Financing the Future

A report on innovative financing mechanisms for major regeneration projects in London

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Greater London Authority
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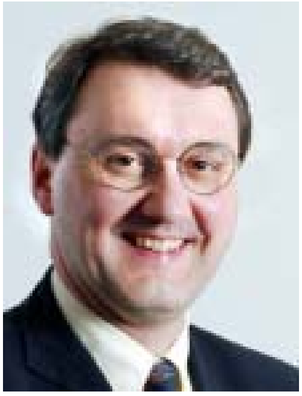
Foreword



This report is, in short, about 'growing pains' - primarily about alternative ways to fund the infrastructure of a growing city, but also about whether our new regional tier of government can 'grow up' and has the maturity to take greater responsibility for the financing mechanisms that will make such investment possible. The thesis underlying the report is simply put - the regeneration such infrastructure investment will unlock can generate economic growth; given innovative funding mechanisms, this gain can be partially captured through taxation and charges, and the finance used to kick-start the process.

The difficulty is the need for innovation, with the Treasury historically cautious since the price of over-optimism usually ends up being paid by there. Nonetheless, the evidence we received during our scrutiny shows there are workable models, learning lessons from abroad. Indeed, some changes have already been introduced by the present government, with all party support, notably on business improvement districts.

Until the argument for greater flexibility is won, we believe more can be done within existing rules, to learn from best practice and speed up some developments which seem to take years to bring to fruition despite the benefits being apparent to everyone involved.

On behalf of the Committee, I'd like to express our gratitude to GLA staff and outside agencies and witnesses for presenting evidence to us, and to our own Secretariat staff for so ably supporting our deliberations despite difficult circumstances. Please let us have your thoughts in response to this study.

Mike Tuffrey
Chair of the Economic and Social Development Committee

April 2004

The Economic and Social Development Committee

The Economic and Social Development Committee was established by the London Assembly on 10 April 2002.

Mike Tuffrey (Chair) – Liberal Democrat

Eric Ollerenshaw (Deputy Chair) – Conservative

Angie Bray – Conservative

Jennette Arnold – Labour

John Biggs – Labour

Darren Johnson – Green

The Committee's terms of reference are to examine and report on social and economic development matters of importance to Londoners and the strategies, policies and actions of the Mayor as they relate to social and economic development issues, the London Development Agency and other Functional Bodies where appropriate. The Economic and Social Development Committee is particularly required to examine and report to the Assembly on the implementation and revision of the Economic Development Strategy.

Contacts:

Pina Ardu, Assistant Scrutiny Manager
pina.ardu@london.gov.uk
020 7983 6541

Katy Shaw, Committee Co-ordinator
katy.shaw@london.gov.uk
020 7983 4416

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Executive summary

The funding framework for urban regeneration in London, like the rest of the UK, has rested largely on a number of grant-based programmes supported by statutory and non-statutory land use planning initiatives, such as Section 106 agreements, whereby developers contribute to the cost of providing infrastructure and services.

However in recent years, partly due to the constraints on public sector resources, there has been a growing recognition that alternative approaches, such as broader fiscal incentives, are needed to fund regeneration and major infrastructure projects as a supplement to the traditional grant-based funding system.

With this investigation we sought to explore and examine innovative ways of financing major regeneration and infrastructure projects, drawing from examples of practice in other countries.

We found that many of the innovative tools of joint public/private finance that are used to generate funding for major projects in other countries are not currently available in London.

We heard that there is a strong case for the introduction of more creative financing mechanisms for public/private co-investment into major regeneration and infrastructure projects, such as "value capture" mechanisms. However, without Treasury approval, many of these mechanisms have no chance of ever being used.

Despite some recent efforts within Government to innovate in finance, more radical moves are needed to increase the financing available for city and regional economic development and to leverage private investment into large-scale regeneration and infrastructure projects. We recommend that the Treasury should relax its current local government finance regulations to give regional and local government institutions greater freedom to develop financing solutions for major regeneration and infrastructure projects locally.

The report also highlights that, until the argument for greater flexibility is won, more could be done within existing rules to learn from best practice and make best use of existing programmes and new mechanisms which are coming into use, such as Business Improvement Districts.

1 Introduction

1.1 The London Assembly investigates issues of concern to Londoners. This report sets out the findings and recommendations from an Assembly investigation into Alternative Funding of Regeneration.

