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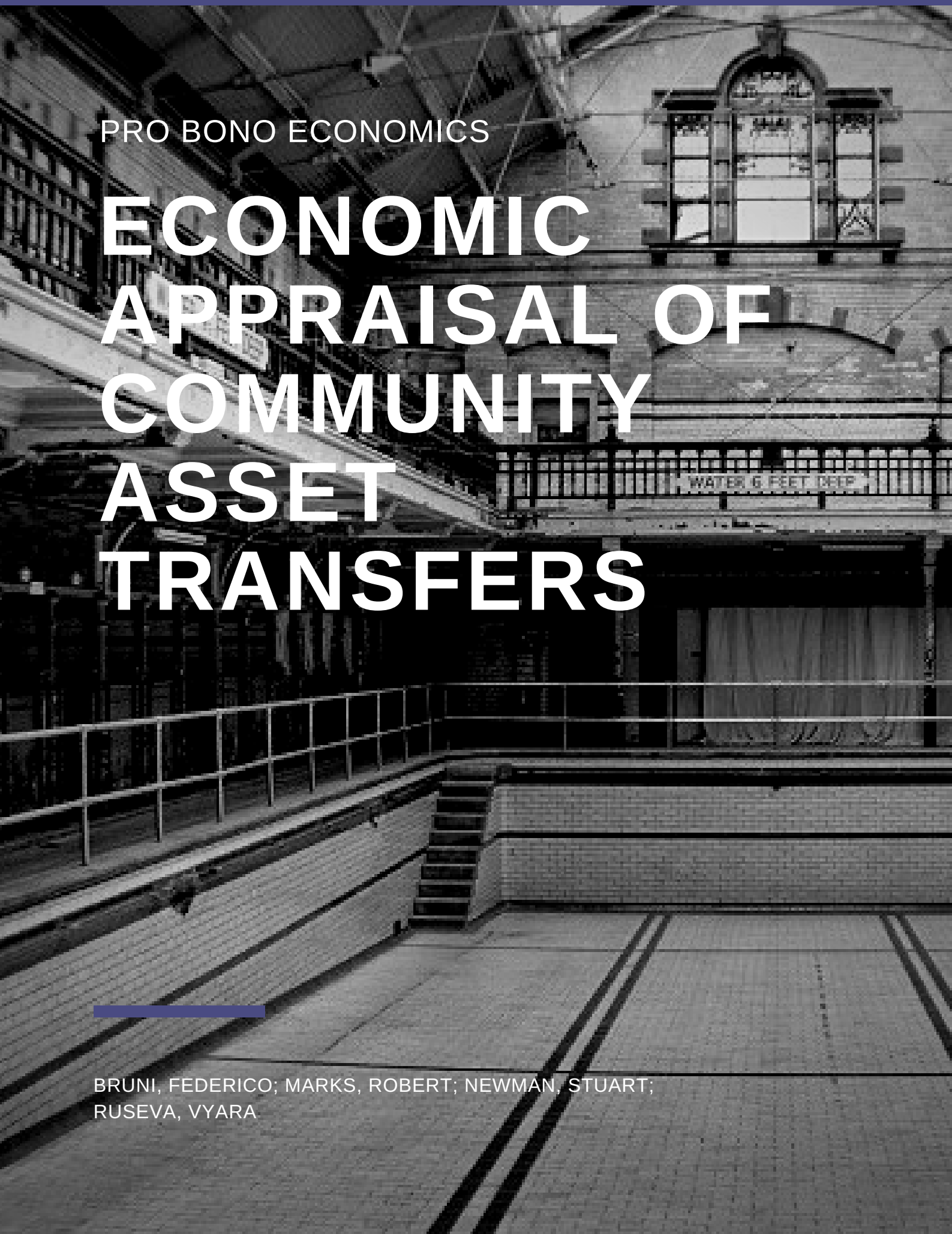

