

REPORT: Mersey Gateway Executive Board
DATE: 7 April 2008
REPORTING OFFICER: Strategic Director - Environment
SUBJECT: Mersey Gateway Strategic Outline Business Case

1.0 PURPOSE OF REPORT

1.1 This report provides an update of the business case that was submitted to the DfT in July 2005 to reflect the considerable developments in the scheme since that time. The information reported provides a summary of the Mersey Gateway Strategic Outline Business Case that has been prepared by the Mersey Gateway Project Team and accepted by the Mersey Gateway Officer Project Board.

2.0 RECOMMENDED: That Members

i) Note that Mersey Gateway still benefits from policy support at National, Regional and Local levels.

ii) Agree to the additional project objective "*To restore effective network resilience for road transport across the River Mersey,*" to align the project aims with the Eddington recommendations.

iii) Agree the principal elements of the tolling proposals which are designed to maximize the opportunity to deliver the project within the funding limits and to provide a best value option for funding toll discounts and a Mersey Gateway sustainable transport programme.

iv) Note that the current financial analysis results show that the project remains on course to be delivered within the funding limits agreed with Government, with toll levels based on the current Mersey Tunnels charges.

v) Note that the value for money parameters required by Government as a funding condition are satisfied but the headroom available to satisfy the condition has been reduced.

3.0 SUPPORTING INFORMATION

THE STRATEGIC CASE

3.1 The planning process for Mersey Gateway will test the extent to which the project proposals fit with planning and economic policies expressed at national, regional and local levels. At the national level the Government's most recent statement of its transport policy is in the White Paper '*Towards a Sustainable Transport System*' – the Government's response to Eddington and Stern. The White Paper

sets out the challenge for transport in a world faced with climate change and associated economic considerations. The White Paper acknowledges that congestion is increasing on many motorways and strategic rail and road routes. The motorway boxes are examples of road networks particularly under pressure and links connecting the M62 and the M56 and forming the route across the Runcorn Gap (including the SJB) features in the top category. Network resilience (described as the ability of travel networks to return to normal service patterns following incidents or disruptions) is also a key consideration that has a significant effect on reliability.

3.2 Eddington stresses the importance of reliable transport and network resilience for business but similar requirements apply to ensure that effective civil contingency plans are in place. Mersey Gateway would provide the additional road capacity required to restore network resilience for road river crossings between the Mersey Tunnels and M6 at Thelwall. These benefits to the regional road network are reflected in the Highways Agency expressed support for Mersey Gateway. To ensure the potential operational benefits are realised the following additional project objective has been proposed in the SOBC.

- To restore effective network resilience for road transport across the River Mersey.

3.3 The need to combat climate change is also being embedded in Government policy. The White Paper referred to above also foreshadows the approach intended by Government to limit carbon products in transport. The Mersey Gateway tolling proposals combined with the outputs from the on-going Mersey Gateway Sustainable Transport Study (commissioning of the study was approved by the MGEA in January) will deliver carbon benefits by removing congestion without inducing additional traffic and by improving travel choice for Halton residents.

3.4 The project is supported by the North West Regional Assembly and features as a scheme of Regional and Sub-Regional Significance in the emerging Regional Spatial Strategy. There is no other transport project in the North West Region in the planning stage which offers such strong support to local policies and objectives, which would serve to meet local, regional and national objectives and which serves both the local, regional and national highway networks. Mersey Gateway continues to benefit from strong support in the Regional and Sub-Regional economic programmes.

3.5 At a local policy level the promotion of Mersey Gateway in a formal planning sense relies on a few key policies in the adopted Halton Unitary Development Plan (April 2005). The Programme Entry funding approval by the Department for Transport in March 2006 enabled the supporting policy for Mersey Gateway to be developed in more detail and brought up to date. These supporting policies will be embraced in the next iteration of the Community Strategy, the Corporate Plan and the Local Development Framework. To understand the wider issues and opportunities

arising from Mersey Gateway and to consider how best to capture the benefits arising, the Council have commenced preparation of a Mersey Gateway Regeneration Strategy. The outcome of the Regeneration Strategy will also inform the Councils priorities for physical investment and urban renewal. Local consultation on regeneration options is currently taking place and during the summer it is planned to put final proposals in the public domain to inform the consideration of the Mersey Gateway formal Planning Applications

