



Russell George AM
Chair
Economy Infrastructure and Skills Committee

31 January 2018

Dear Russell

At the scrutiny session of the Economy, Infrastructure and Skills Committee on 17 January, I said I would write to you with additional information in response to the following issues raised by the Committee, which I will respond to point by point:

- *In relation to the Welsh Government procuring a 3% stake in the sports car maker TVR, whether there will be a Welsh Government observer on the board of TVR, and details of who provided independent advice to the Welsh Government as part of the due diligence process in obtaining the equity stake*

We send an observer to meetings of the Board of TVR Automotive Ltd and in addition, the Development Bank of Wales undertakes independent financial monitoring of the company. It is the Welsh Government senior official with responsibility for managing the TVR account, who attends meetings. We have no voting rights at the company Board meetings but the person attending can make informal observations, though it is not within the remit of the role of the observer to make an active contribution in any decision making. The main function of the observer is to monitor discussions.

Prior to committing to the share purchase, we commissioned commercial and legal due diligence from the Automotive Sector Team within KPMG, Hugh James Solicitors and also received advice from Finance Wales, drawing on their broad experience of this type of transaction.

- *The timescales for the development of the enabling plans for each of the four foundational sectors which you agreed to send to the Committee when they are available*

As I indicated at Committee, there is not a uniform deadline for the publication of the plans but the aim is for all the plans to be produced by the end of this year.

- *Details of which of the existing 48 advisory boards will remain and which will be disbanded as a consequence of the establishment of the new Ministerial Advisory Board, and details of the membership of that Board*

I will be making an announcement on the formation of the new Ministerial Advisory Board this Spring. As part of that, I will be setting out which of the current boards, panels and groups that we have established and appointed with the specific purpose of providing advice within the Economy and Transport portfolio, will be brought to a close.

- *Details of the Welsh Government's position on Community Transport permitting in light of changes proposed by the UK Government, including details of the work the Welsh Government is doing with the sector to help them manage the impact of changes*

The legislative framework for issuing Community Transport permits is a non devolved matter. I understand that the Community Transport permit regime will continue to be a matter reserved to the UK Government following commencement of the Wales Act enacted in 2017. In preparation for the forthcoming public consultation about Community Transport proposed by the UK Government, we have taken steps to ensure that any potential impact on the sector in Wales is fully considered by the Department for Transport when taking a decision in relation to this important sector.

In 2013 approximately 605 people were employed in the delivery of Community Transport services in Wales, a decrease of 16.7% from the 726 people who were employed in the sector in 2010. In the same period, 1,861 volunteers completed 167,000 hours of voluntary work in the community transport sector in Wales. Any proposals to impose restrictions on community transport organisations to bid for public sector contracts could seriously undermine these important services.

- *Details of the outcome of the negotiations with the UK Government on the devolution of franchising powers, the transfer of ownership of the valleys lines and future funding, once discussions conclude in February. We would be grateful if you could include a summary of agreed working arrangements between the Welsh and UK Governments for the future management and operation of the franchise*

On the matter of future funding arrangements, I had a positive discussion with the Secretary of State for Transport in September, and reached agreement on a number of matters that enabled the procurement process to continue whilst discussions between officials were underway. I have attached a copy of correspondence I sent to the Secretary of State for Transport following this meeting that sets out these arrangements in more detail (Annex A). The discussions, between Welsh Government, HM Treasury and Department for Transport officials, are due to conclude in February and from this point I will be able to provide further details on the arrangements.

On the Core Valley Lines asset transfer, work is progressing in a way that allows us to proceed and announce a successful bidder as planned. Welsh Government, HM Treasury and Department for Transport officials are developing the process for the transfer of owners, which is purely an administrative process between Governments. The transfer will be cost neutral to the public sector, and will complete following a period of due diligence that will take around 18 months.

