Inquiry into the Pricing of Public Passenger Transport Services

Final Report

INDEPENDENT PRICING AND REGULATORY TRIBUNAL
OF NEW SOUTH WALES

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Final Report

Review Report 1996/10

October 1996

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The Tribunal released the following interim reports for this review. Copies of the reports are available from the Tribunal's office.

Interim Report No 1	*Government Payments for Public Transport*
Interim Report No 2	*Buses and Ferries*
Interim Report No 3	*CityRail*
Interim Report No 4	*Fare Structures*
Interim Report No 5	*Framework for Public Transport Pricing*
Interim Report No 6	*Fair Fares: An Overview*

The Tribunal has released the following research papers. Copies of these reports are available from the Tribunal's Office

Research Paper No 4	*Road Pricing: Finding the Problem*
Research Paper No 6	*Fares and Ticketing Policies and Practices: International Review*
Research Paper No 7	*Estimation of Public Transport Fare Elasticities in the Sydney Region*

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Foreword

The Independent Pricing and Regulatory Tribunal's major inquiry into urban public passenger transport services has involved a comprehensive program of research and public consultations over the last year. The Tribunal issued six Interim Reports in March 1996, and has benefited from a range of comments and submissions from transport operators, various government departments, community interest groups and members of the public. Following the release of the Interim Reports a second round of public hearings was held.

Complementing this review, the Tribunal is currently conducting a review of pricing principles and the operation of the Countrylink services of the State Rail Authority. This review follows a reference from the Premier under Section 12A of the Independent Pricing and Regulatory Tribunal Act.

This Final Report condenses into one volume the Tribunal's final thinking and recommendations arising out of this process. However, this report does not attempt to summarise all of the material contained in the Interim Reports. The Tribunal considers that much of the information and the general thrust of the conclusions and recommendations in the Interim Reports remain valid. This Report also takes into account the Tribunal's Determination of maximum public transport fares to be charged by CityRail and the State Transit Authority from 7 July 1996.

The Tribunal has refined its thinking in some area, and this Final Report confirms the Tribunal's proposed approach and major recommendations with respect to public passenger transport in the State.

This report sets out the Tribunal's assessment on a range of matters that are relevant to the delivery of urban passenger public transport services in New South Wales. The Tribunal has detailed an approach it intends to follow over the coming years in setting fares for both CityRail and the State Transit Authority. Further, the Tribunal has put forward its views about issues that are the responsibility of the transport operators, the Department of Transport and Treasury, and importantly, the Government. Two of the areas of focus for the report are the structure of Community Service Obligation contracts and franchising for bus services.

A key issue for the Tribunal and for the community is to determine what is an appropriate ("fair") contribution from taxpayers towards running and maintaining public transport. Conversely, what is a reasonable contribution from those who use public transport to make towards the running, maintenance, infrastructure and capital costs of the services they use?

A major concern of the Inquiry has been how to get better value from the very large amounts of taxpayer money that flow to public transport - usually well in excess of $1 billion each year. Very closely related is the issue of ensuring that the passengers who use and pay for public transport get value for their money.

The Tribunal believes that there is scope for reviewing the main areas of government expenditure on public transport so that there are better transport solutions and equity outcomes, that is, greater value from that expenditure. Part of the approach proposed by the Tribunal involves an increase in the share of funding by passengers through a phased and modest increase in some fares.

Key objectives for the public transport system and some of the major constraints on fares are:

- in view of the important externality benefits associated with public transport, the public transport businesses should attain (State Rail Authority - SRA) or improve (State Transit Authority - STA) financial viability in order to continue to improve services that maintain and increase patronage levels and switch passenger choices from private to public transport modes
- fares should be set so that the major passenger groups (ie commuters), who are potentially able to switch, do not transfer from public transport to private cars
- fares should be set in relation to efficient costs and impacts on travel mode choice
- any real fare increases should be phased in to minimise the impact on passengers, especially welfare recipients and low income earners.

The Tribunal believes that the Government should:

- develop better and more appropriate standards of service provision across both public and private operators which are aligned to customer needs and willingness to pay
- revise institutional arrangements to establish a more competitive bus service through the tendering of franchises
- review the targeted concessions provided to users of public transport
- review the structure of CSO contracts with private and public transport operators to encourage efficient operation and maximise the public benefit from such CSO payments.

In setting fares in future, the Tribunal will

- set the level of fares on the basis that further productivity gains can be achieved by transport operators
- ensure fares are set consistent with encouraging growth in patronage on public transport services
- remove pricing anomalies and have regard for equity and environmental considerations.

Having completed this review, the Tribunal proposes to proceed with a study of transport priorities for the year 2000 and beyond. This study would consider future public transport pricing in the context of strategies to improve public transport delivery and improved understanding of environmental impacts, and methods of cost effectively providing transport services to the benefit of both users and taxpayers.

Thomas G Parry
Chairman

October 1996

Acronyms

BCA	Bus and Coach Association
CBD	Central Business District
COAG	Council of Australian Governments
CPI	Consumer Price Index
CSCTG	Central Sydney Community Transport Group
CSO	Community Service Obligation
DoT	Department of Transport
EPA	Environment Protection Authority
IPART	Independent Pricing and Regulatory Tribunal of NSW
ITS	Institute of Transport Studies
MSL	Minimum Service Level
NCC	Nature Conservation Council
NCOSS	Council of Social Service of New South Wales
NRMA	National Motorists and Roads Association
PPTC	Peninsula Public Transport Coalition
RAC	Rail Access Corporation
ROR	Rate of Return
RTA	Roads and Traffic Authority
SRA	State Rail Authority of NSW
SSTS	School Student Transport Scheme
STA	State Transit Authority of NSW
WSROC	Western Sydney Region Organisation of Councils

1 INTRODUCTION AND KEY RECOMMENDATIONS

In August 1995, the Government Pricing Tribunal[1] commenced a review of the pricing policies of government agencies supplying urban public passenger transport services in NSW. Attachment 1 list the terms of reference for this review.

The Tribunal released interim reports on the review in March 1996. The Tribunal received public submissions on the interim reports and held a public hearing on 26 April at the Sydney Hilton. A summary of submissions is enclosed (Attachment 2).

This report summarises and finalises the Tribunal's review of matters relevant to urban passenger transport services in NSW. The report considers the recommendations of the interim reports in the light of the many submissions made to the Tribunal. The report also takes into account the Tribunal's determination of maximum fares for CityRail and the State Transit Authority (STA) for the year 1996/97, which was released after the interim report.

The focus of this review has been passenger transport within urban areas. The report considers a number of issues which are particularly relevant to the CityRail passenger services of SRA and the bus and ferry services of the STA.

The terms of reference for the review require the Tribunal to also review the operation of Countrylink rail passenger services. The Premier recently issued draft terms of reference for a review of Countrylink services under Section 12A of the Independent Pricing and Regulatory Tribunal Act. The review of Countrylink services will continue throughout the remainder of 1996 with a final report due for release early in 1997.

In undertaking this review of public transport services, the Tribunal is aware that in part it is exploring areas of social policy and funding for social programs. These are clearly responsibilities of government. The Tribunal has no plan nor any brief to determine social policy objectives nor set social policy programs. Rather, the Tribunal, as required by the terms of reference for this inquiry, has endeavoured to provide government with an independent and considered view regarding social policy programs and concessions in the context of public passenger transport.

Two key areas of criticism of the Tribunal's interim reports relate to the absence of information on community education and a belief that the environmental and social benefits of public transport have not been fully investigated.

The Tribunal recognises that a better informed community is likely to make better use of public transport systems. Comments on how community education could be improved are made later in this report. One aspect of community education is the Tribunal's responsibility to provide information to the community which will enable it to evaluate the level and application of government subsidies and the performance of government transport authorities. The Tribunal's inquiry process has supplied and will continue to provide information to the community to serve this objective.

Environmental and social benefits are often cited as reasons to subsidise public transport. Consequently, there have been demands for enhanced public transport. However, during

[1] Following amendments to the Government Pricing Tribunal Act 1992, the Tribunal was renamed the Independent Pricing and Regulatory Tribunal of New South Wales from 19 January 1996.

the course of this review the Tribunal has observed the low reliance on public transport by Sydney commuters, compared to use of other modes. There may be a change in the offing. Three factors support the view that the usage trend is upwards:

1. Sydney Buses experienced a 5.1% patronage growth during 1995/96
2. the private bus operators report similar growth in patronage
3. a 2.7% increase in patronage on CityRail during 1995/96. [2]

For decades the use of public transport has declined (with occasional reversals) while the population of Sydney has continued to increase. However, the Tribunal is encouraged by the recent rise in patronage of bus and rail services. A key question is whether this growth can be maintained as the operators anticipate. The Tribunal's concern is to ensure effective use of community expenditure while examining ways of satisfying the community's transport needs with minimum environmental impacts.

The Tribunal accepts that there are important environmental benefits from rail transport in particular and these justify a substantial subsidy. The extent of the environmental benefits depends on the usage of public transport. Survey evidence suggests that usage will not vary significantly with the fare changes discussed in this report. The Pill paper[3] which was drawn to the Tribunal's attention by the Nature Conservation Council of NSW, specifically warns against excessively low public transport fares. Similarly, Ziebots and Laube support the need for price increases above CPI. [4]

Some empirical evidence suggests that people can be attracted to public transport by specific aspects of quality. The Pill paper suggests that levels of cleanliness, reliability, safety and speed relative to the private car are critical to achieve a transfer to public transport. However, investment decisions on quality improvements need to evaluate the full costs and benefits and determine the extent to which passengers should pay for improvements through higher fares.

The Tribunal supports the continuation of land use policies which encourage higher density development close to public transport modes. The ability to walk from your residence to connect with public transport is the key element in determining transport mode selection.

As part of its Clean Air 2000 program, the NRMA has conducted a survey of Sydneysiders. The results of this survey show that,

> "Consistent with the 1995 study, the issue most strongly endorsed for action was local air pollution around Sydney."[5]

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2 In a press release on 19 September 1996, the Minister for Transport, Brian Langton indicated that there had been a 6.8 million rise in CityRail passenger journeys and a 9.9 million rise in State Transit bus patronage since 1995.

3 Pill J, Transit and the Automobile: Toronto's Experience, Toronto Transit Commission, 1992, p 2.

4 Ziebots M & Laube F, LinkUp, Occasional Paper No. 2, 1996, p 4.

5 NRMA Clean Air 2000 Project Team. *Monitor of public attitudes - Air quality & the car 1996*, p 3.

With regard to solutions to the air pollution problem, the survey found that,

> "Overall the most effective perceived solution was *"better access and improved public transport"* with 78% claiming it would be a *very* or *quite effective* measure. This suggestion was particularly strong in the Sydney West and Wollongong regions, which are generally not serviced by public transport to the extent of inner metropolitan areas.
>
> The related and second most effective measure was *"reducing the cost of public transport"*, considered by 68% of respondents (and 73% in Newcastle) to be *very*, or *quite effective*. More women than men thought that this would be a *very effective* measure."[6]

The social objectives of public transport continue to be achieved by a system of extensive concessions. The concession system ensures that some targeted groups have easy access to the benefits provided by public transport. However, some concessions may not be directed to those most in need. The Tribunal will continue to review the concession system and suggest methods to increase equity and access for disadvantaged people, while improving the value government receives from this expenditure.

Having completed its review of pricing policies for urban public passenger transport services, the Tribunal plans to proceed with a study of transport priorities for the year 2000 and beyond. This study is being undertaken to ensure that quality information on public transport continues to be made available to the community. The proposed study will go beyond the issue of fares and include:

- strategies to improve public transport and understanding of its environmental impacts
- methods of providing transport services cost effectively.

Recommendations

Chapter 2

The Tribunal believes that government payments to CityRail need to be explicitly segmented and identified as three categories: general deficit CSO subsidy, below rail CSO subsidy and concession payments.

The Tribunal considers that the medium term strategy for Sydney Buses should be to remove the need for CSO funding.

The Tribunal believes that there is a need to review minimum service standards and actual service delivery by private operators and the STA across the entire bus and ferry networks. Such a review needs to ensure that the Government's transport policy objectives are in fact being met and funded appropriately.

The Tribunal believes that, given the growing significance of concession travel, the mechanisms for reimbursing all transport operators for the provision of concession travel need to be reviewed. The Tribunal prefers government reimbursement on a negotiated lump sum basis.

The Tribunal recommends a move towards the strict separation of the purchasing and the ownership responsibilities of the Department of Transport, as required under the purchaser-provider model.

[6] Ibid, p 7.

The Tribunal recommends that the availability of targeted concessions be reviewed on the basis of identified target groups and according to the government's social objectives.

The Tribunal recommends establishing an appropriate framework for reviewing the concessions provided to all groups.

The Tribunal recommends that the Government take steps to standardise the availability of existing pensioner excursion fares across all metropolitan transport operators. The Tribunal believes that a change in the method of reimbursing transport operators for providing concession travel will limit the potential cost implications for government.

Notwithstanding a change in the reimbursement methodology, if there is the need to fund an extension of the availability of the concession to private bus operators, a modest increase in the excursion concession fare is an option to be considered.

The Tribunal believes that there is no strong case to limit the availability of pensioner and senior citizen concession fares during peak commuter periods.

The Tribunal recommends that the Government consider:
- *reviewing the process for funding the SSTS along the lines of a funder-provider model*
- *monitoring the effects of changes in the SSTS to contain costs.*

If further changes in funding and administering the SSTS are considered, the Tribunal suggests that consideration be given to adopting a parental contribution with appropriate safety nets that take into account capacity to pay (that is, some form of means test).

Chapter 3

On expiration, all current private bus contracts should be replaced by a competitively tendered franchise system.

In the interim, the Tribunal recommends that DoT improve the reflectivity of the private bus cost index. The new index should be the subject of an annual independent audit.

The long term implications of the STA's capital expenditure program should be considered in detail, including a full analysis of the farebox impact of a superior quality fleet.

In order to earn a "reasonable" ROR on assets, the STA should:
- *achieve best practice in operations*
- *clarify the CSO program*
- *match its capital investment program with an appropriate level of service quality.*

Following satisfactory cost reductions and the removal of CSOs for Sydney Buses, the Tribunal will reconsider the case for real fare rises to finance capital expenditure or business growth. In the interim, the Tribunal will permit fare rises which are broadly in line with the CPI and will continue to correct fare anomalies to improve customer equity.

