

THE INFRASTRUCTURE COMMISSION

World class infrastructure for a world city

November 2010

Commission process

Throughout 2010, the Infrastructure Commission canvassed the opinions of business leaders and stakeholders, as owners, investors, advisers on, and users of London's infrastructure. The Commission's public call for evidence generated written submissions from nearly 50 parties and was followed by evidence sessions with 15 expert witnesses, roundtables with the main economic regulators and discussions with London First members.

This is the executive summary of the full report – World class infrastructure for a world city – which is available on the London First website, along with further details of all participants and evidence received.

London First is grateful to all those who gave generously of their time and experience and particularly to the Commissioners, whose collective knowledge has refined the report into a comprehensive proposition for ensuring London's infrastructure can continue to support the capital's competitiveness as a world city and role as the powerhouse of the UK economy.

The London First Infrastructure Commission

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Executive summary

Well-functioning infrastructure networks are essential to London's competitiveness and future economic growth. Infrastructure – by which we mean water and sewerage, waste, transport, energy and telecoms – enables the city to function. It provides the underpinnings for successful commerce, the foundations for improved productivity and is a critical component of London's global competitiveness.

London is a world city and the gateway to international investment in Britain. Its unique concentration of economic activity is at the heart of the country's economy; the capital generates more in tax than it receives in public spending by a margin of £14-19 billion a year. Maintaining the infrastructure which enables London to continue to make this contribution is vital to maintaining its competitiveness and to the prosperity of the UK's economy as a whole.

London First members – London's larger businesses – have expressed concerns that London's infrastructure is not adequate for a world city; a view which a number of studies have reinforced. With population forecast to grow by 1.3 million by 2031 the pressures are set to increase. London First, in response, established this expert Infrastructure Commission in early 2010 to examine both private and public sector provision and consider how London's infrastructure can continue to support its status as a world class business location and driver of the UK economy.

Our approach has been to seek the right level of infrastructure provision, balancing costs with the capacity, reliability, quality and resilience needed to support our global competitiveness. As well as considering new infrastructure for London, we also believe that we can get better value from existing networks through improved efficiency, coordination and management. We make a series of practical recommendations, covering a range of industry sectors, to deliver short, medium and long term improvements to the way London's infrastructure is run, planned, financed and delivered. These recommendations are summarised below; some common themes are:

- the need for better long-term planning by government, at both a national and London level, coupled with practical policy frameworks which take into account London's distinctive concentration of economic activity and give the private sector the clarity and certainty it needs to invest;
- a greater understanding, on the part of London's utilities, of London businesses' requirements of the infrastructure they provide; and
- a more transparent and devolved approach to the delivery of London's infrastructure by the public sector, notably in transport. The future of London's transport provision should be decided and funded at a London level, with political and governance structures which reflect this responsibility and which enable the Mayor to be the unambiguous champion of Londoners, while Transport for London (TfL) focuses on delivering better value.

Planning for long-term infrastructure investment

Joined up policy

Infrastructure assets tend to have long lives, be expensive to develop and, thus, require a combination of planning and revenue certainty to support their delivery. In the UK, there are essentially three forms of provision:

- privately provided monopoly network infrastructure, which is subject to economic regulation and effectively guaranteed a return when efficiently provided;
- privately provided infrastructure which is subject to market and policy risk; and
- publicly provided infrastructure, principally for this report, in London's transport.

We believe that the provision of network infrastructure by the private sector has broadly been fit for purpose, with the significant caveat that the national regulatory framework has not always taken sufficient account of central London's distinctive economic characteristics or the long term nature of infrastructure investment: these points are explored below.

With regard to private infrastructure subject to market risk, there can be a disconnect between wider public policy objectives and the detailed frameworks which underpin infrastructure provision by the private sector. An example is the targets set out by government for carbon reduction which have been established through primary legislation but have not been accompanied by the right incentives and policy certainty to support private sector investment.

Private sector investment in infrastructure subject to market and policy risk requires greater policy certainty from government. This requires clear up-front statements of government policy in key strategic areas, better coordination within government and more rapid implementation of the detailed policy frameworks which can provide the certainty and longevity which the private sector needs to make the business case for infrastructure investment.

