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## Select Committee on Transport, Local Government and the Regions [Second Report](#)

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### VII. CONCLUSION

73. It is four years since the Government announced its intention to develop the PPP deal to modernise the Underground. Its development has taken an excessively long time and has distracted London Underground Limited from the business of running a quality Underground service. Continued under-funding and uncertainty in funding provision over this period has prevented London Underground Limited from reducing the maintenance backlog. A viable long-term solution for funding London Underground must be put in place immediately.

74. The PPP for the Underground is the most complex infrastructure PPP ever developed. The 'codification' of London Underground's operations has led to the development of a series of very complicated contracts. The funding structure is experimental. Given the strategic importance of London Underground, the decision to adopt such a structure constitutes a significant risk. We are not convinced that 'shadow running' provides a basis to understand how well the system will work under PPP. **We conclude that it is inevitable that the PPP will lead to significant and expensive disputes over the contracts and between staff and employers.**

75. The expected revenue stream from fares to pay for infrastructure improvements is significantly lower than when the PPP was proposed. The affordability of the various elements of the PPP deal has only been considered well after the financing mechanism for the deal was selected, contrary to the advice of the National Audit Office. Public subsidy constraints have pushed back the proposed capacity increase of 15 per cent for the network from Year 20 to Year 30 of the contract. The capacity improvements offered by the PPP will not even meet the demand forecast for the existing Underground network. That capacity constraint will have knock on-effects to London's competitiveness, other transport networks and land-use patterns, as well as the future revenue stream from the Underground. The failure of the proposed deal to provide adequate funds will not only affect the travelling public but will also lead to an erosion of value for money. **The Government must provide the funds to meet the target of a 15 per cent increase in capacity by Year 20 of the 30-year programme. The potentially vast cost to London and the nation's economy of failing to meet that target justifies a considerable increase in Government subsidy.**

76. The allocation of risk between parties is critical to the success of the PPP. As the Secretary of State acknowledged "There will be some people who would like the Government to take on the risk because they have a financial interest in getting us into that position."<sup>[172]</sup> The risk profile for the Underground is enormously complex and it is difficult to be confident that all of the risks can be identified and quantified. It is clear that the Government has retained significant amounts of risk and will ultimately retain the responsibility for ensuring the continued running of the Underground. **Our considerations above show that the shortage of funds has already constrained capacity improvements and it is likely, therefore, that risk transfer has also been limited. If little risk can be transferred to the private sector then the rationale for the PPP is seriously undermined.**

77. **A number of key factors in the assessment of value for money are subjective and difficult or impossible to quantify. There are clear differences in opinion between experts in the engineering, management and finance fields involved in**

**the process about these factors. There is also considerable risk that the cost of the project will be inflated after the first review period where prices are not fixed. This risk has been amplified by decisions to delay significant amounts of capital spending to these later periods when they will be more 'affordable'. We note that the Secretary of State accepted that it will not be possible to provide a definitive answer regarding the value for money of the bids and we therefore recommend that the Government does not approve the PPP deal.**

78. In December 2000 the National Audit Office asked London Underground Limited to consider the possibility of one or more bids failing the value for money test. Those options are only now being considered by the Government, a year later. Other options should have been developed earlier. Transport for London have proposed an alternative management plan; we have not been able to evaluate that plan in detail over the course of the inquiry. **We recommend that the Government should develop alternatives to the PPP in conjunction with the Mayor and Transport for London.**

79. It is imperative that a decision not to proceed with the PPP should not delay investment in the long-term needs of the Underground. We believe that experience gained from the PPP bid development and the expertise within London Underground Limited will enable such decisions to be taken whilst a new management plan is put in place. **Investment decisions to upgrade the network should be undertaken in parallel with the handover of the Underground to the Mayor.**

80. It is clear that past failings of London Underground Limited have been the result of funding uncertainty and a shortage of funds. Long-term secure funding is essential to modernise the Underground to produce a system capable of sustaining London's role as a world city. In recommending that the PPP deals are rejected, we are certain that any alternative management system must be guaranteed the necessary levels of funding over a long period, as is the case for other areas of transport through the 10 Year Plan. We note that London Underground Limited's chief reason for supporting the PPP is that it provides certain long-term funding. **We recommend that, whatever scheme is chosen, the Government provides the same type of long-term funding commitment to the Underground as was envisaged under the PPP.**

81. The surplus from the fare box is envisaged to contribute a significant proportion of the investment and maintenance requirements for the Underground under all of the options considered. That revenue has been declining since 1998 and there is now a deficit, principally due to rising operational costs. The Mayor stands to be responsible for any shortfall in the funding from this source. Such a shortfall could have serious consequences for other areas of London's transport budget. **It is essential that the Government and the Mayor of London revise their estimates of the contribution of fares to the investment programme. The Government must commit to funding any resultant financial shortfall and by doing so ensure that it neither compromises the investment plan nor creates pressure for above inflationary fare increases.**

82. The Committee notes the constructive relationship between Transport for London, the Government and the Strategic Rail Authority in planning and contracting a number of extensions and new rail projects outside of the PPP. Those new lines are an important part of London's Integrated Transport Strategy and are necessary to relieve pressure on the Underground network. **We welcome the Strategic Rail Authority's decision to fund completion of the East London Line extension by 2006. We recommend that the Government continues to support Cross Rail and the Hackney-SouthWest Line as part of the Mayor's transport strategy.**

