Cynulliad Cenedlaethol Cymru
Y Pwyllgor Cyllid
National Assembly for Wales
Finance Committee

Ymchwiliad i ffynonellau cyllid cyfalaf Llywodraeth Cymru
Ymatebion i'r Ymgynghoriad

Inquiry into the Welsh Government's capital funding sources
Consultation Responses

Mai 2019
May 2019

*Ar gael yn Gymraeg /Available in Welsh

CFS 01	Tirion Group	Tirion Group
CFS 02*	Archwilydd Cyffredinol Cymru	Auditor General for Wales
CFS 03	Banc Datblygu Cymru	Development Bank of Wales
CFS 04	Scottish Futures Trust	Scottish Futures Trust
CFS 05	Gerald Holtham	Gerald Holtham
CFS 06	KPMG	KPMG
CFS 07	Capital Law	Capital Law

David Ward
CEO Tirion Group Ltd
Written Evidence to Welsh Government Finance Committee: 23rd April, 2019

Developing Effective Funding Models for Mixed Tenure Housing

1.0 Scope of Evidence

This evidence has been restricted to consideration of Welsh Government's role in helping non-regulated "not for profit" housing providers to access Institutional Finance to support mixed tenure housing provision as part of a more comprehensive strategy to stimulate housing provision. The proposed interventions would not just be applicable to such organisations but could also facilitate increased delivery by the Registered Social Landlord (RSL) sector.

The evidence does not cover the following aspects although I would be happy to discuss these matters as part of the oral session:

- The Registered Social Landlord sector and the role of equitization in facilitating increased scale of delivery; and
- The role of loan and grant finance to support the SME housebuilder sector in provision of open market homes for sale.

2.0 Institutional finance "the opportunity"

2.1 Institutional investors are seeking long-term, index-linked cash flows to match their long-term annuity obligations. Housing currently represents just 1% of UK institutional fund investment compared to 47% in the Netherlands, 15% in France and 13% in Germany. Pension funds are now actively seeking long-term investment alternatives to gilts to improve their returns. RSLs and not-for-profit providers like Tirion are attempting to secure long-term finance no longer readily accessible from the traditional banking sector to support delivery of mixed-tenure housing. Tirion believes that this type of facility, which matches income streams, provides a natural hedge and should form part of a portfolio of loans.

2.2 Typically, institutional investors are offering 20-50 year debt, at highly attractive investment yields, which can significantly reduce the cost of development finance reducing or negating the need for public sector subsidy. In some cases, investors have launched their own vehicles and are looking to acquire housing assets to hold on a long-term basis.

2.3 Institutional investors offer particularly attractive yields for affordable housing due to historically low void rates and this reduces the viability gap between affordable and market housing.

2.4 The potential scale of investment should not be under-estimated. Tirion Group alone is targeting institutional investment of £350 million in Wales and typically individual funds have allocated investment of at least £1bn for housing assets in the UK. L&G are believed to have allocated up to £10bn for investment in affordable housing in the future.

3.0 Barriers to Securing Investment

3.1 Whilst the opportunity to tap into Institutional appetite for residential assets is enormous, it remains a fact that in most cases the funds wish to invest in completed / existing assets. Forward funding for pre-construction and construction activities remains very rare.

3.2 This dis-connect between the development process and long-term investment is further exacerbated by the required lot sizes, at which, most investors wish to transact. In many cases the institutions require investment lot values of between £30 and £50m. This means that additional “warehouse” finance is required so that portfolios can be built to reach this critical mass. Tirion is fortunate in that it’s investor is prepared to transact on our units at a much lower value of circa £15m and there are signs that the wider Institutional market is moving in this direction in recognition of the specific characteristics of the residential sector i.e. portfolios made up of small individual units each with their own value.

3.3 The consequence of this dis-connect is that there is a shortage of assets in which institutions can invest. Even where units are being constructed they are not available in sufficient lot value size. This is partly due to much more stringent regulation of the traditional banking sector following the 2008 global financial crisis and consequently greatly reduced appetite to provide development finance. This is further exacerbated by the current practise of valuing assets according to an RICS red book procedure which results in a significantly lower value than that which institutions are prepared to lend against. This further constrains the level of funding Banks can offer for the pre-construction, construction and warehouse phases of large residential projects.

3.4 This has created a vicious circle of dis-connected flows of finance, i.e. the link between development finance, warehouse finance and the long-term debt being offered by the Institutions, that Welsh Government financial interventions should seek to address.

4.0 The Role of WG

4.1 Fiscal restraint will continue to restrict the availability of Social Housing Grant in the medium to long term. However, it is also true that during this period the shortage of all types of housing tenure will grow. It seems sensible that SHG going forward should target the Social Rented Sector and therefore those most in need. It is also clear that Social Rented housing is unlikely to be viable without grant, or without cross-subsidy, in most housing markets in Wales.

4.2 The Planning system seeks to deliver community benefits including social rented housing via the s106 and CIL systems. Values in most parts of Wales do not support sufficient investment in community facilities and the social rented sector. In these circumstances WG interventions should focus on delivering a mixed tenure approach, with the possibility of cross funding (at least in part) the social rented sector on all large-scale projects in Wales. This requires mechanisms that remove elements of financial risk associated with pre-construction, construction and warehouse phases of large developments. In the majority of cases this could be achieved directly through loan finance and in some cases this could be coupled with grant to deal with abnormally high site preparation costs.

4.3 The most effective method in terms of levering private investment in mixed-tenure housing is for WG to take subordinate positions in providing a proportion of debt during the pre-construction, construction and warehouse phases of projects.

5.0 Developing an Effective Model Using Existing Finance

5.1 The effective deployment of Financial Transaction Revenue would appear to offer the best opportunity to support mixed-tenure housing development in the short to medium term. It also offers the best opportunity to minimise financial risk to the public sector. Examples of how FTR loan finance could be deployed include:

- Pre-construction – 100% loans for design, planning and statutory consents – loans would be repayable at the point that construction finance is secured;
- Site preparation works – 100% for site remediation and preparation – generally repayable at the point that construction finance is secured. Where sites are in public ownership, the loan would not be repayable if, for whatever reason the project does not proceed. This is on the basis that the works would have added the equivalent value to those sites that remain in public ownership;
- Construction phase – Up to 30% loan against development costs – loan to be subordinated to senior lender – loan to be repaid at the point warehouse finance is secured; and
- Warehouse phase – Up to 30% loan against warehouse finance costs – loan to be subordinated to senior lender - loan either to be repaid at the end of the construction phase on drawdown of institutional debt or long-term quasi-equity position taken against the loan to provide long-term revenue stream or dividends.

5.2 It should be possible to provide a rolling loan facility for housing providers to reduce the peak debt of any single organisation at the relevant stages of the development process.

5.3 Using the principles set out above it will also be possible to integrate the de-carbonisation of new development into loan programmes. The investment profile for energy investors closely matches that of institutional investment in housing being long-dated with low yields. Tirion are at the forefront of proving the commercialisation of this approach with our partners Pobl and Sero Energy with Innovative Housing Programme grant support our development at Parc Eirin in Tonyrefail.

6.0 Quantifying the Risk

6.1 Adopting a strategy that is predicated either on 100% debt or sub-ordinated debt structure comes with financial risk. However, containing risk should be relatively straightforward particularly if the debt provider (WG or other public sector organisation can adopt a long-term position on the value of assets if necessary). A broad-brush assessment of the risk context is as follows:

- Pre-construction – 100% loan – inherently the greatest risk but with the lowest financial impact – risk mitigated where the site has an Local Development Plan allocation or even better an Outline Planning Consent.

- Site preparation works – 100% loan – where the site is in public ownership it can be argued there is no risk as the works are directly adding to the value of the site. Where the site is in private ownership a legal charge can be placed on the land. The risk here is if the end value of the site remains lower than the loan offered.
- Construction phase – Up to 30% junior loan against development costs – this carries the greatest risk in the development phase due to potential for cost overruns and depreciation of values during the construction phase but still significantly lower than current average grant levels.
- Warehouse phase – Up to 30% junior loan against warehouse finance costs – relatively low risk as debt against completed units.

7.0 The Future – WG Equity Investment?

7.1 Deploying the above loan mechanisms will result in significant increases in the delivery of mixed-tenure housing on large regeneration sites. We can envisage a situation where selling land to housebuilders as part of the development strategy for large sites would cross-subsidise the provision of homes for affordable homes. However, it is unlikely to negate the need for Social Housing Grant to deliver large numbers of homes for Social Rent across Wales.

7.2 In these circumstances Welsh Government should consider its role in providing equity for both not-for- profit housing providers (e.g. Tirion) and RSLs. This could operate on the following basis:

- SHG is replaced with time-limited WG equity investment, to fund new homes for social rent via a financial transaction;
- The WG equity share would be according to need i.e. the discount required to achieve social rent levels;
- WG would forgo the return on its equity share, with the housing provider charging a maximum market rent on its share, giving a genuinely affordable submarket rent level overall; and
- The housing provider would repay WG its equity stake within a 20-year period through the re-financing of the debt against the growth in value of the assets. Alternatively, at the point the rental cashflows are providing enough surplus WG could take a slice of long-term rental income.

7.3 The risk associated with this structure is that property and rental values fall over the 20-year deferred period. This is highly unlikely.

8.0 Conclusion

8.1 There is a huge opportunity to tap into Institutional Investors' appetite for residential assets. Existing funding instruments can be better utilised to help housing providers access this investment through existing vehicles, such as Tirion Homes and RSLs, and new partnerships formed with local authorities and other public sector landowners playing a major role.

8.2 The proposal for a new Housing Land Authority could also play a pivotal role in managing the supply of development land.

8.3 There is an excellent opportunity to integrate the de-carbonisation of new development into the loan programmes, providing household cost benefits to tenants, improving the viability of projects and reducing the carbon impact of new housing.

8.4 The key conclusion is that increasing capital investment in housing, and particularly affordable housing, is not about seeking new sources of finance but rather creating mechanisms that allow existing forms of finance to join up through the public sector taking an element of acceptable risk in the development process.

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Dear Llyr

Finance Committee inquiry – Welsh Government capital funding sources

To assist the Finance Committee in its inquiry into Welsh Government capital funding sources, I am pleased to provide written evidence to the Committee. The enclosed paper has been prepared on my behalf by staff of the Wales Audit Office.

The paper summarises evidence that may be of interest to the Committee arising from previously published Wales Audit Office material. It also provides signposts to some highly relevant work already published, or currently being undertaken, by other organisations including Audit Scotland and the National Audit Office.

As experience in Wales and elsewhere shows, all public-private finance programmes carry the challenge of balancing good value for money for the public sector with providing enough incentives to make the model attractive for private investment.

I am aware that the Committee has a particular interest in the Welsh Government's new Mutual Investment Model. In that regard, we are planning to undertake some follow-up audit work on the 21st Century Schools programme once Band B is further progressed, and so this is likely to take place in 2021-22. In undertaking that work we would expect to consider the extent to which, and how, the Mutual Investment Model has been applied in practice.

More generally, there is an extensive body of previous audit work (most notably by the National Audit Office) which highlights some of the potential challenges and pitfalls presented by alternative capital funding models. The lessons of experience show that when it comes to securing value-for-money, the devil is in the detail of how relevant contracts for projects are established and managed.

The balance of risk transfer is particularly important and it is vital that officials have a good grasp of this – not only in understanding the position at the outset of a long-term contract, but also as that balance of risk sharing evolves during the life of the contract. Too often in the past, the public sector has found to its cost that risks supposedly transferred at the outset to an external funder or contractor in fact reverted back to the taxpayer when a project later ran into significant difficulties. Ensuring that contractual provisions are sufficiently watertight to stand up to challenge when those risks materialise has also often proven to be problematic.

I and my colleagues stand ready to continue to support the Committee in its inquiry, and I hope that this written evidence is of assistance to you.

Yours sincerely

ADRIAN CROMPTON
Auditor General for Wales

Enc: Finance Committee inquiry: Welsh Government Capital Funding Sources paper

WALES AUDIT OFFICE
SWYDDFA ARCHWILIO CYMRU

Date issued: 23 April 2019

Finance Committee inquiry

Welsh Government Capital Funding Sources

Introduction

1 In the context of the terms of reference for its inquiry, this paper highlights evidence that may be of interest to the Committee arising from published Wales Audit Office material. It also signposts to some relevant work published or being undertaken by other organisations. In addition, we are aware that Audit Scotland has an audit underway looking at revenue financing of assets, specifically the Non-Profit Distributing and Hub models. Details about the plans and timing for this work are available on the Audit Scotland website.

2 Our work in auditing public bodies' financial statements would seek to ensure that different capital funding arrangements are properly accounted for, with appropriate disclosures of assets, liabilities and contingencies so that their annual accounts give a 'true and fair view'. Nevertheless, our audit coverage of the practical application of different funding models has, to date, been limited. This is because some of these models (including the Mutual Investment Model) are new/emerging, and the fact that Wales has only made very limited use of the Public Finance Initiative (PFI) and Public Private Partnership (PPP) models that have been widely deployed in England.