PRO BONO ECONOMICS

ECONOMIC APPRAISAL OF COMMUNITY ASSET TRANSFERS

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POWER TO CHANGE

Power to Change (PtC) is an independent trust, established in 2015 to support and develop community businesses across England.
It was set up in response to growing recognition of the challenges faced by communities in maintaining vibrant local places with access to shops and services, opportunities for employment and skill development, a strong local fabric and a sense of positive future.
Core to this is a recognition of community business as a new model for local change. All of PtC's programmes are directed to achieving this. The Power to Change Research Institute evaluates Power to Change programmes against these long-term outcomes.
Power to Change has been established as a ten-year initiative. Its aim is to accelerate the growth and impact of community business. Its ambition is to create better places through community business. Success at the end of these ten years would mean that community business is a better recognised and more highly-valued approach to addressing local economic, social and environmental challenges.

PRO BONO ECONOMICS

Pro Bono Economics (PBE) is a charity supporting third sector organisations in measuring performance, improving services and tracking outcomes
PBE seeks to improve the effectiveness of the charitable sector, in particular when evaluating the impact of its activities, and when presenting these results to an external audience. It also aims to provide a mechanism by which the economics profession can contribute to a well-functioning charitable sector, both as an end in itself and as part of professional development for economists.
Through PBE, economists offer their services free of charge to charities who request help, mainly addressing questions around measurement, results, impact and value. Many charities are without the tools to do this, or to do it sufficiently well to satisfy funders and the public.
As Power to Change aims to support community businesses, local authorities and other commissioning bodies in appraising, implementing and evaluating CATs, with a specific focus on social value, its values and its mission are aligned with those inspiring PBE's projects.
This is why PBE is proud and enthusiastic to support Power to Change's activity with this report and hopes to make an impactful contribution to the CAT environment with this product.

1. PURPOSE OF THIS GUIDE

Community Asset Transfers (CATs) have become a central part of the operating model of community businesses (i.e. businesses driven by a philosophy of community benefits, enterprise, inclusiveness and community control). CATs often play a crucial role in allowing community businesses to unlock economic and social benefits for service users and the community as a whole.

These benefits can be generated by a more innovative and effective use of the asset per se as well as by the services delivered in or through the asset transferred. In particular, community businesses are often recognised as the only type of organisation whose model can support the sustainable continuation of service provision (e.g. through mobilising volunteers, by developing innovative revenue generating activities or by having access to alternative sources of funding). Community businesses are often believed to be more effective at engaging people and delivering social outcomes than other types of organisation because they are close and directly accountable to their community.

At the time of writing, more than 60% of councils have a CAT policy in place, and more than 70% Has an up-to-date asset management strategy, to which community businesses can refer when expressing an interest in taking over a publicly owned asset in their local area (Gilbert, 2016). In 2014, LAs have reported more than £2.5bn of assets deemed surplus (Audit Commission, 2014). In 2017, NHSE reported £280m of surplus land (NHSE, 2017).

Not only do these trends indicate the potential of CATs in supporting local communities and the British economy as a whole, they also highlight the crucial role played by LAs and public organisations in ensuring that CATs deliver value for money, and in comparing the costs and the benefits delivered by specific CATs with alternative asset disposal options.

This brief guidance document aims to provide public authorities with clear, accessible and directly applicable guidelines in conducting economic appraisals of CATs. This guide cross-references and complements a more detailed report published by PBE on the economics of community asset transfers (PBE, 2017).

Section 2 defines CATs, relevant assets and social value, whilst section 3 outlines the key steps through which a public authority should go when appraising a CAT. Section 4 focuses on different ways to estimate the costs of CATs and section 5 on various methodology to appraise their benefits. Section 6 outlines how to account for risk, optimism and time whilst section 6 concludes.

2. DEFINITIONS

COMMUNITY ASSET TRANSFER

A CAT involves the transfer of the ownership and/or the management of an asset (typically public land or buildings) from its public sector owner (usually a local authority or a clinical commissioning group) to a community organisation (often a community business) for less than market value, in order to achieve social, economic or environmental outcomes in the community in which the asset is located.