The Tribunal supports discounts for "Ten" tickets of between 15 and 20%.

While supporting increases in TravelPasses, the Tribunal will consider the extent of increases for these tickets annually.

All franchise areas should be open to competitive tender at the end of the five year contract. There will need to be appropriate incentives, sanctions and penalties to ensure contract requirements are met.

Standard fares could be determined on the basis of information provided in the tender process and adjusted periodically.

The Tribunal proposes to continue to conduct annual determinations for the STA bus and ferry services. A medium term price path will be established once the STA has satisfactorily addressed numerous critical financial issues.

The Tribunal supports the realignment of discount levels and will support modest increases in all ferry fares to improve cost recovery.

The Tribunal believes that the Government should consider competitively tendering ferry routes on Sydney Harbour.

The Tribunal recommends that the Government review the ownership of ferry wharves in the light of national competition policy and the COAG Competition Principles Agreement.

The Tribunal considers that Sydney Ferries should review the scheduling of the Manly Ferry and JetCat services so that the services do not compete with each other.

Chapter 4

The Tribunal believes that CityRail can reduce office costs through a rationalisation of its office accommodation and a facilities management program. Surplus space should be divested or sub-leased.

Significant scope for productivity improvements exists within CityRail's operations. The size of potential efficiency gains will become apparent following the submission of CityRail's segmented accounts. In the interim, the Tribunal encourages CityRail to continue to pursue real cost reductions of at least 2.5% per year.

The Tribunal believes that CityRail should be able to attain much higher levels of cost recovery for above rail costs on the CityMet service. A substantial government subsidy will still be required for the below rail costs. This subsidy will recognise the externality benefits of the rail service to the community. Targeted concessions to particular groups will entail specific subsidies.

The Tribunal believes that CityRail's fares for outer suburban customers should increase in line with CityMet fares. However, the Tribunal recognises that such increases will fall very far short of those necessary to achieve improved levels of cost recovery. It is unlikely that the outer suburban services can ever achieve levels of recovery of operating costs comparable to those achievable by CityMet.

The Tribunal believes that a medium term price objective for CityRail that phases in a weighted average increase in real terms of 15% over the four years from 1996/1997 to 1999/2000 is both sustainable and equitable. However, the Tribunal recognises that annual adjustments may require some variation from this broad objective. To be consistent with the major objectives and constraints for the passenger rail service set out in this report, annual adjustments will be targeted to different fare categories.

The Tribunal proposes phasing in real increases in CityRail's periodical and multi-ride tickets over the period to 1999/2000 consistent with the major objectives and constraints set out in this Report.

The Tribunal proposes phasing in real increases for "cash" single and return fares and off-peak fares over the period to 1999/2000 consistent with the major objectives and constraints outlined in this report.

The Tribunal proposes to continue to conduct annual determinations for CityRail's urban passenger train services.

Chapter 5

The Tribunal proposes to research further the environmental and social benefits of providing public transport.

In recognition of the need for continuing public education, the Tribunal proposes to undertake a study of transport priorities for the year 2000 and beyond.

2 GOVERNMENT CONTRIBUTIONS

This chapter considers the payments made by government for public transport. These contributions are separated into:

- community service obligations
- targeted concessions
- capital funding.

2.1 Introduction

A major concern of the inquiry into public transport has been how to get better value from the large amounts of taxpayer money (subsidies) that flow to public transport. Very closely related to this issue of getting better value for taxpayers, is the issue of ensuring that the passengers who use and pay for public transport get value for their money.

The NSW Government makes a substantial contribution to the funding of urban passenger public transport. In its submission, the NSW Treasury quotes a net outlay by government of $1 billion. This contribution is made up of capital funding, concession reimbursements and Community Service Obligation (CSO) payments to operators. It does not include the servicing of the State Rail Authority (SRA) debt taken over by the government. In addition, the government spends approximately $900 million a year on capital works for roads in NSW.[7]

The overall situation with respect to payments by government to transport operators is shown in Table 2.1.

Table 2.1 Government Contributions to Transport Operators

	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96
			($ million 1994-95)			
CityRail (including capital)	732.8	783.4	813.6	828.4	720.5	875.4
STA (including SSTS & concessions)	168	180	177	168	152	135
Private Buses (including SSTS)	88.8	93.9	94.7	95.6	97.4	101.5
Total	989.6	1057.3	1085.3	1092.0	969.9	1111.9

Source: CityRail, STA and DoT

A version of this table appeared in the interim reports. In response to the interim reports, the Bus and Coach Association (BCA) has noted that the contribution to urban private bus operators is overstated. For example, the report quotes contributions of $287 million in 1994/95. Of this amount less than $124 million was for urban bus services being $101 million for urban route bus operators (SSTS) and $23 million for pensioner reimbursements (both urban and country). The remaining $163 million represents SSTS payments for

[7] NSW Budget Paper No 4, pp 58-65. This is capital funding to the Roads and Traffic Authority. Maintenance is about $700 million. The Commonwealth and local government also spend money directly on roads which adds substantially to the total of road expenditure in the state.

country bus services. The figures in the above table include payments for urban services only.

The basis for some of the government payments to both public and private operators needs to be reassessed. Interim Report Number 1, *Government Payments for Public Transport*, states that the reimbursement of CSOs and targeted concessions to public and private operators may not be giving the government the best value for its transport dollars. It is important that the government and the community clearly understand what funds are being provided to public sector agencies and for what purposes. The Tribunal believes that there needs to be both greater transparency and a clearer categorisation of the actual payments by government to both the STA and SRA for general operating subsidies, CSOs, targeted concessions and capital funding.

2.2 Community service obligations (CSOs)

2.2.1 CityRail

The government has had CSO contracts with the State Rail Authority (SRA) since 1990/91. Since 1993/94 the CSO contracts have been with the individual business groups of SRA, namely CityRail, Countrylink and Freight Rail.

Funding arrangements for CityRail appear to provide little incentive to CityRail to increase farebox revenue or patronage. Costs not recovered from farebox revenue and concession reimbursement are met by government funding. Management initiatives that increase farebox revenue would result in a reduction of government funding.

The interim report notes that the structures of subsidies paid to the SRA and the STA differ. The STA's CSO payments are explicitly segregated, while the SRA receives a general subsidy which in effect allows CityRail to meet its cashflow requirements.

The STA receives a "pricing CSO" (for fares below private buses)[8] and a "service level CSO" (for non-commercial services) from the government.

The SRA receives a general subsidy which includes "pricing" and "service" elements as well as an element of operating subsidy. Separation of below rail line funding is essential to the managing of track maintenance costs which have been identified as the area of highest potential efficiency gains.[9] However, the merit of separating SRA funding to include a pricing CSO is minimal as this necessitates the development of an arbitrary benchmark for efficient fare levels. Furthermore, the Tribunal questions the concept of a pricing CSO. The Tribunal sets fares that are appropriate in the circumstances. The Tribunal does not see why operators should be given compensation because some other fare was not chosen. Subsidies should be paid because the government requests non-commercial services to be provided, or wants to subsidise the cost of the track. All the rest is deficit and should be seen as such. Of course, the non-commercial nature of CityRail and the absence of a clear separation between purchaser and provider, does make it hard to isolate the various aspects of subsidy.

8 The STA's pricing CSO reimburses STA for fares which are less than a comparative private bus fare. The service CSO pays STA for providing non-commercial services in excess of the minimum service level.

9 See Industry Commission Report No. 13, Rail Transport Vol II, 1991 p 162 and Bureau of Industry Economics, Rail Freight Update 1993, Research Report 52, p 42.

The Tribunal believes that future CSO contracts with CityRail should include three separately identified components:

- targeted concessions
- deficit funding
- below rail subsidy.

In their submissions, CityRail and the Department of Transport (DoT) support the concept of identifying each element of the payment to the SRA. The DoT states,

> "The Department will continue to work towards the development of CityRail CSO funding so that it is more segmented, with the costs of subsidy and concession categories being explicitly identified. … The need to ensure that inefficiencies are identified in order that they can be addressed will continue to be taken into account in funding determinations."[10]

The Department of Transport has indicated that it plans to implement an explicitly segmented funding structure for CityRail. From DoT's perspective, moving to a segregated funding structure has been hampered by an insufficient breakdown in costs for the former State Rail Authority. Following the restructure of rail,[11] this will be achievable. However delays in finalising capital structures (balance sheets, particularly debt levels) for State Rail and the STA are both serious and unfortunate. The delays have delayed implementation of a segmented CSO structure to finalise CityRail's 1996/97 CSO contract. The Tribunal seeks an urgent settlement of capital structures to enable CSO segmentation and optimal capital expenditure planning.

Recommendation

The Tribunal believes that government payments to CityRail need to be explicitly segmented and identified as three categories: general deficit CSO subsidy, below rail CSO subsidy and concession payments.

2.2.2 STA

Formal CSO contracts have been in operation over the past five years, governing the performance of STA in delivering its contracted services.

Current contracts are divided into three elements, reflecting the services the government is paying for: pricing, service and concession.[12]

Until 1994/95, the Government provided the STA with sufficient funding to allow it to break even. There has since been a considerable reduction in the total government contribution to STA. This has been achieved largely through reductions in deficit funding. The Tribunal considers that STA can remove both the pricing and service level CSO payments for Sydney Buses through efficiency gains. STA has indicated it can remove Sydney Buses' service level CSO, currently $2.1 million, in the near future. The only CSO would then be for targeted concessions.

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10 Department of Transport, submission to Tribunal. April 1996, p 3.

11 The SRA has been restructured since 1 July 1996. Infrastructure, freight and maintenance activities have been separated from the business of providing passenger services.

12 The STA's pricing CSO reimburses the STA for fares which are less than a "commercial" fare. The service CSO pays STA for providing non-commercial services which are in excess of the minimum service level. The concession CSO reimburses STA for offering government determined concessions, eg pensioner and senior citizen travel.

As discussed in chapter 3, the Tribunal considers that the real solution lies in successful implementation of a competitive franchising model. Until such a model is in place the extent to which commuters and taxpayers are funding inefficiencies within STA will remain hidden.

The Tribunal strongly encourages the STA to use cost efficiency gains to further reduce and eventually eliminate the need for a pricing CSO for Sydney Buses (forecast at $15.1m for 1996). The STA's 1995 submission agreed that minimum efficiency gains of $23m were achievable in the medium term. The Tribunal is concerned that recently provided financial models of the STA assume that the pricing CSO will average 11% of passenger revenue and will grow with passenger revenue to $26m in 2005[13]. The STA has made significant endeavours to reduce total CSO payments for buses from $91.3m in 1991/92 to a forecast level of $17.2m in 1996.[14] The Tribunal wants to see this progress towards the elimination of CSO funding continue.

Pricing CSO

Through the pricing CSO, the government reimburses the STA for offering fares below the maximum approved fares for private bus operators. The intention is to ensure that the STA is not disadvantaged by regulated fares which may be less than commercial.

In the interim report, the Tribunal suggests that the way in which the STA is reimbursed for the pricing CSO for buses is inappropriate. The Tribunal's concern is in the use of the maximum private bus fare scale as the benchmark for the payment of pricing CSOs.

The STA considers that both the pricing CSO and the benchmark used are appropriate. While the NSW Council of Social Service (NCOSS) agrees with the Tribunal's recommendation, it believes that the Tribunal has not faced the issue of the appropriateness of the CSO itself. Highlighting the inequity of the pricing CSO, NCOSS states,

> "It is inequitable to transport users for a price subsidy to be provided to the STA when it is not provided to private bus operators. The Tribunal should recommend the pricing CSO be reformulated to assist bus services on an area needs-based formula (regardless of the ownership of the bus service)."[15]

While there is an equity issue here, the rationale behind the pricing CSO needs to be considered. The stated purpose of the pricing CSO is to reimburse the STA because its regulated fares are below a commercial level. However, the approach used does not consider whether the commercial rate is appropriate for the government operators. The method does not compare the costs of the government and private operators or whether those costs are efficient.

In its submission, the BCA argues that it is not possible to identify an appropriate private bus operator for comparison of fares. The fare schedule has been designed to be uniform within a set area, eg metropolitan Sydney. Contracts within that area have a uniform maximum fare schedule but may have differing levels of service**.** As the fare schedule is a maximum schedule and many operators actually charge less than the schedule, most offer discounts.

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13 These models result from a Capitalisation Study undertaken by Price Waterhouse for NSW Treasury and the STA.

14 STA Annual Reports since 1991 and models provided by STA - 1996.

15 NCOSS submission to Tribunal, p 7.

In its submission to the Tribunal, the STA sought fare increases for Sydney Buses for 1996/97 which would remove the pricing CSO. The Tribunal believes that removing all pricing CSOs is a priority issue. However, the Tribunal is concerned about the fares outcome which would result. The Tribunal considers there are alternative approaches to removing the pricing CSO such as efficiency improvements.

The Tribunal notes two outcomes of the current approach to calculating the pricing CSO:

1. Since it is based on the comparative maximum commercial fare, increases in the commercial fare have caused increases in the pricing CSO
2. While the fare is less than the maximum commercial fare, increasing patronage will lead to increases in the pricing CSO.

Hence the importance of having a reasonable and appropriate commercial fare.

As noted earlier, the Tribunal questions the merit of a pricing CSO as a useful concept. If the Tribunal sets fares correctly, the CSO payment is just another word for deficit. In practice, it involves comparing the STA fare with private fares.

The Tribunal proposes eliminating all CSO pricing or service funding for Sydney Buses, retaining only the CSO to subsidise concessions. Government funding of Sydney Ferries and the Newcastle services should consist of global deficit funding, concessions and targeted service CSOs.

Recommendation
The Tribunal considers that the medium term strategy for Sydney Buses should be to remove the need for CSO funding.

Service CSO

The service level CSO provides a transparent mechanism for government to reimburse the STA for providing non-commercial services in excess of the minimum service level requirement. Non-commercial services generally relate to off-peak or higher frequencies during the day. The service CSO is provided at a level deemed equivalent to efficient costs. Similar payments are not made to private bus operators.

The STA has undertaken to quickly eliminate the service CSO for Sydney Buses ($2.2m 1996/97). The Tribunal supports this elimination based on the efficiency gains available and the immaterial size of the subsidy. The service CSO for Sydney Ferries and Newcastle services appears to be a more permanent feature and is expected to remain constant at an approximate total of $14.1m. The Tribunal supports segmentation of service CSO funding by each service to allow payment and service levels to be monitored.