3 In July 2018, we published our Guide to Welsh Public Finances. That guide set out the main sources of funding for public services in Wales and described the processes for making budget decisions across the main devolved public bodies in Wales. It also looked at some of the key factors that public bodies consider in setting their financial plans.

4 The guide referenced the July 2012 report by the Finance Committee in the fourth Assembly on Borrowing Powers and Innovative Approaches to Capital Funding[1]. While the landscape has moved on, that report and much of the evidence that Committee received does remain relevant in the context of this latest inquiry. Indeed, our understanding is that the Mutual Investment Model has itself arisen from work that the Welsh Government undertook to consider models for revenue financing infrastructure investment in response to one of that Committee's recommendations, including the Non-Profit Distributing model which was launched by the Scottish Government in 2007. Our October 2011 Picture of Public Services report had noted that non-profit distributing was one of a number of

[1] The Finance Committee in the third Assembly had also reported in September 2008 on its Inquiry into Public Private Partnerships.

potential sources of funding for investing in infrastructure in the context of cuts to capital funding.

5 The 2012 Finance Committee report also recognised that underpinning the consideration and application of any capital funding models is a need to ensure that there is robust asset management across the public sector, supported by the development of relevant skills and capabilities.

The Mutual Investment Model and the 21st Century Schools and Education Programme

6 In May 2017, we published our report on the 21st Century Schools and Education Programme. We noted the planned use of the Mutual Investment Model to design, build, finance and manage new-build schools[2]. At the time of our report, the Welsh Government had not confirmed its funding plans and the appetite of local authorities to adopt the Model remained unclear. However, many councils told us that they were struggling to find the funding to continue to invest in schools. Councils had already significantly increased their borrowing and sold off assets to fund their contribution to Band A of the programme.

7 Our report noted that new governance arrangements, particularly around the public-private Mutual Investment Model, would be required for Band B. We noted that the Welsh Government would need to provide central support for the procurement process for any private finance for the programme and be able to ensure that the programme aligns with other programmes funded through the Mutual Investment Model as well as the Welsh Government's wider private finance initiatives.

8 Our report acknowledged that several important areas of difference between the Mutual Investment Model and the Private Finance Initiative, which the Welsh Government intends will promote the public interest, increase transparency, and enhance value for money. We understand that the Committee has already received a technical briefing on the Model, but we had outlined these differences at the time of our report as follows:

- the Welsh Government is able to invest in the company that is created to design, build, finance and maintain the asset. This ensures that the public sector has a share in profits of the project company;
- the Welsh Government is able to appoint a director to the Board of the company formed to deliver the project giving greater say and visibility on decision-making; and
- the service payment will be made by a monthly revenue charge over a 25-year period and will not start until the facilities are built and ready for use.

9 We made clear in our report that introducing a form of public-private finance will necessarily carry new risks for the programme which the Welsh Government will need to

[2] We also noted that the Welsh Government had initially intended to adopt the Non-Profit Distributing Model used by the Scottish Government but that that model had faced challenges following an Office of National Statistics ruling that some of the projects funded through the model could not be counted as off-balance sheet.

manage carefully as it moves into Band B. We considered that the Model was unlikely to be suitable for all projects in the programme, including refurbishments or bespoke projects, those likely to result in long and complex consultations, where there are complex land ownership issues or if there is a doubt about the long-term demand for places. It was also not clear to us if voluntary aided schools could participate in a revenue funded programme. And, as experience in Wales and elsewhere shows, all public-private finance programmes carry the challenge of balancing good value for money for the public sector with providing enough incentives to make the model attractive for private investment. We also noted that the Model would require some changes to the approach to procurement which may not be popular, or even feasible, for some councils.

10 We have supported the Public Accounts Committee (PAC) in its consideration of matters arising from our report in, and since, mid-2018. In written evidence following an oral evidence session on 25 June 2018, the Welsh Government provided further commentary on issues raised by the Committee in respect of the Mutual Investment Model, including the safeguards that would be in place to ensure high quality building standards for school buildings in light of issues that had arisen in Scotland.

11 The PAC then wrote to the Welsh Government, noting that it had concerns about whether the Mutual Investment Model represented the best value in the round. The PAC highlighted that oral evidence from both Colegau Cymru and the WLGA suggested that the Model was not ideal and that they would prefer other options. However, some later written evidence from the WLGA did acknowledge the Model's potential benefits. The PAC also sought re-assurance on various other issues, including some specific to the Model:

- That alternative options – capital and supported borrowing – had been fully exhausted.
- That the Welsh Government, as a whole, had identified that the school building programme is the most appropriate programme for using the Model.
- That there is an appropriate 'pause and review' moment to reflect in the round as to whether the Model is a good value-for-money method for building schools and colleges.

12 In addition, the WLGA had suggested that Mutual Investment Model contracts would look to transfer risks associated with the energy efficiency of the design of buildings to the private sector. The PAC therefore asked the Welsh Government to clarify how it expects that risk transfer to work.

13 The Welsh Government responded to those concerns in written evidence in August 2018 and provided a further written update in late February 2019. The February 2019 update outlined changes to the intervention rates for projects supported by the Model and otherwise. Those changes have closed the gap between the intervention rates for different

projects, which may have a bearing on the appetite of local authorities and further education institutions for the Model[3].

14 The Committee may wish to explore matters arising from the Welsh Government's written evidence to the PAC as part of its inquiry. We are planning to undertake some follow-up work on the 21st century schools and education programme once Band B is further progressed, but this may not be until 2021-22. We would expect to consider the extent to which, and how, the Mutual Investment Model has been applied in practice as part of that work.

The Mutual Investment Model - road projects and the Velindre Cancer Centre

15 We have noted the October 2018 report by the Economy, Infrastructure and Skills Committee on The State of Roads in Wales and its commentary and recommendations on the Mutual Investment Model. We are aware of the Welsh Government's plans to use the Model for sections 5 and 6 of the A465 scheme (Dowlais Top to Hirwaun). We have been looking into the A465 project recently because of the cost and time overruns on section 2 of the scheme (Gilwern to Brynmawr). We do not have any current plans for value-for-money work on the remaining sections of the scheme.

16 In respect of the Velindre Cancer Centre project (where construction work is yet to commence on site), we are currently liaising with finance officers at Velindre NHS Trust to understand how the Mutual Investment Model for the new hospital is intended to work and we will need to confirm the accounting arrangements in due course. However, we do not have any current plans for value-for-money work on the project.

Other recent audit evidence that may be relevant when considering capital funding sources

17 Our work on waste management in Wales has highlighted the example of the private finance initiative arrangements entered into by Wrexham County Borough Council. Our October 2018 report on Procuring Residual and Food Waste Treatment Capacity noted that the Council had not participated in the Welsh Government's Waste Infrastructure Procurement Programme. While we did not examine the detail of the Council's arrangements, our report noted that the Private Finance Initiative arrangements included provision of a Mechanical Biological Treatment facility for residual waste with a capacity of 55,000 tonnes per year. The facility started to operate and to take the Council's waste in July 2015, and the contract will expire in March 2038. We noted that the gate fees for

[3] An increase from 50% to 65% for all capital funded mainstream school and college projects; an increase from 50% to 75% for capital funded special schools and pupil referral units; an increase from 75% to 81% for Mutual Investment Model projects.

Wrexham's residual waste treatment facility are more than double the median cost of the residual waste projects under the Waste Infrastructure Procurement Programme[4].

18 More generally, the Committee may be interested in the contractual arrangements put in place through the Waste Infrastructure Procurement Programme. We noted that six of the ten projects under the Programme were for service contracts for waste treatment capacity where private sector providers have built facilities at their own cost and risk (albeit that the long-term service contract commitments from local authorities may have given them the confidence to do so). The remaining four projects (three food waste and one residual waste) included the construction of a facility, paid for in part by the local authority partners over the course of the contract as part of the gate fees. In those four cases, the facility will revert to local authority ownership at the end of the contract. The Welsh Government provided capital contributions totalling £3.5 million for the three food waste projects. We made a recommendation in our report about the provision of ongoing contract management support for local authorities.

19 Our July 2016 report on Coastal Flood and Erosion Risk Management in Wales noted that the Welsh Government had identified additional funding for coastal protection – by developing the 2018-2021 Coastal Risk Management Programme – but had not developed a long-term funding strategy beyond 2020-21 or helped councils to secure options for external funding, including for example levies and partnership funding with, for example, private sector organisations that stood to benefit from schemes. We noted that some stakeholders had raised concerns that the Welsh Government had not explored all of the options available to fund coastal flood risk management. Among other things, we recommended that the Welsh Government should develop a strategy to identify long-term funding for coastal protection including funding from across government departments and external bodies, and particularly to deliver multiple benefits. We suggested that the Welsh Government should learn from the partnership funding model in England to understand how councils there had been able to attract external funding for projects.

Other general reflections

20 As the Finance Committee in the fourth Assembly touched upon in its report, it is important that decisions about funding models are underpinned by robust asset management arrangements. We have noted examples of improvements in public bodies' capital planning in some of our recent work, for example in our July 2017 report on the Implementation of the NHS Finances (Wales) Act 2014. Nevertheless, public bodies, including NHS Wales, still need to do more to plan for the long-term and we have also highlighted in previous work the limitations arising from the Welsh Government's own financial planning horizons. The work of the new National Infrastructure Commission for

[4] Our November 2018 report on Municipal Recycling also noted that the Private Finance Initiative contract was a factor in the relatively high costs reported by the Council for kerbside collection of dry recyclables and its overall household waste services.

Wales, launched by the Welsh Government in November 2018, will also now be a crucial part of the process of identifying and planning for Wales' future infrastructure needs.

21 Our report on the 21st century schools and education programme provides an example of the potential benefits of a long-term approach to capital funding. We found that the certainty of funding over multiple years enabled councils to move away from a short-term 'patch and mend' approach to a more strategic approach to renewing and upgrading their school estates.

22 While there are specific considerations in Wales, not least because of the Well-being of Future Generations (Wales) Act, some of the general principles of effective capital strategies and programming are already set out in guidance from other professional bodies. For example, the Chartered Institute of Public Finance and Accountancy has produced guidance material on capital strategies and programming.

23 The Finance Committee in the fourth Assembly also touched on the question of whether public bodies have the right capacity/capability to consider and exploit the opportunities provided by an increasingly diverse range of funding models, including City/Growth Deal funding. As shown in a related context through our work on Public Procurement in Wales, concerns about capacity/capability across the public sector are, if anything, even more of an issue now as austerity has continued to bite.

24 Whatever capital funding models are deployed, the lessons of experience here and elsewhere show that when it comes to securing value-for-money, the devil is in the detail of how relevant contracts for projects are established and managed. These issues are picked up in some of the evidence that the Economy, Infrastructure and Skills Committee received during its inquiry on the state of roads and by the conclusions and recommendations in its report. The balance of risk transfer is particularly important, as well as ensuring that contractual provisions are sufficiently watertight to stand up to challenge when those risks materialise.

25 Whilst written in the context of their experience of auditing Private Finance Initiative projects, many of the principles that the National Audit Office (NAO) set out in its 2006 framework documents[5] would also appear relevant in more general terms when considering choices about funding models and the practicalities of project delivery. In 2015 the NAO issued a briefing paper: 'The choice of finance for capital investment', which provides a helpful overview of the topic. More recently, the NAO has also published a briefing on the rationale, costs and benefits of PFI; its use and impact; the ability to make savings from operational contracts; and the introduction of PF2.

26 Finally, the Committee may be interested to know that we will be taking forward local audit work across all local authorities on the topic of financial sustainability. Our work will examine medium- and longer-term financial strategy, budget management, cost pressures,

[5] In May 2006, the National Audit Office published Volume 1 and Volume 2 of its 'Framework for evaluating the implementation of Private Finance Initiative projects'.

efficiency and savings plans, and levels and use of reserves. We anticipate reporting the findings from that work in some way at a national level once the local audit work is completed.

Wales Audit Office

April 2019

ENDS

BANC DATBLYGU CYMRU
DEVELOPMENT BANK OF WALES

Development Bank of Wales's response to the Finance Committee inquiry into the Welsh Government's capital funding sources.

1. The Development Bank of Wales's mission is to unlock potential in the economy of Wales by increasing the provision of sustainable, effective finance in the market.
2. Development Bank of Wales supports Welsh businesses with Loans from £1,000 to £5million to start, strengthen or grow and Equity investment from £5,000 to £5million for established businesses. In recent years funds have been created to provide patient capital with loan terms up to 15 years.
3. In addition the Development Bank of Wales provides seed finance for pre-revenue tech start-ups and property development loans. It often co-invests alongside banks, crowd funders, grant providers, investors and other lenders. The 'gap funding' model means the Development Bank of Wales can work alongside other investors to make a deal happen by co-financing the element of the deal which is unattractive to the private sector due to the risk or lack of security.
4. With the exception of £10m funding from Clwyd Pension Fund, the Development Bank of Wales invests Welsh Government finance through a number of funds targeted at Welsh small to medium sized enterprises (SME). This is in the form of Welsh Government Core Capital, Financial Transaction Capital and the European Regional Development Fund (ERDF).
5. Historically a number of the funds managed by the Development Bank of Wales' predecessor, Finance Wales, were financed by loans from UK Banks and the European Investment Bank. This is no longer the case due to limitations on Government borrowing.