1.2 The aim of the scrutiny was to examine the use of innovative mechanisms for financing large-scale regeneration and infrastructure projects in London, in addition to traditional Government grant programmes.

Terms of reference

1.3 The terms of reference of the scrutiny, agreed on 2 December 2003 were to:

- Review and examine what progress has been made in London in the development of innovative mechanisms for funding regeneration projects, including Business Improvement Districts.
- Identify key successes and barriers to progress in developing innovative mechanisms for funding regeneration projects in London.
- Identify national/international case studies for comparison, with particular focus on the area of large-scale regeneration and infrastructure projects.
- Explore and examine innovative ways to fund large-scale regeneration and infrastructure projects in London, with reference to examples of practice from case studies.
- Make appropriate recommendations to the Mayor, the Government, the LDA and other key stakeholders.

The scrutiny process

1.4 The Committee held a scrutiny session on 2 March 2003. The single session examined and discussed the use of alternative ways of financing large –scale regeneration and infrastructure projects in London, in addition to traditional Government grant programmes. The Committee received evidence from a range of representatives including the London Development Agency (LDA), Transport for London (TfL), Professor Tony Travers of the London School of Economics, the Royal Institute of Chartered Surveyors (RICS) and London First.

1.5 This report brings together the key points from the scrutiny session, and written evidence received from stakeholders.

2 National context

2.1 The increasing interest in the potential use of fiscal incentives as a mechanism for stimulating urban regeneration in the UK has been highlighted by a number of sources in recent years.

2.2 The report of the Government Urban Task Force *"Towards an Urban Renaissance"*[1], published in 1999, advocated the provision of tax relief to encourage greater involvement by key players in the physical regeneration process and the deployment of tax disincentives to divert property development away from sensitive greenfield areas and steer it towards inner urban areas.

2.3 In April 2000 the Government set up the Social Investment Task Force (SITF) to "assess ways in which the UK could achieve a radical improvement in its capacity to create wealth, economic growth, employment and an improved social fabric in its poorest communities." This was based on the belief that, for regeneration strategies to have a lasting effect, they need a real economic base. The Task Force's final report *"Enterprising Communities: Wealth beyond Welfare"*[2] put forward five specific proposals, including a Community Investment Tax Credit; a Community Development Venture Fund; bank disclosure on lending in under-invested areas; greater latitude for investment in Community Development initiatives and support for Community Development Finance Institutions.

2.4 As a result of the Social Investment Task Force, five proposals have been enacted and developed by the HM Treasury and government. A recent report published by the UK Community Development Trade Association (CDTA) updates policy progress and action since the SITF and shows the significant progress has been made in implementing the SITFs recommendations.

2.5 Overall, in the past five years substantial progress has been made in the UK towards introducing some new tools that do leverage institutional and commercial participation into local and regional development, particularly in the areas of SME's finance, town centre development, social and community enterprise and small-scale regeneration projects. These include:

- Regional Venture Capital Funds
- High Tech Start-up Funds
- Regeneration Investment Funds
- Community Development Financial Institutions (CDFIs)
- Community Investment Tax Credits
- Business Improvement Districts (BIDs)

2.6 Each of these tools will take some time to bed down, and it will be a while before any evaluation is possible.

2.7 The changes that the Government is undertaking are very welcome and much needed. Greater flexibility and "room for innovation" are important pre-requisites for attracting private investment into regeneration markets.

2.8 However, whilst there are clearly efforts within Government to innovate with public finance, our investigation found that there is a need for more radical

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[1] *Towards an Urban Renaissance,* Final report of the Government Urban Task Force, June 1999

[2] *Enterprising Communities: Wealth beyond Welfare,* Final Report of the Social Investment Task Force, October 2000

moves to increase the financing available for city and regional economic development and to leverage private investment, particularly in relation to the financing of large-scale regeneration and infrastructure projects.

2.9 In this respect, the Government has even set up an intra-government Committee, known as "MISC 22", to undertake its own search for innovative funding mechanisms, with focus on the Thames Gateway. MISC 22 has, by all accounts, found nothing new and has, according to some accounts, been wound up.[3]

2.10 More specifically, in relation to Crossrail, a government-appointed review headed by Adrian Montague, deputy chairman of Network Rail, is exploring the viability and funding options on the scheme before advising ministers whether or not to proceed. Though it is understood that the report of Adrian Montague's inquiry has been submitted to the Secretary of State for Transport in January, nothing has so far been made public about the content of the report.

