Report to:	Finance, Resources and Corporate Committee
Date:	12 July 2022
Subject:	**Inflationary pressures on Capital Programmes**
Director:	Melanie Corcoran, Director of Delivery
Author:	Dave Haskins, Head of Transport Implementation

Is this a key decision?	☐ Yes ☒ No
Is the decision eligible for call-in by Scrutiny?	☒ Yes ☐ No
Does the report contain confidential or exempt information or appendices?	☐ Yes ☒ No
If relevant, state paragraph number of Schedule 12A, Local Government Act 1972, Part 1:	
Are there implications for equality and diversity?	☐ Yes ☒ No

1. Purpose of this report

1.1 To report on the current position regarding escalating costs across the capital programme, which is most acute in the West Yorkshire plus Transport Fund (TF).

1.2 To provide information on the impact inflation is having on the delivery of the capital programme and consider options for how this could be managed.

2. Information

2.1. At its last meeting the Committee considered a paper outlining the potential risks due to the recent unexpected growth in inflation. The focus was on the impact on the revenue budget and work is continuing to understand the scale of expected additional costs and options to manage this.

2.2. The report highlighted that work was underway to understand the impact on the capital programme and this paper provides further information on that.

2.3. The infrastructure programmes delivered by West Yorkshire Combined Authority and the five partner councils include projects which are reporting cost increases as a result of increased inflation costs on construction materials. Scheme sponsors and contractors are reporting less control over their supply chain costs.

2.4. The programme most adversely affected is the West Yorkshire plus Transport Fund (TF), which commenced on 1 April 2015 and is now in its eighth year of operation, but we are now seeing inflation increases across other programmes too. In recent years inflation was averaging around 2% and therefore the recent rapid increase is putting pressure across the whole programme. This includes the Transforming Cities Fund (TCF) programme and the projects due to be funded from the City Region Sustainable Transport Settlement (CRSTS) programme as current inflation costs already exceed the 7% level budgeted for in the bid.

2.5. When the TCF Programme was developed in 2019 inflation costs were included at 3% in the original three year programme. The TCF programme is now being delivered over five years to deliver the higher scenario of schemes so inflationary impact is greater than anticipated at bid stage even without inflation running at current levels. A significant rise in construction inflation costs has taken inflation levels (ONS data from March 2021) to 7.3%.

2.6. Inflation is affecting economic regeneration programmes but to a lesser extent as the Brownfield Housing Fund is supporting schemes where market failure is evidenced and a fixed contribution to overall scheme costs are agreed. Therefore, inflation increases are dealt with purely by the sponsor.

2.7. Beyond inflation there are a number of other challenges having an impact on the original funding allocation given. Factors such as Covid, Brexit, the Ukraine crisis and a change in Government and local policy around road usage with more focus on sustainable transport, including public transport and active travel, resulting in re-design and a re-focus of schemes. These challenges have all contributed to the cost escalation of projects within our capital programmes.

West Yorkshire plus Transport Fund (WY+TF)

2.8. Planned over-programming on the WY+TF is currently £151 million and it is expected this will increase over the next year as schemes are reviewed and updated, as they move towards on-site delivery. There is pressure to reduce this over-programming to bring the Transport Fund back in line with the original allocation of £1 billion. In comparison the TCF programme is not currently over-programmed and had a programme risk pot to cover increases. The risk pot is now allocated in principle and working with scheme sponsors there may be emerging costs that could be unfunded. Therefore, it would be prudent to review the programme at this stage to ensure that it remains affordable within the funding allocated. The CRSTS programme is over-programmed by approx. £100m with 7% allocated to cover inflation costs.

2.9. Given that the WY+TF is more adversely affected, this section looks at the implications for this £1 billion programme which is funded as follows.