Recommendation 1

We welcome the establishment by government of Infrastructure UK (IUK), which has the potential to play an important role in meeting the objectives set out in Recommendation 1 above, and its publication of the National Infrastructure Plan. The utilities' economic regulators should have a statutory duty to have regard to the Plan when conducting their periodic reviews and to set out clearly their reasons if they do not comply with its timescales or objectives.

Recommendation 2

Improving land use planning policy for infrastructure

Planning consistently ranks as one of the main concerns to companies looking to invest in UK infrastructure. The land use planning framework has made the provision of much infrastructure slow, expensive and, in some cases, has prevented any provision at all.

Recommendation 3

The Government must ensure that its reforms to national and local planning frameworks for infrastructure maintain timeliness and predictability for infrastructure providers as well as improving democratic accountability.

New approaches to financing and funding infrastructure

Recommendation 4

The Commission welcomes action by Government to reduce the policy risks that the market cannot price. Where market risks remain, which deter investment that Government believes is justified in terms of social benefits, Government should provide transparent and targeted subsidy, either directly or via network utilities.

A way of financing infrastructure that has been mooted by a number of bodies, including the Mayor of London, is Tax Increment Financing (TIF). This mechanism involves the private or public sectors financing infrastructure which is then funded by the increased tax receipts which flow from development.

Recommendation 5

The forthcoming review of local government finance should explore creating the flexibility for local authorities to finance infrastructure improvements through new mechanisms such as TIF.

In London decisions about public expenditure on infrastructure investment are not taken in such a way that the costs are borne by the people who benefit. Londoners pay taxes to central government which are part-recycled back in grants to London government, sometimes decided on an annual basis, and often accompanied by restrictions on how they are spent. This reliance on central government grant undermines London's ability to plan and fund infrastructure investment.

Recommendation 6

Tax, spending and decision making for London should be aligned. The Government should give the Mayor flexibility over how he spends the grant he receives, so that he is able to direct his resources to meet the priorities of London rather than central government. The Government has announced a review of local government finance and this should explore ways of rebalancing the tax system so that central government raises less in tax from London, with the Mayor raising more of his own resources in a manner that is transparent and equitable between London's residents, visitors and businesses.

London-wide strategic planning

The Mayor should play a greater strategic role in the planning and delivery of London's infrastructure:

Recommendation 7

- first, as a pan-London client in regulators' periodic reviews. The Mayor, given his own regulatory functions of land planning and the role his other strategies play in London's economic development, should be a statutory consultee in the economic regulators' periodic reviews. Given the Mayor's electoral mandate, his views on the levels of provision that London needs should carry particular weight. The economic regulators should have a duty to comply with the Mayor's position, or, if deemed inappropriate, to explain why; and
- second, there should be greater coordination between investment programmes in different sectors. The Mayor should make representations on London's overall needs to IUK as it updates its National Infrastructure Plan and IUK should, similarly, have a duty to comply or explain.

Infrastructure provided by the private sector

London's energy, communications, water and sewerage utilities moved into the private sector in the 1980s and 1990s. The network infrastructure the utilities provide, which is typically characterised by natural monopoly, is subject to oversight by economic regulators, who protect customers from the abuse of monopoly power, either by promoting competition or acting as a proxy for the market.

The Commission believes that the regulatory processes for striking a balance between service levels and prices across regulated networks have broadly worked well and provided a fit-for-purpose network infrastructure. There is due process to determine the balance between affordability, through the prices consumers pay, and outputs, with independent scrutiny of the efficiency with which the two are linked, and there has been substantial investment in the UK and London's infrastructure networks post privatisation. The evidence we have taken suggests that regulator-sanctioned investment, funded from consumers' bills, can continue to be financed in this way in future.

However, the various regulatory regimes do not always take sufficient account of the unique economic characteristics and core functions of London's central area, or the needs of businesses (in terms of security of supply, resilience and so forth) when determining the balance between service standards and prices.

Recommendation 8

The utilities need to understand more clearly the service levels that business users in London, particularly in central London, want and are willing to pay for. In conjunction with their regulators the utilities should devise ways in which business users' preferences can be reflected in the outcomes of their periodic reviews.