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6. As finances come under increasing pressure it is important that wider funding sources from the private sector, pension funds and other players in Wales, including Local Government and the Social Sector, are considered. The Development Bank of Wales stands in a good place to work with multiple stakeholders to devise funding mechanisms that are co-ordinated and complementary to drive maximum impact for the Welsh pound.

Conventional Funding (including Financial Transaction Capital)

Welsh Government Core Capital

7. Very few Development Bank of Wales funds are financed using Core Capital. This is due to two factors. First is the reduction in availability of core capital resulting from UK level real term cuts to the Welsh Government block grant and the increased costs of delivering capital projects. The other main driver is the increase in availability of Financial Transaction Capital (FTC) in recent years. A percentage of FTC has to be repaid to HM Treasury so must be invested in projects or funds that can generate a financial return. The Development Bank of Wales is a natural choice for deploying FTC.

8. Traditionally the choice of whether to deploy grant or repayable finance has been a binary decision. However there are many instances where projects can become viable with only a small element of grant alongside access to commercial finance.

9. In recent years three funds have been created (the £40m Wales Stalled Sites Fund, £50m Wales Tourism Fund and £55m Wales Commercial Property Fund) which consist of Welsh Government core funding which is used to finance a Welsh Government managed grant element alongside FTC which is deployed as commercial finance by the Development Bank of Wales. For the three funds a total of £33m core capital (WG grant) will drive an initial investment of £145m in Welsh businesses. The impacts are further increased for funds like the Wales Stalled Sites Fund which, on its own, will be recycled to make up to £200m of investments through its life.

10. Returns made on Core Capital can be used by the Development Bank of Wales to recycle and reinvest or seed successor funds.

11. Recycling of funds can also dramatically increase the impact of the initial investment. A good example was the £10m Wales Property Development Fund launched in 2013, using Core Capital, which invested over £34million during its life and is on track to repay the Welsh Government its initial stake of £10m. Its successor fund, the £30million Wales Property Fund is, through recycling, forecast to invest up to £272million.

European Regional Investment Funds (ERDF)

12. One of the largest forms of funding for the Development Bank of Wales has been the EU financed ERDF. This is very similar to Welsh Government Core Capital in that it allows the Development Bank of Wales to create a legacy through returns which can be re invested in Welsh businesses.

13. It is estimated that £60m of legacy will be created by the Wales JEREMIE Fund and around £130m from the current fund; the Wales Business Fund. If these funds were to be followed by similar finance through the UK Shared Prosperity Fund, the Development Bank of Wales could build up sufficient reserves to become fully sustainable in its core mission to provide access to finance to Welsh SMEs.

Financial Transaction Capital (FTC)

14. The majority of new Funds created by the Development Bank of Wales have been financed using Financial Transaction Capital (FTC). To date the total FTC allocation to the Development Bank of Wales, including Help to Buy - Wales, totals around £820 million; this represents 80% of the total FTC which has been allocated to the Welsh Government.

15. The Development Bank of Wales is working closely across Government Departments to understand their challenges and help to develop products and services that will help them to deliver their programme for Government objectives.

Government Loans (including borrowing limits)

16. The recent increase in borrowing limits by Welsh Government is welcomed in the light of budgetary constraints. In its first eight years the predecessor to the Development Bank of Wales, Finance Wales, was mainly funded through borrowings. It cannot borrow now due to the restrictions on Government borrowing and there are no current plans to allot any of the Welsh Government's borrowing powers to finance funds operated by the Development Bank of Wales.

17. FTC is however a more cost effective means of financing certain funds managed by the Development Bank of Wales. If at some stage FTC were to be withdrawn as a form of funding for the Welsh Government it would be necessary to reconsider other forms of borrowing to support Development Bank of Wales investments.

Borrowing Powers of Welsh Government Bodies

18. The Development Bank of Wales does not currently have the powers to borrow. The 2009 Wales JEREMIE Fund was constructed with a proportion of loan capital from the European Investment Bank. The Wales JEREMIE Fund was the first to repay its loan in full to the European Investment Bank. The cost of the finance reduced the legacy that could be created by the fund and the fund itself was more complex to deliver due to the commercial arrangements with the lender.

19. Whilst the Welsh Government has FTC to administer it is difficult to see an advantage in external borrowing as this will be more expensive and less flexible. The only exception relates to equity funds where external finance would make delivery of such funds much easier due to State Aid rules around equity investment.

The Mutual Investment Model

20. The Development Bank of Wales is currently assisting the Welsh Government with aspects of the delivery of this new model of investment.

The financial risks and costs of borrowing for different funding models or for specific models.

21. The risks and costs of borrowing can result in the transfer of costs to the end beneficiary. As a development bank we invest where the private sector often will not due to the risks and costs involved. Development Bank of Wales manages this with investment comprising different funding sources and careful management of the investment portfolio.

22. Each new proposed fund is put forward using a detailed financial model and a 5 case business plan. Funds are then assessed throughout their lives through monthly and quarterly management information and independent reviews at key stages. Where a fund begins to underperform corrective action is taken quickly to rebalance the portfolio. Where new, innovative funds are created the Development Bank of Wales agrees review points with the funder when the fund performance is formally reviewed.

23. The funds currently operated by the Development Bank of Wales encompass a wide range from very high risk (early stage seed funding) to low risk (management succession funding). This diversification spreads the risk and costs on a portfolio basis rather than isolating risks and costs on a project by project basis. The Development Bank of Wales keeps a closely monitors the overall forecast returns on its FTC commitments. This helps to inform the risk appetite for future funds.

How funding sources could be used to deliver an effective capital funding strategy.

24. Funding sources can be used effectively through the Development Bank of Wales in the following ways:

25. Core funding and the replacement to EU ERDF (UK Shared Prosperity Fund) will create a legacy of funding which can reinvested. If this form of funding continues, over time the funds would become self-sustaining i.e. could be continued with little or no further investment from Government.

26. Use of Private sector finance alongside Government funds increases the impact per pound. The ‘gap funding’ model currently attracts an equal amount from the private sector thus doubling the impact. This increases further if the private sector invest alongside the Government at fund level as is the case with the £10m pension fund investment in the Management Succession Fund.

27. The use of Commercial finance alongside Government grant has the capacity to deliver far greater impact from reducing grant funding. The Wales Tourism Fund will deliver £50m investment from just £10m grant. The idea that the choice between grant and commercial finance is a binary decision needs to be challenged.

28. Recycling of funding is particularly important in the context of FTC. Rather than having a single short term fund, FTC and Core Capital can be used over a more extended period. Not all funds are candidates for recycling but the increase in impact for those that are suitable is substantial. A good example is the £30million Wales Property Fund which, through recycling, is forecast to invest up to £272million.

29. In delivering programmes for Wales, it is important to align with other funders such as Local Authorities and the Social Enterprise sector. There is potential for Central Government programmes to align its finances with Local Government initiatives to deliver greater impact.

Scottish Futures Trust
Evidence for National Assembly for Wales – Finance Committee
Inquiry into the Welsh Government's capital funding sources

Scottish Futures Trust has been invited to give evidence to the Committee and this paper is intended to assist members in advance of oral evidence from Peter Reekie, SFT's Chief Executive on 1 May 2019.

1. Background to SFT

Scottish Futures Trust is an infrastructure agency established by Scottish Government in 2008. Its overall aim is:

> "to improve the efficiency and effectiveness of infrastructure investment and use in Scotland by working collaboratively with public bodies and industry, leading to better value for money and providing the opportunity to maximise the investment in the fabric of Scotland and hence contribute to the Scottish Government's overarching purpose to increase inclusive economic growth"

In order to deliver the aim, SFT works between policy and delivery across all sectors, geographies and stages of infrastructure life-cycle, collaborating with Scotland's public and private sectors to:

- **PLAN** asset investment and management effectively across sectors and places – **doing the right thing**
- **INNOVATE** in approaches to funding, financing and delivery – **maximising the things we can do**
- **DELIVER** projects and programmes to drive life-cycle value and vibrant construction and related industries – **doing things well**
- **MANAGE** existing assets, estates and contracts productively – **making the most of the things we have**

SFT is publishing its 2019-24 Corporate Plan and 2019-20 Business Plan over the coming days. Members will be able to access these on our website: www.scottishfuturestrust.org.uk.
SFT has grown over 10 years to a team of 70, drawn from across the public and private sectors, characterised by:

Infrastructure expertise: The team retains technical skills and understanding of infrastructure systems and economics, social infrastructure design, costing and briefing/development, housing and commercial property development, asset and facilities management, digital and low carbon infrastructure, space planning, programme and change management.

Commercial / financial acumen: The team includes many senior individuals with 10-20+ years each of experience in infrastructure related debt and equity financing, financial advice and structuring across the public and private sectors, commercial deal structuring and legal documentation, transaction management, investment decision making and governance, corporate governance, commercial contract understanding and management and approaches to dispute resolution

2. Relevant Work Areas

SFT has investigated and implemented public and privately financed approaches to investment in public infrastructure across Scotland including:

- A programme of 10 major infrastructure projects with a value of approximately £1.5bn delivered using the "Non-Profit Distributing" (NPD) model of privately financed investment and spanning the roads, hospital and colleges sectors;
- The hub programme of institutional public private partnerships for community infrastructure developments which comprises 5 hub companies across Scotland developing and delivering schools, health centres, council and blue light facilities and other community infrastructure under both capital funded and profit-sharing private financed arrangements. The hub programme has delivered approximately £1.6bn of assets with a further £600m in construction, including 41 Design, Build, Finance and Maintain (DBFM) privately financed projects.
- Tax Incremental Financing (TIF) and Growth Accelerator (GA) projects which use local authority borrowing powers to raise finance to invest in public infrastructure which enables private economic development, with the finance being repaid either through an increment in tax-take retained by the Authority (TIF), or Scottish Government revenue funding for the outcomes delivered by the overall investment.
- National Housing Trust affordable homes, of which over 2,000 are now occupied across Scotland, and which have been delivered through limited liability partnerships (LLPs) established between SFT, Local Authorities and (under one variant of the approach) private developers.

3. Comments on Inquiry Considerations

SFT is careful to differentiate between the funding and financing of infrastructure and it may be helpful for the Committee to understand our use of language in this regard:

Any asset ultimately has to be paid for (or **funded**) either as it is built or as it is used. Funding for infrastructure assets come either from public sector budgets, or from "customers" in the form of user / occupier / developer charges.

If the asset is paid for as it is used, a form of **finance** (which comes with an expectation of repayment) can be raised to build the asset[1]. Financing can be either public sector borrowing or private debt / equity.

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[1] An exception is an asset financed using corporate or national debt where the debt stock is increased in perpetuity to pay for the asset. As this form of borrowing is not available to Scottish Government we do not consider it across our work

In respect of the forms of funding and financing mentioned in the terms of reference for the Inquiry:

Conventional Funding – capital budgets is a form of funding infrastructure assets as they are built using public budgets.
Conventional Funding – financial transactions is a form of financing which must ultimately be repaid to HM Treasury. Members will know that FTs must be lent outside the public sector boundary and utilised by a privately classified entity for a purpose which has an associated funding stream (for example rental income) which can eventually repay the finance.
Government Loans & Bonds – are again forms of financing which either increase the Government's debt stock in perpetuity (if regulations allow) or must be repaid using funding from future capital / revenue budgets or customer charge.
Capital Receipts create an additional source of funding over and above budget allocations.
Borrowing Powers of Bodies – In Scotland, Local Authorities have separate borrowing powers from Scottish Government which are used by them as a source of financing for assets, ultimately funded by their own future budgets or customer charges.
Mutual Investment Model – is an arrangement to use private finance to pay for the creation of an asset which must be classified to the private sector, and where the public sector funds the asset as it is used through revenue budgets over a 25-30 year period.

4. Scotland's Public Private Partnership Models

SFT manages Scottish Government's programme of privately financed infrastructure investment funded from revenue budgets as assets are used. Since 2011, this programme has been delivered through the NPD and hub DBFM arrangements.

The programme was launched in the 2011/12 Scottish Government Budget[2]. The context of the decision to deliver a progamme of privately financed infrastructure was set out in Chapter 3 of the budget document:

> "Capital investment is vital to strengthening recovery and supporting sustainable economic growth. It sits at the heart of our economic strategy. The Scottish Government views the severe cuts in capital spending imposed by the UK Government as deeply damaging. We will do all we can to mitigate their effects."

The rationale for using privately financed investment was also set out in the budget document:

> "As a result of our concern about the effect of the rapid and deep reductions in capital spending flowing from decisions in the UK Spending Review and the implications that these will have for the pace of implementation of the capital programme and the strength of the Scottish economy, the Scottish Government will explore all possible means to support higher levels of infrastructure investment than would be possible through the capital budget alone. This effort will be particularly important to support recovery and sustainable economic growth, as capital budgets will fall sharply in 2011-12 and are likely to remain low for several years.