Funding Source	Funding £(m)
Transport Fund Gainshare (agreed as part of the Growth Deal)	600
Department of Transport - Majors	183
West Yorkshire Match Fund (borrowing funded through Transport Levy)	217
Total	**1,000**

2.10. The £151 million over-programming could potentially increase in the near future to £215 million due to the impact of current inflation rates. Currently we have £342m expenditure on schemes either delivered or currently in construction, development costs incurred of £75m and a further £62m of development costs approved. This gives total current commitment of £479m leaving a balance of £521m indicatively allocated but not yet with final approvals in place. The table below details current levels of expenditure on Transport Fund:

Schemes complete	£228m
Schemes on site	£113m
Approved costs on development	£136m
Total	**£479m**

2.11. A significant number of additional funding requests are starting to emerge on these projects, which cannot be accommodated within the overall funding allocation plus overprogramming. Sponsors have been supported to consider value engineering, de-scoping and re-designing within individual projects and individual programmes have been reviewed on an annual basis. It is difficult to reduce costs further without significantly affecting the outputs and outcomes of schemes and programmes. This position has been discussed with officer groups across West Yorkshire to understand options to respond to this.

2.12. There is additional pressure on the programme as the focus from Government has moved more towards sustainable active travel and bus priority. Some transport projects were designed prior to this shift and schemes require a review in terms of strategic fit.

2.13. The original WY+TF programme included 33 named projects each with an allocated sum of funding which totalled £1.27 billion based on prices in 2012. It consists of both individual projects and projects within operational/delivery programmes which include the Corridor Improvement Programme, Station Gateways Programme and the Rail Parking Package. The total number of projects in the programme has now increased to 114. This is as a result of the development of projects within operational programmes or individual projects that have been phased. A couple of new projects were also added in following a call for projects in 2017 (approved in 2018), these are the Leeds Inland Port (which is now unable to proceed) and City Connect Phase 3 (which is close to completion).

2.14. The ambition of local partners at the start of the WY+TF was to deliver the whole programme within 10 years (by 2025/26), even though the grant funding allocations will come in as £30 million each year until 2034/35, using the local contribution to balance cashflow and funding timing differences. Based on current project timescales the Transport Fund programme will be largely delivered by 2026/27.

2.15. An approach to managing cost increases on projects which are on site was approved at the Combined Authority meeting of 8 June 2021 WYCA - Modern Gov). An approach in relation to what criteria needs to be met such that exceptional circumstances should apply to be able to apply for additional funding through the CA assurance process was approved at Place, Regeneration and Housing Committee on 8 March 2022 WYCA - Modern Gov.

Options for Capital Programme Delivery

2.16. A number of options have been considered to respond to the emerging funding gap and it is likely that a blend of approaches will be needed to ensure the continuing focus on delivery. A review of existing projects is required that focuses not only on cost but that also considers any risks relating to deliverability and/or strategic fit, from which a range of approaches could be taken:

1. Continue as is / maintain status quo
2. Use gainshare or other funding to fund cost increases
3. Partners to deliver projects within their own funding allocation
4. Re-define projects to align with strategic objectives
5. Pause projects and add to pipeline for future funding opportunities/deliver over a longer timeframe as new funding becomes available, and return indicative funding to the programme
6. Stop projects and return indicative funding to the programme

2.17. The first option is to continue as is/maintain status quo and continue to push for value engineering, de-scoping and re-design. Many projects have already maximised their value engineering options. Similarly, any further de-scoping or re-design may result in projects that no longer meet the programme objectives and/or are no longer viable in terms of benefits.

2.18. A second option would be to apply gainshare to address overprogramming and inflation issues. This in the short term would address funding gaps but it would not be a longer-term option as inflation is likely to continue to increase which means project costs will continue to increase. The current capital allocation in gainshare has already been earmarked to funding the higher scenario TCF schemes. Similarly, it would not assist with addressing issues for the projects that are not affordable, have deliverability issues and may no longer have a strong strategic fit.