While the five year review processes have broadly worked well, we believe that they should be accompanied by longer term strategic direction statements, say for 25 years (which currently exist in water), which fit better with the long lead times required for infrastructure investment.

Recommendation 9

Economic regulators should determine long term strategic direction statements for network utilities and each periodic review determination should state how the shorter, typically five year investment programme ties in with this longer term statement.

Electricity transmission and distribution

Rather than building new capacity in anticipation of future demand, energy distribution companies currently are only able to earn a return on new capacity where demand is immediate. This approach works well where future growth is uncertain. In areas with high concentrations of economic activity, such as central London - where growth is more certain and ad-hoc additions to the distribution network are difficult, time-consuming and expensive - providing capacity in line with forecast demand would support development.

Recommendation 10

The licensed electricity distributor should consult with central London businesses to establish the level of anticipated demand and establish proposals to build capacity to meet this need on a more integrated, forward-looking basis. Ofgem should establish a mechanism to permit the forward funding of capacity enhancement against reasonable demand forecasts.

Similarly, the resilience of the UK's energy networks is uniformly set.

Recommendation 11

The licensed electricity distributor should also consult with central London businesses to explore the costs of reinforcing the distribution network to improve resilience and establish the willingness, in practice, to pay for this reinforcement. Ofgem should have regard to this evidence when conducting its periodic reviews.

Connecting new customers to London's distribution network is a complex process because of the legacy characteristics of the network and the ways in which capacity is added.

The Key Performance Indicators for electricity distribution should be amended to capture connection metrics from a customer perspective, based on consultation between business and the distribution provider, and subject to determination by Ofgem.

Recommendation 12

The Mayor has a policy for a quarter of London's energy to be supplied via local generation - decentralised energy - from facilities such as combined heat and power (CHP) by 2025.

We welcome district-wide decentralised energy schemes where they make economic sense, but question whether it is sensible for London to have a distinctive energy policy around electricity generation, with London-specific targets. It is right that the Mayor has a view of London's energy needs, and what should be done locally both to support carbon reduction efforts and maintain security of supply, but this should be integrated with national energy policy. In this area, as in others, the Mayor's power lies at least as much in exhortation as in regulation.

Recommendation 13

Water and sewerage

The road congestion caused by the large scale renewal programme is not included by economic regulator Ofwat as a cost when it determines an acceptable level of leakage. As argued below, the utilities should face time-based charges for digging up those strategic roads which cause the most congestion.

Ofwat should allow within its periodic review determination sufficient revenues to enable an efficient operator to meet permit charges levied by London government, to incentivise the swift completion of road works and thus reduce the road congestion they cause.

Recommendation 14

Water shortages are not unusual in London and the South East. Any changes to the regulatory system must be carefully judged so as not to undermine investors' confidence or to prejudice the industry's ability to finance its substantial investment programme.

There is also a need to improve London's performance in disposing of waste water.

And while water and sewerage companies have a statutory duty to produce 25 year strategic plans, it is unclear how these currently reconcile with the outcomes funded from the five year price controls.

Recommendation 15

Ofwat should:

- review regulatory mechanisms to remove disincentives to bulk trading between water companies and, with this model in place, look at what new infrastructure is required;
- allow the funding required, on a commercial risk basis, to construct the Thames Tideway Tunnel to reduce sewerage discharge into the Thames; and
- explain more transparently how each five year price control period's programme fits with Thames Water's 25 year strategic direction statement and its statutory water resource management plan.

Much of London is on a flood plain. The risk of tidal flooding in London is mainly managed by the Thames Barrier, and the Environment Agency's work suggests that this will provide sufficient protection through to 2070. Planning Policy Statement 25 sets out the mitigation measures to guard against local flooding which new development must take. This typically requires the provision of flood compensation storage which, in London, is very expensive.

Recommendation 16

The Environment Agency should adopt a more flexible approach to dealing with flood risk mitigation from new development in London in order to deliver high flood resilience at lowest long term cost.

Waste

The planning system can be an important barrier to the provision of capacity to meet London's waste disposal needs. While the Mayor has the power to take over applications for waste facilities that treat over 20,000 tonnes of waste per annum, affect more than one borough and are of strategic interest, this would not necessarily cover the smaller scale waste from energy facilities that he wishes to encourage through his waste strategy.