An agreement in principle in respect of the transfer of rail franchising functions to the Welsh Ministers was reached with the UK Government in November 2014. It was agreed that functions for transfer would attach to specific services in the Wales and Borders franchise, ensuring that the Welsh Ministers become the appropriate

franchising and designating authority for those services. Settling the precise scope of the transfer has however, been complex, principally due to the nature of the services within the Wales and Borders franchise which includes England-only services and a number of services that repeatedly cross the border between England and Wales. In 2016, the Secretary of State for Transport confirmed that the functions for transfer would attach to services wholly in Wales. This was subsequently confirmed to include both Wales-only services and those parts of cross-border services within Wales.

The Welsh Ministers (Transfer of Functions) (Railways) Order 2018 is due to begin the Parliamentary process in late February 2018 and it is intended it will go before the Privy Council at its meeting on 23 May 2018. The current timetable from the Department for Transport indicates that the Order will come into force in late June 2018.

As functions being transferred relate only to Wales and Borders franchise service operations in Wales, I have agreed that the Welsh Ministers will be acting under agency agreement arrangements pursuant to section 83 of GoWA 2006 in order to exercise the Secretary of State for Transport's functions to award the franchise and manage service operations in England (including the English component of cross-border services and England-only services). The agreement already in place sets out the principles to be applied in respect of the Secretary of State for Transport's restrictions and obligations for the management of services on the English side of the border post contract award.

The final position is to be confirmed in a third agency agreement ahead of the contract award, which Transport for Wales is currently developing with the Department for Transport. As the Order is not expected to have commenced by the intended date of the franchise contract award, the third agency agreement will be required to enable the Welsh Ministers to act as the Secretary of State for Transport's agent for awarding the contract in respect of services in Wales.

- *A comparison of benefit cost ratios for investment in different types of transport projects, including active travel, and how they compare to that for the M4 relief road*

I have addressed this further on in my response.

I am also writing in response to your letter of 18th January in which you requested information on issues that Members were unable to raise in the session due to time constraints:

- *Details of the steps you are taking to mitigate the financial risks associated with the transfer of the Core Valley Line – particularly the risk of latent defects potentially leading to significant financial liabilities*

As part of the ongoing development of our proposals for the Core Valley Lines, Transport for Wales are working with Network Rail to ascertain information regarding staff and the infrastructure to assess the current condition of the network, the current and future risks associated with it, and ways in which these can be managed.

Furthermore, as part of the process to transfer ownership of the Core Valley Lines, we will agree the funding required for the operation, maintenance and renewal of the railway that currently goes to Network Rail. This will take account of the condition of the railway following the latest round of Network Rail renewals work. There will also be an agreed process in place with the Department for Transport for handling latent defects during an initial period. After that period, and following our investment in the railway, this will be managed through Transport for Wales. As part of this work Transport for

Wales are considering processes that emulate Network Rail's own liability protections for the longer term. This work will be concluded as part of the due diligence work over the next 18 months.

- *Details of why section 2 of the A456 dualling programme is currently projected to be delivered 23% over the approved budget*
- *Details of using the new Mutual Investment Model of project funding to deliver section 2 of the A465 project, including what the benefits of this approach are, and how its effectiveness be evaluated*

Section 2 of the A465 is being delivered as an ECI contract. My written statement of 27 November provided members with an update on the findings of the commercial project review for the A465, Section 2

<http://gov.wales/about/cabinet/cabinetstatements/2017/A465/?lang=en>

My officials are continuing to actively manage the project to identify ways of mitigating the project position. As part of this work, we are in discussions with Costain on a number of matters around the allocation of risk in the contract. We are clear in our view about where risks sit within our contract with Costain and will do everything that we can to protect tax payers from these significant additional costs. The resolution and negotiation of such issues is a confidential and commercially sensitive process, and we are unable to disclose specific details.