[3] Travers T., Glaister S. Funding London's Development, London School of Economics and Imperial College, October 2003, p. 11

3 London progress

3.1 In recent years considerable research has been undertaken in London to explore alternative ways of funding regeneration and particularly on the role of private finance in local development and regeneration. The London Development Partnership established a working group in 1998 to review the impact of private finance across a range of economic development and urban regeneration objectives in London. The programme provided an overview of the range and scope of the instruments available to lever in private finance for economic development and regeneration across London.

3.2 Its final report *London's Leverage*[4], published in July 2000 found that the fundamental challenge was not boosting the overall supply of public funding available for urban economic development. The challenge was to find more efficient ways of connecting public money and the many stand-alone projects and schemes operating across London to the needs of the market and private finance.

3.3 The LDA and other organisations involved in regeneration and economic development in London are building on the analysis and recommendations of the *London's Leverage* report by putting in place appropriate programmes to involve the private sector in economic development and regeneration projects in the capital.

The London Private Investment Commission

3.4 In April 2002 the LDA, Greater London Enterprise and the Corporation of London established a London Private Investment Commission (PIC) to provide advice and guidance from the Financial and Professional Services Sectors on how to improve the flow of private capital into London's urban economic development and regeneration priorities. The PIC aims to provide a more unified approach so that public and private sector organisations across London work together to leverage the most from the opportunities and mechanisms, which have recently been introduced in the UK[5], including Business Improvement Districts, Community Development Tax credits etc.

Business Improvement Districts (BIDs)

3.5 Business Improvement Districts are a North American tool for securing private sector involvement in area renewal schemes. In their simplest form, BIDs assume service delivery and janitorial roles (such as cleaning streets, improving parks and providing safer environments). However, as BIDs mature, they may go on to develop their focus to undertake promotional functions and operate business development programmes and, possibly implement capital project improvements, though we were told this kind of investment currently seems unlikely in London.

3.6 BIDs are now being introduced worldwide as a means of allowing businesses to help regenerate the areas in which they are based. It is estimated that more than 27,000 BIDs now exist in twelve countries.

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[4] *London's Leverage,* Executive Report of the London Development Partnership Private Finance Working Group, July 2000

[5] See paragraph 2.7

3.7 Enabling legislation for BIDs has now been introduced in the UK and the draft BID regulations have recently been published for consultation.

3.8 Central London Partnership is running a programme on behalf of the LDA, to encourage London's town centres and industrial areas to prepare for the roll out of the Business Improvement Districts in London. The aim of the London BIDs programme is to ensure that London optimises the use of this new tool when it come on tap in 2004 and 2005. The programme provides technical assistance and capacity building for nascent BIDs throughout London[6].

3.9 Julie Grail (Partnership Director, Central London Partnership) informed us that BIDs are now being progressed in nearly all of London's boroughs, with 9 London pilots currently planning formal BID votes by 2006 (Bromley, Holborn, Pool of London, Kingston, Waterloo, Bankside, Paddington, Piccadilly Circus, and New West End Co.).

3.10 We very much welcome the introduction of Business Improvement Districts in London and the work being undertaken to ensure London's readiness to take advantage of this tool to regenerate town centres and commercial areas throughout the city. We look forward to seeing the benefits of BIDs spread across London and particularly to the establishment of more BIDs schemes in Outer London other that Inner London.

Other initiatives and programmes

3.11 We heard that a number of other initiatives have been developed and progressed by the LDA and its partners, particularly in the areas of SMEs finance, town centre development, social and community enterprise and small-scale regeneration projects. Recent initiatives include:

SME Finance Working Group. This group is providing oversight and co-ordination for all SME finance programmes in London, and is pursuing a single shared strategy (with multiple strands) for SME access to finance in London.

SME premises rental guarantee fund. On advice from the PIC, the LDA is looking into how a rental guarantee might be used to overcome the concern of developers and investors of the early stage lettings risk of small business accommodation developments in London. The LDA is pursuing the establishment of this fund.

Capital Fund (Regional Venture Capital Fund). The LDA appointed commercial fund managers and launched the Regional Venture Capital fund for London in 2003.

