

## **Summary**

It is essential that the likely net cost of a proposal from the public sector's point of view is identified within the appraisal. This enables a comparison with the total benefits of the project in order to assess the overall value for money of the proposal.

Cost to Government refers to all costs incurred by the public sector as a whole, net of any revenues. The total net cost consists of investment costs, operating and maintenance costs, grant/subsidy payments, revenues, and taxation impacts.

Investment and maintenance costs are most likely to be relevant in the case of roads-related proposals, e.g. new roads and bus lanes. Costs and benefits incurred by the private sector should be covered under "Economy" rather than Cost to Government.

However, in many cases the revenues of private sector public transport operators are unlikely to cover the investment and operating costs of a proposal. As a result, some form of grant or subsidy may be required, and any such payments represent a cost to the Government.

Revenues are most likely to be relevant in the context of road user charging and parking strategies.

Some proposals, particularly those aimed at promoting modal shift, could have a significant impact on indirect tax receipts. These impacts represent costs to the Government and, where appropriate, the appraisal should assess the expected change in indirect tax revenue attributable to changes in the transport sector.

All costs and benefits should be adjusted for optimism bias and risk (see Chapter 12).

## **11. COST TO GOVERNMENT**

### **11.1 Introduction**

- 11.1.1 This chapter provides guidance on how to assess the net cost of a proposal from the public sector's point of view. This cost can then be compared with the total benefits of the proposal in terms of the environment, safety, economy, integration, and accessibility in order to assess overall value for money.
- 11.1.2 Cost to Government refers to all costs incurred by the public sector as a whole, net of any revenues. The total net cost consists of investment costs, operating and maintenance costs, grant/subsidy payments, revenues, and taxation impacts. In all instances costs presented should be adjusted for optimism bias (ref. Chapter 12).
- 11.1.3 Costs and revenues to private sector operators should be separately identified – see Chapter 8. If there is any ambiguity about whether a cost should be allocated to the public or the private sector (e.g. in the case of public-private partnerships), advice should be sought from the Executive.
- 11.1.4 In the AST, all impacts should be expressed both in terms of Present Values and in terms of annual costs at current prices – see Chapter 5 for more details.
- 11.1.5 As the unit of account for the AST is market prices, it may be necessary to adjust costs to reflect indirect taxes.

### **11.2 Investment Costs**

- 11.2.1 These should include all infrastructure and other capital costs incurred by public sector operators which are additional to those incurred in the do-minimum scenario. Given that most public transport services are provided by the private sector, this category of public sector cost will usually only be relevant in the case of new or improved roads and car parks. Grants to private sector operators are separately identified – see §11.4.
- 11.2.2 In addition to construction costs, fees, design, land acquisition and other preliminary works should be costed. Costs should be entered into the AST as negative amounts.

### **11.3 Operating & Maintenance Costs**

- 11.3.1 Operating and maintenance costs should include the annually recurring costs incurred by the public sector in running and maintaining the facility. Again, this is most likely to be a significant issue in the case of roads projects rather than public transport projects. Where new road capacity is provided, provision must be made for the additional maintenance costs of the infrastructure in comparison to the do-minimum scenario.

- 11.3.2 Public sector operating costs will not always be confined to roads proposals, however. For example, road user charging can involve significant operating and collection costs. Also, where options (e.g. new parking policies, road user charging, and bus lanes) include significant changes in the level of enforcement, these should be taken into account.
- 11.3.3 In the SPT area and, to a lesser extent, other areas the public sector may also be directly responsible for providing passenger information and other services and facilities, e.g. car parks. In such cases, additional costs will fall under public sector operating costs. However, these costs may be excluded from the appraisal if changes in costs are likely to be insignificant.
- 11.3.4 As for investment costs, operating costs should be recorded in the AST as negative amounts.

#### **11.4 Grant and Subsidy Payments**

- 11.4.1 In the majority of cases, private sector operator revenues are unlikely to cover the investment and operating costs of a proposal, and hence some form of grant or subsidy will be required to deliver actions by private sector operators (e.g. ScotRail, bus operators, etc). Any such grant represents a cost to the Government.
- 11.4.2 At the appraisal stage funding agencies are unlikely to be able to give commitments or to be precise about the amounts of support likely to be available. However, the deficit arising from private sector provision without the benefit of grant or subsidy will be indicative of the level of support likely to be required to deliver the strategy or project (although it should be noted that the private sector is likely to require an additional profit margin/return on capital). However, consideration should also be given to whether the level of grant or subsidy would be likely to meet the relevant decision criteria published by funding agencies.
- 11.4.3 In some cases, there may be a need to disaggregate the market into different operators in order to assess overall subsidy requirements. For example, a rail enhancement may lead to a loss of bus revenue but there will generally be no requirement to compensate the bus operator (though this should still be recorded as a disbenefit to bus operators).
- 11.4.4 Grant and subsidy payments are transfer payments, and hence the assumed level of subsidy provision should not affect the overall NPV of a proposal – it simply affects the distribution of costs and benefits between different parties. The figure recorded under Cost to Government should be equal to, but of opposite sign to, the figure recorded in the Grant/Subsidy section of Private Sector Operator Impacts in the Transport Economic Efficiency section of the AST.
- 11.4.5 However, the level of required subsidy will affect the Benefit:Cost to Government ratio. As the proposal progresses, it should be possible to refine assumptions about the required level of subsidy (e.g. based on actual tenders for providing the required service).

11.4.6 In some cases, it may be possible to identify potential developer contributions. In effect, these are 'negative grants'. Again, such contributions represent transfer payments and should be recorded both as a benefit to the public sector and a cost to the private sector (see Chapter 8).

## **11.5 Revenues**

11.5.1 Public sector revenues are most likely to be relevant in the case of road user charging and where a proposal would impact on parking revenues. Revenues are related to user charges, as user charges represent money transfers from users to the Government, although in many cases the revenues will subsequently be re-invested in the transport system.

## **11.6 Indirect Tax Revenue**

11.6.1 It has been noted by Sugden (1999) that strategies or plans which substantially promote public transport stand to cut HM Customs and Excise's indirect tax receipts by shifting expenditure from cars and car fuel, which are heavily taxed, to public transport services on which the indirect tax rate is extremely low. Similarly, a saving in fuel costs for drivers (e.g. due to a road improvement) will lead to loss of tax revenue to Government.

11.6.2 These impacts represent costs to the Government, and hence it may be necessary to assess the expected change in indirect tax revenue to the Government due to changes in the transport sector.

11.6.3 More detail on this issue can be found in GOMMMS Appendix F.