Recommendation 17

The reluctance by local authorities to grant planning permission for waste facilities increases the costs of their development and undermines the Mayoral strategy of London becoming self-sufficient in waste disposal by 2031. Planning powers for waste in London therefore sit best at the Mayoral level and the referral threshold for planning applications for waste treatment facilities should be reviewed and reduced to support the development.

London's transport

London's transport infrastructure is struggling to cope with current peak demand and this problem will be compounded by population growth. Meeting this capacity challenge requires a combination of greater investment, changes in policy and improvements in efficiency, supported by increased transparency.

Transport for London (TfL) should be reformed to ensure a clearer and consistent delineation between its client and delivery functions. The Mayor, as the elected representative of London, should not be the defender of TfL's operations but, rather, its overall client. He should set overall strategic policy which it is TfL's role to implement, either by delivering services directly or commissioning services effectively. The Mayor should be the unambiguous champion of Londoners' interests.

Recommendation 18

London's underground

The tube is vital to London. Over half (56% in 2008) of people entering central London during the weekday morning peak, 7am to 10am, use the underground. Modelling developed by TfL estimates that 47 per cent of commuters travel in crowded conditions in the morning rush hour. Without investment in modernisation, the tube will be unable to cope with the growth in demand.

The fundamental challenge in getting the tube network to deliver the outputs that London needs is that, unlike the privatised utilities, it is not self-funding. The revenue from consumers does not meet the total costs of provision and thus public subsidy is required. There are good public policy reasons why this should be the case however the reliance on subsidy (which until the creation of the tube public private partnership (PPP) was generally determined on an annual basis) has led to a necessarily short term approach to investment planning and delivery. This has resulted in a significant backlog of maintenance work and a pressing need for capacity improvements.

Significant public investment in the underground will remain necessary for the foreseeable future. Key priorities in the medium term are the underground capacity upgrades agreed in the tube PPP and Crossrail. Looking beyond those, detailed planning work should begin now on further medium to long term projects to increase capacity in line with forecast growth in demand, including Crossrail 2.

Recommendation 19

For a variety of reasons the tube PPP, set up by Government in 2003 to manage the 30-year investment programme, proved unsustainable. Following its collapse, the best features from this model – namely greater transparency, independent scrutiny and certainty over long-term investment and outcomes – need to be incorporated into a new structure, drawing on the experience of other sectors.

Recommendation 20

The transparency and efficiency of London Underground would be improved by governance reforms to create a Regulated Asset Base model, overseen by an economic regulator. While this would not provide additional funding for the underground, it would set out clearly, for the medium-term, the level of resources required based on independent verification of capital and operating expenses. It would thus provide a solid platform for London to argue its case to the Treasury for investment – or to make the fare increases or service provision cuts – necessary to keep the system functioning.

Rail

Much of London's commuter rail network is now operating at capacity in peak hours. The capital needs additional capacity to tackle existing overcrowding and, critically, to support future growth. However, existing projects will not in themselves sufficiently address the capital's transport needs over the coming decades. In the light of current spending constraints serious consideration needs to be given to the prioritisation of Network Rail's spending programme on lines, trains and stations for the current and next five year control periods. The Department for Transport (DfT) is currently reviewing the rail franchising model.

Recommendation 21

The Mayor should engage with the DfT and train operators to ensure that any reforms to rail franchises and structures, and future investment programmes, reflect London's priorities of rail services which meet rising demand, are more responsive to passengers' needs, and perform safely and efficiently. The DfT should be placed under a statutory duty to have regard to the Mayor's views on franchise specifications and his willingness to pay for additional services and, as with the economic regulators, either act on his proposals or explain why not.

Roads

London's 13,800km of roads serve two equally important functions: they enable people and vehicles to go about their business; and they are conduits for other infrastructure, with water, energy and IT infrastructure running beneath them. Fundamentally, London's roads lack the capacity to meet demand; and, even were funding no object, it is generally impracticable to provide significant additional new capacity. Accordingly, we see two principal areas for action to improve travel on London's roads, both of which would be supported by allocating responsibilities in a more coherent way. The first is better management of the existing road network, the second increased demand management through road pricing.