In the interim report, the Tribunal queries whether the maintenance of this CSO means that the minimum standard is set too low or the actual service standards of the STA are inappropriately high. An issue to be dealt with is that private operators are required to meet only the (lower) minimum service standards. The Tribunal proposes that government review and compare the minimum services levels of private operators and the STA.

The BCA has criticised this proposal. The BCA indicates that the Passenger Transport Act creates "competition between contract regions" and that the minimum service levels are being reviewed constantly. As operators are encouraged to provide services above the minimum level, the average service levels are increasing,

> "Over time there should be constant growth in the minimum threshold levels due to the actual growth in frequency provision by the industry leaders."[16] ...
>
> "the Act insists that operators' commercial contracts have the service levels constantly upgraded to:
>
> (a) reflect any change in the patronage grading of the region, due to changes in demographics that may have affected the patronage potential;
>
> (b) reflect any movement in the average frequency levels being provided for the time being by all commercial contractors in similar contract regions … Such a revised "average" becomes the new "minimum".
>
> Such a review of minimum service levels is currently being carried out by the Department of Transport in accordance with the principles enunciated in the Act.
>
> This method whereby the market place (through the concept of competition between regions) determines the minimum service levels, is far preferable to the bureaucratic directives proposed in the Tribunal's reports, where new service standards are to be specified without any clear market or demand-related principles."[17]

As evidence of the success of the Act in promoting growth in services, the BCA quotes the results of a survey from a recently released report,

> " • On average there has been a 21% increase in the number of services provided on bus routes operated by the private bus industry.
> • The greatest increases occurred during off-peak periods, where on average there has been a 33% increase in the number of services provided.
> • The average increase in the number of services provided during peak hours for Sydney, Newcastle, the Central Coast, Wollongong, and major NSW country towns is 16%."[18]

Notwithstanding these arguments, the Tribunal notes that submissions from groups such as the Central Sydney Community Transport Group (CSCTG) suggest that the minimum service levels are in need of review.[19] This would seem to be due to the STA's minimum service levels being higher than those of private buses.

NCOSS proposes that,

> "Minimum service levels be set on the same formula across STA and private bus areas."[20]

In response to this, the DoT indicates that if the minimum service levels of the STA are to be applied to private operators there are likely to be calls from the private industry for a subsidy.

In its submission,[21] the STA welcomes a review of minimum service levels in the light of its service level CSO. The STA believes that as well as the minimum service level, there is a need to review the quality of service.

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16 ITS Certificate of Transport Management Course - Module 1, Topic 5, quoted in BCA submission p 6.

17 BCA, submission to Tribunal, April 1996, pp 6-7.

18 Roger Graham and Associates Pty Ltd, *Changes to Private Bus Services Resulting from the Passenger Transport Act 1990,* quoted in BCA Submission, pp 7-9.

19 CSCTG, submission to Tribunal, April 1996, p 13.

20 NCOSS, submission to Tribunal, p 7

The BCA shares the confidence of the STA management, that it can remove the service level CSOs from Sydney Buses.[22]

The DoT is reviewing and updating service levels.[23] This process will be based on the 1991 census and will be reviewed again when the 1996 data becomes available. After removing those services for which the STA is paid a subsidy, STA levels will be compared with the private operators' service levels. The new minimum service levels will then be applied. It is unclear whether the STA and private operators will have equivalent minimum service levels.

In the case of services which are not commercially viable, such as some of the ferry services, it is important that, if these are to be subsidised, they be funded by government explicitly as CSO services. It is for government to decide whether a particular transport service should be subsidised. For example, the government explicitly subsidises the Parramatta RiverCat service. There are other non-commercial services that would require prohibitive fare increases to achieve reasonable levels of cost recovery. These need to be explicitly identified and funded by government via CSO payments to transport operators.

Recommendation
The Tribunal believes that there is a need to review minimum service standards and actual service delivery by private operators and the STA across the entire bus and ferry networks. Such a review needs to ensure that the Government's transport policy objectives are in fact being met and funded appropriately.

2.3 Concessions

The government subsidises the fares of a number of specific groups, such as pensioners, seniors and school students. These targeted subsidies are made available across the government bus and rail networks (STA and SRA) and, to a lesser extent the private bus networks. Targeted subsidies are additional to any general subsidy to public transport (such as for externality reasons) which result in fares that are lower than might otherwise apply.

The Tribunal recognises that CSOs and concessions are policy issues for the government of the day. However, it is clear that there are a number of anomalies and inequities in the current arrangements for providing and reimbursing targeted concessions. These are discussed in Interim Report No 1, *Government Payments for Public Transport.*

Present government subsidies are poorly targeted. NCOSS infer that passengers with good access to CityRail and government-owned bus services enjoy better services and lower fares than those who do not.

The Tribunal believes that there are several ways in which government expenditure can be better focused.

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21 STA, submission to Tribunal, April 1996, p 12.
22 BCA, submission to Tribunal, April 1996, p 10.
23 DoT, submission to Tribunal, April 1996, p 9.

On specific concessions the Tribunal has identified four areas for consideration and review:

1. reimbursement of concessions
2. anomalies with targeted concessions
3. the funder-provider model
4. School Student Transport Scheme.

2.3.1 Reimbursement of concessions

In Interim Report No 1, the Tribunal raises the issue of whether the government should reimburse operators for targeted concessionary travel on a full fare basis, at marginal cost or on some other agreed basis, eg marginal cost plus a fixed cost contribution.

A number of submissions have expressed concern about changing the way that operators are reimbursed.

The BCA is worried that changing the method of reimbursement to recover marginal cost only would have a significant impact on its members' businesses.[24] In its submission, the BCA states that its patronage peaks differ substantially from those for the rest of Sydney. Apart from the school peak hours, the commuting peak is no longer the most heavily patronised period of the day. The times when concession holders wish to travel are already the peak times for many bus operators. In the BCA's view, marginal costs should not be charged at these times.

The BCA points out that its contracts provide for it to be reimbursed for actual fares foregone. Thus, the method of reimbursement could not change whilst the current contracts are in force.

The STA also argues against reimbursing concessionary travel on a marginal basis.[25]

There is a case for reviewing the way in which targeted concessions are reimbursed to transport operators. The main alternatives are:

1. reimbursing at marginal cost rather than full fare for off-peak concessions travel
2. reimbursing on a negotiated lump sum basis for all concession travel on individual transport franchise operations.

The Tribunal supports the negotiated lump sum as a more commercial solution. This method maximises government purchasing power, simplifies funding, gives cost certainty and removes the subjectiveness required by other cost and usage estimates.

Recommendation
The Tribunal believes that, given the growing significance of concession travel, the mechanisms for reimbursing all transport operators for the provision of concession travel need to be reviewed. The Tribunal prefers government reimbursement on a negotiated lump sum basis.

[24] BCA, submission to Tribunal, April 1996, pp 18-21.
[25] STA, submission to Tribunal, April 1996, pp 12-14.

2.3.2 Purchaser-provider model

An important element in targeting concession fares and reimbursing the transport operators (both private and public) is the separation of "funder" and "provider" functions. The Tribunal supports the development of a robust funder-provider model in which the decision to fund a targeted social policy program is separated from the provision of the service. The area of government that is responsible for funding a targeted social policy program (whether pensioners, unemployed people or school students) will then have an incentive to ensure that the actual targeted concession delivers the policy outcome required, and to negotiate the best possible commercial terms for the (bulk) purchase of the services to be delivered. The funder-provider model has been successfully implemented in Queensland, where the Department of Family Services reimburses Queensland Railway for concessions.

The BCA considers that a purchaser-provider model is inappropriate for the private bus industry because:

> " (a) Marginal cost pricing not being applicable to pensioner or school-pupil travel.
> (b) Treasury already receives the benefit of discounted fares when calculating pensioner reimbursements to the private sector (compared to the system adopted for State Transit).
> (c) Bus operators have an obligation to offer the same range of fares to all passengers, without discrimination.
> (d) It is not possible to negotiate fare scales (including concession fare reimbursements) mid-term, without destroying the commercial nature of the contracts and affecting the service standards that form part of these contracts."[26]

These comments do not directly criticise the purchaser-provider model. Rather they are arguments against the use of marginal costs as a basis for reimbursing concessionary travel.

Recommendation
The Tribunal recommends a move towards the strict separation of the purchasing and the ownership responsibilities of the Department of Transport, as required under the purchaser-provider model.

2.3.3 Targeted concessions

There are major anomalies and inequities in the current arrangements for targeted concessions. For example, the Tribunal is concerned that the concessions offered by government and private operators differ. The Tribunal is also aware that the mechanisms for reimbursing concessions vary by type of service provided.

The Tribunal believes that a clear framework for the application of social policy in the passenger transport area needs to be implemented. At the moment there are a number of equity issues:

- lack of access to the pensioner and senior citizen excursion fare on the private bus network
- differential concessions between pensioners, senior citizens and other groups that the government may wish to better target (people who have disabilities or are unemployed)
- absence of any "needs" or "means" basis for better targeting the (often generous) transport concessions presently enjoyed by groups such as pensioners, senior citizens and school and tertiary students.

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26 BCA, submission to Tribunal, April 1996, p 41.

Any increase in the availability of concessions may require additional funding. A change in the way in which transport operators are reimbursed for providing concession travel may limit the cost of increasing the availability of concessions. A review of targeted concessions on the basis of need, better reflecting income and wealth, would also limit the cost of any increase in concessions. The Tribunal stresses that these are matters for government policy.

The Tribunal recommends that the availability of targeted concessions be reviewed on the basis of identified target groups and according to the government's social objectives.

In the responses to the interim report there has been general agreement that the anomalies in concessions need to be addressed. Treasury concurs with the principle of removing the various anomalies, particularly the pensioner and senior citizen excursion ticket. However, the implementation of changes to reduce anomalies may reduce passenger revenue and increase the government's contribution.

The Department of Transport has indicated to the Tribunal that targeted concessions are being examined under the guidance of the Social Justice Committee of Cabinet with a report due later this year.

Recommendation
The Tribunal recommends that the availability of targeted concessions be reviewed on the basis of identified target groups and according to the government's social objectives.

Areas where anomalies exist include pensioner and senior citizen travel, unemployed travel, people with disabilities and tertiary students. The Tribunal believes that there is no justification for the anomaly relating to pensioner and senior citizen travel on private buses. The government should explore ways of removing the distortion.

The BCA supports this extension on the basis that private operators are reimbursed for actual usage. The Council on the Ageing supports removing this anomaly. It suggests a single charge of $2 to replace the existing $1, $2 and $3 fares. Fares for the excursion scheme have not increased since 1988.

Recommendations
The Tribunal recommends establishing an appropriate framework for reviewing the concessions provided to all groups.

The Tribunal recommends that the Government take steps to standardise the availability of existing pensioner excursion fares across all metropolitan transport operators. The Tribunal believes that a change in the method of reimbursing transport operators for providing concession travel will limit the potential cost implications for government.

Notwithstanding a change in the reimbursement methodology, if there is the need to fund an extension of the availability of the concession to private bus operators, a modest increase in the excursion concession fare is an option to be considered.

In the interim report, the Tribunal notes the issue raised by both the STA and CityRail of pensioners and senior citizens travelling in the peak.[27] The operators consider that concession holders travelling during the peak impacts on the availability of buses and trains

[27] IPART. *Interim Report No 1 Government Payments for Public Transport*, March 1996, p 32.

for commuting travellers. Despite this concern, evidence provided to the Tribunal suggests that the bulk of pensioners travel outside the morning peak.[28]

Recommendation
The Tribunal believes that there is no strong case to limit the availability of pensioner and senior citizen concession fares during peak commuter periods.

2.3.4 School Student Transport Scheme (SSTS)

Travel to and from school is funded through the SSTS. The SSTS has evolved from a focused assistance program for rural students in remote areas to a general scheme available to all school students who satisfy the eligibility criteria. SSTS currently provides assistance to 70 per cent of NSW school students.

Table 2.2 illustrates that the total cost of the scheme has increased by 51% since 1989/90. Over the same period, the Sydney CPI has increased by 28.7%.

Table 2.2 School Student Transport Scheme costs

	1989/90	1990/91	1991/92	1992/93	1993/94	1994/95	1995/96 (est)
Total student population [(a)] (000)	1,033.6	1,030.6	1,037.3	1,050.2	1,052.2	1,052.3	1,052.3
Total SSTS beneficiaries (000)	641.8	643.1	659.2	693.8	736.2	728.0	708.3
Total cost [(b)] $m	227.6	264.1	286.8	305.0	314.8	324.1	343.9
Cost per beneficiary ($)	354.7	410.6	435.1	439.6	427.7	445.2	485.5

Source: NSW Budget 1995-96 Budget Paper No 2 Budget Information, Table 4.1.
NSW Budget 1996-97 Budget Paper No 2 Budget Information, Table 4.1, section 4 p 163.)

Notes (a) Figures from Department of School Education's annual census.
(b) Includes SSTS payments to the STA and SRA. Includes rural and urban students carried by private bus.

Apart from fare increases and student population growth, a significant factor in the increasing costs over recent years has been the dezoning of schools; that is, the ability to send children to a school other than the nearest local school.

In 1995, SSTS provided free travel to all students residing further than a radial distance of 1.6 km or a walking distance of 2.3 km from their school.

As noted in Transport Interim Report No 1, in the 1995-96 Budget, the NSW Government announced changes to the SSTS:

1. For the 1996 school year, the distance high school students (must travel to qualify for the SSTS), will be extended from a radius of 1.6 kilometres to 2 kilometres. The distance criterion for primary school students will remain at 1.6 kilometres. There is no distance criterion for infants.[29]
2. In 1996, all students eligible under the distance criteria will continue to travel free, to and from school.
3. From the beginning of the 1997 school year, a maximum taxpayer subsidy of $450 will be introduced for each eligible student in the greater metropolitan area[30]. All eligible

[28] Ageing and Disability Department, submission to Tribunal, October 1995, Table 2A.
[29] Infants students are in Kindergarten to Year 2.
[30] Sydney, Newcastle, Wollongong and the Central Coast.

students will continue to receive free travel to and from school to the maximum value of $450 per annum. Parents will be required to meet any transport costs in excess of $450.