[2]https://www.webarchive.org.uk/wayback/archive/20170107125418/http://www.gov.scot/Publications/2010/11/17091127/23

"In general, funding infrastructure investment through public capital ensures the lowest cost of finance for a typical project. Under the current public finance framework, the Scottish Government does not have the flexibility to borrow to fund additional capital expenditure. However, there is an overwhelming economic and financial case for providing this flexibility to borrow as soon as possible.

"In the absence of borrowing powers, there are a number of levers which can be used to help to expand Scotland's public infrastructure programme. While ensuring these levers are used sustainably and responsibly, the Scottish Government – working closely with the Scottish Futures Trust and local authorities – will work to maximise their positive impact. Therefore, in addition to its planned capital investments in 2011-12 and future years, the Scottish Government will:

- take forward a new, affordable pipeline of revenue financed investment worth up to £2.5 billion, to be delivered through the Non-Profit Distributing (NPD) model; and
- make full use of innovative measures such as Tax Incremental Financing, the National Housing Trust and investment through the JESSICA Fund."

The value for money sought from the NPD programme is the additionality of capacity to invest in infrastructure over and above traditional capital budgets which it brings, and the widely recognised value to the economy of that investment. It was recognised that the cost of finance would be higher than public borrowing and that maximising value for money, and ensuring affordability across the programme was critical.

4.1 Value for Money

SFT has sought to maximise value for money across the investment programme by:

- adopting profit capping (NPD)[3] and profit sharing (hub DBFM) approaches to capture investment up-side for the public sector and improve on the value offered by older PFI contracts
- having an expert central team managing standard contract documents to ensure commercial consistency and reduce market bidding costs
- reducing the scope of contracted services to exclude catering cleaning etc. (soft facilities management)
- selecting projects and programmes of investment to be taken forward with characteristics suited to private finance arrangements
- managing a programme of "key stage review" assurance across all projects to share good practices across procuring authorities and ensure the correct steps have been completed before projects proceed
- for smaller projects, using a programme approach (hub) to bring consistency, reduce transaction costs and develop longer term partnering arrangements between the public and private sectors
- Maximise community benefits of SME engagement and training delivered across projects and programmes
- Bring a public sector mindset to the delivery of projects through placement of a Public Interest Director on the board of each delivery company.

[3] Found by the ONS and Eurostat in 2015 to be classified to the public sector under ESA10 guidance and therefore no longer pursued as the key characteristic of delivering additional investment is no longer achieved

4.2 Affordability

From the outset the programme has delivered within an affordability limit. This year, the budget includes capping the revenue funding for infrastructure investment at 5% of Scottish Government's Resource budget (excluding social security). This figure includes annual revenue budget impact of Scottish Government capital borrowing, , historic PFI project unitary charge payments and the Scottish Government's share of payments made under NPD and hub DBFM projects. These payments are expected to peak for contracted and committed payments at 3.2% in 2020-21 and 2021-22

4.3 Monitoring

The Scottish Government and SFT maintain a high level of transparency over revenue funded investment projects and have been commended by the international Infrastructure Transparency Initiative for the data points published in respect of major investment projects[4]. Important aspects of transparency, which SFT continuously seeks to build upon, include:

- Six Monthly Capital Investment Project Reporting to the Parliamentary Audit and Post Legislative Scrutiny Committee[5];
- Publication of annual unitary charge information[6]
- Publication of 5% affordability cap monitoring in budget documentation[7]
- Publication of NPD and hub DBFM contracts and Financial Models [8]
- Publication of hub project pipeline information[9]
- Publication of hub programme community benefits delivery monitoring[9]

5. Future Investment

In the 2018-19 Programme for Government[10], a new National Infrastructure Mission was established to support inclusive economic growth through an increase in infrastructure investment by £1.5bn, or approximately 1% of 2017 GDP, per annum by 2025-26. The Office for the Chief Economic Advisor has published evidence linking infrastructure investment to economic growth[11].

This ambitious mission to deliver additionality of investment cannot be delivered using the currently projected levels of Scottish Government capital budgets and borrowing powers.

Scottish Government Borrowing Powers are limited both annually and in aggregate in the Fiscal Framework[12]. In its 2014 evidence to the Smith Commission on Proposals for Further Devolution to Scotland, SFT argued that Scotland should have the powers to be able to determine the right level of

[4] http://infrastructuretransparency.org/news/cost-research-finds-major-learning-opportunity-for-scotland-and-cost-members/
[5]https://www.parliament.scot/S5_Public_Audit/General%20Documents/Major_Capital_Projects_Progress_Report_-_September_2018.pdf
[6] https://www.gov.scot/publications/pipeline-npdhub-projects-unitary-payment-charges/
[7] https://www.gov.scot/publications/scottish-budget-2019-20/ (Page 45)
[8] https://contracts.scottishfuturestrust.org.uk/category/hub
[9] https://www.scottishfuturestrust.org.uk/page/hub
[10] https://www.gov.scot/programme-for-government/
[11] https://www.gov.scot/publications/exploring-economic-rationale-infrastructure-investment/pages/1/
[12] https://www.gov.scot/publications/fiscal-framework-factsheet/pages/borrowing-powers/

infrastructure investment to affordably meet its economic and social objectives, and how this investment is both funded and financed. SFT's evidence pointed out that Scotland has unlimited powers to take on future repayment obligations through PPP-type arrangements and that "It appears inconsistent that borrowing powers, which could provide both flexibility and a lower cost of finance for investment, should have a cash value borrowing limit imposed as a reserved matter[13]". SFT suggested that the annual and total limit on Scottish Ministers borrowing powers be removed. This proposal was not adopted in the revised Fiscal Framework and Scottish Ministers Borrowing Powers remain capped.

In the light of this ambitious National Infrastructure Mission, and constrained borrowing powers, it is likely that additional forms of financing will be required to deliver the Mission. Public Financing, for example Local Authority borrowing powers, which are independent of the limited powers of Scottish Ministers, are likely to be better value than private financing approaches. Wherever possible, these will be considered under approaches such as SFT's Growth Accelerator[14]. It is however possible that forms of private financing will be required in order to deliver the Mission. Following the reclassification by ONS and Eurostat of NPD projects to the public sector this approach is no longer able to deliver additionality of investment under a privately financed PPP approach and will not be used any further. SFT is currently examining profit sharing finance schemes, such as the Welsh Mutual Investment Model, to help secure both the investment needed and best value for the taxpayer.

In this investigation, we have had substantial engagement with the local, UK and European construction markets which have faced substantial challenges in recent years, exemplified by the demise of Carillion in early 2018. It is essential that our future approaches to project selection, development of project pipelines, funding and financing structures and procurement methodologies allow us to deliver high-quality assets which meet Scotland's economic and social needs **from** the construction industry, and provide opportunities **for** the indigenous construction industry, which represents around 6% of Scotland's economy to invest in productivity, fair work and wider social and environmental benefits.

6. Conclusion

We hope this evidence is useful to the Committee in its inquiry into the Welsh Government's capital funding sources. It focusses on SFT's experience of privately financed approaches to investment in public infrastructure as we though this may be of the most use. SFT has experience of innovation in financing and delivering affordable housing, and in enabling private development through our Tax Incremental Financing and Growth Accelerator approaches. Peter Reekie will be pleased to expand on the evidence in this paper, or provide information on other areas of our work if that would be helpful in oral evidence.

Scottish Futures Trust
April 2019

[13] https://www.scottishfuturestrust.org.uk/storage/uploads/Smith_Commission_SFT_31_October.pdf
[14] https://www.scottishfuturestrust.org.uk/page/growth-accelerator

Capital Funding Sources for the Welsh Government.

The following remarks may appear rather obvious, even trite. It may be worthwhile, however, to state some rather basic points as a background to the discussion.

Need for a proper plan

Firstly, if the Welsh Government (WG) is going to optimise its use of capital funding sources it needs to have a medium-term investment plan extending out 5 to 10 years. It began the process of constructing such a plan some seven years ago when the first Wales Infrastructure Investment Plan (WIIP) was produced. That plan, however, was little more than a wish-list of projects put forward by spending departments and collated by the Finance Department. There were no priorities established among the projects and no target dates for their completion. Their financing depended on the capital budget allocated to each department. Two projects were earmarked to be financed by what has evolved into the Mutual Investment Model.

At that time, it was not possible to calculate from the WIIP what the borrowing requirements of the WG would be. It had been WG. practice to consider only the next three years because HMG announced Barnett allocation in a three-year cycle. Of course, there was no certainty about revenue beyond that horizon but it is necessary to make projections in planning investments. Where uncertainty is acute a scenario approach can be adopted. Even with such projections, however, a borrowing requirement can still not be calculated without target dates on all projects. At the time of the first WIIP, if the plan had been to complete the target list over 20-plus years there would have been little need to borrow at all given expected revenues. If the plan was for ten years it would have been necessary to borrow several billion pounds.

Since then things have evolved quite a lot. The 2018 interim report on the WIIP recognized the need for a co-ordinated all-government approach to establishing priorities. There was recognition of the need to make longer term economic and revenue projections and apparently techniques for doing so have been developed and are being refined. The statements in the report about how the WIIP would be drawn up in future were all exemplary. One might have hoped that after seven years they would be established procedures rather than good intentions but no doubt austerity can be blamed.

Which should be published

Secondly any long-term investment plan should be published in full. With a priority ordering of large projects and target dates for meeting them, the required expenditure can be compared with revenue projections and a borrowing programme derived. There is no reason why any of that should be secret. The public can discuss the priorities and timing, encouraging public debate and buy-in. With projects, provisional costings and dates in the public domain for 5 to 10 years ahead, there are likely to be plenty of offers of assistance and suggestions from private sector companies and financiers for ways to obtain capital. Lobbying is always self-interested but can also convey information and ideas to the public

authority, which of course must remain alert and sceptical. The 2018 report is a big advance on its 2012 forebear and the government is to be commended on publication of the project pipeline.
It is full of retrospective case studies with glossy pictures showing completed projects with copy that reads like a press release from an advertising agency. That cannot be criticized; politics is also about salesmanship and it is appropriate to point to what has been achieved. But the selling is more authoritative and persuasive when there is full information on a worked-up future plan behind it. Everyone should understand that plans change and evolve under the pressure of events, especially long-term ones, so governments should not be fearful of giving hostages to fortune.

Three sources of finance

When such a plan exists there is a known borrowing requirement. The Welsh government now has limited but not insignificant powers to borrow from the Debt Management Office who will issue UK government bonds (gilts) to finance. That is likely to be the cheapest form of borrowing. Local authorities can also tap the gilt market in effect by borrowing from the Public Works Loan Board. That is also cheap finance but the Welsh government itself is not supposed to use it to exceed the borrowing limits imposed on it by the Treasury. It can work in conjunction with local authorities but it must not be seen too obviously to be relieving them of their debt burdens. The third major source of capital is private finance of which the Mutual Investment Model is an example.

The principle behind private finance is that the private provider of capital for a project is supposed to take on much of the risk associated with it. That may be construction risk, maintenance or operation risk. Although the public sector ultimately pays for the services it is procuring it has to demonstrate that risks have been shifted if the project is to come off its balance sheet, It is then, in effect, paying a lease on an asset perhaps with associated services rather than borrowing to construct the asset. If the asset reverts to the public sector at the end of a contract period, it is employing a form of what used to be known to consumers as hire purchase. Like all hire purchase agreements this turns out to be more expensive in the long run than outright purchase. Interest charges are higher reflecting the risks being run by the provider of the capital. In practice shifting risk is not so easy since the state is always responsible in the end for providing the services that the infrastructure is there to sustain – which makes the higher interest charges a bit irritating.

When should they be used?

The Welsh government says in the 2018 report on the WIIP that it will always use the cheapest sources of finance first before resorting to more expensive forms. That sounds sensible and if you are proceeding hand to mouth it is the best you can do. If a medium-term plan is in existence, however, one can do better. With such a plan it would be clear whether the borrowing requirement over any time period was likely to exceed the amount of the cheapest finance available (gilts). If it did not there is nothing to discuss; all borrowing would be done through issue of UK bonds via the DMO. Where the borrowing requirement exceeds the available gilt borrowing however, things are more interesting. Then there is the possibility of matching finance and projects rather than simply using up gilts first.

The aim should be to minimize the total cost of the borrowing programme. The significant fact to bear in mind is this: gilt interest rates are the same whatever the money is used for; that is not true of private finance. Recall that the interest rate on a private finance deal (including MIM deals) will reflect the risk born by the financier. It follows that private finance should be used for the least risky projects. Riskier projects should be financed with gilts. Risk can take several forms: construction, maintenance operation. A project can be sliced up in numerous ways. The state could acquire an asset itself and license a private operator to run or maintain it, for example, so the comparison is not straightforward. Nonetheless the principle is clear. Carve up projects appropriately and use private finance where the risks to the financier are relatively low.

A second consideration is how the project will ultimately be paid for. For services free at the point of delivery, like much health, education and most road provision, the taxpayer foots the bill. Some services, like use of railways and toll roads or bridges incur user charges. Taxes, like death, are held to be inevitable but with most services for which you pay there is an element of choice. This means the government may be more relaxed about the financing cost of services that are self-financing. This argument, however, does not dominate the first one; minimizing overall cost should be the priority.