The Mayor's Transport Strategy needs to have a more proactive and realistic approach to network management in the context of the growing demands being placed on roads. This includes greater transparency about future demand and its projected impact on congestion, together with a clearer process for assessing and choosing between competing options for utilising scarce capacity, recognising the equal importance of roads as conduits for utilities infrastructure.	Recommendation 22
TfL's essential role should be as strategic commissioner of services on the road network; as part of this TfL should explore the scope for securing further service improvements and efficiencies through long-term integrated network management contracts.	Recommendation 23
TfL's responsibility should be extended to the whole of London's strategic road network and the Mayor and London boroughs should be given greater powers from central government over traffic control and signs.	Recommendation 24
TfL and London's boroughs should devote more resource and give a higher priority to detailed measures to improve traffic flows, including more active management of traffic lights, better management of road works and more support for freight consolidation.	Recommendation 25
In the medium to long term, a more sophisticated system of demand management, extending beyond the central London congestion charge zone, should be implemented.	Recommendation 26
TfL should consider targeted tolling schemes as a means of relieving congestion and supporting investment in additional capacity.	Recommendation 27

Maximising the use of scarce resources

Against a backdrop of tough public expenditure constraints it is doubly important that everything is done by TfL to maximise its output from its resources.

Exploiting assets more effectively

TfL should consider placing all of its property assets in a new body, Property for London, to enable a more focused and vigorous management drive on efficient asset utilisation.	Recommendation 28
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Recommendation 29

TfL should undertake a systematic assessment of its small scale and operationally self-contained transport assets. In each of these cases an assessment should be made of the relative benefits of public as against private sector ownership on key issues such as long-term asset management and investment, day-to-day operations and financing costs – as well as taking into account the potential value of any sale receipt.

Managing demand

Recommendation 30

Building on recent initiatives to encourage travel alternatives and spur innovation by making its data publicly available, TfL should support initiatives to take pressure off its congested networks at peak, such as low cost cycle infrastructure, better local travel information and tailored travel advice for local residents and businesses.

Recommendation 31

TfL should take advantage of the greater cost transparency and flexibility provided by smartcards to use its tariff structure more efficiently to shift demand when its networks are operating at, or beyond, peak capacity. This may in time require more sophisticated technology to be deployed.

Prioritising services

A number of TfL services have expanded significantly by increment over recent years.

Recommendation 32

TfL should implement a transparent process to review the scope for scaling back on lower priority requirements on public transport service quality, frequency and coverage, to optimise services and costs.

Fares and concessions

Recommendation 33

The overall level of subsidy across TfL's operations is unaffordable in the current economic climate and would arguably be less necessary in a more efficient operational and investment model. The Mayor should continue to increase fares in real terms on the underground linked to a suitable affordability measure, such as real earnings growth, and should align London bus fares more closely with those of other UK cities. Similarly, the Mayor should review the structure of London's fares and concessions to strike a better balance between social equity and transport efficiency.

Changing TfL's culture over the medium term

TfL's savings programme has doubled since its previous Business Plan, with £1.3 billion in savings now assumed to 2011-12, and more than £5 billion in total over the period of the Plan. This is welcome and should be accompanied by greater transparency.

The current lack of transparency or independent scrutiny of TfL's operations makes difficult any firm assessment of the scope for further efficiency gains. However the privatisation and subsequent regulation of UK utilities has revealed that substantial efficiencies can be realised from large, public sector monopoly service providers with many characteristics similar to TfL.

TfL should put mechanisms in place that provide greater transparency over its efficiency programme and that monitor actual progress being achieved.

Recommendation 34

The Commission welcomes the recent creation of the Independent Investment Programme Advisory Group which will provide an independent, impartial source of expert advice to the TfL Board on all aspects of the delivery of the TfL investment programme. However, we see this as a first step.

Building on the recent creation of the Independent Investment Programme Advisory Group, TfL needs to take further steps to increase transparency and comparability within TfL. This includes: independent benchmarking; reformed project and risk management; and a revised approach to procurement, service standards and specifications; to secure safe and efficient world class operations, assets and services.

Recommendation 35

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