Objective 2 – Access to Finance. Through the Private Investment Commission, the LDA has worked with GOL and Business Link for London to put in place a new framework for the use of the funds.

Supporting London Community Development Financial Institutions. Community Development Financial Institutions (CDFIs) are a new form of licensed financial intermediary for community investment and are able to offer investors a new incentive, Community Investment Tax Relief (CITR). The London CDFIs Programme has been developed over the last 12 months with key partners operating in the CDFI field.

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[6] Further details can be found at www.londonbids.info

Thames Gateway Model Development. Work was undertaken by the LDA and its partners to consider:

- mechanisms for leveraging private investment into the land acquisitions which will be necessary to mount a successful bid to host the Olympics in 2012; and
- business models for schemes which capture the enhanced land and property values resulting from infrastructure investment in the Thames Gateway.

3.12 Overall, we welcome the work and activity being undertaken in London to improve the ability to leverage private finance into regeneration and local development. However it is still early days for much of these activities and it will be a while before any evaluation is possible.

Challenges for London

3.13 As Tony Travers highlighted, it is important to note that despite these specific initiatives, in a current regulatory and financial environment in which over 95% of all taxation is set by central government and where all capital expenditure by English regional and local government is subject to Treasury control, the ability of London to adopt mechanisms for public/private co-investments is significantly constrained.

3.14 A major challenge – due to the large amount of resources required - is the financing of large-scale regeneration and infrastructure projects. Many large projects are planned in the capital, requiring billions of pounds of investment, including Thames Gateway, Crossrail and the Olympic Games. None of these projects are currently funded and it seems unlikely that the government will provide grant funding to cover the entire capital expenditure plans, partly due to constraints on Government funding and the large costs of these projects.

3.15 The LDA is working to find ways to fill a significant gap in the financing and funding of these projects, with particular focus on the Thames Gateway Area. A critical issue in this area is the provision of infrastructure, including transport, water, power lines, sewage treatment, which require significant levels of investment.

3.16 In relation to transport infrastructure, a number of proposals have been put forward by Transport for London to use innovative mechanisms for financing and funding existing operations and future planned projects. The proposals focus principally on the use of mechanisms for value capture, particularly *Tax Increment Financing*[7] *(TIF)*.

3.17 Examples from other cities, particularly in North America and Europe show that Tax Increment Financing and a number of other mechanisms, which are not available in London, such as bond issues and joint venture arrangements, can be effective tools for leveraging private investment into major projects. This area will be addressed in more detail in the following section.

[7] See paragraphs 4.10-4.13

4 Innovative financing for major projects

4.1 Traditionally, large-scale projects in London and the rest of the UK have been funded entirely by central government. However, this now seems increasingly unlikely, partly due to constraints on government resources and fears about the ultimate costs of major projects.

4.2 As Tony Travers highlighted in a recent report prepared for the LDA[8], it is clear the Government believes London - and thus its taxpayers – should in future bear a greater proportion of its own infrastructure developments than in the past. However no means have yet been put in place to give London's regional or local government the freedom necessary to pay for such projects. This has led to the current impasse over the funding of all major projects in London and increasing uncertainty over their realisation.

4.3 The following paragraphs outline some of the key challenges and barriers in relation to the financing of large-scale projects and consider a number of possible alternative financing mechanisms, which have been highlighted in the evidence we received for this investigation.

Challenges and barriers

4.4 At the *national level*, London's investment potential using its own resources is strongly constrained by the UK's highly centralised public finance system. Greg Clark (Director of London Promotion and International Initiatives, LDA) argued that unlike other major European and North American cities, the LDA and the Boroughs have relatively little fiscal or financial autonomy and relatively few of their own public investment vehicles, although this is changing slowly. In the main, London depends on Government transfers and programmes for the bulk of its economic development efforts, which limits the flexibility of city agencies to develop local solutions to local needs and to achieve the levels of spending required.

4.5 Thus, London needs major capital investment, but does not have all the powers or resources to deliver them. The city has not independent tax base sufficient to deliver its own projects. The Greater London Authority and the boroughs are just about capable of smaller, local projects, but only central government has the political power, financial resources and access to Parliamentary powers necessary to drive key projects forward. However – as our witnesses told us – the Government is yet to put up the funding for many projects which are deemed to be necessary in London, or is willing to create the means for the city itself to allow these projects to go ahead.