The ideal project for private finance, therefore, is one of which there are plenty of past instances so the risks are known and can be managed successfully. Anything highly innovative is likely to be expensive. Moreover, if the user will pay for the service so that servicing costs can be met out of user charges, so much the better. It follows that if the M4 relief road is to be built it should be financed by MIM since motorway construction is a routine procedure. Moreover, the case would be reinforced if it were a toll road – for which there are strong arguments. There is no obvious reason why tax payers in Anglesey should pay for commuters around Newport. And if the latter don't want to pay a toll they have the option of crawling along through the Bryn Glas tunnel. Wales' gilt allocation would then be used for riskier projects, which would certainly describe the Swansea Bay lagoon or the Carmarthen to Aberystwyth railway, should those be contemplated. Of course, that assumes the WIIP is ambitious enough to exceed capital budgets and the gilt allocation and that it includes some innovative projects. Those assumptions may or may not apply.

Gerald Holtham
24:iv:2019

KPMG’s Response to the Inquiry into the Welsh Government’s capital funding sources

May 2019

Contents

1 Foreword

KPMG is a professional services firm employing around 15000 people across the UK. Within Wales, KPMG employ around a 100 staff across many professional services disciplines.

KPMG has a leading role in developing infrastructure across the world. In the UK we have more than 150 staff wholly dedicated to infrastructure and capital projects, covering a broad range of sectors and offering expertise across the whole lifecycle of an infrastructure asset.

This includes infrastructure strategy, economic analysis, policy and regulation, developing business cases, procurement, financial/commercial structuring, transaction negotiation and due diligence, financial modelling, project management, cost monitoring, restructuring services, tax and accounting.

The comments below are drawn from conversations with a number of senior practitioners within the firm and reflect genuinely held views. Our team cares about building better infrastructure for everyone, enabling better delivery or public services through high quality built environment, protecting our environment and supporting innovation. We have no ideological of financial interest in any particular infrastructure finance model, preferring to select the best solution for a given project.

This document is the KPMG response to the inquiry into the Welsh Government's capital funding sources.

2 About the Author

This document represents the views of a number of senior practitioners at KPMG rather than the views of an individual. However, they have been pulled together by Gwyn Llewelyn, a Director in our Infrastructure Advisory Group who has spent the last 14 years advising on the delivery and financing of public infrastructure with a recent focus on healthcare, education and local government.

Gwyn has advised on financings using a wide variety of commercial structures, including Aberdeen City Council on the UK's largest municipal bond, the Scottish Non-Profit-Distributing model, concession models and several PFI contracts in England. He is part of an advisory group to the National Infrastructure Commission looking at the evidence base to support private finance into infrastructure.

Gwyn will be present to speak with you on 15th May.

3 Context for the Review

The backdrop to this review is the challenge posed in creating infrastructure fit for the 21st century that includes improving broadband speeds and mobile coverage, enabling housing development, improving our health and education infrastructure to improve social outcomes, decarbonising our energy networks, reducing journey times, investing in water networks, increasing our resilience to climate change and the impact of new technology.

This requires major investments from both the public and the private sectors, and in a changing landscape. The rapid development of new technologies will create new funding and financing challenges, and the UK's relationship with the European Investment Bank (EIB) will change as we leave the EU potentially further restricting access to low cost capital.

4 The Structure of Our Response

The response sets out thoughts on the areas identified for investigation by the review although does not cover them strictly sequentially as many of the issues discussed are interlinked and overlap. We instead provide general commentary on the use of public and private funding and cover the identified topics where relevant.

5 Commentary on UK infrastructure finance market

The UK has a large, well-established and technically expert finance market for investment in infrastructure. It has a global reputation in all aspects of finance and is the go-to market for overseas territories seeking best practice.

As a result the UK attracts talented individuals and global investors alike, further enhancing the diversity of expertise and innovation across all the financial markets and professional services.

This is supported by a consistent legal and regulatory environment enabling all parties to be confident of both fair and predictable treatment.

The UK regulators have a strong reputation as independent, clear and open institutions establishing further the trust between the private and public sectors.

The use of consistent trusted contractual structures and financing methodologies increases the understanding of the risk balance available in UK infrastructure.

The financial expertise is complemented by large UK based engineering firms with the technical skills to deliver complex projects helping to de-risk the provision of financing to UK infrastructure.

The UK's place as a leading OECD country within the G7 can also be viewed as a supporting pillar to the UK infrastructure finance market. The broader economic stability and prospects that this brings helps give the UK infrastructure finance a comparative advantage through association.

As a result of all the above there is plenty of money, debt and equity, ready to invest in UK infrastructure as long as projects have the right risk profile and investment characteristics. This availability of private capital to support projects is valuable where it can demonstrate advantages over the use of public capital, or it can supplement it.

6 What are the weaknesses in the infrastructure finance market?

The current uncertain political environment is a deterrent to investment.

There is political uncertainty regarding policy for private finance, with the abolishment of PFI and its replacement PF2 in England, the NPD model paused in Scotland and MIM model just beginning in Wales. The opportunity to help drive future policy is welcome, this consultation in itself signals further uncertainty to the market when MIM is trying to establish itself.

Historic Government focus on balance sheet treatment driving commercial solutions has weakened the industry's reputation, leading to some deals that are not necessarily right for a particular transaction but are financed that way to avoid the need for capital budget.

This is particularly an issue for the construction industry. MIM style project structures seek to pass significant risk to main contractors, few of whom in the UK have the financial standing to bear that risk, particularly when many smaller subcontractors in the supply chain refuse to have the risks passed on down to them.

Construction is a low margin business and whilst competition for new public sector work continues to be heavily price-led this will continue. But to paraphrase one CEO of an international contractor "3% margin businesses cannot take 50% risks". The criticism of PFI/PF2 in England leading to excess profits is rarely set against the collapse of Carillion, Interserve, Jarvis, Ballast Wiltshier et al.

Press coverage of infrastructure tends to focus on the negatives. There is no consistent voice standing up for the positive transformation that infrastructure can bring. Proper informed debate is undermined by headline grabbing sound-bites.

Delivering projects in the UK is typically more expensive than in other jurisdictions. The reasons for this are complex (and not necessarily negative) but lengthy and costly bidding processes can act as a significant deterrent or barrier to entry.

7 Appraising the merits of different forms of finance

Too often, the debate around source of finance for a project focusses on a comparison to UK gilt rates. This is incorrect. All academic and corporate finance literature is clear that investment appraisal should be based on the risk level of the investment, not the party borrowing the money.

To explain the point, in an efficient market the expected return generated by an investment increases with its level of risk, with risk measured as volatility of return[1].

An investment grade borrower (such as a public body) will have a low cost borrowing rate as they themselves are stable with limited volatility – they can be trusted to repay borrowing. A higher risk borrower with unstable income will have a higher cost of borrowing as there is less certainty on whether they can repay their borrowing.

The value of an investment is not different for the investment grade borrower than the higher risk borrower just because he has a lower underlying cost of funds. The value of an investment is driven by the risk of the investment (how likely is it to repay funds), not the party investing in it.

If the reverse was true, it would encourage borrowers with a low cost of capital (such as public bodies) to borrow heavily and invest in risky projects, as risky projects on average return a higher amount. Such a strategy would be widely discredited (although we can see it happening from time to time across English local authorities who are borrowing cheaply from the Public Works Loan Board and making speculative investments into real estate, unfortunately).

Why are we covering this? Because the government gilt rate represents the cost of borrowing for UK government, not the required return that should be sought from an investment into infrastructure given its risk level. In fact, the gilt rate becomes an irrelevance apart from the fact that it also underpins the market cost of borrowing. A capital project should be appraised using a project specific rate (usually as a discount rate for future cash flows), which unless there is a market failure, should be a market rate reflecting the risk of the investment. Comparing cost of finance with looking at risk allocation, whilst tempting, should be left to the tabloids.

8 Why can the government borrow cheaply?

Putting it another way, the only reason government can borrow so cheaply is its right to tax in the future. This is established through the credit rating methodologies used to rate sovereign

[1] (this is a slight simplification to ignore adjustment for idiosyncratic risk, but the point holds and it is not the purpose of this paper to discuss the valuation of risk in depth)

credit risk. [2] The market rate for finance is typically driven by the equilibrium between supply and demand for capital, the largest moving parts of which are pension and insurance funds. Put simply, the market rate represents the rate we expect our pension fund managers to achieve on an investment with any given risk level with our retirement savings, given other available options. Just because government can borrow more cheaply to raise capital doesn't mean it should, as that capital is cheap because it is taking into account the right of government to tax future generations. In other words, it is taking bets with the taxable income of future generations for a lower return than we are happy to accept from our pension funds with our own income. That doesn't sit well.

9 Funding versus financing

Most infrastructure is funded in one of two ways – either through user charges or through tax payers. Private finance can be used for both as set out in the simplified diagram below.

Funding/ Financing	Public finance	Private finance
User Charges	Gilt borrowing, repaid through user charges	Private infrastructure, regulated assets, concession models
Tax payers	Gilt borrowing, repaid through tax income	DBFM structures, such as MIM

There are exceptions, where infrastructure can be paid for not by the user but by other beneficiaries, such as land value uplift or developer charges.

Ultimately, in our view, the biggest challenge for Welsh Government capital financing is one of funding not one of financing. Is the funding generated by user charges for infrastructure, or the increases to tax receipts it is likely to generate over time, sufficient to fund the capital cost plus appropriate borrowing costs. Can sufficient revenue be generated from assets to pay for them. If so, a myriad of options exist for raising the finance to deliver them whether public or private.

The decision of public or private finance then boils down to a number of factors, the most pertinent of which are:

- The risk to the public balance sheet and whether the public sector is well placed to take and manage that risk
- The incentives the finance creates on the delivery and operation of that infrastructure. Private investment being at risk can be a powerful incentive to meet contractual obligations.
- Tying in private sector expertise in delivering and operating complex infrastructure
- The level of control, influence and flexibility demanded by the public sector over an assets

[2] The right to tax is of primary importance. When we advised Aberdeen City Council on their £400m+ municipal bond, the ratings agencies took the view that a local authority does not have sufficient right to tax and so only qualifies as sub-sovereign, meaning the cost of finance was some 100bps+ higher than gilts.

— Whether there is any market failure in the private financing market that justifies government intervention.

The latter two points are worthy of further exploration below.

10 Control, influence and flexibility

A frequently levied criticism of private finance is that is leaves the public sector with complex and inflexible contracts. In many instances this is justified.

PFI contracts in particular are complex, often negotiated by specialist advisors not the people who will ultimately be left to manage them. Steps have been taken with MIM to address this, but it is likely they will still be more complex that public capital.

Change within such a contract can be costly, with consent needed from lenders and investors for change.

As a result of the complexity of contract, we have found many instances where projects are managed on the basis of custom and practice rather than contractual obligation, so the contracts are not followed. In some of these instances it results in the public sector not getting what they are paying for.

The industry (public and private) can take some criticism for treating contracts for a road the same as a hospital or schools. Simplifying the argument slightly, but a road is a strip of tarmac whose performance lies in being kept open and safe. A hospital is a building of complex public service delivery with changing needs and models of healthcare. It necessarily needs more flexibility and active contract management – on both sides of the table. Unfortunately, standard form contract and management practice have not always delivered such active management and true partnership. There are good exceptions to that criticism.

11 Market Failure

Whilst it is frequently noted that there is a 'wall of private capital' available to well-structured projects, typically this is capital seeking investment grade projects (ie long term and low risk). As technology develops, it is hard to match that to the risk of the types of infrastructure being developed. Easy examples are emerging technologies in battery storage, electric vehicle charging points, drones, heat networks, tidal lagoons, 5G networks. These are investments that are higher risk than traditional building projects, with shorter life spans. More and more the lifespan of infrastructure is not governed by its physical life but how long before technological obsolescence. Can we really appraise the building of car parks over 40 years when market commentators are suggesting autonomous vehicles and low rates of vehicle ownership in 25 years? As such, there is a clear financing market failure for new and novel assets.

There is also a market failure for financing of very large assets, such as nuclear power stations, where co-ordinating private finance is challenging without government intervention.

Taking that to its logical conclusion would suggest that government should be reserving its limited capital to areas of market failure which are typically larger and higher risk projects, leaving private capital to finance infrastructure where there is a proven market rate for capital and better understood risk – such as schools, hospitals. That can be counter-intuitive and contrary to the general adverse media that accuses the use of private capital for such assets as profiteering or having limited risk transfer.

12 What models of finance are appropriate for the future

Generally, moving away from making financing sourcing decisions on the basis of balance sheet treatment and more on the basis of value for money and addressing market failure has to be a good thing. That is not to say we don't appreciate the budgetary constraints facing government, rather that they shouldn't be the overriding factor.

This will allow more appropriate sharing of risk between parties – ESA2010 government accounting treatment has a checklist of more than 80 commercial considerations and often contracts are designed to tick the ESA2010 box rather than what is commercially sensible.