Once the level of our liability has been confirmed, decisions will then be made on how best to fund any shortfall, recognising what the opportunity costs of this increase will be. Future budget profiles will reflect these increases so that the impact can be considered as part of the ongoing delivery of the national transport finance plan. Notwithstanding the dispute, my officials and Costain are fully committed to delivering the project as quickly and efficiently as possible. Whilst we will mitigate against further cost increases and time delays where possible, we will not compromise on the quality of the project we committed to at the Public Inquiry in Spring 2014.

To reiterate, the A465 section 2 is not being delivered using the Mutual Investment Model (MIM) of project funding. Instead, sections 5 and 6 between Dowlais and Hirwaun are being delivered using the Welsh Government MIM and will complete the A465 Heads of the Valleys Dualling.

With capital budgets remaining under unprecedented pressure, we are working harder and smarter to attract new investment and, to ensure that capital expenditure delivers the greatest benefits in the most effective way. The key features of the MIM are:

- It allows the public sector to share in the profits of the private partner, which addresses concerns about windfall gains. The MIM removes soft services, from these contracts, which led to expensive, inflexible contracts and was a real bone of contention in the old PFI model;
- It embeds transparency – about costs and performance – and the requirement to review efficiency, effectiveness and performance every two years;
- It removes equipment, which can be funded more efficiently from public capital;
- It has important provisions to secure community benefits; sustainable development, where the private partner is obliged to help us in the delivery of the Well-being of Future Generations Act; as well as incorporating our commitment to an ethical employment code.

A Value for Money analysis is conducted as part of a separate component within the Outline Business Case for the scheme. It compares the costs of different procurement models for constructing the scheme, and then the costs of operating and maintaining it once operational. The total cost will be based on a contract to construct and then operate and maintain the road for a period (normally around 30 years) after it is opened. The Value for Money within the business case will compare these costs with those required to deliver the same services procured in a more conventional way. In the case of the A465, this work is ongoing and will be reported to Ministers before the scheme begins its procurement process.

The premise of the MIM is that the risk is placed with the party that is most able to deal with it. Therefore construction risk is passed to the private sector and we pay for a service (rather than directly for construction), so in the case of A465 the ability to use the road which is maintained to an agreed standard. Welsh Government does not pay for this service until it is operational, incentivising the contractors to deliver to programme. Deductions will be made to the annual service payments if the operator doesn't meet stringent operational requirements which we will actively manage.

The project is currently progressing through the Statutory Process to seek the powers to build the road with a Public Inquiry planned for April. This improvement to the A465 is critical to the social and economic regeneration of the Heads of the Valleys area. It will improve access to key services, jobs and markets supporting inward investment to areas such as the Ebbw Vale Enterprise Zone.

- *In the context of the M4 relief road project, details of the Welsh Government's assessment of what constitutes high, medium and low value for money in terms of Benefit Cost Ratios, including the basis / authority for this*
- *Details of how the decision to undertake additional work around Newport Docks has affected the Benefit Cost Ratio for the M4 relief road, including the BCR pre and post the decision, and an explanation of how both the increase in cost and the delay have affected the BCR*

Whilst the treasury 'Green Book' does not specify classifications of BCR, Department for Transport Guidance advises Value for Money for BCR as:

- **Poor** - below 1.0
- **Low** - between 1.0 and 1.5
- **Medium** - between 1.5 and 2.0
- **High** - between 2.0 and 4.0
- **Very High** - greater than 4.0

Transport (rail and road) schemes assessed under 'WebTAG' treasury guidance consider the core journey time savings benefit in isolation, and then may consider some wider agglomeration and productivity benefits. Active travel schemes often monetise other benefits such as health, air quality, carbon reduction and noise savings. These are not monetised for road or rail schemes. We use the WebTAG process as a way of capturing the benefits of active travel infrastructure.