- 3.6 As part of the development of a sustainable and integrated transport system for the Borough, the Council has commissioned a Mersey Gateway Sustainable Transport Study. The key objective of the first phase of investigation was to identify and assess public transport options which would be likely to be commercially viable and practically affordable and which would also be complementary to, and be supported by the Mersey Gateway Project as a whole. In summary, the report recommended that a bus based transit system utilising new as well as existing infrastructure and facilities would be the most achievable and affordable way forward and enable step change improvements to be delivered in the short to medium term. The report recognised that the development of light rail should not however be precluded but this should be seen as an option for the longer term. Consequently the Mersey Gateway scheme now includes passive provision for LRT infrastructure to be provided in the future, supported by the potential for a lower deck to be constructed in the New Bridge providing for access and egress through the bridge abutments..
- 3.7 The Mersey Gateway Sustainable Transport Study has progressed to more detail since it was reported to this Executive Board in January 2008. Potential schemes that will deliver the required improvements to bus services, and cycling and walking facilities have been identified. The Study is on-going and is based soundly on the relief of SJB and the Mersey Gateway Regeneration Strategy. A series of focused public consultations and group interviews have been undertaken to understand the views of Halton's residents on public transport in Halton now and in the future with the Mersey Gateway Project.
- 3.8 The Sustainable Transport Study is aimed at delivering service improvements in 2015. As such there is a long lead time to put in place the delivery process. The current requirements are for proposals to be developed sufficiently to inform the consideration of the Planning Applications for Mersey Gateway. A series of draft strategy elements have been developed from which specific proposals will emerge and be evaluated. These will be developed, tested against the consultation responses and prioritised but they provide a clear statement of the Council's intent to maximise the opportunities provided by Mersey Gateway to improve integrated and sustainable transport. Examples of the schemes under consideration are:-
- Creation of a Sustainable Transport Corridor across the Silver Jubilee Bridge

- Connections between SJB and Widnes and Runcorn main service and retail centres.
- Creation of a Halton Transit Network under a single service brand name.
- Quality Partnership or Contracts with bus operators
- High Frequency Strategic Bus Corridor for Local Services
- Design and Access Specifications for Public Transport Interchange Hubs
- Enhancement of the Local Distributor Bus Network
- Door to Door Service
- Halton Hopper upgrade
- Regeneration of the Runcorn Busway
- Expansion of the Real Time Information for Public Transport
- Cycling and Walking Core Network

3.9 The above options have considerable potential to increase travel choices and to reduce the impact of tolls for local trips. In addition, around thirty percent of Halton residents do not have access to a car or van. Many of these are in deprived social and economic groups. Although tolling the Mersey Gateway will not have a direct impact on travel options for the non-car ownership group, any benefits in sustainable transport access will extend to this large group. Mersey Gateway presents a step change in the prospects for delivering sustainable transport options for Halton residents. The proposed concession arrangements (see below) include provisions for Halton Borough Council to share in the toll revenue, where the revenue passed to the Council will be used to support toll discount schemes and would also provide funding for the preferred sustainable transport programme.

TOLLING STRATEGY

3.10 The Council has established a tolling policy that is intended to allow successful delivery of Mersey Gateway within funding limits agreed with Ministers. The principal objectives of tolling are:

O7. To operate a toll concession scheme, within the limits of affordability, so as to mitigate the impact of tolls on local users who are currently able to use the SJB free of charge, many of whom are frequently crossing the river and some fall within social inclusion target groups;

O8. To manage demand to ensure the delivery of transport and environment benefits, by maintaining free flow traffic conditions on the Mersey Gateway and SJB and delivering priority for public transport on the SJB; and

O9. To transfer demand risk to the Concessionaire for the duration of the concession, by allowing the operator to manage that demand through the toll charged, within the constraints of the legal powers and the regulations agreed in the Concession Contract, consistent with the objective of protecting local users.