4. Other administrative measures will be taken in 1996 to contain costs. These measures include moving towards ensuring payments to operators are based on actual trips taken.

These measures were expected to achieve savings of about $100 million in a full year.

In its submission, the BCA provides a breakdown of these savings (Table 2.3).

Table 2.3 Projected savings from changes to SSTS

Expenditure item	Private buses ($m)	Other* ($m)	Total saving ($m)
High school eligibility at 2 km	12.5	7.5	20
Reduction in country fare scales and reduction in rate paid to country non-commercial contract holders	15	-	15
Payment for actual numbers travelling (in lieu of payment for 92%)	22.5	7.5	30
$450 cap in 1997	25	10	35
Total	**75**	**25**	**100**

Source: BCA submission, p 27
Note: * Other relates to STA buses, SRA trains, all ferries, taxis etc.

Earlier this year the government revised its criteria so that all students who live further than 2.9 km walking distance or 2.0 km radial distance from their school are now eligible for the SSTS. The proposed maximum taxpayer subsidy for the 1997 school year was removed. The Tribunal notes that, as shown in Table 2.2, the effect of these amendments has been that the previously projected reduction in costs of this scheme will not eventuate.

The Tribunal is aware that approximately $100 million of the cost of the SSTS is for transporting country students. However, the Tribunal notes that even with the steps taken to reduce the cost of the SSTS and with an estimated 19,300 fewer students being carried in 1995/96, the cost of the scheme has increased by $19.8 million.

Unless there is a substantial reduction in school travel, there will be little further change in costs. The service provided to school children is substantially free. The current approach means that the costs are now largely met by the government. If the cost to government is to be reduced then, unless significant operating cost reductions are achieved, parents will need to pay more. If a parental contribution is introduced it should address affordability objectives by, for example, excluding recipients of the family allowance supplement from such a contribution.

In its submission, Treasury concurs with this approach.[31]

Recommendations

The Tribunal recommends that the Government consider:

- ***reviewing the process for funding the SSTS along the lines of a funder-provider model***
- ***monitoring the effects of changes in the SSTS to contain costs.***

If further changes in funding and administering the SSTS are considered, the Tribunal suggests that consideration be given to adopting a parental contribution with appropriate safety nets that take into account capacity to pay (that is, some form of means test).

[31] NSW Treasury, submission to Tribunal, April 1996, p v.

2.4 Conclusion

The Government contributes approximately $1 billion towards the provision of urban passenger transport services. These payments are in the form of CSOs and targeted concessions.

The Tribunal believes that the basis for some of the government payments needs to be reassessed. Of primary concern for the Tribunal is that the government and the community receive value for each dollar spent. The Tribunal considers that there needs to be both greater transparency and a clearer categorisation of the actual payments by government to both the SRA and STA for general operating subsidies, CSOs and targeted concessions.

3 BUSES AND FERRIES

This chapter examines the operation of the bus and ferry services provided by the State Transit Authority. Each of the business groups are discussed:

- Sydney Buses
- Sydney Ferries
- Newcastle Buses and Ferries.

3.1 Introduction

The Department of Transport (DoT) contracts with the STA and private bus operators to provide services for particular areas at specified minimum levels. The STA operates services mainly in the eastern part of the metropolitan area, the lower North Shore and the Warringah area, servicing the Sydney Central Business District (CBD). Private buses in Sydney operate generally in the area outside the former tram network and outside the Warringah and Northern Beaches area, where government buses operate. Private bus services developed from the 1930s to serve Sydney's new areas of population. Private buses carry commuters to and from railway stations, carry students to and from school, and provide an alternative to private vehicles for other passengers. Recently, private operators have introduced commuter services to the Sydney CBD.

An STA business group, Newcastle Buses, provides bus services in urban Newcastle. The Department of Transport contracts provide private bus companies with access to the major regional centres near Newcastle via the Newcastle Buses service area. The growth areas on Newcastle's outskirts are served by private bus companies catering largely for school student travel. Three private operators service the newer, outer-western areas of Newcastle. Their services are not CBD focused and are not integrated with Newcastle Buses. A further six private operators run services through the Newcastle Buses area to Charlestown and the Newcastle CBD.

The Department of Transport also contracts with the STA to provide ferry services in Sydney and Newcastle.

Sydney Ferries has a fleet of 26 vessels that provide a wide range of services classified under four major groupings. These are:

1. Outer harbour services, specifically the Manly ferries and JetCats
2. Inner harbour services including Mosman, Watsons Bay, Balmain and Hunters Hill
3. Parramatta RiverCat services including Abbotsford and Meadowbank
4. Tourism cruises and charter hiring.

Newcastle Ferries utilises two vessels to operate a service across the Hunter River from Stockton to the Newcastle CBD. The service provides fast access to the CBD for Stockton residents.

The Tribunal sets the maximum fare for the STA (Sydney Buses, Sydney Ferries and Newcastle Buses and Ferries). Maximum fares for private bus operators are set by the Minister for Transport. These maximum fares are determined prior to the signing of contracts. Once the fares have been determined, they remain in force for the duration of the contract. Fare adjustments are (normally) made annually[32] based on an index comprising a weighted average of driver wages, diesel costs and the CPI. The DoT is currently reviewing this index with a view to removing the CPI component and increasing the other cost components to enhance reflectivity.

Arguing that fares should not vary between operators, the New South Wales Council of Social Service (NCOSS) proposes that fares for private operators should be calculated on the same basis as for government services.[33] The Tribunal could take responsibility for setting fares for the private operators. However, this would require a variation to current contract arrangements with private operators and might also require legislative changes to the Passenger Transport Act and the IPART Act.

Under current contract arrangements fare structures are set at the beginning of the contract period by the Minister for Transport. Annual fare adjustments for private operators reflect merely movements in the cost index. The Tribunal proposes that a franchising model be adopted when present contracts expire. Fares charged under the franchise system would be determined as part of the tender process.

Recommendation
On expiration, all current private bus contracts should be replaced by a competitively tendered franchise system.

In the interim, the Tribunal recommends that DoT improve the reflectivity of the private bus cost index. The new index should be the subject of an annual independent audit.

3.2 Sydney Buses

Fundamental considerations in determining Sydney Buses' fare increase are:

- the extent to which the STA can reduce costs or increase productivity
- optimal levels of capital expenditure
- the need for an appropriate target for a Rate of Return (ROR)
- the payment and impact on pricing and service level CSOs.

Efficient costs

Data provided by the STA shows that it recovers less than the costs of providing its services. STA forecasts for 1996 indicate total operating costs of $320.8m with 56.1% of costs being recovered from fare revenue (excluding concession reimbursements). Overall, cost recovery has improved from 38.8% in 1990/91. However, the extent to which fares recover efficient costs is not clear.[34]

In estimating efficient costs the STA compares its fare structure and costs with that of the maximum schedule for private bus operators. The STA's view is that this comparison shows where it stands in relation to best practice. NCOSS suggests that this comparison is

32 Except for 1996 when driver wage increases lifted the private bus cost index above CPI and a two stage increase was used to reduce any impact on customers.

33 NCOSS, submission to Tribunal, October 1995, p 16.

34 Efficient costs are those costs incurred by an organisation which is deemed to be operating at best practice.

not valid because the STA serves higher population densities and has commuter passenger loadings which lead to lower costs per passenger.[35]

Because operating environments and fare systems differ, the Tribunal advises that care be taken in comparing Sydney Buses' costs with those of Sydney private operators and in assuming that private operators are operating at best practice. On this point, the conclusions of previous analyses have been mixed. The interim report[36] highlights further areas where the STA could improve to reach the efficient cost of best practice.

Fares and government funding should be based on the efficient cost of operations, and not on the current cost structure so that operators have an incentive to improve their efficiency and tax payers are not funding inefficiencies.

Productivity improvements

In the interim report the Tribunal presents results from a number of cost studies. Each of these shows that the STA's costs are greater than those of a private operator providing the same service.

When examining all the studies, the Tribunal paid particular attention to the most recent report which was prepared by Travers Morgan.[37] This report calculates a cost differential of $78m between the actual cost of Sydney Buses and estimated costs where private operators provided the same services. Sydney Buses claims that of this only $23m can be eliminated through medium term efficiency gains. The Tribunal's interim report states that is the minimum level of savings achievable through efficiency gains and encourages the pursuit of gains beyond this.

The STA's submission and subsequent information provided to the Tribunal maintains that costs could reduce by only $23m. In reducing the potential gains to $23m, the Tribunal considers that the STA has overstated its uncontrollable costs. STA has not fully pursued potential productivity and efficiency gains available by:

- increasing driving or operating hours toward the level of paid hours
- employing the majority of new drivers on casual/part-time terms
- aligning the employment conditions of all future and, where possible, current drivers to private sector levels
- reducing overheads and administration costs.

Having witnessed substantial labour productivity gains across numerous government authorities under regulation, notably water and electricity, the Tribunal believes similar gains are available in transport.

The Tribunal recognises that the gains listed above require cultural change. Nevertheless, the Tribunal believes that efficiency gains similar to those estimated by Travers Morgan are possible in the longer term. The Tribunal questions whether a private sector operator providing the same service would continue to pay the higher costs.

[35] NCOSS, submission to Tribunal, April 1996, p 8.

[36] IPART Transport Interim Report No 2 *Buses and Ferries*, March 1996.

[37] STA, submission to the Government Pricing Tribunal, September 1995, p 71.

Considerable scope for improvement exists between current STA costs and efficient cost levels. The Tribunal would like to see greater incentives for progress in this area provided within the CSO contract (see CSOs chapter 2).

The Tribunal will continue to closely monitor the costs of State Transit's bus business in comparison with 'best practice' benchmarks world wide, taking into account differences in terrain, population densities and industry characteristics.

Capital expenditure

The capital structure of the STA is being shaped and driven by current and future capital expenditure programs. The appropriateness of the current capital expenditure program is dependent upon the reasonableness of patronage growth assumptions.

Following 7.2% growth for the year to March 1996, the STA's 1996 submission forecasts growth in Sydney bus patronage of 25% over the next five years (and possibly within three to four years). To accommodate this forecast high growth patronage the STA has embarked on a large capital expenditure program of over $160m to be completed by the year 2000. The predominant feature of the STA capital program is a major bus fleet replacement program purchasing at a rate of over 75 vehicles per annum.

Contracts to be completed by 1999 are for: 30 Midi ($6.6m), 125 Volvo ($37.5m) and 300 Scania ($87.1m) buses.[38]

The Midi buses will operate routes featuring flexible pick ups and set downs across Sydney. This innovative approach will alleviate accessibility problems currently experienced in some outer regions.

Unreasonable levels of capital expenditure on fleet replacement could impinge on the STA's ability to service debt and/or place substantial upward pressure on fare levels or CSO levels.

The STA fleet standards are already above current, and likely future, Department of Transport minimum standards and private sector levels. At the public hearings the Tribunal sought information on the patronage and revenue impact of the shift toward a superior fleet. Using evidence on the willingness to pay for fleet quality from London Buses,[39] the STA has estimated that each $1 spent on capital improvements produced a $1.04 improvement in farebox revenue.[40] This was based on the assumption that customers would value Sydney Buses' superior quality at 60% above private buses. However, this analysis is flawed because it compared an average private bus to a new STA bus and did not fully consider the effects of mixed age fleets. Forecasts for quality driven patronage increases should be based on improvements to the average fleet quality and not on the quality achieved with new buses. The STA's analysis also fails to consider the capital expenditure programs of private operators which although targeted at lower service levels than STA, will improve average fleet quality.

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38 NSW Budget Paper No 4 1996-97, p 114.

39 Steer, Davies and Gleave, *Value of Quality - London Buses*, 1995.

40 STA. Correspondence to Tribunal, 20 August 1996.

Recommendation
The long term implications of the STA's capital expenditure program should be considered in detail, including a full analysis of the farebox impact of a superior quality fleet.

Rate of return (ROR)

A commercial enterprise will invest in new capacity only if it expects to earn a commercial return over the life of the investment. The 1996 STA submission states that a suitable target ROR on net assets is 15% per annum. The Tribunal notes that this target utilises an historical cost approach in which assets are not revalued. The conversion of asset valuations from historical cost to replacement cost is estimated by the STA to halve the equivalent target rate of return to approximately 7%.

NCOSS supports the STA's achieving a reasonable rate of return:

> "Maximum bus fares should be set so the return on net assets does not exceed 10%"[41]

In principle, the Tribunal agrees that the STA should have a positive ROR, but believes that Sydney Buses can achieve, at least in part, this through efficiency gains rather than through price increases.

The Tribunal will continue to balance the tension between achieving a commercial ROR and maintaining acceptable fare levels which reflect efficient costs. Within this context the Tribunal needs to investigate whether the STA has developed the best strategy for investment.

In its submission, Treasury has expressed its concern that the STA will not be able to achieve a positive ROR and cost savings while holding fares down.[42]

Recommendation
In order to earn a "reasonable" ROR on assets, the STA should:
- ***achieve best practice in operations***
- ***clarify the CSO program***
- ***match its capital investment program with an appropriate level of service quality.***

Quality of service

Travers Morgan estimates that $16.4m of the cost disadvantage, compared to private operator's providing the same service, can be attributed to quality of service.[43]

A distinction needs to be made between quality of service and levels of service which exceed the minimum service levels.

Quality of service relates to standards of service delivery such as the provision of a customer service hotline, air conditioned buses and uniforms. *Minimum service levels* relate to quantity and frequency of services as prescribed in the service contract.

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[41] NCOSS, submission to Tribunal, April 1996, p 14.
[42] NSW Treasury, submission to Tribunal, April 1996, p iv.
[43] STA, submission to Tribunal, April 1996, p 27.