83. If the Government decides to proceed with PPP it should take into account the following points:

- The timescale for auditing the operational implementation of Version 3.0 of the Safety Case and approving Version 3.1, barely one month, is too short to identify the full range of operational difficulties that might be encountered in practice. It is not clear that the interaction between the commercial elements of the PPP contracts and the implementation and profile of safety on the Underground has yet been given enough consideration. **We therefore recommend that the Health and Safety Executive give themselves more time to establish whether Version 3.0 of the Safety Case produces safe working practices, to allow operational difficulties to be more clearly identified, before considering approval of Version 3.1. We find it disgraceful that the Health and Safety Executive has only been given one month to reach such important conclusions.**
- Monitoring the safe performance of the Infracos is the responsibility of London Underground Limited. The costs of the monitoring process will be significant and it is not clear that London Underground Limited have enough staff to meet the increased work load that they will face. **We recommend that the Government fund the increased monitoring costs to ensure that the public sector has sufficient control over safety and performance monitoring of the Infraco operations.**
- We are concerned that the register of assets against which the future costs of the improvements to the Underground have been estimated is insufficiently developed and incomplete. Despite improvements in the maintenance of an asset register we consider that London Underground Limited will be subject to cost inflations after the first review period if conditions are worse than currently understood. The existence of 'grey assets' about which little is known is unacceptable. **The establishment and maintenance of a complete register of all assets is a priority for the Underground network and should have preceded the PPP contract negotiations.**
- We remain unconvinced that the arbiter will have sufficient powers to prevent the

incumbent infrastructure companies pressing for more favourable terms at the seven and a half year reviews. **We recommend that the arbiter's office be established early in the PPP contract and well resourced to ensure that the dispute resolution mechanism is genuinely independent of the parties involved.**

- We are concerned that the division of the network will lead to different operational practice, and training, which may make future unified control of the network more difficult. **We recommend that London Underground and the Infracos enter into an agreement to develop combined training programmes to minimise the potential divergence of working practices and standards.**
- Managing, monitoring and implementing the PPP will require a significant increase in the number of skilled staff available in both the public and private sector companies. We are concerned that there is a shortage of such skills for both the Underground and mainline networks and that the uncertainty in both areas is leading to a flow of skills out of the sector. **We recommend that London Underground and the Infracos work closely with the trade unions and professional institutions and the Strategic Rail Authority to develop a National Rail Academy.**
- The improvements in the Underground will take a number of years to come on stream and during this time there will be considerable disruption. The upgrading of the Underground will require close co-ordination and co-operation between the maintenance and operational elements of the Underground network and the bus network. **We recommend that Transport for London be given lead responsibility for the co-ordination of major upgrades on the Underground to reduce disruption to the travelling public.**

84. Insufficient attention has been given to the development of a hybrid structure of mixed private and public sector Infraco management should one or two of the bids fail the value for money test. A mixture of public and private sector Infracos will add further complexity to the management of the network. By definition, those Infracos that fail a value for money test will be the highest risk concessions. Those are the ones that the public sector will take on. Retaining one Infraco in the public sector may not enable the full range of benefits of unified public sector control to be delivered and therefore prove an unsatisfactory half-way house solution. **We recommend that the Government should not pursue a mixture of public and private Infraco operations if one of the bids fails. The benefits of retaining all of the three Infrastructure companies in the public sector as a single integrated operation must be re-examined.**

85. The Committee has identified several features of the development of the PPP deal which should be addressed in future public private financing assessments.

- **The initial forecasts that the PPP would provide a saving of £4.5 billion over public sector management were inadequate and flawed.** A more thorough analysis of the alternative options should have been undertaken at an earlier stage. The linkage between the financing of the scheme, the requirements of the Underground network and public sector affordability have been ambiguous. The Committee is concerned that in developing the PPP deal the Government decided first how the Underground should be financed and then addressed what could be afforded. The miscalculation of the contribution of fare box surplus to the investment programme has particularly served to highlight these shortcomings. **The Government should follow the National Audit Office's advice to address the affordability and funding provision for infrastructure projects before deciding on the financing mechanism.**
- **The bidding process has been hugely disruptive to operations and staff morale.** We are concerned that matters such as the upgrade of engineering standards (costing between £5 million and £10 million) were delayed due to financial restrictions when £100 million has been spent on consultants' fees to develop the PPP deal.
- The PPP has provoked widespread public debate. The Committee deprecates the level of information provided about the nature of the PPP contracts throughout the process. We welcome the Secretary of State's decision to provide the public with some of the

details that will inform this important decision. **Greater effort must be made to divulge those elements of such contracts that do not directly affect the Government's negotiating position to the public at an earlier stage.**

86. A principal cause of the atrocious state of the London Underground has been the failure of the Treasury to provide adequate long-term funding over a number of decades. The Treasury is also, according to the evidence we received, one of the principal instigators of the PPP scheme. We were therefore appalled that despite its leading role it refused to make itself accountable to Parliament by giving evidence to the Sub-Committee during the inquiry. That refusal threatens to undermine the Departmental Select Committee system. Those Ministers who make decisions must be accountable to Parliament for them.

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