4.6 To narrow the focus to Crossrail, Irving Yass (Director of Policy, London First) pointed out how we are at "a curious impasse where the Government seem to be waiting for a proposition to come forward on how there could be a business contribution to Crossrail, without being willing to discuss either part in any of this in detail. How much it is going to cost is not, at the moment, for discussion either in or outside Government, nor are they willing to discuss what kinds of mechanism would be acceptable to the Treasury"[9].

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[8] Travers T., Glaister S. Funding London's Development, London School of Economics and Imperial College, October 2003, p. 20

[9] Minutes of Economic and Social Development Committee 2 March 2004

4.7 The LDA's submission highlighted that a number of challenges and barriers also exist at the *operation level*, many of which are not necessarily unique to London, which are restricting private investment into regeneration. These include:

- Perception of risk and poor returns
- High transaction costs
- Low prioritisation
- Fragmented or unconventional ownership patterns
- Poor information flow
- Burdensome bureaucratic processes and requirements
- Differing timeframes of the public and public sector
- Delivery capacity
- Lack of business confidence and certainty
- Lack of statutory, or well understood vehicles

Possible alternative funding mechanisms

4.8 As highlighted by Greg Clark, many of the innovative tools of joint public/private finance that are used to generate funding for major projects in other countries are not currently available in London. The following paragraphs outline a number of possible alternative funding mechanisms, drawing from international examples from North America, Asia and Europe, which have been highlighted during our investigation.

4.9 The options outlined below would, to varying degrees, ensure that owners and occupiers whose properties benefited from transport and other improvements would contribute towards their cost.

<u>*Tax Increment Financing/Value capture finance*</u>

4.10 Tax Increment Finance (TIF) was proposed by Lord Rogers's Urban Task Force (DETR, 1999) as a possible method for urban areas to re-invest in their physical assets. The Task Force had found such mechanisms in use in North America and believed they could play a part in the "urban renaissance" Lord Rogers hoped to kick-start within Britain. Chicago, in particular, has used mechanisms of this kind extensively.

4.11 TIF works by capturing part of the gain generated by rising land values in the immediate vicinity of a major infrastructure development. To do this, it would first be necessary to designate a zone around a new railway line, road or other asset. The value of properties within the zone would then be monitored, so as to make it possible to compare changes within the zone with those outside. Insofar as values within the zone rose more quickly than values outside, the difference would be attributed to economic benefits of the new infrastructure.

4.12 A levy of this kind would potentially produce a revenue stream of millions of pounds a year from, say, a major railway development. One estimate of the existing capital value of properties that would be likely to benefit from Crossrail has been put at £70 billion, inferred from existing rateable values of £5.4 billion. Hillier Parker estimated that the overall full yield (at today's prices) from a relatively modest levy might – over time – be £1.4 billion. Of course, this amount would come in over a number of years, as value additions worked their way through to capital (and thus to rental) values[10].

4.13 Despite some limitations, there is a clear case for a TIF mechanism as a way of allowing London to undertake projects that would allow it to develop. Market realities would be very important in determining which projects went ahead and which did not. Crossrail is the most widely-discussed beneficiary of TIF financing, indeed Transport for London have undertaken extensive internal research on the subject. In fact, once the mechanisms were put in place (there would need to be legislation to allow TIF-funded schemes) a range of smaller schemes might be able to proceed. Regeneration proposals involving infrastructure within the Thames Gateway would, in a number of cases, be easier to justify if the beneficiaries from redevelopment were to contribute to capital costs.

Bonds

4.14 Bonds have received much attention as a possible means of raising resources for public transport and other major infrastructure projects in London. Although by no means new to British local government, bond issues have been used rarely in recent years. Discussions about alternatives to the government's public-private partnership for London Underground raised the possibility of using revenue bonds of the kind used in the United States to fund infrastructure. This method was used, for instance, to pay for the renewal of the New York Subway during the 1980s and 1990s[11].

4.15 The advantage of bonds of this kind is that they are a cheap, tradable, way of borrowing and can be tied to the projects concerned. The need to explain the use to which money will be put, and then to report on the effectiveness with which resources have been used, ensures that considerable discipline is brought to bear on projects. In many American states, a referendum is held when it is proposed to issue a bond to finance a particular package of infrastructure investments. Thus the public must assent to the long-term cost of projects.