The core BCR of the M4 Project is **1.7** for journey time benefits alone. Including some productivity and agglomeration benefits the BCR is **2.29**. This includes the costs of Newport docks enabling works but does not monetise any economic benefits of those measures. These details were published to the M4 Inquiry on 20th December 17 with supporting economic assessment reports:

Social, cultural and environmental benefits of the scheme, such as air quality and noise improvements in Newport are not monetised. Similarly, environmental disbenefits, such as woodland clearance, are not monetised, although consideration is being given to 'ecosystem services' assessment to look at monetisation of these aspects and provide information on the subject to best inform decision making.

The table below demonstrates the step changes in BCR resulting from the now committed removal of Severn crossing tolls and then the docks works costs as published on 20/12/18 in the Public Inquiry document 'Revised Economic Assessment Report Supplement No.2'.

M4 Project BCR	Half tolls assumption (as assessed at March 2017)	Severn tolls removed (as assessed at June 2017)	Severn tolls removed and docks works costs included (as assessed in December 2017)
Transport BCR	1.66	1.87	1.70
BCR including some wider benefits	2.27	2.52	2.29

A Table of BCRs for road, rail and active travel schemes is included in Annex B to this note. It must be noted however that there are inconsistent types of benefits monetised between projects assessed against Treasury 'WebTAG' guidance, generally road and rail projects, that consider purely journey time saving and active travel projects that monetise other benefits.

The BCR for any scheme represents an important input into the overall appraisal of a transport schemes, in the initial "screening" of proposals and comparison of options. However it is an economic benefit analysis, not a value for money analysis, in order to determine whether the project would deliver a positive economic outcome if it were constructed.

The BCR forms only one part of the decision making process as to the viability of a project and captures only part of the total benefits. While it can be updated to include the wider economic benefits of improved accessibility to/from jobs and markets, it does not include for instance the social benefits such as improved accessibility to key public services (eg schools, hospitals etc), improved provision for Active Travel (eg cyclists, walkers and equestrian users) and improved connectivity between adjacent communities.

The BCR also does not consider any environmental benefits such as improved resilience to climate change, improved pollution control and habitat creation or the benefits of the scheme during construction in terms of use of local labour and materials, appointment of local SMEs and work done with local communities.

You also requested information on the following issues as and when they become available:

- *Details of the timescale for the development of the regional business plans referred to on page 23 of the Economic Action Plan*

The regional business plans have to be worked upon jointly with stakeholders in the region – we will respect the spirit of that partnership and each Chief Regional Officer will discuss a timeline for delivering their regional business plan with partners in the region. However, we expect that all regional business plans will be in place before the end of the year.

- *Full details of the specific funds that are to be consolidated into the Economy Futures Fund, both initially at the point of launching the Fund and those that are intended to be 'transitioned' into the Fund in the longer term, (Including the amounts of the money involved)*

Between now and the end of the financial year we will be taking a close look at all of these funds and bring as many of them as possible within a single Economy Futures Fund. Over time, we would hope to bring more funds under the common umbrella of the Economy Futures Fund. We cannot place a figure on this at this stage, because we do not yet know how many or which funds will be part of the Fund in its initial stages.

In my previous letter to you of 21st November, I advised that I would provide you with an update on the Active Travel Review. I will be making an Oral Statement on Active Travel on 27 February and the funding review will form part of that Statement.

I also advised that I would provide you with an update on the A465, which I have addressed earlier in my response.

Yours sincerely



Ken Skates AC/AM

Ysgrifennydd y Cabinet dros yr Economi a'r Seilwaith
Cabinet Secretary for Economy and Infrastructure

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Llywodraeth Cymru
Welsh Government

Rt Hon Chris Grayling MP
Secretary of State for Transport
Department for Transport

transportsecretary@dft.gsi.gov.uk

4 October 2017

Dear

Chris,

I would like to follow up on our constructive meeting on 7 September.

I am glad we had the opportunity to meet and agree the way forward on the issues outstanding that would facilitate your authority for the Welsh Government to proceed to issue the tender documentation. We agreed that there was sufficient agreement to proceed with the procurement process and issue the tender documents on 26 September.