SOCIAL VALUE

Social value can be defined as the wider social, economic, community or environmental benefits delivered by an intervention. At the time of writing, 24% of LAs have a social value policy, and 33% actively use social value when procuring or commissioning (PBE, 2017, p.35).

The General Disposal Consent Order (2003) introduced the requirement for local authorities to consider social value when justifying any under-value asset transfer, but removed the requirement to seek consent for the disposal of land at under-value (up to £2,000,000 or less) when the authority considers it “will help it to secure the promotion or improvement of the economic, social or environmental well-being of its area” (General Disposable Consent Order, 2003).

The Social Value Act (2012) made a further step in the direction of embedding social value in the decision making process of public authorities by introducing the requirement for commissioning bodies to think about social value, at the pre-procurement phase, for all services worth over £209,000.

In short, social value should be formally considered when appraising CATs transferring assets at under-value or services worth over £209,000. In general, policymakers at both a local and national level are increasingly considering social value regardless of whether it is mandatory by law. This is a cultural change triggered by innovative and impactful legislation that this guidance aims to support and strengthen.

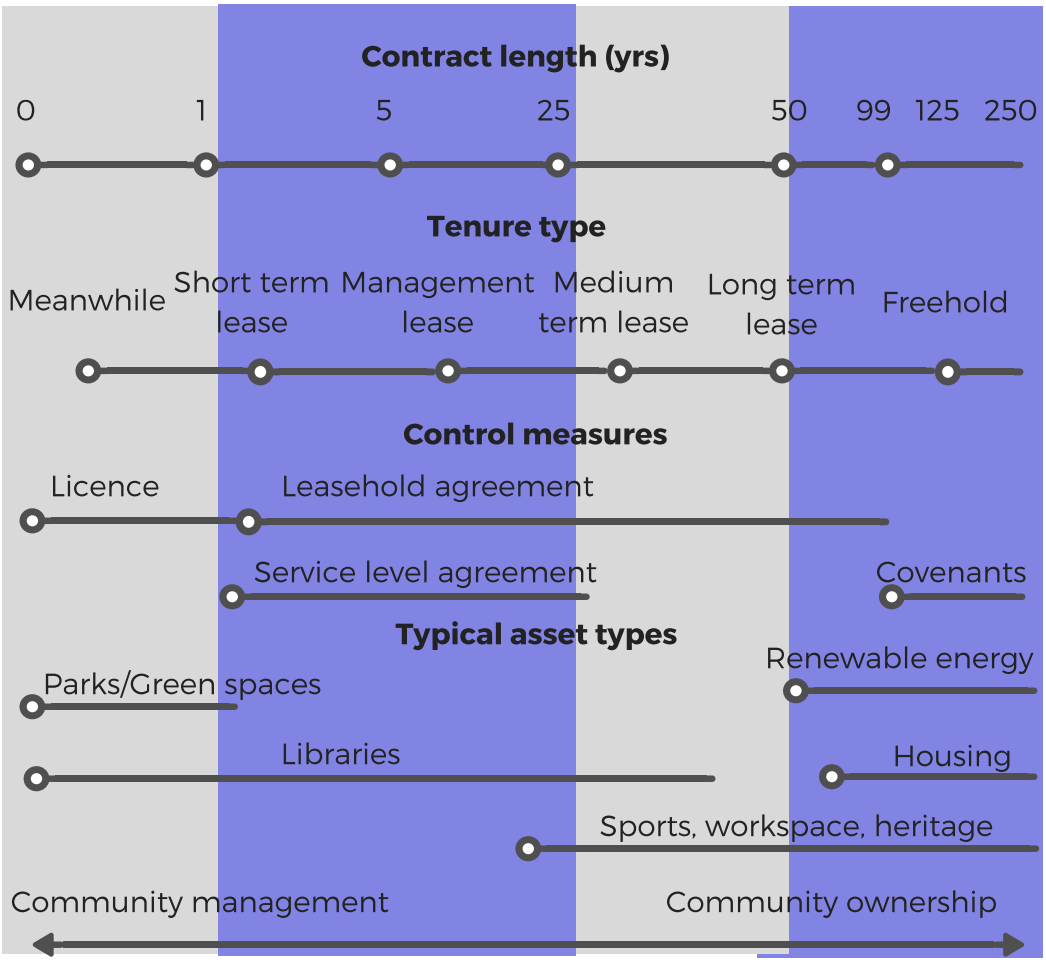
RELEVANT ASSET

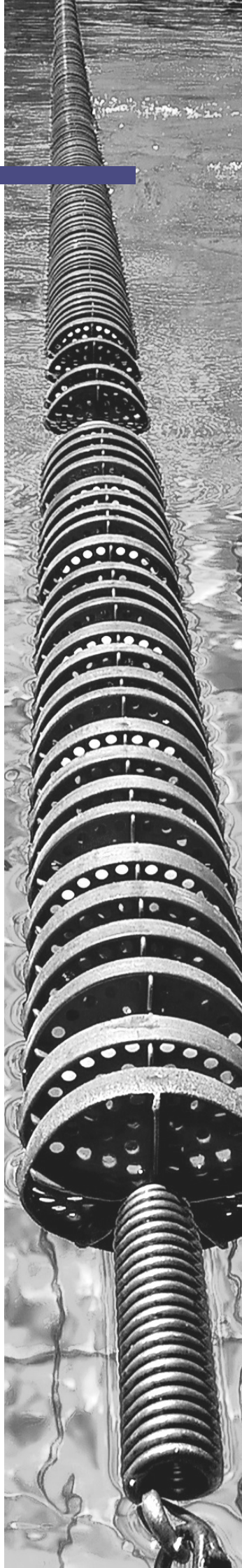
Although any type of asset can be transferred through a CAT, the assets most frequently involved in CATs are community centres, swimming pools, town halls, libraries and parks (Locality, 2017).

As shown by figure 1 below, community involvement in the ownership and management of an asset can take different forms. This guidance applies to the forms of community ownership outlined in the right-hand side of figure 1 below, namely medium and long term (25+ years) leasehold and freehold arrangements and to assets whose value is estimated to be above £1m.