The STA states that:

> "Part of the Sydney Bus cost structure is committed to the delivery of a standard of service which exceeds the "normal" quality of service. These costs are incurred at the discretion of Sydney Buses in its drive to attract additional patronage. Such costs are not "uncontrollable" as implied in the Interim Report. Rather they are deliberately incurred as they make a significant contribution to the relatively high levels of patronage carried by Sydney Buses.[44]

The Tribunal has questioned the STA concerning the need to incur such high costs and whether passengers are prepared to pay for a superior quality service. In answer, the STA has provided the results of Australian and international studies. The Tribunal believes that if patronage growth from quality is as strong as STA claims real fare increases may be unnecessary. The STA highlights the results of a study by London Transport Buses which provides comprehensive valuations of individual bus service attributes:

> "The study sought to identify those areas where service improvements could be made, prioritise them from the passengers' perspective and provide monetary valuations for them.
>
> The study found that passengers were prepared to pay 26.1 pence to move from the current service to the 'perfect service', with the perfect service comprising a series of attributes consistent with each respondent's notion of their most preferred service improvements. This is equivalent to around 60% of the average London bus fare."[45]

While STA continues to use a mixed fleet of old and new buses, customers are likely to have confused expectations of quality.

In support of the STA's view that quality boosts patronage, the Nature Conservation Council claims:

> "Australian and international experiences demonstrate that increased expenditure on service levels results in increases in patronage."[46]

Regarding Toronto, Pill states

> "Service is always more important to riders than the fare level. At typical fare levels, fare elasticity is about one third of the service elasticity. That is, service level and quality are about three times more important in determining whether a person will choose transit, than the fare level is."[47]

The STA stresses that expenditure on quality should be excluded from any comparison with the private sector as it does not reflect the efficiency of delivery of a given level of service.

The Tribunal believes the STA should ask its customers whether they are willing to pay for higher quality and if so, how much.

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44 STA Submission to Tribunal, April 1996, p 27.
45 STA. Supplementary correspondence. 20 August 1996.
46 Nature Conservation Council, submission to Tribunal. April 1996, p 2.
47 J Pill, Transit and the Automobile: Toronto's Experience. Paper presented at the Competing with the Car Conference sponsored by the Conservation Council of Victoria, Melbourne. March 1992, p 2.

Minimum service levels

The government pays service CSOs for services greater than the minimum which are regarded as uneconomic. The STA believes it can remove the service CSO for Sydney Buses over time.[48]

The BCA asserts that minimum service levels (MSLs) are continually being recalculated under the Act:

> "The Act insists that operators' commercial contracts have the service levels constantly upgraded to:
> (a) reflect any change in the patronage grading of the region, due to changes in demographics that may have affected the patronage potential;
> (b) reflect any movement in the average frequency levels being provided for the time being by all commercial contractors in similar contract regions (ie regions with a similar patronage grading). Such a revised "average" becomes the new "minimum"."[49]

Although the MSLs are updated, they may need to be realigned with the government's transport policy objectives. This may be the case for some STA services.

The BCA submission implies that the Tribunal wants the STA to be paid a service level CSO for all services above the MSL. However, although most services above the MSL are uneconomic and receive a service level CSO, some STA services above the MSL are profitable. The STA must identify the unprofitable services and implement marketing strategies to improve viability and demand.

Treasury supports a review of MSLs relative to travel demand patterns.[50]

Is an overall fare increase warranted?

The Tribunal has previously stated

> "There is no case for an overall increase in fare levels for the STA. Whether overall fare levels should be kept constant in nominal or real terms over the proposed period for the medium term price path is a matter to be considered in finalising the Inquiry. The scope for cost reductions and the argument regarding a commercial rate of return will determine this issue."[51]

In its submission the STA gives elimination of the pricing CSO as an argument for real fare increases. As discussed earlier, the Tribunal does not support such a view.

The Tribunal believes that in the case of Sydney Buses there is no argument for either a pricing or a service level CSO. Service CSOs can be eliminated by reviewing services provided against the MSL. The Tribunal considers that efficiency improvements could eliminate the need for a pricing CSO.

The Tribunal appreciates that some of the efficiency improvements cannot be achieved in the short term and require cultural change. Sydney Buses will need a transition period from the current CSO environment to one of no CSOs.

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48 STA, submission to Tribunal, April 1996, p 1.
49 BCA, submission to Tribunal, April 1996, p 6.
50 NSW Treasury, submission to Tribunal, April 1996, p 17.
51 IPART, Transport Interim Report No 6 *Fair Fares: an Overview*, March 1996, p 10.

STA has expressed concern that freezing real fare increases is stopping business growth. The Tribunal has a broader view. It wants to balance fare levels, community welfare effects, standards of service and patronage impacts. Individual customers will have different views regarding what is the correct balance. The STA has yet to demonstrate to the Tribunal that it has the optimal settings to necessitate a real fare increase to finance capital expenditure commitments.

Recommendation
Following satisfactory cost reductions and the removal of CSOs for Sydney Buses, the Tribunal will reconsider the case for real fare rises to finance capital expenditure or business growth. In the interim, the Tribunal will permit fare rises which are broadly in line with the CPI and will continue to correct fare anomalies to improve customer equity.

Fare structure

In its submission for the 1996/97 fare determination, the STA states that it intends to move to a finer distance based fare structure. However, it does not propose to introduce a distance based fare structure in 1996/97.

Treasury supports reducing anomalies in fare bands. Other submissions, support narrower fare bands[52]. NCOSS considers that as with the private operators, STA fare bands should be based on sections.

> "STA fare bands should be made narrower. Fare bands for Government and private bus services should be brought in line, at least for the most common distances (up to 9 sections)."[53]

The Tribunal notes that private buses in the metropolitan area currently use a 35 band (section) distance based system. Long term integration may be enhanced by public and private buses sharing a common fare structure and ticketing.

Resolution of this central issue requires a decision as to whether costs for Sydney buses are largely fixed or variable, ie distance based. Moving to narrower bands would be sensible if bus costs were distance based. In support of distance based fares, STA has provided an analysis based on route cost information to the Tribunal.

Arguing that bus costs are largely fixed (and not distance based), Professor Richmond from the Institute of Transport Studies advocates a simple two band fare system.[54]

Professor Richmond contends that bus operating costs on a defined route are largely fixed. Once a bus is timetabled, it must run. Costs such as the driver, fuel, and capital become fixed in nature. A flatter structure provides the best reflection of costs It also provides significant simplicity benefits and would reduce over-riding. (That is people staying on beyond the distance allowed by the fare paid.)

The Tribunal sees merit in each of these approaches, but has insufficient information to determine whether one is better than the other. The current five band system may require reform as over 98% of customers use the first three bands. A new system which amalgamates the last two long distance bands and divides the section 3-9 band may have benefits of simplicity and equity.

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52 Mr A Parker, submission to Tribunal, 1996.
53 NCOSS, submission to Tribunal, April 1996, p 14.
54 J E Richmond, Professor of Transport Planning, Institute of Transport Studies, 1996 , submission, p 1.

Sydney Buses should provide detailed proposals for changes to cash fares and the fare structure.

Penalty-free transfers

In the interim report, the Tribunal proposes that Sydney Buses allow penalty free transfers between its own buses.

Both the STA and BCA have indicated that the STA already allows penalty free transfers on buses at designated transfer points. Sydney Buses believes that:

> "The existence of cash single ride transfer tickets and the ability to complete free transfers on the TravelTen ticket at designated transfer points meet the bulk of demand for transfers within the Sydney Buses network. It has to be recognised, however, that transfer arrangements need to be tightly controlled on revenue protection grounds."[55]

Although it is possible to transfer at selected points, the STA does not seem to promote the capacity to do this. As leisure and commuting trips increase in diversity, expansion of the transfer system will be necessary. Promoting transfers will enhance service integration and patronage.

Multi-ride and multi-mode tickets

For the bus business, the Tribunal maintains that any increases in fares should standardise discounts by focusing on the multi-ride and multi-mode tickets.

The STA does intend to standardise discounts for multi-ride (TravelTens, FerryTens and bus/ferry TravelPasses) and multi-mode tickets (rail/bus/ferry TravelPasses) and has suggested that the appropriate level of discount should be 15-20%. NSW Treasury supports a discount of the order of 15-20%. NCOSS supports the gradual reduction of the TravelTen discount to within a range of 15-20%.

The Tribunal notes that, in general, the current discounts of the multi-ride tickets remain well above this percentage. When multi-rides were introduced they had a discount of 20%. This relativity was eroded in 1988 when single ride fares were increased by 12.5% without a corresponding increase in the TravelTen fares. The 20% discount has not been restored despite increases over the past few years in multi-ride tickets and the freezing of cash fares. For all but the Purple TravelTen tickets, discounts exceed 20%. Smaller increases are needed for the other TravelTen tickets.

The Tribunal recognises that there are benefits to commuters and the STA in providing discounts and accepts that 20% is a reasonable discount. On this basis, there is scope for the shorter distance TravelTens to increase by up to 25%. However, the Tribunal will not support such an increase in one move due to the high impact of such a charge on people with low incomes. Results of a study by the ITS[56] imply higher modal transfers when multi-trip fares increase.

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55 STA, submission to Tribunal, April 1996, p 19.

56 Hensher & Raimond, summarised in IPART, Research Paper No 7, *Estimation of Public Transport Fare Elasticities in the Sydney Region,* October 1996.

Recommendation
The Tribunal supports discounts for "Ten" tickets of between 15 and 20%.

TravelPass tickets provide commuters with a flexible ticketing arrangement at generous discounts. Based on an analysis of usage data the STA estimates these discounts at between 34% and 58%. Commuter groups and NCOSS question the calculation of this discount.

The Tribunal has asked previously for more detailed analyses of the trips undertaken by TravelPass holders and calculation of the discounts. Recent TravelPass patronage data provided by the STA shows that discount levels average between 30 and 40%. Discount reductions arising from the 1996/97 determination are modest and the Tribunal recognises that the discounts remain high.

In its submission, Treasury recommends that the price of multi-modal tickets be more closely related to the costs of the individual components.[57] Accepting the high level of usage and the fact that they are primarily used by commuters, NCOSS supports the proposal to increase real fares for bus travel with the Red TravelPass.

The Tribunal notes that contrary to a suggestion made in the interim report, most private bus operators offer some discounts. The BCA has provided survey results showing eight of the 11 major private operators offer some discounts with the average discount being 22%.

As the discounts offered for the TravelPass tickets do not reflect the number of trips taken each day, the Tribunal believes that the TravelPass provide cheap travel to commuters. However, the Tribunal does not wish to set a specific discount for TravelPasses.

Recommendation
While supporting increases in TravelPasses, the Tribunal will consider the extent of increases for these tickets annually.

Franchises

In the interim report, the Tribunal proposes that all franchise areas be open to competitive tender at the end of the five year contract.

The introduction of competitive tendering for bus franchises across an urban area could solve many of the problems that currently arise with respect to government funding. There are several possible models for competitive tendering for a bus franchise area (see box below).

In tendering a franchise, the Government could seek competition on one or a combination of:

- the fares to be charged
- the services above the minimum which are to be provided
- the payment to government or the subsidy from it.

For example, a well designed tender could allow the government to specify minimum service standards, including non-commercial service requirements such as night and weekend frequencies. All targeted concession requirements, including pensioner, senior

[57] NSW Treasury, submission to Tribunal, p iv.

citizen and school student travel, could be specified explicitly and could be funded by the relevant "purchaser" department as part of the franchise. The tender could specify maximum fares or could be designed so that actual fares were an outcome of the tender process. Franchise areas would be open to competitive tender again at the end of the franchise term (say five years).

This proposal prompted a wide range of responses.

The Central Sydney Community Transport Group (CSCTG) does not support the concept of automatic five-yearly tendering for bus contracts in exclusive franchise areas.[58] The CSCTG argues that the current system ensures the stability of the industry and the services offered. CSCTG believes a five year contract would be too short for investment planning and operators' knowledge of unique areas is essential for service planning. CSCTG claims that

> "The inclusion of the concept of the potential operator of a 'franchise area' paying the government for the right to operate transport services is a new and dangerous concept."[59]

In its submission the Peninsula Public Transport Coalition believes that the five year contract period is too short. The BCA also contends that five years is too short for contracts, asserting that operators need some measure of certainty for long term capital financing.

The CSCTG questions whether the purported cost efficiencies of franchising would be outweighed by the inefficiencies in undertaking the tasks.

In its submission the BCA is critical of the Tribunal for its proposed model.[60] The BCA considers that the Tribunal's proposal demonstrates a lack of understanding of the bus industry. In the BCA's view, the existing New South Wales model, which was used as a model for the privatisation of Melbourne bus services, provides better outcomes than can be achieved by competitive franchising.

The Tribunal notes that competitive tendering has been introduced in many places. Adelaide and Perth have introduced competitive tendering for bus routes with five year contract terms. Further, terms beyond five years reduce the government's control of services and its ability to adapt services to changing needs. Despite arguments against the idea, the Tribunal considers that a five year tender period is appropriate.

Treasury supports the franchising proposal, but is aware there are implementation issues.[61] The DoT has indicated that there are constraints within the current contracts for implementing a widespread competitive tendering market.[62] However, where operators do not meet set performance standards the service will be put up for a competitive franchise.

A concern expressed by the CSCTG is that the STA service area may be broken up.[63] The CSCTG believes that Sydney Buses provides a range of services which would be not available if smaller operators were running its routes.

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58 CSCTG, submission to Tribunal, April 1996, p 1.
59 CSCTG, submission to Tribunal, April 1996, p 4.
60 BCA, submission to Tribunal, April 1996, pp 42-45.
61 NSW Treasury, submission to Tribunal, April 1996, p 18.
62 DoT, communication with Tribunal, August 1996.
63 CSCTG, submission to Tribunal, April 1996, p 3.

The CSCTG agrees with the imposition of sanctions and penalties for not meeting contract requirements.[64] If automatic five yearly tendering proceeds, the CSCTG suggests an alternative approach.[65]

Types of contract

Fixed price contract - involves a certain price being proposed for a given amount of service over a specific contract length, usually expressed in cost per unit of service, such as per service kilometre or per service hour. There are two basic forms of fixed price contract: pure fixed price contracts and indexed fixed price contracts.

Incentive contracts - encourages improved quality through the incorporation of incentive payments linked to achieving and maintaining specified standards.

Cost plus contract - sets payments at actual costs plus a profit margin.

Period contract - Generally, price negotiation is annual and begins in the second year of the contract. Periodic price negotiation can be costly, because price competition is limited to only a part of the contract (such as the first year) and the winning contractor has a degree of market power over price in subsequent negotiations, which are non-competitive. Further, such negotiation consumes additional administrative time. Periodic price negotiation can create large auditing burdens in verifying contractor costs.