4.16 Bonds are simply one of a number of possible ways of borrowing money. But they offer a number of potential advantages. In particular, they allow bond holders to assure themselves that their lending is part of a coherent capital spending plan that is being prudently managed and regulated, thus assuring them of security. Such security could assist in providing the secure funding that would make it more likely that London projects will go ahead.

4.17 We heard that London's Social Housing organisations area already succeeding with issues of private debentures in the capital markets and the issuing of bonds by transport and regeneration authorities is likely to attract similar kinds of investors[12].

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[10] Travers T., Glaister S. Funding London's Development, London School of Economics and Imperial College, October 2003

[11] Travers T., Glaister S. Funding London's Development, London School of Economics and Imperial College, October 2003, p. 20

[12] Written evidence by the LDA

Real Estate Investment Trusts (REITs)

4.18 REITs are long established in the USA, Australia, and some other European property markets where they have grown rapidly since the early 1990s. One of their main advantages is that they open both the residential and commercial property markets to the small investor, so boosting this key sector of the economy and widening tenants' choice.

4.19 The Government announced in the pre-Budget review of a public consultation on the advantages of introducing a Real Estate Investment Trust (REIT) for the UK. The precise regulations governing the UK REIT will not be known until after next year's public consultation. But the idea is that there will be a tax transparent investment vehicle for property, meaning investors are taxed only on individual dividends and not on rental income or capital gains.

4.20 Existing Venture Capital Trusts are a tried and trusted vehicle for raising capital for smaller company investment in the UK. Extending this existing model to Real Estate investment would be a relatively easy development.

Business rates

4.21 Another possible way of raising additional resources for major projects, as highlighted by our witnesses, would be through increases to business rates or National Non-Domestic Rates (NNDR)[13] or supplementary rates.

4.22 The idea of a levy on the non-domestic rate (NDR) is not new. The Corporation of London published a study in 1994 outlining such a scheme[14]. An NDR levy could operate either across the whole city or within smaller areas. Payments would be based upon an additional rate-in-the-£, to be paid by all NDR payers within the area. The logic for the levy would be similar to that for the TIF scheme outlined above. Resources would be raised from owners and occupiers who stood to benefit from new infrastructure. The smaller the area within which the levy operated, the more precise would be the link between levy and benefit.

4.23 The overall yield of the NNDR in London in 2002-03 was £3.7 billion. The rate-in-the-£ set to deliver this was 43.7p. The rate base is concentrated is inner and central London, though even outer boroughs in some cases have a substantial rate base by national standards. A 5 per cent levy on the 2002-03 NNDR across the whole of London would have yielded over £185 million. An inner London-only levy would have produced just under £120 million.

4.24 The yield of an NNDR levy of this kind could either be used as a direct payment for new infrastructure or, alternatively, be used to make interest payments on borrowing undertaken against the yield of an NNDR levy over, say, 20 or 30 years. The latter is clearly a very different proposition, involving additional NNDR payments for a generation. However, the scale of investment that could be backed by an NNDR levy would be considerable. A London-wide levy of, say, 5 per cent on the existing rate would produce almost £200 million per annum. This, in turn, would finance borrowing of perhaps £4 billion. The cash increase in the yield of NNDR in England in the period since the last major reform of local government finance in 1993-94 has been 44 per cent, compared with 87 per cent for council tax (ODPM, 2003a).

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[13] Business Rates, or National Non-Domestic Rates (NNDR), are collected from businesses and others who occupy non-domestic property.

[14] Glaister S. and Travers T. (1994), An Infrastructure Fund for London, London: Corporation of London

4.25 As our witnesses highlighted, there are a number of problems with the current system of business rates. Firstly, business rates are subject to an RPI cap, which means increases are limited to the rate of RPI inflation (generally 2 to 3 per cent per year).

4.26 Secondly, business rates are paid by occupiers of non-domestic properties. Therefore, while occupiers would pay the additional levy, property owners would derive the benefits of raising capital values. There is no doubt this would generate opposition amongst taxpayer.

4.27 Thirdly, business rates are collected nationally by the Treasury, which then reallocates them back to the local authorities based on their standard spending assessment. This does not allow for any "value capture" to take place at local and regional level.