The principles outlined in this guidance can be applied to less valuable assets and to less durable forms of community ownership, especially when these are seen as a 'stepping stone' towards a more long-term oriented agreement in the future (PBE, 2017, p.11).

FIGURE 1: Spectrum of asset types suitable for CAT depending on lease length and tenure types





3. ECONOMIC FRAMEWORK

A good economic framework provides a robust method for analysing projects and proposals and ensures that decisions have the best chance of promoting the public interest. The paragraphs below set out the key steps that every public authority should take in order to ensure that community asset transfers deliver good value for money for the community in which they are implemented and, ultimately, for the taxpayer (PBE, 2017, p.17).

RATIONALE FOR INTERVENTION

Community asset transfers are an investment in the community. This is the case even when CATs are not accompanied by a grant or by direct financial costs to the public authority, as the public authority is foregoing potential capital receipts or alternative uses of the assets. In other words, it is incurring an opportunity cost. As in all public investment proposals, decisions around CATs need to be underpinned by a credible economic rationale.

From an economic perspective, there are three main reasons why a public authority might want to consider CATs:
(1) to make existing services run more smoothly (allocative efficiency);
(2) to save money (technical efficiency);
(3) to distribute services or resources more fairly across society (equity).
Additionally, but no less importantly, CATs can be justified by expected positive impacts on people and organisations that are not directly involved in the asset transfers (positive externalities, directly related to the concept of social value).

The first step of a robust and credible economic appraisal of a CAT is to identify the rationale underpinning the transfer: the reason why the public authority is considering this specific form of investment in the community (PBE, 2017, p.18).