The CSCTG proposes that all bus franchise tenders be subject to independent and transparent review. This system would require the Department of Transport to monitor bus operations and conformity to contract through a system of penalties. Repeated non-performance would result in the cancellation and retendering of the franchise.

Until competitive tendering is implemented the government and the Tribunal will seek to continue to pressure STA to reduce costs for all services via efficiency improvements. This will ensure that the full benefits of franchising are available to the government when a tendering system is introduced. By becoming more efficient and approaching private sector cost levels the STA will ensure that it is well placed to secure franchises in the competitive tender environment.

As a part of franchising initiative, there is potential for substantial benefits from managing targeted concessions within a funder-provider framework. Targeted concessions including pensioners and school children could be funded by the relevant purchaser department as a part of the franchise agreement.

The Tribunal will continue to explore and encourage new proposals to enhance competition and usage of urban passenger transport services.

64 op cit, p 5.
65 op cit, pp 11-12.

Recommendation

All franchise areas should be open to competitive tender at the end of the five year contract. There will need to be appropriate incentives, sanctions and penalties to ensure contract requirements are met.

Standard fares could be determined on the basis of information provided in the tender process and adjusted periodically.

Medium term price path

For the other industries it regulates, the Tribunal has put a medium term price path in place. For example, for Sydney Water the Tribunal has introduced a four year price path based on CPI-X.

The benefit of a medium term price path is that it provides greater revenue and investment certainty to the operator and owner.

The issue is essentially a question of whether the Tribunal should continue with annual determinations for public transport fares or put in place a medium term price path.

In making a medium term price determination, the Tribunal needs to ensure that State Transit can deliver its functions and meet its objectives. The Tribunal also needs to ensure that the interests of customers are protected and that fares do not increase too rapidly or inappropriately. An important consideration in adopting a medium term price path is the need for significantly greater information. This places a burden on the regulated public utility which may not be justified.

After all, the private bus industry has some investment certainty provided by a medium term price path based on fare rises escalating by an agreed bus cost index.

To enable a medium term price path for Sydney Buses to be established, the Tribunal requires the following critical elements of business to be finalised:

- STA's capital structure
- STA's capital expenditure program
- the elimination of pricing CSOs
- satisfactory progress on efficiency gains.

Recommendation

The Tribunal proposes to continue to conduct annual determinations for the STA bus and ferry services. A medium term price path will be established once the STA has satisfactorily addressed numerous critical financial issues.

3.3 Ferries

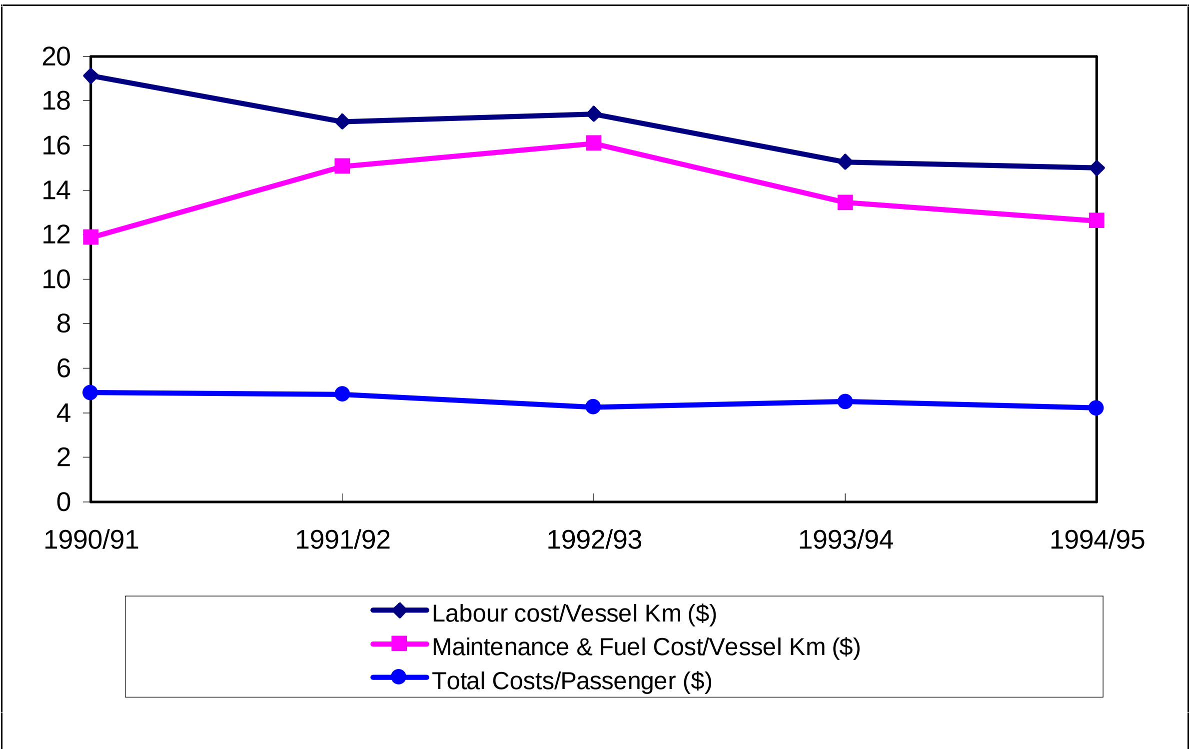
Ferry operations have shown a gradual improvement in performance. Over the past five years total expenses have fallen by 16% while passenger revenue has been relatively stable.

Performance indicators used in the interim report on ferry services showed that total costs and labour costs per vessel kilometre were falling. However a decline in ferry patronage has led to a deterioration in the cost effectiveness of ferry operations. This has meant increased costs per passenger. In its submission, the STA suggests that:

> "This analysis is quite misleading and does not accurately reflect the continuing improvement in Sydney Ferries' performance."[66]

The following graph uses revised data provided by the STA.

Figure 3.1 Performance indicators, Sydney Ferries



Source: STA Annual Reports.

Recent financial models provided by the STA indicate bullish growth forecasts for Sydney Ferries totalling 24% over the next five years. If this patronage growth can be achieved, while holding costs relatively constant, cost recovery will rise from a current level of 56% to approximately 76%. While the patronage forecasts are ambitious, they provide targets for a strategic marketing campaign and will be assisted by growth in the tourist and leisure markets.

66 STA, submission to Tribunal, April 1996, p 34.

Efficiency improvements

In its submission, Matilda Cruises provides data on “Rocket” ferry services which could provide a benchmark for STA ferry services. The basis for this comparison is now dated. However, the analysis shows that for all routes Matilda Cruises could operate at significantly less cost than Sydney Ferries.

The Tribunal is cautious about drawing conclusions on the efficiency of Sydney Ferries’ operations. The analysis makes comparisons to Sydney Ferries’ routes by way of cost per passenger. The higher cost of Sydney Ferries reflects the low patronage of the services relative to the size of vessel being used and the use of on-board fare collection by Matilda. On commuter services, on-board collection is clearly inappropriate for Sydney Ferries given the volume of peak demand and ticket integration requirements.

The STA cites differing operating environments as the basis for higher costs. Specifically, Matilda operates ‘shuttle’ services while the STA adheres to a timetable. Matilda’s vessels do not carry large peak (commuter) loads, and Matilda does not conform to an integrated ticket system. The STA is required to operate non-commercial services eg off-peak services to Hunters Hill and Mosman, while Matilda focuses on profitable niche markets or DoT contract services.

One clear conclusion which can be drawn from this comparison is that Sydney Ferries’ services are under patronised and some routes would be better operated by smaller vessels. The STA supports this conclusion and has pursued a policy of preferring smaller vessels in its current and future investment program.

The key question for the Tribunal is whether the ferries being used by Sydney Ferries are the optimum specification (size, speed, crewing requirements) to perform their transport task. This question will be particularly relevant when Sydney Ferries purchases new fleet. There may be benefits in ensuring vessels are interchangeable on routes to facilitate flexible allocation of the vessel most suited to meet anticipated demand and reduced customer inconvenience if they break down.

Fares

In the interim report, the Tribunal reveals there was a $14.8m revenue shortfall for Sydney Ferries from a revenue requirement of $41.4m. A key strategy for Sydney Ferries is to increase revenue without increasing costs. Many services are clearly poorly patronised. Sydney Ferries could increase its cost recovery by increasing boardings on most services. As suggested above, this may mean replacing some of the existing fleet with smaller, flexible fleet which can be tailored to service patronage levels.

In the long term the government should evaluate the merit of competitively tendering ferry services which carry few passengers.

The interim report suggests that ferry services are of two types: those which could recover costs and hence are commercial and those which are chronic loss making services. In its submission the STA did not dispute this view.

Analysis of STA route cost data suggests that for some services small increases in the full fare would improve cost recovery. However, the Tribunal notes that most ferry travellers do not buy the single adult fare. They purchase multi-trip, TravelPass and concession tickets rather than single or return tickets.

The STA should propose combining increases in prices with reductions in service levels to eliminate the revenue shortfall on commercial ferry services.

Fares on the chronic loss-making ferry services should increase by a similar amount to fares on the services that can better cover costs. The government should consider whether these perpetual loss-making services should continue at reduced levels or, indeed, at all. If they continue, ongoing support through an explicit CSO payment will be required. In reviewing the need for these services the government should consider whether the current size of vessels is appropriate to the needs of particular routes.

In the interim report, the Tribunal indicates that it considers there is a case for a closer relationship between fares and distance travelled. In response to this suggests,

> "Sydney Ferries wishes to reaffirm its commitment to the staged implementation of distance based fares for the inner harbour when the appropriate technology is available."[67]

For the annual determination of fares from July 1996, the Tribunal has approved the introduction of a second inner harbour zone for travel greater than 10 km, thus creating a second inner harbour fare band.

Multi-ride and multi-mode fares

FerryTen tickets were introduced in 1989 but, unlike the bus TravelTen tickets, were never offered at a low discount. The range of discounts varies from Inner Harbour (Zone 1) FerryTens which offer a discount of 41% from the single ride price to the JetCat Ten which offers a discount of 20%. Unlike the TravelTen tickets, there is no need to maintain relativity among the FerryTen tickets. Therefore, the increases may differ for each ticket. STA is seeking to reduce FerryTen discounts to around 30% while the JetTen will be kept at 20% of the full fare.

Recommendation
The Tribunal supports the realignment of discount levels and will support modest increases in all ferry fares to improve cost recovery.

Competition issues

In its submission, Matilda Cruises raises two issues related to competition policy:

1. Access to particular routes for operators other than the STA
2. Charges set for access to wharves.

The STA is contracted to provide most ferry services in Sydney Harbour. Matilda Cruises has a commercial contract with the DoT to provide ferry services from Circular Quay to Darling Harbour, Greenwich, Longueville, Hunters Hill and Riverview.

Matilda Cruises believes that all Sydney's ferry routes should be open to competitive tender and that the STA should compete without being subsidised.[68]

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[67] STA, submission to Tribunal, April 1996, p 31.

Opening up the ferry routes to tender could be a means of encouraging efficiency improvements in the ferry system.

Recommendation
The Tribunal believes that the Government should consider competitively tendering ferry routes on Sydney Harbour.

No single organisation owns all the wharves. The Ports Authority owns some, STA owns some, and local councils own others. Matilda Cruises uses some of these wharves to provide ferry services.

Matilda Cruises states

> "State Transit's ferry division owns a number of wharves around Sydney Harbour. In order for another operator to utilise such wharves, a sizeable fee is charged by State Transit which has the effect of preventing any competition at the wharf, no matter what the origin of the non-STA ferry that requires such use."[69]

The Tribunal considers that Matilda Cruises is a marginal user of these facilities and should pay only marginal costs or a nominal fee for limited access to the wharves.

In response to Matilda Cruises' questioning whether wharf ownership should be in the hands of a ferry operator, the Tribunal notes that, if the wharves were considered an essential facility, ownership of the wharves by the STA would not accord with national competition policy. However, the wharves have not been declared essential facilities and an access regime has not been established.

The STA's setting of access charges is an immediate issue for Matilda Cruises. It is also an issue for the future competitive operation of ferry services in Sydney.

Recommendation

The Tribunal recommends that the Government review the ownership of ferry wharves in the light of national competition policy and the COAG Competition Principles Agreement.

Service levels

In its interim report, the Tribunal proposes that the government should consider whether perpetual loss-making services should continue at reduced levels or, indeed, at all (where alternative public transport options exist). Loss-making services require continuing support through an explicit CSO payment.

In general, submissions suggest that service levels should not be decreased. The STA believes that:

> "It is the prerogative of government to set service levels for Sydney Ferries."[70]

The Tribunal does not disagree with this view. The Tribunal believes that government should assess its service requirements for Sydney Ferries. Where the government wishes to run uneconomic services, the government should fund those uneconomic services through explicit and transparent CSOs.

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68 Matilda Cruises, submission to Tribunal, April 1996, p 22.
69 op cit, p 20.
70 STA, submission to Tribunal, April 1996, p 31.

The Tribunal notes that some of the ferry trips carry very small numbers of passengers, eg the first journey each morning. The Tribunal appreciates that it is necessary to move vessels from their overnight mooring to the start of their peak journeys. However, the Tribunal believes that Sydney Ferries should review the timing of its morning trips. In the interim report, the STA is noted to have suggested that savings on the Manly services could be made by decreasing the service level currently required by the DoT. The STA estimates that savings of around $3.2m per annum, could result. This would reduce pressures for fare increases to recover costs and cause minimal passenger disruption. Overall, ferry timetables should not be considered permanent base levels and should be reviewed regularly to realign services with demand and reduce costs where possible.

Capital expenditure

The main feature of the current capital expenditure program is the acquisition of an additional RiverCat at a cost of $7.5m as part of the Olympic transport program. Future acquisitions will assist flexibility and improve fleet utilisation levels. As mentioned previously, future vessels should be selected on the basis of average peak demand rather than maximum demand. This will lower costs where smaller vessels are better suited to patronage levels.

Service standards

STA ferry services comply with all regulatory requirements, of the DoT, the RTA, the Waterways Authority and the EPA. The STA is required to comply with service standards required under the DoT CSO contract. Services must meet the following general aims:

- high levels of frequency, timeliness, safety, reliability and cleanliness
- accessible, current and understandable timetables
- polite, courteous and helpful staff
- the alignment of services with the travel needs of customers
- increase accessibility of services to all passengers.