<u>Delivery vehicles</u>

4.28 The government's extensive use of Private Finance Initiative (PFI) and Public-Private Partnership (PPP) arrangements is evidence of a desire to undertake projects in ways that shifts part of the project risk away from the public sector, so helping to keep projects off balance sheet. Thus, the major programme of PFI hospitals and schools which is currently being constructed will not score as public sector capital expenditure at the time of construction, but will instead appear as revenue expenditure – a service charge for use of the asset concerned – in the years ahead.

4.29 Any use of TIF would have to bear this Treasury approach in mind. The borrowing related to projects would almost certainly have to be undertaken by an institution outside the public sector. Borrowing by the boroughs, the LDA, TfL or the GLA (or a controlled company) would, under existing local government finance legislation, count as public expenditure. Major infrastructure projects could be undertaken using a number of possible institutional mechanisms. A number of these are briefly summarised below:

- *PFI/PPP arrangements*. Although the PPP for the London Underground proved highly controversial, London authorities – including the GLA – have used PFI-type deals to undertake many projects. Private companies or consortia are asked by a public sector client to bid to design, build, finance and maintain a major project according to a specified brief. Repayments are then made by the client over the lifetime of the asset.
- *Public interest companies and trusts*. It is possible for the public sector to set up companies or trusts that it does not dominate or control. In the past, London's Underground and buses were run by the London Passenger Transport Board, a private trust whose members were – by law – appointed by institutions outside government. More recently, the government has created Network Rail as a not-for-dividend company at arms length from Whitehall. Crucially, the borrowing of institutions of this kind is not counted as being on the public sector balance sheet.
- *Joint ventures*. It is possible for the LDA and London boroughs to create joint ventures with developers and other private sector partners. Such vehicles will be in the private sector, so long as local government does not have a controlling interest. The benefits of joint ventures of this kind is that they allow those participating (including local authorities) to benefit from

the rising values of land. It will also be possible to borrow money against expected increases in value. In this way, value can be captured to facilitate new infrastructure within or near a development. The bigger the venture, the greater the possible value capture.

4.30 Evidence submitted by the LDA highlighted that the difficulty with such ventures is that they often involve many partners and/or some property owners may not wish to join in (or may delay joining in the hope of bigger gains at a later date). Assembling and developing land at Kings Cross and Wembley, or redeveloping areas such as Park Royal, have been subject to significant difficulties and delays, caused by the number of landowners, local authorities and developers involved.

The Government's view

4.31 As part of this investigation we wrote to the ODPM seeking their view with regard to the use of innovative mechanisms for financing large-scale regeneration and infrastructure projects, particularly value capture mechanisms.

4.32 The evidence we received from the ODPM makes clear that "at present, the Government has no plans to impose new taxes on businesses or households to capture value uplifts to pay for infrastructure provision"[15].

4.33 The ODPM's submission highlighted a number of possible alternative funding structures, which are currently under consideration by the Government, including land pooling, Business Improvement Districts, Inherent land value and Public/Private Partnerships.

4.34 The response seemingly demonstrates the Government has yet to introduce significant innovations in relation to regeneration finance. We believe the Government must accept the case for the need of alternative methods of funding and allow for greater devolution of financial powers to regional and local government institutions.

[15] Written evidence by ODPM, p.1

5 Looking forward

5.1 We have asked our witnesses what could be done to resolve the impasse over the financing of major regeneration and infrastructure projects in London and allow these projects to go ahead.

5.2 The key message was that – under present legislative and regulatory framework - only the Treasury has the power to break the current deadlock and drive major projects forward.

More creative financing mechanisms

5.3 Our investigation found that there is a pressing need to establish more creative financing mechanisms for public/private co-investment into major regeneration and infrastructure projects. The evidence we received highlighted the role the use of innovative tools, such as bonds and value capture mechanisms, play in leveraging private sector co-investment into regeneration in other countries.

5.4 It was argued that there is a strong case for the introduction of similar tools, particularly value capture mechanisms, in London. However, without Treasury approval, many of these mechanisms have no chance of ever being used and it seems clear from our investigations that the Treasury does not currently plan to facilitate a means of this kind into existence, at least in the immediate future.