OBJECTIVES

The second step public authorities need to make is to accurately identify and clearly outline the objectives and scope of the CAT. In this context, it can be helpful to focus on four questions:

(1) What does the authority want to achieve (outcomes – high-level benefits to society, e.g. reduction in avoidable A&E admissions of elderly people living alone)?
(2) What actions are required to achieve these outcomes (outputs – steps on the way, e.g. community café for elderly individuals at high risk of fall)?

(3) What are the mechanisms through which these outputs are expected to translate into outcomes (e.g. giving old people a safe place to spend the time)?
(4) How can success be measured in this context (targets, e.g. % of preventable hospital admissions, number of people attending the community centre)?

These factors need to be Specific, Measurable, Achievable, Relevant, and Time-bound (SMART) and it is fundamental to be clear, transparent and credible about the expected causal links between outcomes and outputs (PBE, 2017, p.20).

OPTIONS AND COUNTERFACTUALS

Once objectives have been defined and outlined, a range of alternative options to manage and own the asset under analysis should be identified. In order to develop alternative options, a series of relevant factors characterising the transfer (e.g. timing of the transfer, length of the contract, extent to which the community is involved in the management of the asset) should be identified.

For each of these factors, different alternative options should be identified (e.g. 5, 25, 100 years; leasehold, freehold, rent) and ranked depending on the extent to which they contribute to the project's objectives.

The two to three combinations of alternative options for each factor that are most likely to meet the stated objectives should be shortlisted and analysed more in detail.

In this exercise it is essential to consider a low-impact option, in order to have a clear baseline from which to compare the costs and the benefits of different options (i.e. a counterfactual). A low-impact option can be a do nothing (i.e. take no action) or a do minimum option (i.e. low risk maintenance of current situation), depending on what is most viable. In other words, decision makers should continuously ask themselves: "what would happen in the absence of the CAT?" (PBE, 2017, p.22).

COSTS AND BENEFITS

Once a list of three to four options has been developed and agreed with key stakeholders, it is important to consider all the costs and benefits generated by each option, including a low-impact option. Appraisers should consider the effects these options are expected to have on all those affected by it (e.g. not just old frail people but also their families, the NHS, social care workers, etc.).

Costs and benefits should then be extrapolated across the life of the project for every financial year in which the project is expected to run. Costs can be subtracted from benefits to estimate the net value of the project, or benefits can be divided by the costs to create a benefit-to-cost ratio. The latter provides an estimate for the return on every pound spent, so anything above one is a worthwhile project in value for money terms.

Sections 4 and 5 of this report provide further guidance on how to assess costs and benefits.

EVALUATION AND MONITORING

Finally, after implementation, periodic reviews should be set up in order to monitor and evaluate whether the project is delivering outcomes in line with what forecasted in the appraisal process. Stakeholders will need to assess whether the objectives are still relevant, if they are being met, and where implementation of the project can be improved. These evaluations require the project to systematically collect data on financial performance and planned outcomes.

Stakeholders should ensure these data are accurately measuring the correct things by periodically reviewing key elements of the project. Furthermore, as new information about costs and benefits become available, these can be incorporated into the initial analysis to provide insights into the accuracy of the original analysis. This facilitates the analysis of new projects so that mistakes can be avoided in future (PBE, 2017, p.28).

4. COSTS

After having identified a group of three to four short-listed options, the first step appraisers should make is to list all the costs that each option is expected to generate. In the context of CATs, it is helpful to distinguish between costs to the public authority (e.g. maintenance of a library), costs to the public sector as a whole (e.g. a decrease in VAT receipts), costs to community businesses and other businesses (e.g. legal advice on the CAT) and costs to the economy as a whole (e.g. closure of a road or a park).

The sections below cover the four most important cost groups to account for when appraising a CAT. The most important factor is clearly the value of the asset under analysis (covered in the first sub-section), followed by one-off costs (costs that occur only once at the moment of the transfer), recurrent capital costs (costs generated by the asset per se recurring periodically) and recurrent revenue costs (costs generated by the operation of the asset recurring periodically), covered in the second, third and fourth sub-section, respectively.