Once balance sheet treatment is removed as a decision making factor, it allows better partnership between the public and private sector. Examples would include:

- Joint funding, with some public and some private capital. This could be through public sector capital contributions alongside private finance, something we have experience of with an example being the Royal Papworth Hospital PFI in Cambridge that opened earlier this year, which combines 40% public capital with 60% private capital. Of the private capital, 50% of the senior debt was provided by EIB and the all-in cost of finance was less than 4%, but still transferred all construction and operational performance risk to the private sector. Such models seem worthy of further exploration.

- Mixed funding. Increasingly infrastructure is not delivered as a single asset for a single owners (a hospital delivered for a health trust, for example), but infrastructure systems of multiple assets delivered to make an area work, i.e. a life sciences park may need NHS involvement, university involvement, local authority involvement, pharmaceutical and industry involvement etc. They may need new transport links, key worker housing, commercial buildings and laboratory infrastructure. The deals needs are complex and bespoke, and need to be worked through on the basis of what is the best form of government intervention to make the project happen. Sometimes but not always that intervention will be the public sector providing all the capita.

- Targeted risk taking. Often there is a market failure in private investment because of specific risks. This tends to be in areas where high impact low probably events can severely impact lenders downside cases. In these cases government intervention by underwriting certain specific risks (maybe only in an extreme downside event) can be all that's needed through some form of financing guarantee.

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Capital Law

Inquiry into the Welsh Government's capital funding options

9 May 2019

Introduction

We provide this brief paper in anticipation of giving evidence to the National Assembly for Wales' Finance Committee on 15th May 2019 in relation to the funding sources available to the Welsh Government.

Our approach

"*We see the Mutual Investment Model (MIM) proposal as the only viable tool to provide significant finance to fund ambitious Welsh projects*"

Our observations in this document are targeted towards the way this may be achieved, and are split into three areas:

- Delivering an effective funding strategy
- MIM and value for money; and
- MIM v PPP / PFI

The focus of this inquiry is broad. Therefore, our approach is to concentrate on the specific elements which are relevant to our business.

Delivering an effective funding strategy

"*Best practice in relation to delivering projects is reliant on an effective funding strategy*"

Given our involvement in significant projects (such as the M4 Relief Road and Hinkley Point C) several very clear best practice themes arise in relation to project delivery and an effective funding strategy must be based around these.

An effective funding strategy must have regard to the specific requirements of a project and the maturity of the project. In the most basic of terms the lifecycle of a project has four distinctive steps:

Step 1 Project Pipeline - identifying a pipeline of projects around which a strategy can be formulated.

Given that a project pipeline will extend beyond the electoral cycle, the project will require multi-political party support and be in the public interest generally. The Well-being of Future Generations (Wales) Act 2015 facilitates this Step by requiring that that all public sector projects must improve our social, cultural, environmental, and economic well-being.

Step 2 Project Feasibility – identifying specific projects within the pipeline for delivery

Once the pipeline of projects has been established the next step is to consider the requirements for delivering a specific project along with identifying and mitigating risks. This step typically revolves around the following:

- Funding – identifying at an early stage an appropriate source of funding for delivery of the project.
- Pooling resources – there have been several projects throughout Wales that have used a public to public collaborative approach. Local Authorities have worked together with suppliers, to produce efficiency savings in costs and share work practices. In turn, this increases the value of prospective contracts, making them more attractive to the market.
- Market engagement - yields benefits in relation to cost estimation, risk management, and ease of delivery.
- Defining the project and specification – this is the initial process of defining the project requirements, which will be informed by the other elements of this step.
- Procurement – planning and choice of procurement route is crucial at this stage.

Step 3 Project De-risking - carrying out the de risking steps and delivering the project.

This is the implementation stage of the strategy and is the process of getting the project "Delivery-ready" and builds on the feasibility step. The key elements here are:

— Clearly defining the project and specification – this is a priority at this stage and the outcome should be a clear scope based on up to date market price information. The projects specification must be approached in a way that allows the prospective contractors to price clearly.
— Early Contractor Involvement – is a useful tool at this stage to develop the specification.
— Funding – any preconditions relating to the project delivery funding should be considered / satisfied at this stage and requirements and obligations incorporated into the specification / procurement process as required.
— Procurement – is the final element of this step and must be carried out in a way that demonstrates transparency, fairness, integrity, competition, and accountability. Planning and choice of procurement route is crucial at this stage. Competitive dialogue (where candidates are invited to take part in a dialogue process, during which the nature of the project may be discussed and possible solutions may be developed) has a proven track record for delivering projects and is a good precursor to collaborative working during project delivery.

Step 4 Project Delivery – appointed contractor delivers the project in accordance with the specification.

This is the final step and the key here is a project that is delivered on time and within budget and relies on the following:

— Funding – ensuring that the funding requirements are satisfied promptly to ensure cash-flow into the supply chain; and
— Collaborative working – there needs to be a framework to provide quick decisions on key issues and effective mechanisms to communicate with stakeholders, manage risks, and resolve conflict. Controlling risks is central to this – with the party best placed to handle the risk being tasked to do so.

It is clear from the generic lifecycle above that funding is key at each step. This also highlights that the level of funding and the type of funding will vary during a project. For example, Project Delivery will require the highest level of funding but the amount of funding should be clearly definable. Project Feasibility, on the other hand will require a lower level of spend but the extent of the expenditure will be speculative in nature in order to explore mitigation options to ensure price certainty at Project Delivery.

In summary an effective funding strategy depends on multiple sources of funding (ranging from conventional funding to public / private partnership models such as MIM) appropriate to the relevant point within a project's lifecycle.

MIM and value for money

"*The premium paid for finance and delivery of a MIM project does lend itself to the principle of - Something for Something*"

Put simply MIM is a form of project agreement to fund and deliver "off balance sheet" privately financed public projects. Given that WG do not have access to the level of capital funds, the MIM proposal is the only viable tool to provide significant finance to fund ambitious / high value projects. Therefore, the fact that MIM is more expensive than direct funding is a moot point.

However, the MIM model is not necessarily in search of the lowest price but rather best value. Consideration should be given to the ancillary benefits available. For example, those driven by the Well-being of Future Generations (Wales)Act 2015.

For example, in relation to the dualling of A465 (project earmarked for MIM funding), the procurement focus will be on:

- £300 million being spent with Welsh companies (70% of the total spend)
- Creating 140 apprentice roles
- Community benefits.

The comparison with debt funding is not so clear cut. If the MIM project proposed has a clear specification which in turn can be accurately priced the investment risk is minimised. The aim is to provide a project which requires a defined level of funding (i.e. the risk of cost overrun is minimal) which is offset by the annual payments. In effect the aim is for the level of return to be guaranteed – meaning that lenders risk, and in turn its rate of interest, is reduced. This should make the project competitive with the rates of debt funding available.

MIM v PPP / PFI

"The MIM process must be collaborative and have regard to the lessons learnt from PPP/PFI projects."

The MIM and PPP / PFI models have a number of factors in common but MIM has the benefit of hindsight and must have regard to the lessons learnt from PPP / PFI models. The table below provides a comparison of the three models.

	Private Finance Initiatives (PFI)	Private Finance Initiatives (PPP)	MIM
1.	PFI is a form of PPP where a private sector company finances and provides a public service that might include construction, maintenance and operation, for which they are paid by a public authority.	Although PPP technically includes PFI and Concession Contracts (payment recouped via tolls) it is more commonly associated with Institutional PPP where a joint venture company is established jointly by a public authority and a private company to provide a public service	MIM is a form of project agreement to fund and deliver "off balance sheet" privately financed public infrastructure projects. In effect a Public Private Partnership (PPP) – to enable private partners to build and maintain public assets
2.	Funding – usually traditional bank debt funding repayable by the authority.	Funding - usually traditional bank debt funding repayable by the authority.	Funding – combination of equity and debt funding to SPV No direct repayment of debt by the authority but an annual payment for facilities management paid by authority
3.	Design and construction – SPV procures the supply chain and is usually asked to take a great deal (if not all) of the project risk from the authority. However, the price will reflect this.	Design and construction – as per PFI	Design and construction – SPV procures design and construction but the project specification is intended to be de-risked prior to it being handed over to the SPV.
4.	Facilities management – anticipated that hard and soft facilities management. This is the main criticism of PFI as costs escalated.	Facilities management – as per PFI	Facilities management – hard facilities management only (limited to identifiable maintenance) and not soft maintenance (e.g. replacing street lights) this responsibility to remain with the authority.
5.	Control – Authority tending to maintain control by being a significant shareholder in the SPV (on-balance sheet risk)	Control – Authority has 50 per cent or more share in profits and has veto / approval rights (on balance sheet risk)	Control – 15% - 20% equity stake for the Authority with a nominated director to the board of the SPV i.e. limited control (off balance sheet)

Conclusion

The challenge / opportunity will be to advance the project pipeline supported by a robust funding strategy. This will make sure that several ambitious and high value projects are capable of delivery.

Ymatebion i’r Ymgynghoriad yn y Gymraeg

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Cyfeirnod: AC/130/caf **Dyddiad cyhoeddi:** 23 Ebrill 2019

Annwyl Llŷr

Ymchwiliad y Pwyllgor Cyllid – ffynonellau cyllid cyfalaf Llywodraeth Cymru

Er mwyn cynorthwyo'r Pwyllgor Cyllid yn ei ymchwiliad i ffynonellau cyllid cyfalaf Llywodraeth Cymru, mae'n dda gennyf gyflwyno tystiolaeth ysgrifenedig i'r Pwyllgor. Paratowyd y papur amgaeedig ar fy rhan gan staff Swyddfa Archwilio Cymru.

Mae'r papur yn crynhoi tystiolaeth a all fod o ddiddordeb i'r Pwyllgor, yn codi o ddeunydd a gyhoeddwyd o'r blaen gan Swyddfa Archwilio Cymru. Mae hefyd yn cynnwys cyfeiriadau at beth gwaith perthnasol iawn sydd wedi ei gyhoeddi eisoes, neu waith sydd wrthi'n cael ei wneud, gan sefydliadau eraill gan gynnwys Swyddfa Archwilio'r Alban a'r Swyddfa Archwilio Genedlaethol.

Fel y dengys profiad yng Nghymru a mannau eraill, mae pob rhaglen gyllid cyhoeddus-preifat yn cario'r her o gydbwyso gwerth da am arian i'r sector cyhoeddus gyda darparu digon o gymhelliant i wneud y model yn ddeniadol i fuddsoddiad preifat.

Rwyf yn deall bod gan y Pwyllgor ddiddordeb arbennig ym Model Buddsoddi Cydfuddiannol newydd Llywodraeth Cymru. Gyda golwg ar hynny, rydym yn bwriadu cynnal peth gwaith archwilio dilynol ar raglen ysgolion yr unfed ganrif ar hugain ac addysg, unwaith y bydd Band B wedi ei ddatblygu ymhellach, ac mae hyn felly yn debygol o ddigwydd yn 2021-22. Wrth ymgymryd â'r gwaith hwnnw, byddem yn disgwyl ystyried i ba raddau, a sut, y mae'r Model Buddsoddi Cydfuddiannol wedi cael ei ddefnyddio'n ymarferol.

Yn fwy cyffredinol, mae yna gorff helaeth o waith archwilio blaenorol (yn fwyaf nodedig gan y Swyddfa Archwilio Genedlaethol) sy'n tynnu sylw at rai o'r heriau posibl a'r peryglon a ddaw drwy fodelau cyllid cyfalaf gwahanol. Dengys gwersi profiad, pan ddaw hi'n fater o sicrhau gwerth am arian, fod y peryglon i'w gweld ym manylion y modd y mae contractau perthnasol ar gyfer prosiectau yn cael eu sefydlu a'u rheoli.

Mae trosglwyddiad balans y risg yn neilltuol o bwysig ac mae’n hanfodol bod swyddogion yn amgyffred hyn yn dda - nid yn unig o ran deall y sefyllfa ar ddechrau contract tymor hir ond hefyd wrth i’r balans o rannu risg esblygu yn ystod oes y contract. Yn rhy aml yn y gorffennol, mae’r sector cyhoeddus wedi darganfod, mewn ffordd gostus, fod risgiau y tybid eu bod wedi cael eu trosglwyddo ar y dechrau i gyllidwr allanol mewn gwirionedd wedi troi’n ôl i’r trethdalwr yn ddiweddarach ar ôl i’r prosiect fynd i drafferthion. Mae sicrhau bod darpariaethau contract yn ddigon tynn i sefyll i fyny i her, pan fydd y risgiau hynny’n dod yn realiti, hefyd wedi troi allan i fod yn anodd iawn.

Mae fy nghydweithwyr a minnau yn barod i barhau i gynorthwyo’r Pwyllgor yn ei ymchwiliad, a gobeithiaf fod y dystiolaeth ysgrifenedig hon o gymorth i chi.