5.5 We agree with our witnesses that the Treasury should reconsider its position on this matter and facilitate innovative funding mechanisms into existence to allow London to undertake projects that would allow it to develop. Alternatively it is for central government to provide more resources to allow key regeneration and infrastructure projects, such as Thames Gateway, the Olympic Games and Crossrail to go ahead. What is clear is that the present impasse cannot go on without detrimental effects on London's economic and social development and on the quality of life of Londoners.

> *Recommendation 1*
>
> **The Treasury should review its current regulations regarding local government finance to allow regional and/or local government institutions greater freedom to develop financing solutions for major regeneration and infrastructure projects locally.**

5.6 We also believe the GLA, ALG and other key stakeholders in London, including the private sector, should more actively lobby the Treasury to relax current local government finance regulations to enable the introduction of innovative financing tools, such as "value capture" mechanisms, for the financing of major projects. In particular, we believe that all relevant stakeholders should act more jointly to increase the effectiveness of their lobby efforts.

Recommendation 2

The Mayor, London Development Agency, ALG, jointly with the private sector and other key stakeholders should more actively lobby the Treasury to enable the introduction of innovative mechanisms for public/private co-investment in regeneration by highlighting the benefits these mechanisms could bring to London

Optimising the use of existing tools

5.7 Representatives from the LDA stressed the importance of making an optimum use of existing powers and new mechanisms, which are coming into use, including Business Improvement Districts. In this context we believe that the LDA could improve its effort to publicise opportunities and promote the sharing of best practice actively across London.

5.8 We also believe it is important the LDA consistently monitor the use and effectiveness of existing and new financial tools in order to seek optimum benefit from their use.

Recommendation 3

The London Development Agency should seek to optimise the use and effectiveness of existing programmes and new mechanisms, which are coming into use, by promoting opportunities and the sharing of best practice actively across London

Appendix 1 Summary of Recommendations

Recommendation 1

The Treasury should review its current regulations regarding local government finance to allow regional and/or local government institutions greater freedom to develop financing solutions for major regeneration and infrastructure projects locally

Recommendation 2

The Mayor, London Development Agency, ALG, jointly with the private sector and other key stakeholders should more actively lobby the Treasury to enable the introduction of mechanisms for public/private co-investment in regeneration by highlighting the benefits these mechanisms could bring to London

Recommendation 3

The London Development Agency should seek to optimise the use and effectiveness of existing programmes and new mechanisms, which are coming into use, by promoting opportunities and the sharing of best practice actively across London

Appendix 2 Public session and witnesses

2 March 2004	Greg Clark, Director of London Promotion and International Initiatives, London Development Agency
	Meg Kaufman, Policy Manager, Investment, London Development Agency
	Gareth Blacker, Director of Development, London Development Agency
	Mel Barrett, Director of Business Services, London Development Agency
	Irving Yass, Director of Policy, London First
	Professor Tony Travers, Director, Greater London Group, London School of Economics
	Shashi Verma – Principal – Corporate Finance, Transport for London
	Dr Jim Whelan, Royal Institute of Chartered Surveyors

Appendix 4 Principles of Assembly scrutiny

The powers of the London Assembly include power to investigate and report on decisions and actions of the Mayor, or on matters relating to the principal purposes of the Greater London Authority, and on any other matters which the Assembly considers to be of importance to Londoners. In the conduct of scrutiny and investigation the Assembly abides by a number of principles.

Scrutinies:

- aim to recommend action to achieve improvements;
- are conducted with objectivity and independence;
- examine all aspects of the Mayor's strategies;
- consult widely, having regard to issues of timeliness and cost;
- are conducted in a constructive and positive manner; and
- are conducted with an awareness of the need to spend taxpayers money wisely and well.

More information about scrutiny work of the London Assembly, including published reports, details of committee meetings and contact information, can be found on the London Assembly web page at www.london.gov.uk/assembly.

Appendix 5 Orders and translations

For further information on this report or to order a bound copy, please contact:

Pina Ardu, Assistant Scrutiny Manager
Assembly Secretariat,
Greater London Authority,
City Hall, The Queen's Walk, London SE1 2AA.
pina.ardu@london.gov.uk
Tel: 020 7983 6541

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Greater London Authority
City Hall
The Queen's Walk
London SE1 2AA
www.london.gov.uk
Enquiries **020 7983 4100**
Minicom **020 7983 4458**

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