ASSET VALUE

Because of the very nature of CATs, the most important part of a robust economic appraisal is the valuation of the asset under analysis. In this context, it is fundamental to focus on the market value of the asset and not on its book value, as it captures the actual cost of the CAT to the public authority, especially in the case of under-value transfers.

Market value can be defined as "the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm’s-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently, and without compulsion".

In contrast, the book value is the value of an asset as it appears on an organisation’s balance sheet and is typically based on the original cost of the asset less any depreciation, amortization or impairment costs made against the asset. Book value estimates should not be used in economic appraisals unless it has proven impossible to estimate the market value of the asset under analysis.

Timely and constructive engagement with stakeholders and market experts is fundamental in order to estimate the market value of the asset transferred to the community, especially in the case of under-value transfers.

More specifically, Circular 06/03 (Local Government Act 1972 general disposal consent (England) 2003) prescribes that the disposal of land for less than the best consideration that can reasonably be obtained (as is often the case in CATs) must be supported by a report prepared and signed by a qualified valuer (a member of the RICS).
In line with the Circular, an under-value asset transfer needs to refer to the unrestricted value of the asset: i.e. the market value plus any additional amount which is expected to be available from a special purchaser (e.g. a developer expecting to enjoy incremental economic benefits and synergies upon integration of the purchased asset with their own), ignoring the reduction in value caused by any voluntary condition imposed by the authority (e.g. planning restrictions determined by the authority and not by other public bodies).
In the case of leaseholds, the unrestricted value is the value of the authority's interest subject to the proposed or assumed lease. In other words, it will be the value of the right to receive the rent and other payments under the lease plus the value of the reversion when the lease expires.
Finally, a discount may be applied in connection with the consideration for either the grant of an option or the exercise of an option or where the value of the completed scheme is less than the development cost. For example, this might be used where there is low demand or high costs associated with land reclamation or decontamination.

ONE-OFF COSTS

Once the difference between the value of the CAT and the market value of the asset has been estimated, appraisers should focus on the other one-off costs associated with the CAT and the alternative options to which the CAT is being compared. These costs can be capital costs, e.g. refurbishments, re-configurations, health and safety adjustments, or revenue costs, e.g. legal fees, early termination of utility contracts, removal costs.

RECURRENT CAPITAL COSTS

Appraisers should then account for the different types of recurrent capital costs generated by the alternative options under analysis. These include maintenance, lifecycle, hard facilities management and other types of capital costs. In principle, a different management or ownership structure should not have a significant impact on these costs.

However, there are some circumstances in which community ownership might have an impact, e.g. LAs sometimes get better deals on utilities and maintenance due to economies of scale. Moreover, if the use of the asset is expected to change with the CAT, it is important to ensure that this change is adequately reflected in cost estimates.

RECURRENT REVENUE COSTS

Similarly, appraisers should account for the different types of recurrent revenue costs generated by the alternative options under analysis. These include staff, supplies, soft facilities management and other lines of expenditure specific to the nature of the organisation and the services under analysis.

Any recurrent cost, regardless of whether it is revenue or capital, should be adjusted for inflation in order to reflect the fact that prices tend to increase from one year to another. For capital costs, Tender Price Indexes should be used, for revenue costs Consumer or Retail Price Indexes.

5. BENEFITS

The three sub-sections below focus on the three main steps that a public authority needs to make to estimate the benefits delivered by a CAT. First, it should clearly identify the relevant benefits (first sub-section). Second, it should estimate the most tangible and measurable. Third it should attempt to estimate the value of less tangible and measurable outcomes.

RELEVANT BENEFITS

From the beginning of the appraisal process, it is fundamental to clearly distinguish between the benefits delivered by the CAT and those delivered by the services delivered in or through the asset transferred to the community.

This distinction is crucially important: failing to appropriately and accurately distinguish between these different types of benefit will make it impossible for the public authority to appraise whether the CAT under analysis delivers good value for money.
Public authorities should always establish, together with all stakeholders involved, whether the services provided by the community business could be delivered in a different asset or in the same asset under different ownership and management structures.