The Tribunal notes the conflict between achieving high service standards and improving cost recovery. However, the performance of Sydney Ferries can be enhanced through programs focusing on:

- further efficiency gains
- realignment of the required service standards by the government to better match the transport needs of potential and existing customers
- improving patronage.

Manly services

In the interim report, the Tribunal notes that JetCat and ferry services to Manly are essentially competing services. The Tribunal suggests that either of these services could be profitable if the other was no longer provided.

The Peninsula Public Transport Coalition (PPTC) supports the Tribunal's concern:

> "We have consistently drawn attention to the dubious wisdom of spending $16m on JetCats and tying up wharves … for their competing use, as against adding a fifth ferry to the fleet."[71]

[71] Peninsula Public Transport Coalition, submission to Tribunal, April 1996, p 9.

The Tribunal does not support the purchase of a fifth ferry and the STA does not want to remove either the JetCat or the ferry from the Manly service. In supplementary submissions the STA has stated that the market is sufficient to warrant maintaining both a premium JetCat and a ferry service.

> State Transit proposes a combination of fare increases and service initiatives to move both services towards commercial viability.[72]

Recognising the recreational nature of weekend travel the PPTC proposes that:

> "JetCats run only on weekdays and Saturday mornings."[73]

The PPTC also notes that the differential between the ferry fare and the JetCat fare (currently $1.20) does not fully reflect the cost structure of each service nor the premium nature of the JetCat service.

Recommendation
The Tribunal considers that Sydney Ferries should review the scheduling of the Manly Ferry and JetCat services so that the services do not compete with each other.

3.4 Newcastle Bus and Ferry Services

The urban population of Newcastle is almost 300,000. Of these, 77% live within Newcastle Buses' service area. Passengers who use public transport often have little or no alternative. They include pensioners, school children, tertiary students, low income earners and social welfare recipients. Passenger farebox revenue represents around 30% of total revenue, including CSOs and concessions. The market is difficult to service as only 25% of all public transport journeys have the Newcastle CBD as their destination.

The STA has indicated that the Newcastle bus market is substantially different from that of Sydney. Newcastle services are forecast to achieve a cost recovery ratio[74] of 25.7% for 1996, compared to Sydney Buses at 65.4%. Nevertheless, the BCA considers that the Newcastle service resembles many of the service areas operated by its Sydney members and is viable.

In the interim report, the Tribunal endorses the introduction of a time based fare structure on a trial basis for Newcastle Buses. A proposal by the STA for a time based fare structure was approved in the recent annual determination and will apply from January 1997.

However, the BCA believes Newcastle should be profitable and is opposed to the introduction of time based fares. The BCA is particularly concerned that time based fares do not reflect the cost of providing journeys:

> "By adopting time based pricing, Newcastle buses would be locking themselves into a permanent requirement for service CSO payments. The Association believes that Newcastle is more than capable of supporting a high frequency commercial bus network."[75]

The Tribunal has noted earlier in this report that it has not been convinced that bus costs are best reflected by the distance travelled. The Tribunal has permitted a trial of time based fares as a potential method of improving patronage and cost recovery on bus services. The

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72 State Transit Authority, submission to Tribunal, April 1996, p 30.
73 Peninsula Public Transport Coalition, submission to Tribunal, April 1996, p 9.
74 Cost recovery ratio: passenger farebox revenue (not including concessions) divided by total expenses.
75 BCA, submission to Tribunal, April 1996, p 40.

Tribunal has a strong preference for the competitive tendering of bus services. In time the services in Newcastle may be contracted to an operator who will make it a profitable operation. In the interim , the Tribunal agrees with the BCA that

> "Newcastle Buses should be forced to undertake reforms to boost patronage, reduce costs and achieve profitability."[76]

The Tribunal believes that the threat of competitive tendering for the Newcastle routes should be sufficient inducement for Newcastle Buses to make improvements in efficiency and competitiveness.

3.5 Conclusion

Fares for private and public bus operators are set by different authorities. While the Tribunal sets the maximum price for public bus fares, the Minister for Transport sets private bus fares. Consequently, the fares have quite different structures and the increases granted each year vary. Despite this, there are complex interrelationships between the fares. The private fare is used as a benchmark for paying the pricing CSO and for reimbursing the STA for concessional travel.

The private operators are also used as a benchmark for efficiency and potential productivity improvements. Owing to the different environments in which each operator works, comparison is difficult. However, analysis suggests that the STA has considerable scope for efficiency improvements.

The Tribunal considers that cost reductions could be used to offset the need for real fares increases. Once these improvements have been achieved and CSOs eliminated, the Tribunal will consider the case for real fare increases.

The Tribunal proposes that a franchising model be adopted when current contracts expire.

Sydney Harbour ferries have a low cost recovery. Although there may be scope for efficiency improvements, the greatest increase in cost recovery can come about by increasing patronage. The low cost recovery may be a result of using ferries much bigger than required for carrying passengers for most of the day.

Newcastle Buses also has a very poor cost recovery. By increasing patronage these services could increase cost recovery. The Tribunal has approved the introduction of a time based fare for Newcastle Buses on a trial basis. The Tribunal will monitor revenue and patronage impacts of this scheme.

[76] BCA, submission to Tribunal, April 1996, p 40.

4 RAIL SERVICES

This chapter discusses the operation of the passenger rail services provided by CityRail.

4.1 Introduction

CityRail is a business group of the State Rail Authority (SRA) of NSW. Following amendments to the Transport Administration Act, the SRA now provides passenger transport services for urban and rural NSW. [77] The Act makes CityRail purely a train operator, creating a better structure to focus on the core business of moving people.

CityRail is the principal, public transport operator in Sydney and the surrounding region. It operates suburban, outer suburban and regional services in Sydney, the Hunter, the Central Coast, Blue Mountains, Southern Highlands, Illawarra and the South Coast. The CityRail system consists of 296 stations, about 1,500 carriages (1,452 electric and 46 diesel) and about 1,700 km of electrified track infrastructure stretching over 1,018 route kilometres.

CityRail provides over 2,300 services each weekday and employs about 5,200 staff. Approximately 800,000 passengers are carried each weekday. Approximately 70% of journeys occur during the morning and afternoon peak periods when the typical commuter is travelling to or from work.

4.2 CityRail

CityRail is heavily dependent on government funding for its continued operation. The government contributes around $750m a year to CityRail in the form of concession reimbursements, capital funding and operating deficit. In view of this contribution, and in the context of varying demands on government funds for a large range of purposes, there is strong need to assess the value of the massive government contribution to CityRail.

If there is a case for reducing the total contribution to CityRail by taxpayers, this might be achieved in a number of ways - through greater revenue from the farebox (passenger contributions), improvements in efficiency and reductions in total costs, reductions in the level of some services, and reductions in new capital expenditures.

Cost recovery

CityRail's services are divided into three operating segments: CityMet, Outer Suburban and Regional. These segments are very different in terms of costs and revenue. The CityMet segment is bounded by Macarthur and Waterfall in the south, Penrith in the west, Richmond in the north-west, Cowan in the north. This represents CityRail's metropolitan electric services. The Outer Suburban segment serves the area beyond the CityMet region as far as Newcastle in the north, the Blue Mountains (Lithgow) and Wollongong (Dapto). It includes CityRail's inter-city services. The Regional segment is essentially the non-electric services which operate in the Hunter Valley, to the Southern Highlands and to Nowra. The Southern Highlands services are the only Regional services which operate into Sydney station (Central).

[77] The SRA was restructured in July 1996. Ownership and provision of access to the tracks has been placed in a separate corporatised business (Rail Access Corporation). Freight Rail has been separated and corporatised. Track maintenance and control functions have been consolidated in an independent Railway Services Authority. Countrylink is the rural passenger operator of SRA.

As shown in the interim report, above rail operating cost recovery is significantly higher on CityMet services compared with the Outer Suburban and regional segments.

Table 4.1 illustrates the large variation in farebox cost recovery for each business segment.

Table 4.1 Farebox cost recovery by business segment, 1994/95

Segment	Full cost $m	Farebox revenue $m	Farebox cost recovery (%)
CityMet	702	369.1	52.3
Outer suburban	180.5	56.3	31.2
Regional	46.5	5.4	11.6
Total CityRail	**929**	**430.8**	**46.4**

Source: CityRail submission, April 1996, p 1.
Note Farebox revenue includes CSO received for targeted concessions.

Following the restructuring of the SRA, the composition of CityRail's cost structure is changing. As CityRail is now a pure passenger train operator, the most significant change is differentiation of above and below rail costs.

Above rail costs incurred by CityRail in running its passenger transport business include:

- All costs associated with the delivery of passenger services including station operations, electricity, ticketing, revenue protection, passenger security, passenger information and train crewing, but excluding fleet provision and train control.
- Contract costs payable to SRA's Fleet Maintenance Division for routine and periodic maintenance of the fleet.
- Costs incurred by CityRail for plant and equipment and acquisition, including such items as ticketing systems, security systems and computer equipment.
- Head office, divisional management and support costs not directly attributable to a functional area.
- Provision for the future replacement of life-expired CityRail assets.
- Transfers, other accruals and allocated corporate allocations.
- Diesel fuel for regional services.

CityRail's below rail requirements are largely provided by the Rail Access Corporation (RAC), ie track, signalling and other infrastructure used for running the line. Below rail costs include RAC access charges.

Access charges

The access charges are charges levied by the RAC are CityRail's contribution to the cost of:

- infrastructure maintenance and renewal undertaken on behalf of the RAC. This covers routine, major periodic and some capital expenditure on fixed infrastructure assets owned by RAC and used by service providers in the operation of rail services.
- network control
- RAC overhead costs.

In its submission, Treasury states that:

> "Below rail costs (will) continue to be borne by the taxpayer as a more than sufficient offset for the net positive externalities of rail use."[78]

Explicit taxpayer funding for below rail costs means that CityRail do not have to recover these costs and adjusts the cost recovery levels.

Building leases

In its submission, CityRail notes that the initial commercialisation model allocates a cost of $48.2m for building leases.[79] These building leases are for the following SRA owned properties:

- Sydney Terminal (Central)
- Transport House (York Street, Sydney CBD)
- 509 Pitt Street (Sydney CBD)
- Divisional offices
- Stations
- Fleet maintenance depots.

Following the restructuring of the SRA it was anticipated that lease payments would be payable on the above properties. The Tribunal notes that in the restructuring the real estate listed above stayed with the SRA. There is no leasing charges for these buildings. This means that there is no incentive to optimise use of accommodation. CityRail also rents other accommodation, such as 815 George Street, Sydney CBD.

For the SRA owned buildings, better utilisation of the facilities could enable the SRA to lease the accommodation to other occupants. The Tribunal notes that for a small administration staff, the offices of CityRail are spread over many buildings.

Recommendation
The Tribunal believes that CityRail can reduce office costs through a rationalisation of its office accommodation and a facilities management program. Surplus space should be divested or sub-leased.

Productivity improvements

In the interim report, the Tribunal notes that the main components of CityRail's expenditure (inclusive of above and below costs and capital expenditure) are:

- infrastructure capital - 28%
- unallocated overheads and other accruals - 15.7%
- station operations - 12.6%
- train drivers - 7.2%
- train guards - 5.4%

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78 NSW Treasury, submission to Tribunal, April 1996, p vi.
79 SRA / CityRail, submission to Tribunal, April 1996, Section 6 p 5.

Together these account for nearly 70% of total costs. These costs contrast sharply with the proportion of costs attributed to track maintenance of only 4.4% and rollingstock maintenance and servicing of 10.1%.

The Tribunal notes that a significant proportion of the above costs are overheads. The Tribunal believes that this requires detailed scrutiny by CityRail's senior management. Based on this analysis and productivity improvements achieved elsewhere, the Tribunal proposes that CityRail reduce its above rail costs in real terms by 2.5% per annum.

Believing that many of the easy gains have been achieved, Treasury cautions against just expecting future productivity gains.[80] WSROC is also concerned about the effects of further productivity improvements of the order suggested by the Tribunal:

> - Core "front-line" services such as station staff may have to be cut to achieve this figure;
> - CityRail's capacity to meet its target of an 18% increase in patronage may be severely compromised;
> - Cuts may be imposed on those parts of the system … that are deemed to be inefficient. Apart from the equity considerations, this would have the effect of CityRail's imposing a decision regarding service provision which should, as the Tribunal's report acknowledges, be clearly a political decision regarding the level of explicit service CSOs to these services.[81]

From CityRail's viewpoint:

> Efficiencies of this level may not be attainable within the timeframe specified without requiring reductions to be made in front-line customer service areas (eg station staffing).
>
> Such an approach may not be in the best interests of either CityRail or of the wider community. Certainly any review of available efficiency must take into account CityRail's commitment to the provision of quality customer service which, research has demonstrated, requires a significant staff presence on both stations and trains to promote security and to provide assistance and information.[82]

Nevertheless, CityRail acknowledges that cost savings can be made in corporate overheads, train crewing and fleet maintenance (including carriage maintenance).[83] CityRail anticipates that as an outcome of the restructuring of the SRA, CityRail should be able to reduce its corporate overheads by reducing costs in head office functions and streamlining management. It is too early to determine if these reductions have been made.

In its submission, CityRail indicates that under the proposed organisational structure, the number of CityRail employees is expected to fall from 8,277 to just over 5,000.[84] CityRail now advises that the number of CityRail employees is 5,215. The Tribunal notes that much of this reduction has come about through movements between divisions of the former SRA. The Tribunal would like CityRail to provide a breakdown by occupation of its workforce following the restructuring, ie drivers, guards, station assistants and administrative personnel. As a train operator only CityRail should reduce the number of personnel who do not have direct customer involvement.

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80 NSW Treasury, submission to IPART, p 18.

81 WSROC, Response to IPART Transport Inquiry Interim reports, April 1996, p 2.

82 SRA / CityRail, submission to Tribunal, April 1996, section 7 p 1.

83 SRA / CityRail, submission to Tribunal, April 1996, section 7 p 1.

84 SRA / CityRail, submission to Tribunal, April 1996, Appendix E.

The former structure of the SRA did not permit a detailed breakdown of costs. The Tribunal expects that financial management processes put in place under the new structure will enable costs to be monitored more effectively.