- 3.11 In addition to facilitating the investment required to deliver the new bridge, the tolling regime will provide a lever to manage demand, so that free flow traffic conditions are maintained on the new link, thereby locking in the delivery of the projected service reliability and standards throughout the concession. The removal of through traffic from SJB will provide an opportunity to re-establish the existing bridge for local transport use so that the sustainable transport and environmental benefits are delivered. The new traffic model forecasts support the projected benefits from tolls as future traffic levels are suppressed by the tolling charges. The lower traffic levels with tolling prevent any general increase in traffic noise and air pollution (including carbon green house gases) across the Borough that would otherwise occur without the scheme.
- 3.12 Affordability considerations, coupled with demand management and sustainable transport objectives, dictate that most or all private car and commercial cross-river traffic between Widnes and Runcorn must be subject to tolls. This includes traffic across the previously free-to-use SJB. Its proximity to the new MG means that if left untolled it would be impossible to prevent substantial revenue leakage and maintain free flow traffic conditions thereby jeopardising the affordability position and the sustainable transport objectives explained above. The proposed statutory process is to secure tolling powers for MG using the Transport and Works Act and to apply for a Road User Charging Scheme under the Transport Act 2000 for SJB.
- 3.13 The Council envisage the initial toll levels matching the levels charged at the Mersey Tunnels, although during the bidding process prospective operators will have the opportunity to submit variant proposals that may prove more attractive for the Council. The funding agreement with Government assumes that toll revenue will be used to counter unexpected inflation and cost increases. Thus some flexibility in managing the revenue, or revenue projections, from tolls is required both prior to concluding the concession agreement and during the concession period. The statutory process means that it is necessary for the Council as promoter to set the regulatory boundaries for toll charging. The tolling proposals will be drafted to allow the affordability risk to be managed leading up to financial close and thereafter to provide the concessionaire sufficient flexibility and scope to manage demand and its revenue so that it can offer the Council the best value bid.
- 3.14 The Council announced its commitment to prioritising toll discounts for local residents in the results of public consultation published in November 2007. Any discounted or concession scheme for toll charging will need to be constructed so as to be both affordable and acceptable within the terms of UK and EU law in respect of discriminatory pricing and State Aid. One way of providing protection for local users would be to incorporate a discount toll mechanism in the concession agreement, most likely to be based on frequency of use but potentially also linked to the place of residence in the case of private vehicles. The drawbacks with such a proposal are that the cost of the discount scheme would be for bidders to determine and the agreed terms for the discount scheme would be fixed for the concession term. This presents considerable uncertainty for bidders to deal with in estimating the number of users qualifying for discounts and the Council would face potentially expensive change terms should modifications to the discount scheme be required, which is a likely scenario at some stage in the concession period.

- 3.15 On best value terms an alternative scheme for delivering discounted toll levels is preferred. The toll levels required to finance a commercial bid, on top of the PFI Credit subsidy agreed with Government will determine the overall project revenue required to support a bid. In addition to presenting the overall project revenue required to finance their bid, bidders will also have to take into account the extent of toll revenue share they are prepared to offer the Council. The Council would use their share of toll revenue to fund discounts on tolls for local residents or frequent users through a separate concession scheme run by the authority and to provide revenue support for public transport in line with the sustainable transport objectives of MG. This approach is likely to raise the maximum revenue available for mitigating the impact of tolls on local residents and the Council would have flexibility to choose how to spend its revenue share throughout the concession period. The downside is that the funding available to support any discount scheme will only be known initially when commercial bids are return and confirmed when actual toll revenues are received.
- 3.16 It is proposed that bidders (probably in their Standard Bid) should be asked to assume that toll levels are set initially at levels matching those at the Mersey Tunnels, increasing thereafter in line with inflation. It is further proposed that they be told to assume that a fixed level of central government funding is available for the project. It is proposed that bidders should then be asked to bid the level of economic interest in the toll revenue which they are prepared to make available to HBC. This arrangement produces a banded system of project revenues as shown in fig 1.