Following a period of intense work by our officials, we issued the tender documents on Thursday 28 September. Although this was two days later than you and I had targeted, our officials achieved a significant milestone and I would like to thank you for your support in helping us reach this outcome. I would also like to thank you for the hard work and commitment from your officials, particularly during days prior to issuing the documents.

In our meeting we discussed our budgetary positions and the financial context we find ourselves dealing with as part of the devolution of franchising functions. You recognised the Arriva Trains Wales (ATW) has seen cost growth since it was let, in common with other franchises across the UK. In turn I recognised that the track access charge adjustment mechanism, which was a feature of the ATW franchise, is an important part of the funding landscape.

We discussed a shared desire to address the underlying issues, and agreed that discussions should continue between the Welsh Government, Wales Office and HM Treasury as we seek resolution to the financial implications. On this basis I have been content for my officials to sign the Funding and Outputs Agreements in Principle.

In our discussion we recognised that the Welsh Government has approached the procurement of the franchise from a different perspective to the Department for Transport, reflecting how we were intending to achieve our outcomes and how we would manage risks.

Following your offer at our meeting, your officials met with mine to share their experience of how they have approached getting the maximum commercial benefits from franchise procurements. This has helped in our efforts to drive value through our franchise agreement, and will support the case for an appropriate funding settlement from HM Treasury.

We also discussed the importance of stakeholder management, and importantly, where responsibility will reside once the Core Valley Lines asset is transferred to the Welsh Government. I agreed that the Welsh Government should be responsible for working with stakeholders in Wales on matters relating to our actions. You agreed that the UK Government would remain responsible for matters arising across the UK. This provides the right level of accountability and responsibility as we work to deliver our ambitions for the railway.

In relation to these latter points, the First Minister provided an update on Friday 29 September on the Welsh Government's discussions with rail unions, begun by Wales TUC. These discussions form part of how we take forward our ambition to continue to improve the accessibility of our public transport system and follow the National Assembly for Wales' Economy, Infrastructure and Skills Committee recommendation for robust passenger and stakeholder engagement. In doing so we are building upon a clear public response in our consultations, and reflect our duty to provide a transport system that can be accessed by disabled people in Wales,

As a result we have set out a series of commitments, made in addition to the published tender documents, which mean we can move ahead with confidence on our plans for the future Wales & Borders Rail Service and South Wales Metro, and reduce the risk of disruption not only in Wales but across the UK rail network as a result of our transformation of the Core Valley Lines. My officials have now clarified what this means as assumptions for bidders, and I understand this has been shared with your officials.

Based on current service provision on Wales and Borders heavy rail services I do not expect there to be a cost implication for these commitments. Separately, in relation to South Wales Metro services where infrastructure solutions define the type and operation of rolling stock required, these commitments clarify our position and my officials have informed bidders that they can assume the availability of additional, time limited funding to support these ambitions. This funding reflects a future requirement, and therefore it is not my intention to include this additional funding as part of the discussions for an appropriate settlement with HM Treasury that will reflect the growth in costs during the current franchise.

We continue to share common ground on the matter of the advantages of vertical integration for the benefit of passengers. You agreed with the principle that the Welsh Government should be better able to influence decisions that affect the network on which its rail services will operate and noted our suggested that a step towards this could be achieved through two places on the Network Rail Wales Route Board. I understand that my officials have been contacted by the Network Rail Wales Route Managing Director to take this forward.

You also restated your commitment to providing the £125m (2014 prices) contribution to the Valley Lines scheme agreed in November 2014, noting that the Welsh Government would be able to determine how this funding was spent on the future of rail services. Our discussion touched on the degree of flexibility that the Welsh Government could have around the timing of this funding. I understand that this is now being progressed between our officials and officials from HM Treasury.