2.19. The third option is for all partners to take responsibility to deliver their programmes within their current nominal funding allocation. This would allow partners to prioritise their programmes and deliver those projects which are affordable and deliverable. However, we currently run our capital programmes as a strategic regional funding pot delivering schemes across the region, with the only exception to this being the partnership agreement we have with the City of York Council. If we changed to this approach this allows the districts to manage their programmes to deliver the most deliverable and affordable projects first, potentially prioritising these over the more high-risk projects and, instead of bringing maximum benefits to our region, districts may focus on ones that can be delivered rather than those that will bring maximum benefits but are more difficult to deliver. This is not a recommended option as members have previously indicated that the CA needs to ensure funding is treated as regional funding. Allowing districts to take control of their own expenditure, would inject risks to the current strategic West Yorkshire approach to identifying where the best interventions need to be made with the funding available.

2.20. A fourth option is to re-define projects to align with a sustainable transport focus. However, to consider this in isolation would likely lead to significant further design changes which would add in development costs and lengthen delivery timescales.

2.21. The fifth option is to pause projects that are at risk of not being delivered within reasonable timescales, have affordability issues or are not aligned with sustainability priorities. This option would prevent further costs being spent on development of projects which are high risk, allowing funding that has been indicatively allocated to return to the to reduce funding pressures overall. However, pausing them would ultimately lead to further delays on those projects. This approach would require a full review of infrastructure schemes across all capital programmes to finalise which projects are high risk and should/could be paused. Furthermore, these projects would stay in the programme subject to regular review to ensure they remain viable and deliverable strategically, financially, and timely. Projects could be moved to a pipeline project list to be delivered over a longer delivery period once funding becomes available and/or future funding opportunities arise.

2.22. A sixth option is to stop high risk projects which have affordability issues, deliverability issues or issues with strategic alignment. This would prevent further expenditure on development costs for these projects. It would also mean a faster option to reduce over-programming and inflation pressures This again would require a full review across funding programmes

Preferred Option

2.17. On balance it is proposed Option 5 (para 2.21) is recommended which is that projects which are high risk and cannot be delivered in the programme timescales/ realistic timescales or within the funding envelope are paused. This will stop further development costs being spent on projects that are considered high risk. This funding will be returned to the relevant programme funding pot. Work will continue with partners to define the criteria for high-risk schemes and undertake an evaluation of projects against these criteria over the summer. This would enable a decision to be made in the autumn to determine which projects are paused and for all partners to concentrate on delivering the more deliverable projects in the short term and deliver other schemes over longer delivery timeframes as future funding is secured. Similarly there may be a small number of schemes that have significant risk of not delivering within timescales and within budget and these schemes may be recommended to be stopped.

2.18. A collaborative approach is needed to understand which projects across the partner councils and the Combined Authority can be continued in current programmes, paused or stopped. This will affect all partners and Combined Authority sponsored schemes. If the proposed way forward is approved the review will be applied across the whole infrastructure portfolio and further work will be undertaken to understand the impact this would have on the projects to be delivered by each partner and each funding programme. Combined Authority and partner council officers will continue to work closely together to undertaken reviews over the summer, allowing proposals to be brought back to Combined Authority members in the autumn.

3. Tackling the Climate Emergency Implications

3.1 There are no climate emergency implications directly arising from this report.

4. Inclusive Growth Implications

4.1 There are no inclusive growth implications directly arising from this report.

5. Equality and Diversity Implications

5.1 There are no equality and diversity implications directly arising from this report.

6. Financial Implications

6.1 These are contained in the main body of the report.

7. Legal Implications

7.1 There are no legal implications directly arising from this report.

8. Staffing Implications

8.1 There are no staffing implications directly arising from this report.

9. External Consultees

9.1 No external consultations have been undertaken.

10. Recommendations

10.1 That the Committee agrees on the preferred way forward to address over-programming and rising inflation costs.

10.2 That the Committee agrees that some projects are at risk of not being delivered due to affordability, deliverability, or strategic alignment.

10.3 To hold review meetings with each partner to allow for a review of all schemes delivered by each partner across the portfolio.

10.4 That the Committee agrees that the scoring criteria for scoring projects is based on deliverability, affordability and strategic fit/ sustainable travel.

11. Background Documents

11.1 There are no background documents referenced in this report.

12. Appendices

None.