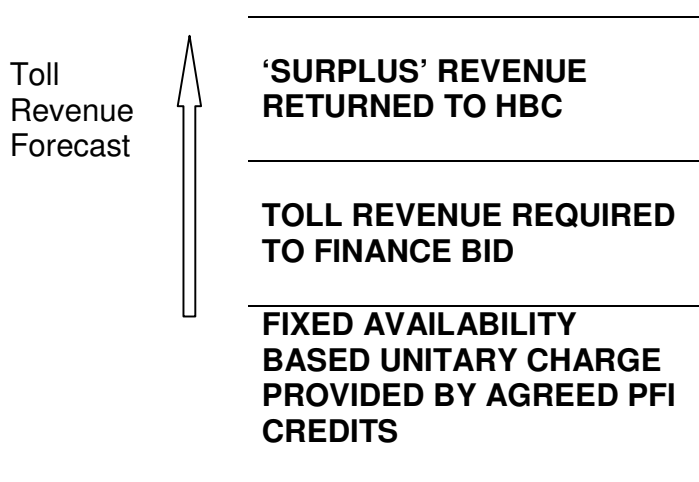


Fig 1. – Project Revenue

- 3.17 The above project funding arrangement has been modelled in the financial analysis reported below.

THE FINANCIAL CASE

- 3.18 The purpose of the Financial Case is to demonstrate that the scheme is based on sound costings and revenues, and that the projections are in keeping with the funding agreement with Government. A review of the financial case has been

undertaken using the financial model produced for the Programme Entry bid but updated with revised input values and assumptions.

3.19 The Scheme Cost Estimate and Quantified Risk Assessment (QRA) have been revised in full by the project team to take account of all changes since Programme Entry. The headline scheme cost results are in table 1.

	Current Assumption (at March 2007 Prices)
Construction Costs	£362,524,000
Maintenance Costs	£21,279,500
Operating Costs	£179,681,581
50%ile Risk	£20,000,000
Optimism Bias	23.5%

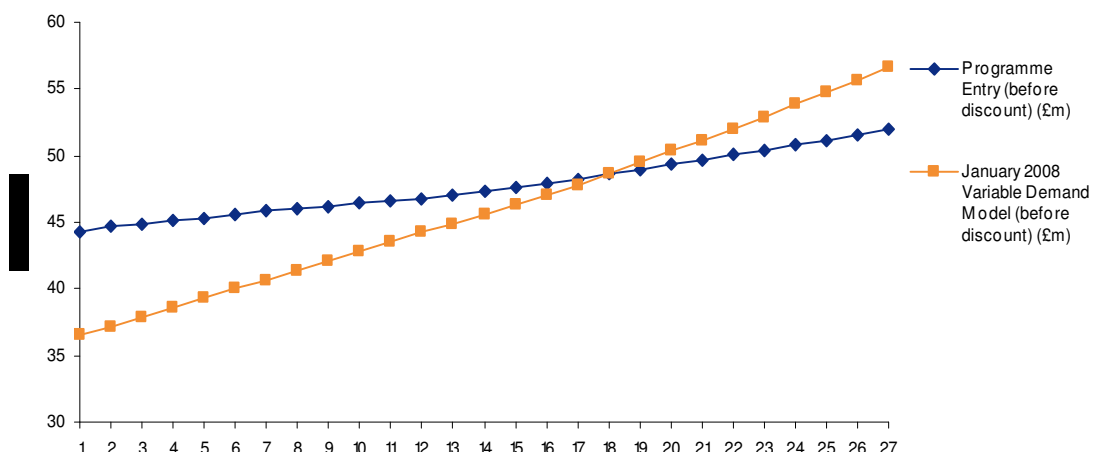
Table 1: Scheme Cost and Risk

3.20 The current traffic forecasts are the product of a very detailed modelling exercise utilising the latest variable demand forecasting techniques and prudent underlying assumptions. The modelling has followed DfT guidance and has been subject to DfT oversight at all stages of development. The traffic forecasts underpin the toll revenue projections and the current results are considered to be much more robust than was the case at programme entry because:-

- Projections show trips being suppressed by toll charges where the level of suppression is reduced as alternative routes become congested
- Underlying growth is modest (at between 1 and 2%)
- Local evidence of cross river travellers paying toll charges equivalent to Mersey Tunnels.