In terms of the transfer of the Core Valley Lines asset, we agreed that discussions were progressing satisfactorily. You offered to follow up with Network Rail to ensure that we have arrangements in place to deal with the transition of ownership, which will help ensure that Network Rail can meet their obligation to transfer an asset in the appropriate condition. You also offered to follow up with Network Rail about the Welsh Government's ability to access Network Rail's infrastructure insurance mechanism. I understand that both these matters are now being progressed by officials.

Finally, it remains vital that rail investment provides benefits across Wales. Passengers across South Wales will be looking forward to the promised start of bi-mode services this autumn, bringing with it the significant increase in capacity on rush-hour services. With the introduction of the new Intercity Express trains passengers in Pembrokeshire must receive the same quality of service as those in Paddington. I also look forward to an update on the development of plans to improve journey times and connections between Swansea and Cardiff, south Wales, Bristol and London, station improvements at Cardiff and Swansea, and, crucially, progress on plans to improve journey times and connections across north Wales. I am happy for my officials to be involved in the development of this work.

*Yours ever,
Ken*

Ken Skates AC/AM

Ysgrifennydd y Cabinet dros yr Economi a'r Seilwaith
Cabinet Secretary for Economy and Infrastructure

Annex B – Benefit to Cost Ratio's (BCRs) of Road, Rail and Active Travel Projects

Scheme	BCR*	Notes
M4 Project	1.7	Core journey time benefits. Source: M4 Inquiry Evidence
M4 Project	2.29	Inc. some wider productivity and agglomeration. Source: M4 Inquiry Evidence
HS2	Currently Estimated to be 1.9 - 2.3	The estimation of the BCR is undertaken using a social cost benefit analysis. The benefits that are estimated therefore include both direct effects for rail passengers and indirect effects on the wider population. The BCR (excluding wider economic impacts) for the entire HS2 scheme has fluctuated between 1.8 and 2.2 with changes in costs, service pattern assumptions, and modelling approaches. When estimates of wider economic impacts are included, the BCR has been estimated between 2.2 and 2.7. The latest economic case (July 2017) calculates a BCR for the scheme of 1.9 (excluding WEIs) and 2.3 (including WEIs). Reference: http://researchbriefings.files.parliament.uk/documents/SN00316/SN00316.pdf https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/634196/high-speed-two-phase-two-economic-case.pdf
Crossrail	1.97	
South Wales Metro	1.82	Outline Business Case
Great Western Electrification	1.13	Transport minister Jo Johnson statement 16/1/18
A483 Newtown Bypass	3	
A470 Cwmbach to Newbridge	1.05	
A303 Stonehenge	0.3-0.5	Core Transport Benefits
A303 Stonehenge	1.3-1.7	Including some wider benefits
A9 Dualling (Scotland)	0.78	Reference: https://www.transport.gov.scot/media/6727/a9-dualling-programme-case-for-investment-main-report-september-2016.pdf
A40 Llanddewi velfrey to Penblewin	Estimated to be 1.0	WEFO Business Case
M4 Junction 28 Improvement	10	Value of Benefits associated with the Scheme has been evaluated at approximately £ 795M.
A470 Maes yr Helmau to Cross Foxes	2.42	

A487 Dyfi Bridge	0.4	
Sustainable Travel Towns	2.6 - 8	University of Leeds and Atkins research for DfT, monetises: <ul style="list-style-type: none"> •Reduced infrastructure costs •Fewer road accidents •Improved air quality •Lower noise levels •Reduced CO2 •Reductions in indirect taxes •Decongestion Source: http://www.its.leeds.ac.uk/aoss/15/cases.html
Car Sharing Schemes	1.95 – 6	
Personalised Travel Plans Schemes	4.5 – 31.8	

* BCR's collated from published Business Cases and/or studies. It is noted that there is variation in the benefits monetised for different projects, the most significant being those road/rail projects using Treasury Green Book/WebTAG guidance and active travel studies. Cells highlighted blue identify Schemes assessed on comparable terms to the M4 Newport Project.