This exercise will generate three categories of benefits:

(1) benefits delivered solely by the community ownership of the asset (e.g. innovation and entrepreneurship generated by the involvement of the community in the ownership and management of the asset);
(2) benefits delivered by the services delivered in or through the asset and that would not be delivered under different ownership or management structures;
(3) benefits delivered by the services delivered in or through the asset and that would be delivered under different ownership or management structures.

Whilst (1) and (2) should be included in the analysis, (3) should be clearly identified and excluded from the analysis as it would significantly bias the result of the appraisal (PBE, 2017, p.14).
Community asset transfers can deliver different types of benefits. In this context, it is helpful to distinguish between tangible benefits and intangible benefits. The former group is composed of benefits that can be analysed and measured, whilst the latter refers to benefits that can be monitored and evaluated less readily (PBE, 2017, p.15).

TANGIBLE BENEFITS

Tangible benefits can have a fiscal value (i.e. costs or savings to the public sector - e.g. delivery of additional services or reduced health, police or education costs), an economic value (i.e. a net increase in earnings or growth in the local economy) and a social value (i.e. wider gains to society such as improvements to health; educational attainment; access to transport or public services; safety; or reduced crime).
In the context of CATs, tangible benefits include: training and employment opportunities, local income generation, reduced crime and vandalism, reduction in hospital admission rates, reduction in the incidence of depression, increased participation and use of assets and services.

The think-tank New Economy Manchester has developed a database bringing together more than 600 cost and benefit estimates derived from government reports and academic studies. They cover the public cost of crime, education & skills, employment & economy, fire, health, housing and social services (New Economy, 2015).

We recommend using this source to estimate tangible benefits of CATs (PBE, 2017, p.39). The data will be reviewed and updated on a regular basis by New Economy as new research and analysis is published. The current version was produced in March 2015 to incorporate updates to a number of documents from which the estimates are sourced.
Intangible benefits

INTANGIBLE BENEFITS

Community Asset Transfers are often expected to deliver benefits that cannot be directly quantified in monetary terms, such as: community empowerment, social inclusion, safeguarding of social services, social cohesion, strengthening of community networks, increased sense of belonging to the local community, enhanced heritage and cultural identity of the local area, stronger relationships of trust in the community, improved quality and user satisfaction, improved participation and use and increased local entrepreneurial activities.

In these instances, a methodology called three stages well-being valuation can be used. This approach draws heavily on HMT's Green Book and has been extensively applied in the context of social housing, in order to estimate the social value created by community investment programmes run by housing providers.

Whilst the econometric techniques underpinning this methodology are relatively complicated, the conceptual intuition behind this approach is very simple.

As shown in Figure 2 below (Fujiwara, 2013), this approach is composed of three steps and is based on responses to large national surveys (PBE, 2017, p.42).

FIGURE 2: GRAPHICAL REPRESENTATION OF 3 STAGES WELL-BEING VALUATION

The result of this 3-stage process is a list of monetary values attached to a variety of social outcomes and collected in a social value bank (HACT, 2016). The social value bank is linked to a series of surveys that can be administered by public authorities and community businesses to measure the impact of their interventions. It also contains a simple cost-benefit model that accounts for the impact that has not been caused by the CAT or by the community business but that would have happened anyhow (i.e. the counterfactual) (PBE, 2017, p.57).

6. OTHER ADJUSTMENTS

RISK AND UNCERTAINTY

Every investment decision intrinsically carries different types of risk. This is particularly the case in the context of public infrastructure and asset transfers, where projects can be delayed, end up being more complex than expected, go over budget, or get derailed by external pressures.