3.21 The graph below presents the current revenue forecasts alongside the forecasts used to support the programme entry submission. It should be noted that to reflect the greater uncertainty attached to revenue projections made to support the programme entry bid only 75 percent of the revenue projections shown in the graph below were used in the PE bid

Toll Revenue - Programme Entry vs January 2008



3.22 The PFI Credit agreed with Government will be used to supplement the current toll revenue projections. For the purposes of the business case financial analysis the term over which the £123m of PFI credit support is received has been determined to best meet the requirements of the project. The result of this calculation is an assumption that the project receives the PFI credit support over a period of 15 years, resulting in circa £12.5m pa in 2011 prices. In net present value terms this annual support does not exceed the £123m PFI Credit award.

3.23 The comparison of current financial assumptions compared with the programme entry bid is given in table 2.

	PFI credit requirement (total)	Unitary charge (Nominal p.a)	Present Value (at 3.5% real to 2011) of			
			Unitary charge	Toll Revenue	Const'n costs	Operating costs
Case Description	£ million	£ million	£ million	£ million	£ million	£ million
Programme Entry	123	11.9	103	633	358	176
Revised Base Case (Jan 2008) for SOBC	123	12.5	103	746	440	122

Table 2: PFI Financial Analysis

3.24 Although the project team are confident that the risk allowances in the financial model are robust, financial risks do remain that could translate to affordability risks in the future. The most significant of these are:

- The ability to effectively match the support from Government to the needs of the project;

- The treatment of toll revenue forecasts by potential concessionaires and lenders;
- The currently assumed Composite Trade tax relief may not be achievable in practise. This has resulted from the abolition of the Industrial Buildings Allowance relief from 2011 as announced in the 2007 budget. This issue is outside the control of the Council and has been discussed with DfT. Should this risk materialise then HBC would wish to discuss with DfT options for making good the funding shortfall that might result. All current financial modelling assumes that Composite Trade treatment is achieved.
- The scale of the proposed Mersey Gateway Project is such that relatively small changes in key parameters such as capital cost, inflation and senior debt interest rate can have a significant impact on the toll revenue required to fund the project

3.25 The current base case financial analysis shows that the revenue received by the project over the contract life is significantly greater than the total requirement and therefore the project is affordable in overall terms. Should the project be delivered with the current financial assumptions confirmed then the Council revenue share (as indicated in the proposed funding structure in Fig 1) available to support toll discounts and to fund the sustainable transport programme would be £190 million cash outturn over the 30 year concession term (equivalent to £52 million net present value at 2011).

THE VALUE FOR MONEY CASE

3.26 The purpose of the Value for Money Case is to demonstrate the likely benefits and disbenefits of the scheme against its likely costs. One of the DfT funding conditions is a requirement for the value for money of the scheme to “be re-assessed against the Department’s value for money criteria in the light of the economic results from the new traffic model before the scheme progresses to public inquiry. It should also be noted that the Department reserves the right to re-consider its offer of funding for the Mersey Gateway if the scheme is re-assessed as offering worse than “medium” value for money. The minimum Benefit Cost Ratio for qualifying as medium value for money is 1.5:1. The current economic results reported in draft to DfT show the project to remain as high value for money with a BCR of just over 2:1. It should be noted that this BCR is lower than the Programme Entry submission (circa 2.8) and hence the headroom to withstand any downward adjustment by DfT has been reduced.

4.0 POLICY, RESOURCE AND OTHER ISSUES

4.1 The Strategic Outline Business Case establishes the resource requirements for the next stage plan that will progress the project through the planning process and procurement, culminating with the start of construction in 2011. A resource plan is in preparation and will be reported to the Mersey Gateway Executive Board in May.

5.0 KEY RISKS

- 5.1 The key risks identified in the Strategic Outline Business Case are covered in section 3 above.

6.0 EQUALITY AND DIVERSITY ISSUES

- 6.1 Mersey Gateway provides an opportunity to improve accessibility to services, education and employment for all.

7.0 LIST OF BACKGROUND PAPERS UNDER SECTION 100D OF THE LOCAL GOVERNMENT ACT 1972

- 7.1 Files maintained by the Mersey Gateway Project Team and by the Highways and Transportation and Logistics Department.