition, TfN will need to consider what, if any, governance changes would need to be made in order to allow TfN to fulfil this role.

These questions will form the basis of further, detailed work that will develop in greater detail how such an approach could be implemented.

4. Management of Risk

The final element of the Funding Framework is the management of financial risk. As with any programme or project, particularly one of this scope and scale, there needs to be clarity with regard to who is ultimately responsible for what risks. This depends not only on the willingness of an organisation to accept certain risks – its risk appetite – but also how it will manage those risks and crucially how it will absorb the financial consequences of risks materialising as issues.

In considering how financial risk can be managed in relation to the LTIP, the following fixed parameters need to be considered:

- Transport for the North has no revenue raising powers of its own and no ability to borrow. Its ability to take risk is therefore limited to the extent of the funding that it receives from the DfT. Under current arrangements Transport for the North has no independent ability to take risk on the proposed programme.
- Transport for the North's Constituent Authorities have limited ability, either individually or collectively, to take risk in relation to the programme. As noted above, their revenue raising powers are limited and where they exist were not granted for the delivery of national strategic infrastructure projects.

By a process of elimination, the only body that has the revenue raising powers and consequent financial resources to take financial risk in relation to a programme at the proposed scale under current fiscal arrangements is central government, specifically HMT.

However, were TfN's proposal for a combined regulatory settlement to be adopted, there are approaches to managing programme risk that would usefully act as a proxy for Transport for the North sharing the financial risks of the programme. These might include:

- Transport for the North managing modal or pan-modal budgets within a fixed envelope over a spending cycle or other time period to be agreed;
- cost overruns at a programme or project level would need to be managed within the fixed budget;
- delivery savings at a programme or project level would likewise accrue to Transport for the North, allowing the offset of overruns or pipeline projects to be brought forward.

This approach would incentivise Transport for the North, its Constituent Authorities and its stakeholders to focus on the most efficient way of delivering STP outputs, allowing to the North benefit from difficult decisions that might need to be taken, whilst at the same time encouraging the close management of project delivery by both Transport for the North and its partners. This is similar to the approach used in Scotland, where Transport Scotland manages programme delivery within a devolved budget settlement.

As noted in the previous section, such an approach would need to be considered in the light of Transport for the North's governance arrangements, and would need to be worked up in detail if this approach were deemed to be suitable. However, it would not only constitute a significant step forward in terms of the devolution of decision making for the North, but would also be a mechanism for managing expenditure in a way that allowed value for money to be achieved.

Next Steps

TfN will now proceed to further refine these proposals, setting out in greater detail how it is proposed that they will work. In order to do this, TfN will carry out the following activities:

i) Engage with DfT, HMT and central government more widely to agree and define exactly what form the proposed budgetary decision-making control would take and demonstrate how it would enhance delivery of infrastructure in the North;
ii) Engage with Members and other stakeholders to further understand their ambition and consider any consequential impacts on TfN governance arrangements;
iii) Develop the detail of the proposed funding powers and associated risk management mechanisms and how these might be delivered;
iv) Consider how these powers and responsibilities would impact on TfN and its Constituent Authorities and in particular, any additional resources that might be required to discharge them;
v) Consider how the proposed changes would impact on DfT, partner bodies (including delivery agencies), and identify how new processes could be adopted (including the transition to the proposed arrangements).