Yn gywir

ADRIAN CROMPTON
Archwilydd Cyffredinol Cymru

Amg: Ymchwiliad y Pwyllgor Cyllid – ffynonellau cyllid cyfalaf Llywodraeth Cymru

Dyddiad cyhoeddi: 23 Ebrill 2019

Ymchwiliad y Pwyllgor Cyllid

Ffynonellau Cyllid Cyfalaf Llywodraeth Cymru

Cyflwyniad

1 Yng nghyd-destun maes gorchwyl yr ymchwiliad hwn, mae'r papur yma'n tynnu sylw at dystiolaeth, a all fod o ddiddordeb i'r Pwyllgor, yn codi o ddeunydd a gyhoeddwyd gan Swyddfa Archwilio Cymru. Mae hefyd yn cyfeirio at beth gwaith perthnasol a gyhoeddwyd neu sydd wrthi'n cael ei gyflawni gan sefydliadau eraill. At hynny, gwyddom fod gan Swyddfa Archwilio'r Alban archwiliad yn mynd rhagddo sy'n edrych ar ariannu refeniw asedau, yn benodol y modelau Dosbarthu a Chanolfannau Heb Elw. Mae manylion y cynlluniau a'r amseriad ar gyfer y gwaith hwn ar gael ar wefan *Audit Scotland*.

2 Bydd ein gwaith wrth archwilio datganiadau ariannol cyrff cyhoeddus yn ceisio sicrhau bod cyfrif priodol wedi ei roi am drefniadau cyllido cyfalaf gwahanol, ynghyd â datgeliad addas o asedau, cyfrifoldebau a digwyddiadau annisgwyl, fel bod eu cyfrifon blynyddol yn rhoi 'darlun cywir a theg'. Er hynny, hyd yma, cyfyngedig fu ymdriniaeth ein gwaith archwilio â'r ffordd y mae modelau cyllido gwahanol yn cael eu cymhwyso'n ymarferol. Y rheswm am hyn yw bod rhai o'r modelau hyn (gan gynnwys y Model Buddsoddi Cydfuddiannol) yn newydd neu ond megis dechrau dod i'r amlwg, a'r ffaith mai dim ond i raddau cyfyngedig y mae Cymru wedi defnyddio modelau Menter Cyllid Cyhoeddus (PPI) a Phartneriaeth Cyhoeddus-Preifat (PPP) sydd wedi eu defnyddio'n helaeth yn Lloegr.

3 Ym mis Gorffennaf 2018, fe wnaethom gyhoeddi ein Canllaw i Gyllid Cyhoeddus Cymru. Roedd y canllaw hwn yn esbonio beth oedd prif ffynonellau cyllid ar gyfer y gwasanaethau cyhoeddus yng Nghymru ac yn disgrifio'r prosesau ar gyfer gwneud penderfyniadau cyllidebol ar draws y prif gyrff datganoledig yng Nghymru. Edrychai hefyd ar rai o'r ffactorau allweddol y mae cyrff cyhoeddus yn eu hystyried wrth wneud eu cynlluniau ariannol.

4 Cyfeiriai'r Canllaw at adroddiad Gorffennaf 2012 gan y Pwyllgor Cyllid yn y pedwerydd Cynulliad ar Pwerau Benthyg a Dulliau Arloesol o Ddefnyddio Arian Cyfalaf[1]. Er bod y tirlun wedi symud ymlaen, mae'r adroddiad hwnnw a llawer o'r dystiolaeth a dderbyniodd y Pwyllgor hwnnw yn parhau'n berthnasol yng nghyd-destun yr ymchwiliad diweddaraf hwn. Yn wir, deallwn fod y Model Buddsoddi Cydfuddiannol ei hun wedi codi o waith yr ymgymerodd Llywodraeth Cymru ag ef mewn ymateb i un o argymhellion y Pwyllgor

[1] Roedd y Pwyllgor Cyllid yn y trydydd Cynulliad hefyd wedi adrodd ym mis Medi 2008 ar ei Ymchwiliad i Bartneriaethau Cyhoeddus-Preifat.

hwnnw, i ystyried modelau ar gyfer ariannu refeniw buddsoddi mewn seilwaith, gan gynnwys y model Dosbarthu Heb Elw a gafodd ei lansio gan Lywodraeth yr Alban yn 2007. Roedd ein hadroddiad Darlun o Wasanaethau Cyhoeddus ym mis Hydref 2011 wedi nodi bod dosbarthu heb elw yn un o nifer o ffynonellau cyllid posibl ar gyfer buddsoddi mewn seilwaith yng nghyd-destun toriadau mewn cyllid cyfalaf.

5 Fe wnaeth Pwyllgor Cyllid 2012 hefyd gydnabod mai'r hyn sydd wrth wraidd ystyried a chymhwyso unrhyw fodelau cyllido cyfalaf yw'r angen i sicrhau bod rheolaeth gadarn ar asedau ar draws y sector cyhoeddus, a hynny'n cael ei gefnogi drwy ddatblygu'r sgiliau a'r galluoedd perthnasol.

Y Model Buddsoddi Cydfuddiannol a Rhaglen Ysgolion yr Unfed Ganrif ar Hugain ac Addysg.

6 Ym mis Mai 2017, fe wnaethom gyhoeddi ein hadroddiad ar Raglen Ysgolion yr Unfed Ganrif ar Hugain ac Addysg. Fe wnaethom nodi'r defnydd cynlluniedig o'r Model Buddsoddi Cydfuddiannol i ddylunio, adeiladu, ariannu a rheoli ysgolion newydd[2]. Ar adeg ein hadroddiad, nid oedd Llywodraeth Cymru wedi cadarnhau ei chynlluniau cyllido ac roedd awydd awdurdodau lleol i fabwysiadu'r Model yn dal yn aneglur. Fodd bynnag, dywedodd llawer o gynghorau wrthym eu bod yn cael trafferth i ddod o hyd i'r cyllid i ddal i fuddsoddi mewn ysgolion. Roedd Cynghorau wedi cynyddu eu benthyciad yn sylweddol eisoes ac wedi gwerthu asedau i gyllido eu cyfraniad i Fand A y rhaglen.

7 Nododd ein hadroddiad y byddai angen trefniadau llywodraethu newydd, yn enwedig o gwmpas y Model Buddsoddi Cydfuddiannol cyhoeddus-preifat, ar gyfer band B. Nodasom y byddai angen i Lywodraeth Cymru ddarparu cefnogaeth ganolog i'r broses gaffael ar gyfer unrhyw gyllid preifat ar gyfer y rhaglen a gallu sicrhau bod y rhaglen yn cyd-fynd â rhaglenni eraill a gyllidir drwy'r Model Buddsoddi Cydfuddiannol yn ogystal â mentrau cyllid preifat ehangach Llywodraeth Cymru.

8 Fe wnaeth ein hadroddiad gydnabod bod yna nifer o feysydd o wahaniaeth rhwng y Model Buddsoddi Cydfuddiannol a'r Fenter Cyllid Preifat, y mae Llywodraeth Cymru yn bwriadu iddynt hybu lles y cyhoedd, cynyddu tryloywder, a gwella gwerth am arian. Deallwn fod y Pwyllgor eisoes wedi derbyn gwybodaeth dechnegol am y Model, ond roeddem ni wedi amlinellu'r gwahaniaethau hyn ar adeg ein hadroddiad fel a ganlyn:

- Gall Llywodraeth Cymru fuddsoddi yn y cwmni a gaiff ei greu i ddylunio, adeiladu, cyllido a chynnal yr ased. Mae hyn yn sicrhau bod y sector cyhoeddus yn cael rhan o elw cwmni'r prosiect;

[2] Fe wnaethom nodi hefyd fod Llywodraeth Cymru yn wreiddiol wedi bwriadu mabwysiadu'r Model Dosbarthu Heb Elw, a ddefnyddiwyd gan Lywodraeth yr Alban ond bod y model hwnnw wedi wynebu heriau yn dilyn dyfarniad y Swyddfa Ystadegau Gwladol na ellid cyfrif rhai o'r prosiectau a gyllidid drwy'r model fel pe baent oddi ar y fantolen.

- Gall Llywodraeth Cymru benodi cyfarwyddwr i Fwrdd y cwmni a ffurfir i gyflawni'r prosiect, gan roi mwy o lais yn y broses o wneud penderfyniadau a bod yn fwy gweladwy; a
- Telir am y gwasanaeth drwy dâl refeniw misol dros gyfnod o 25 mlynedd ac ni fydd yn cychwyn nes y bydd y cyfleusterau wedi eu hadeiladu ac yn barod i'w defnyddio.

9 Fe wnaethom egluro yn ein hadroddiad y bydd cyflwyno ffurf ar gyllid cyhoeddus-preifat o reidrwydd yn dod â risgiau newydd i'r rhaglen, y bydd angen i Lywodraeth Cymru eu rheoli'n ofalus wrth iddi symud i Fand B. Ystyriem nad oedd y Model yn debygol o fod yn addas ar gyfer pob prosiect yn y rhaglen, gan gynnwys prosiectau ailddodrefnu neu brosiectau pwrpasol, y rheiny sy'n debygol o arwain at ymgynghoriadau maith a chymhleth, lle mae yna broblemau cymhleth ynghylch perchnogaeth tir neu os oes yna ryw amheuaeth ynghylch y galw am leoedd yn y tymor hir. Nid oedd yn glir inni ychwaith a allai ysgolion gwirfoddol a gynorthwyir gymryd rhan mewn rhaglen a gyllidid drwy refeniw. Ac, fel y mae profiad yng Nghymru a mannau eraill yn dangos, mae pob rhaglen gyllid cyhoeddus-preifat yn cario'r her o gydbwyso gwerth da am arian i'r sector cyhoeddus gyda darparu digon o gymhelliant i wneud y model yn ddeniadol i fuddsoddiad preifat. Nodasom yn ogystal y byddai'r Model yn gofyn am rai newidiadau yn y dull caffael, na fyddent yn boblogaidd efallai, nac yn ddichonadwy hyd yn oed, i rai cynghorau.

10 Rydym wedi cefnogi'r Pwyllgor Cyfrifon Cyhoeddus (PCC) yn ei ystyriaeth o'r materion oedd yn codi o'n hadroddiad yng nghanol 2018 ac ers hynny. Mewn tystiolaeth ysgrifenedig yn dilyn sesiwn o dystiolaeth lafar ar 25 Mehefin 2018, rhoddodd Llywodraeth Cymru sylwebaeth bellach ar faterion a godwyd gan y Pwyllgor gyda golwg ar y Model Buddsoddi Cydfuddiannol, gan gynnwys y camau diogelu a fyddai yn eu lle i sicrhau safonau adeiladu o ansawdd uchel ar gyfer adeiladau ysgolion yng ngoleuni problemau oedd wedi codi yn yr Alban.

11 Ysgrifennodd y PCC wedyn at Lywodraeth Cymru, yn nodi bod ganddo bryderon a oedd y Model Buddsoddi Cydfuddiannol yn cynrychioli'r gwerth gorau a chymryd popeth i ystyriaeth. Tynnodd y PCC sylw at y ffaith fod y dystiolaeth lafar gan Golegau Cymru a CLlLC hefyd yn awgrymu nad oedd y Model yn ddelfrydol ac y byddai'n well ganddynt ddewisiadau eraill. Fodd bynnag, fe wnaeth peth tystiolaeth ysgrifenedig ddiweddarach gan CLlLC gydnabod manteision posibl y Model. Fe wnaeth y PCC hefyd ofyn am sicrwydd ynghylch amrywiol faterion eraill, gan gynnwys rhai penodol i'r Model:

- Bod dewisiadau gwahanol - benthyca cyfalaf a benthyca â chefnogaeth - wedi cael eu disbyddu.
- Bod Llywodraeth Cymru, yn ei chyfanrwydd, wedi nodi mai'r rhaglen adeiladu ysgolion yw'r rhaglen fwyaf priodol ar gyfer defnyddio'r Model.
- Bod yna adeg 'saib ac adolygu' addas i ystyried a yw'r Model yn ei holl agweddau yn ddull gwerth am arian da o adeiladu ysgolion a cholegau.

12 At hynny, roedd CLLC wedi awgrymu y byddai contractau'r Model Buddsoddi Cydfuddiannol yn ystyried trosglwyddo i'r sector preifat y risgiau oedd yn gysylltiedig ag agwedd effeithlonrwydd ynni ar ddyluniad yr adeiladau. Gofynnodd y PCC felly i Lywodraeth Cymru egluro sut y mae'n disgwyl i'r trosglwyddiad risg yna weithio.

13 Ymatebodd Llywodraeth Cymru i'r pryderon hynny mewn tystiolaeth ysgrifenedig ym mis Awst 2018 a rhoddodd ddiweddariad ysgrifenedig pellach tua diwedd Chwefror 2019. Amlinellai diweddariad mis Chwefror 2019 y newidiadau yn y graddau o ymyriad ar gyfer prosiectau a gefnogir gan y Model ac fel arall. Mae'r newidiadau hynny wedi cau'r bwlch rhwng y graddau o ymyriadau ar gyfer prosiectau gwahanol, a all fod yn dylanwadu ar awydd awdurdodau lleol a sefydliadau addysg bellach am y Model[3].

14 Efallai y bydd y Pwyllgor yn dymuno edrych i mewn i faterion sy'n codi o dystiolaeth ysgrifenedig Llywodraeth Cymru i'r PCC fel rhan o'i ymchwiliad. Rydym yn bwriadu cynnal peth gwaith dilynol ar raglen ysgolion yr unfed ganrif ar hugain ac addysg unwaith y bydd Band B wedi ei ddatblygu ymhellach, ond efallai na fydd hyn tan 2021-2022. Byddem yn disgwyl ystyried i ba raddau, a sut, y mae'r Model Buddsoddi Cydfuddiannol wedi cael ei ddefnyddio'n ymarferol fel rhan o'r gwaith hwnnw.