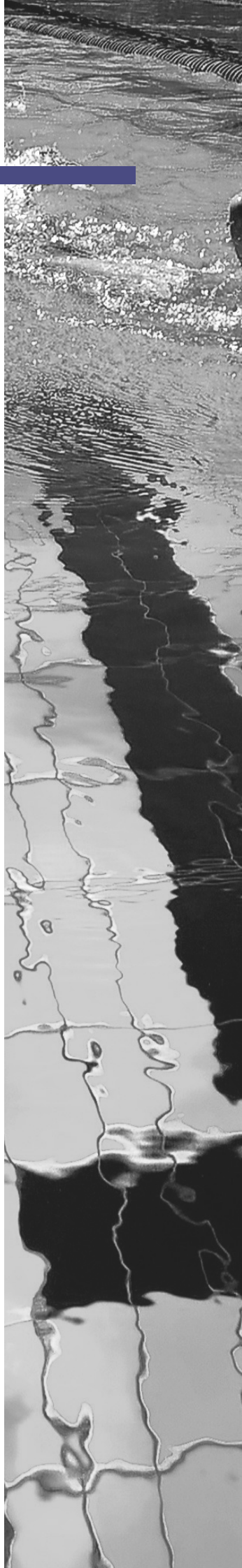
After having clearly defined the costs and benefits of different options, it is important to identify the risks intrinsic to these costs and benefits in order to manage and, where possible, mitigate them. The Treasury's Orange Book (2004) provides a simple framework for assessing risks by combining their expected impact and their likelihood of occurring. These two factors need to be discussed and agreed with stakeholders and decision makers in order to ensure that the vulnerability of the project to certain risks is clearly understood and tolerated by all parties involved.

Risk is caused by uncertainty. Uncertainty is not a problem per se, as long as it is properly understood and dealt with. For example, if a cost or a benefit is expected to be within a specific interval, it is important to show to decision makers what the final impact of the CAT would be under different scenarios defined by that interval.

DISCOUNTING AND OPTIMISM BIAS

In most Western societies, adults tend to have an intrinsic and consistent preference for present benefits compared to future benefits. In other words, we tend to prefer a £100 payment today to a £100 payment in a month. Discounting is a technique used to reflect this. The Treasury's Green Book recommends a discount rate of 3.5% per year – reducing the value of all cost and benefit estimates by 3.5% each subsequent year being assessed.

Similarly, there is a "demonstrated, systematic, tendency for project appraisers to be overly optimistic". In other words, appraisers tend to overstate the benefits and understate timings and costs of most projects. Again, optimism bias is a technique used to reflect this aspect of modern societies. The Treasury's Green Book recommends an uplift to the costs of standard building projects of an average of 13% and work duration by an average of 2.5%.



6. CONCLUSIONS

When considering the opportunities offered by CATs, we recommend that the sector strengthens its focus on evidence and analysis. This is so that public authorities can make evidence-based decisions on how to allocate assets efficiently and effectively to enterprises capable of delivering the best value to local communities.

To support these decisions, we propose a structured economic assessment framework that clearly defines the objectives of the CAT, transparently identifies different options for the use of the asset, and rigorously assesses the costs and the benefits associated with each of these options. The framework provides a robust method to ensure that decisions have the best chance of promoting the public interest.

In synthesis, the assessment framework that we propose recommends that public authorities and community businesses apply the following framework:

Foster the development of constructive, open and transparent relationships at the beginning of the CAT process.

Research the context in which the CAT will operate and identify a rationale underpinning the transfer.

Outline the scope of the project, think about desired outcomes, necessary actions to meet objectives and targets to measure success. These targets should be SMART and consider constraints and dependencies.

Create a comprehensive list of alternative options, eliminating unviable options and those that fail to meet the SMART objectives, to create a shortlist of preferred options.

Always consider a ‘do minimum’ and/or a ‘do nothing’ scenario accounting for what would happen in the absence of the CAT. This is to provide a benchmark for appraisal.

Create a list of everyone affected by the project, list all of the costs and benefits that will impact them, attempt to estimate a monetary value for each one, and adjust them for time (discounting), risk and optimism bias.

Compare cost to benefits ratios across different options and identify the option that delivers more value for money to the local community and the taxpayer.

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