Y Model Buddsoddi Cydfuddiannol - prosiectau ffyrdd a Chanolfan Ganser Felindre

15 Rydym wedi nodi adroddiad mis Hydref 2018 gan Bwyllgor yr Economi, Seilwaith a Sgiliau ar Cyflwr Ffyrdd yng Nghymru a'i sylwebaeth a'i argymhellion ar y Model Buddsoddi Cydfuddiannol. Gwyddom am gynlluniau Llywodraeth Cymru i ddefnyddio'r Model ar gyfer adrannau 5 a 6 o gynllun yr A465 (Top Dowlais i Hirwaun). Buom yn edrych i mewn i brosiect yr A465 yn ddiweddar oherwydd ei fod wedi mynd dros y gost a thros yr amser ar adran 2 y cynllun (Cilwern i Frynmawr). Nid oes gennym gynlluniau ar hyn o bryd ar gyfer gwaith gwerth am arian ar yr adrannau sy'n weddill o'r cynllun.

16 Gyda golwg ar brosiect Canolfan Ganser Felindre (lle mae'r gwaith adeiladu eto i ddechrau ar y safle), rydym ar hyn o bryd yn trafod gyda swyddogion ariannol yn Ymddiriedolaeth GIG Felindre er mwyn deall sut y bwriedir i'r Model Buddsoddi Cydfuddiannol ar gyfer yr ysbyty newydd weithio a bydd angen i ni gadarnhau'r trefniadau cyfrifyddu maes o law. Fodd bynnag, nid oes gennym gynlluniau ar hyn o bryd ar gyfer gwaith gwerth am arian ar y prosiect.

[3] Cynnydd o 50% i 65% ar gyfer yr holl brosiectau ysgolion a cholegau prif-lif a gyllidir â chyfalaf; cynnydd o 50% i 75% ar gyfer ysgolion arbennig ac unedau atgyfeirio disgyblion a gyllidir â chyfalaf; cynnydd o 75% i 81% ar gyfer prosiectau Model Buddsoddi Cydfuddiannol.

Tystiolaeth archwilio ddiweddar arall a all fod yn berthnasol wrth ystyried ffynonellau cyllid cyfalaf

17 Mae ein gwaith ar reoli gwastraff yng Nghymru wedi tynnu sylw at esiampl trefniadau menter cyllido preifat a wnaed gan Gyngor Bwrdeistref Sirol Wrecsam. Nododd ein hadroddiad Hydref 2018 ar Caffael Capasiti Trin Gwastraff Gweddilliol a Gwastraff Bwyd nad oedd y Cyngor wedi cymryd rhan yn Rhaglen Gaffael Seilwaith Gwastraff Llywodraeth Cymru. Er na wnaethom edrych ar fanylion trefniadau'r Cyngor, nododd ein hadroddiad fod trefniadau'r Fenter Cyllido Preifat yn cynnwys darparu cyfleuster Triniaeth Fiolegol Fecanyddol ar gyfer gwastraff gweddilliol gyda chapasiti o 55,000 tunnell y flwyddyn. Dechreuodd y cyfleuster weithio a chymryd gwastraff y Cyngor ym mis Gorffennaf 2015, a daw y contract i ben ym mis Mawrth 2038. Fe wnaethom nodi bod ffioedd y giât i gyfleuster trin gwastraff gweddilliol Wrecsam yn fwy na dwbl cost ganolrifol prosiectau gwastraff gweddilliol dan y Rhaglen Gaffael Seilwaith Gwastraff[4].

18 Yn fwy cyffredinol, efallai y bydd gan y Pwyllgor ddiddordeb yn y trefniadau contract a sefydlwyd drwy'r Rhaglen Gaffael Seilwaith Gwastraff. Nodasom fod chwech allan o'r deg prosiect dan y Rhaglen ar gyfer contractau gwasanaeth am gapasiti trin gwastraff lle mae darparwyr sector preifat wedi adeiladu cyfleusterau ar eu traul a'u risg eu hunain (er mai ymrwymiadau contract gwasanaeth tymor hir gan awdurdodau lleol efallai a roddodd yr hyder iddynt wneud hynny). Roedd y pedwar prosiect oedd yn weddill (tri gwastraff bwyd ac un gwastraff gweddilliol) yn cynnwys adeiladu cyfleuster, y byddai awdurdodau lleol oedd yn bartneriaid yn talu'n rhannol amdano dros gyfnod y contract fel rhan o ffioedd y giât. Yn y pedwar achos hynny, bydd y cyfleuster yn newid yn ôl i berchnogaeth yr awdurdod lleol ar ddiwedd y contract. Darparodd Llywodraeth Cymru gyfraniadau cyfalaf hyd at gyfanswm o £3.5 miliwn ar gyfer y tri phrosiect gwastraff bwyd. Gwnaethom argymhelliad yn ein hadroddiad bod cefnogaeth rheoli contract yn cael ei darparu'n barhaus i awdurdodau lleol.

19 Nododd ein hadroddiad ym mis Gorffennaf 2016 ar Rheoli Perygl Erydu Arfordirol a Llifogydd yng Nghymru fod Llywodraeth Cymru wedi nodi cyllid ychwanegol ar gyfer amddiffyn yr arfordir – drwy ddatblygu Rhaglen Rheoli Risg Arfordirol 2018-2021 – ond heb ddatblygu strategaeth gyllido tymor hir y tu hwnt i 2020-21 na chynorthwyo cynghorau i sicrhau dewisiadau o gyllid allanol, gan gynnwys, er enghraifft, ardollau a chyllid partneriaeth gydag, er enghraifft, sefydliadau yn y sector preifat a fyddai'n elwa o'r cynlluniau. Nodasom fod rhai rhanddeiliaid wedi codi pryderon nad oedd Llywodraeth Cymru wedi edrych i mewn i'r holl ddewisiadau oedd ar gael i gyllido rheoli risg llifogydd arfordirol. Ymhlith pethau eraill, fe wnaethom argymell y dylai Llywodraeth Cymru ddatblygu strategaeth i nodi cyllid tymor hir ar gyfer amddiffyn yr arfordir gan gynnwys cyllid gan adrannau ar draws y llywodraeth a chyrff allanol, ac yn arbennig i sicrhau

[4] Fe wnaeth ein hadroddiad ym mis Tachwedd 2018 ar Ailgylchu Trefol hefyd nodi bod contract y Fenter Cyllido Preifat yn ffactor yn y costau cymharol uchel a adroddwyd gan y Cyngor am gasgliadau nwyddau sych ger y pafin i'w hailgylchu a hefyd ei wasanaethau gwastraff cartref cyffredinol.

buddion lluosog. Fe wnaethom awgrymu bod Llywodraeth Cymru yn dysgu oddi wrth y model partneriaeth o gyllido yn Lloegr er mwyn deall sut yr oedd cynghorau yno wedi gallu denu cyllid allanol ar gyfer prosiectau.

Ystyriaethau cyffredinol eraill

20 Fel y crybwyllodd y Pwyllgor Cyllid yn y pedwerydd Cynulliad yn ei adroddiad, mae'n bwysig bod penderfyniadau ynghylch modelau cyllido yn seiliedig ar drefniadau rheoli asedau cadarn. Rydym wedi nodi yn rhywfaint o'n gwaith diweddar enghreifftiau o welliannau mewn cynllunio cyfalaf gan gyrff cyhoeddus, er enghraifft yn ein hadroddiad ym mis Gorffennaf 2017 ar Gweithredu Deddf Cyllid y GIG (Cymru) 2014. Er hynny, mae'n amlwg bod angen i gyrff cyhoeddus o hyd, gan gynnwys GIG Cymru, wneud mwy i gynllunio ar gyfer y tymor hir ac rydym hefyd wedi tynnu sylw mewn gwaith blaenorol at y cyfyngiadau sy'n codi o orwelion cynllunio ariannol Llywodraeth Cymru ei hun. Bydd gwaith Comisiwn Seilwaith Cenedlaethol Cymru, a lansiwyd gan Lywodraeth Cymru ym mis Tachwedd 2018, hefyd yn awr yn rhan allweddol o'r broses o ganfod a chynllunio ar gyfer anghenion seilwaith Cymru yn y dyfodol.

21 Rhydd ein hadroddiad ar raglen ysgolion yr unfed ganrif ar hugain ac addysg enghraifft o fuddion posibl mabwysiadu agwedd dymor hir at gyllid cyfalaf. Gwelsom fod sicrwydd cyllid dros nifer o flynyddoedd yn galluogi cynghorau i symud i ffwrdd oddi wrth ddull 'trwsio a chlytio' i ddull mwy strategol o adnewyddu ac uwchraddio eu stadau ysgolion.

22 Er bod yna ystyriaethau penodol yng Nghymru, nid lleiaf oherwydd Deddf Llesiant Cenedlaethau'r Dyfodol (Cymru), mae rhai egwyddorion cyffredinol strategaethau cyfalaf a rhaglennu effeithiol eisoes wedi eu hegluro mewn arweiniad gan gyrff proffesiynol eraill. Er enghraifft, mae Sefydliad Siartredig Cyllid Cyhoeddus a Chyfrifyddu wedi creu arweiniad ar strategaethau cyfalaf a rhaglennu.

23 Fe wnaeth y Pwyllgor Cyllid yn y pedwerydd Cynulliad hefyd gyffwrdd â'r cwestiwn a oes gan gyrff cyhoeddus y capasiti/gallu cywir i ystyried a manteisio ar y cyfleoedd a ddarperir gan ystod o fodelau cyllido cynyddol amrywiol, gan gynnwys cyllid Bargen Dinas/Twf. Fel y dangoswyd mewn cyd-destun cysylltiedig drwy ein gwaith ar Caffael Cyhoeddus yng Nghymru, mae pryderon ynghylch capasiti/gallu ar draws y sector cyhoeddus, os yr un, yn fwy o broblem fyth yn awr gan fod cyni wedi dal i gael effaith.

24 Pa fodelau cyllido cyfalaf bynnag a ddefnyddir, dengys gwersi profiad yma ac mewn mannau eraill, pan ddaw hi'n fater o sicrhau gwerth am arian, bod y peryglon ym manylion y modd y mae contractau perthnasol ar gyfer prosiectau yn cael eu sefydlu a'u rheoli. Sonnir am y problemau hyn ym mheth o'r dystiolaeth a dderbyniodd Pwyllgor yr Economi, Seilwaith a Sgiliau yn ystod ei ymchwiliad i gyflwr ffyrdd ac yng nghasgliadau ac argymhellion ei adroddiad. Mae trosglwyddo balans y risg yn neilltuol o bwysig, yn ogystal â sicrhau bod darpariaethau cytundebau yn ddigon tynn i sefyll i fyny i her pan fydd y risgiau hynny yn dod yn realiti.

25 Mae llawer o'r egwyddorion a eglurodd Swyddfa Archwilio Cymru yn ei dogfennau fframwaith yn 2006[5], er eu bod wedi eu hysgrifennu yng nghyd-destun eu profiad o archwilio prosiectau Menter Cyllid Preifat, yn ymddangos yn berthnasol mewn termau mwy cyffredinol wrth ystyried dewisiadau ynghylch modelau cyllido ac elfennau ymarferol cyflawni prosiect. Yn 2015 fe gyhoeddodd y Swyddfa Archwilio Genedlaethol bapur briffio: 'Dewis o gyllid ar gyfer buddsoddi cyfalaf', sy'n rhoi trosolwg ddefnyddiol ar y pwnc. Yn fwy diweddar, mae'r Swyddfa Archwilio Genedlaethol hefyd wedi cyhoeddi briffiad ar resymeg, costau a manteision Menter Cyllid Preifat; ei ddefnydd a'i effaith; y gallu i wneud arbedion drwy gontractau gweithredol; a chyflwyno PF2.

26 Yn olaf, efallai y bydd gan y Pwyllgor ddiddordeb i wybod y byddwn yn datblygu gwaith archwilio lleol ar draws yr holl awdurdodau lleol ar destun cynaladwyedd ariannol. Bydd ein gwaith yn archwilio strategaeth ariannol tymor canol a thymor hir, rheoli cyllideb, pwysau costau, cynlluniau effeithlonrwydd ac arbedion, a lefelau cyllid wrth gefn a'r defnydd ohono. Disgwyliwn adrodd am ganfyddiadau'r gwaith hwnnw mewn rhyw ffordd ar lefel genedlaethol, unwaith y bydd y gwaith archwilio lleol wedi ei gwblhau.

Swyddfa Archwilio Cymru

Ebrill 2019

DIWEDD

[5] Ym mis Mai 2006, cyhoeddodd y Swyddfa Archwilio Genedlaethol Gyfrol 1 a Chyfrol 2 ei 'Fframwaith ar gyfer gwerthuso gweithrediad prosiectau Menter Cyllid Preifat'.