Fleet utilisation is the percentage of the fleet rostered to the timetable at the time of highest weekday demand. As such, it is an indicator of how well CityRail uses its trains. In 1994/95, fleet utilisation was 84%. CityRail projects increasing fleet utilisation to 90% in 1997/98 and to 95% in 1999/2000. These improvements will come about by reducing time that carriages spend being maintained and cleaned. This means that by 1998 there will be an additional 56 suburban and 16 InterCity cars available to meet timetable requirements. Higher fleet availability and utilisation should reduce future capital expenditure requirements.

Recommendation
Significant scope for productivity improvements exists within CityRail's operations. The size of potential efficiency gains will become apparent following the submission of CityRail's segmented accounts. In the interim, the Tribunal encourages CityRail to continue to pursue real cost reductions of at least 2.5% per year.

Capital expenditure

CityRail's projections of above rail capital expenditure are shown in Table 4.2.

Table 4.2 CityRail capital expenditure ($m)

Year	1995/96	1996/97	1997/98	1998/99	1999/2000
Asset Refurbishment[a]	61.5	66.9	56.1	77.9	131.9
Growth[b]	28.4	5.2	8.3	47.0	34.5
Total	89.9	72.1	64.4	124.9	166.4

Source: SRA/CityRail submission to Tribunal, section 6 p 4.
Note: all dollars in $1995/96
[a] rollingstock refurbishment
[b] plant and equipment, enhancements, rollingstock acquisitions and supplementary.

Capital expenditure shown in Table 4.2 is largely associated with purchases of new rollingstock. While some of the expenditure is for asset refurbishment, most is for growth assets. The Tribunal notes that capital expenditure is projected to increase substantially in 1998/99. A major factor in this increase is catering for projected increases in patronage. The Tribunal will scrutinise the bullish patronage growth forecasts submitted by CityRail. The Tribunal cautions against extrapolating from existing growth patterns as a basis for capital expenditure. Patronage growth needs to be monitored and forecasts and rollingstock requirements reviewed prior to signing contracts. If revenue growth fails to match rollingstock expenditure, there will obviously be adverse consequences for the financial viability of CityRail.

Treasury supports this view:

> "Treasury shares the Tribunal's concerns regarding CityRail's proposed capital investment program which has been designed in the expectation of increased patronage levels. The evidence from the past twenty years is that patronage in the morning peak is declining in absolute terms, and this at a time when the population has grown substantially. ... If the forecast increases in demand fail to eventuate, the provision of excess capacity will directly depress cost recovery levels (since there will be higher costs)."[85]

[85] NSW Treasury, submission to Tribunal, April 1996, p 7.

Rate of return

The government contributes 54% of CityRail’s total operating costs on an accrual basis. As noted in the SRA’s submission, substantial fare increases will be required for CityRail to break even prior to pursuing a positive rate of return.

Capital structure

CityRail’s passenger revenue is insufficient to cover its costs of operations and maintenance. Passenger revenue makes no contribution towards the cost of debt and equity finance. These costs are borne solely by the government.

Any net increase in revenue, for example, a fare increase which is not offset by reduced patronage, helps improve this situation. While CityRail relies on deficit funding, the capital structure considerations are largely irrelevant.

Following the restructuring of the rail industry and the creation of separate passenger operators it will be easier to isolate the costs and assets of CityRail. A separate profit and loss statement and balance sheet are essential to the sound financial management of CityRail. Additionally, the resolution of issues such as funding of future capital expenditure and overall debt levels are necessary.

Service standards

As noted in the interim report, quality, reliability, speed and safety standards are of particular concern to passengers. CityRail meets all its operational performance standards with the exception of on-time running. CityRail has established a service reliability steering group to address these issues. The Tribunal seeks information on strategies implemented to improve on-time running.

The Tribunal seeks financial information on the capital and operating costs of maintaining and improving service standards to be analysed as part of the 1997 pricing determination process.

The Department of Transport has specified minimum standards for bus and rail operators in the Greater Metropolitan Region. The agreed minimum performance standards for CityRail include:

- minimum timetable frequencies, differentiated for CityMet, Outer Suburban and Regional services
- maximum load factors in relation to seating capacity
- no passengers may stand for more than 20 minutes, except through choice
- on-time running targets
- maximum number of cancelled services
- number of carriages with no external graffiti
- targets for the proportion of graffiti-free seats
- compilation of a customer satisfaction index.

CityRail provides some services beyond the minimum standards set by the DoT. Generally reflecting CityRail's commercial considerations, these would not meet the CSO test.

Is an overall fare increase warranted?

The Tribunal sees CityRail's main priorities as improving cost recovery, increasing patronage on services, and reducing reliance on subsidies. Cost recovery can be improved by greater efficiency initiatives as well as by revenue growth. Two ways of increasing revenue are through fare increases and patronage growth.

For CityMet services, the Tribunal considers that the shortfall between revenue and efficient operating (above rail) costs can be largely eliminated. Improvements in operating cost recovery for the outer suburban business can be achieved, but it is unlikely to approach levels that can be attained by CityMet. Regional services will not be able to achieve a reasonable level of operating cost recovery, and will require continuing heavy subsidies or use of alternative transport modes or competitive tendering of services to maintain existing service levels.

Recommendations
The Tribunal believes that CityRail should be able to attain much higher levels of cost recovery for above rail costs on the CityMet service. A substantial government subsidy will still be required for the below rail costs. This subsidy will recognise the externality benefits of the rail service to the community. Targeted concessions to particular groups will entail specific subsidies.

The Tribunal believes that CityRail's fares for outer suburban customers should increase in line with CityMet fares. However, the Tribunal recognises that such increases will fall very far short of those necessary to achieve improved levels of cost recovery. It is unlikely that the outer suburban services can ever achieve levels of recovery of operating costs comparable to those achievable by CityMet.

In the interim report the Tribunal proposes a medium term price path that phases in a weighted average increase in CityRail fares of 15% in real terms over the four years to 1999/2000.

Treasury agrees with the need to achieve a better balance in cost sharing between taxpayers and rail users and believes that real increases in fares are necessary. Treasury's objective is to reduce the financial burden on taxpayers and achieve cost recovery for above rail costs within the CityMet network. Treasury's preferred strategy involves recovery of all above rail cost within six years. Treasury's modelling suggests that the Tribunal's approach:

> "Fail(s) to achieve increases in revenue that would manifestly give a fairer balance between the relative contributions of taxpayers and users."[86]

Treasury notes that the side constraints imposed by the Tribunal would effectively result in increases much lower than the proposed 15%. Treasury's preferred strategy provides a 15% real increase in fares over six years, not four. It involves larger increases in individual fares.

NCOSS[87] and WSROC[88] have expressed concern at some of the proposed increases. WSROC believes that fare rises should be only slightly above inflation.

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86 NSW Treasury, submission to Tribunal, April 1996 p ii.

Recommendation

The Tribunal believes that a medium term price objective for CityRail that phases in a weighted average increase in real terms of 15% over the four years from 1996/1997 to 1999/2000 is both sustainable and equitable. However, the Tribunal recognises that annual adjustments may require some variation from this broad objective. To be consistent with the major objectives and constraints for the passenger rail service set out in this report, annual adjustments will be targeted to different fare categories.

Fare structure

CityRail and Treasury have noted anomalies in the fare structure. The main anomalies are:

- fares not related directly to distance
- unequal distance bands
- off-peak fares inconsistent with single and return fares
- weekly tickets not consistent with single journey fares.

Treasury's preferred strategy addresses the anomalies in CityRail's fare structure. Treasury considers that weekly tickets should be priced at the cost of eight single trips, ie a 20% discount. Similarly, the TravelPass should be priced at a 20% discount on the sum of estimated individual trip components.

In its 1996/97 determination the Tribunal has taken steps to remove some of these anomalies.

In setting individual fares, a major consideration is to avoid a significant switching of passengers from rail to private car travel.

Periodical and multi-mode tickets

Consistent with a 15% increase in weighted average fares, the Tribunal proposes a 12.5% increase in periodical and multi-mode tickets.

Because purchasers of periodical and multi-mode tickets travel during the peak, they can reasonably be expected to contribute towards the higher costs of peak travel. The socio-economic characteristics of the group also suggest that they may be able to absorb fare increases. However, the elasticities reported in the interim report suggest that the travel mode choices of this group are far more sensitive to relative increases in fares than those of purchasers of "cash" tickets, such as single and off-peak fares.

Recommendation

The Tribunal proposes phasing in real increases in CityRail's periodical and multi-ride tickets over the period to 1999/2000 consistent with the major objectives and constraints set out in this Report.

[87] NCOSS, submission to Tribunal, April 1996, pp 8-12.
[88] WSROC, submission to Tribunal, pp 4-5.

Single journey and return “cash” fares

Single journey and return tickets are used mainly by people who travel in the peak but who choose not to purchase periodical tickets. Cash fares are not generally used by regular users of the system, such as commuters. However, some commuters choose to purchase cash fares because they consider them to be of better value than the weekly ticket, for example, if they have rostered days off. Additionally, cheaper off-peak fares are available for use after 9 am.

Recommendation
The Tribunal proposes phasing in real increases for “cash” single and return fares and off-peak fares over the period to 1999/2000 consistent with the major objectives and constraints outlined in this report.

Medium term price path

For other industries which it regulates, the Tribunal has established a medium term price path.

The benefit of a medium term price path is that it provides improved revenue/subsidy certainty to the operator and owner.

The issue is essentially a question of whether the Tribunal should continue with annual determinations or establish a medium term price path.

In making a medium term price determination, the Tribunal needs to ensure that CityRail can properly deliver its functions and meet its objectives. On the other hand, the Tribunal needs to ensure that the interests of customers are protected and that fares do not increase too rapidly or inappropriately. An important consideration in adopting a medium term price path is the significantly greater information requirements. This places a large information requirement on the regulated utility which may not be achievable from the available information systems.

If CityRail was to be structured with debt and a rate of return requirement, and the CSOs were eliminated, the Tribunal could set a pricing objective for CityRail to achieve over a period of time. Then CityRail could have a medium term price path. However, it is very unlikely that the CSOs would be eliminated.

In this report the Tribunal has set a guide to future fares rather than a maximum fare increase permitted by CityRail. The Tribunal will review the permitted fare changes each year as part of the annual determination process.

Recommendation
The Tribunal proposes to continue to conduct annual determinations for CityRail’s urban passenger train services.

Rail Access Regime

The interim reports mention a rail access regime for NSW. This regime commenced on 19 August 1996. Like other operators, CityRail now has to pay an access fee to the Rail Access Corporation for use of the NSW rail network. The government will fund this fee with a payment to CityRail. This will ensure a transparent payment.

Access charges are negotiated by the Rail Access Corporation and the operator. The Tribunal does not regulate prices within this regime. The Tribunal's role is to register access agreements, and arbitrate access disputes.

4.3 Conclusion

With cost recovery (including concession reimbursement) from farebox at only 54% of operating costs, CityRail is heavily dependent on government funding for its continued operation. There are many social and environmental reasons for the government to subsidise rail operations. However, the Tribunal believes that users of the rail system should pay a higher proportion of the operating costs. This can be achieved by increasing productivity and through fare increases.

CityRail has made many productivity improvements over the last five years. The Tribunal believes that there is scope for more. Some of the potential improvements require cultural changes and will not be possible in the short term. However, CityRail should be able to achieve real cost reductions of at least 2.5% per year.

The Tribunal believes that CityRail should be able to attain much higher levels of cost recovery for above rail costs on the CityMet service. A substantial government subsidy will still be required for the below rail costs.

The Tribunal believes that a medium term price objective for CityRail that phases in a weighted average increase in real terms of 15% over the four years from 1996/97 to 1999/2000 is both sustainable and achievable. The Tribunal recognises that annual adjustments may require some variation around this broad objective.

5 THE WAY FORWARD

This chapter discusses a range of issues which set the framework for public transport fares:

- meeting the transport needs of the community
- the role of fares
- alternative pricing mechanisms for road transport
- the interface of transport and urban planning
- environmental issues
- adding value to transport services
- community education on the costs and benefits of public transport
- forms of regulation.

5.1 Introduction

The objective of this review has been to establish a framework for the pricing of public transport which will assist transport agencies to meet the transport needs of the community without undue burden on the taxpayer. The early parts of this report have dealt primarily with financial issues relevant to the public transport operators and particular fares.

The argument for government subsidies is that public transport serves:

- a social need by facilitating mobility for those without access to automobiles
- an environmental need by providing an alternative to the automobile and thereby reducing traffic congestion, air pollution and energy consumption.

Public transport operates in a challenging environment. In the interim report the Tribunal notes how conflict between the expectations of the community and the individual choices made by members of that community puts the transport operators and policy agencies in a difficult position. The community appears to regard greater use of public transport as a rational and desirable alternative to private transport's perceived adverse consequences for the natural and built environment. Problems of air pollution and urban sprawl are generally recognised as being key problems facing the community today.

Community appreciation of the impact that use of motor vehicles has on our environment is clear. The NRMA Clean Air 2000 Project Team recently released the results of a survey which confirm the community's concern for air pollution and acknowledge that increased use of public transport is the best way to reduce air pollution[89]. Yet, as individuals, Australians strongly prefer to use a car rather than public transport.

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[89] NRMA Clean Air 2000 Project Team. *Monitor of public attitudes Air quality and the car 1996*, June 1996

Cox summarises why this is the case:

> "As nations become affluent, public transport loses market share to the automobile. … Demographically, as nations become more affluent their urban areas decline in residential and employment density. This results in dispersion of travel destinations, weakening public transport corridors. Psychologically, as nations become more affluent, people tend to use automobiles more, not only because they are a rational response to urban development patterns, but also because the automobile is more than transportation - it is a symbol of personal freedom and affluence. … People will not be coerced into public transport, they have to be attracted; and the automobile is a formidable competitor."[90]

Thus the issue here is not just one of providing a pricing framework. It is one of providing a framework which gives incentives and encouragement for the best transport solution for the community. Improved urban planning may be the most critical factor in this transport solution.

Thus the ultimate objective in providing public transport is to **best meet the transport requirements of people.**

5.2 Meeting the needs of the community

The interim report expresses concern regarding the long term decline in public transport patronage. Statistics provided in the interim report illustrate an alarming decline from 1960 when Sydney's population was 2.3m. The population has now grown by 70% to over 3.9m in 1996. Over this same period, journeys on CityRail have fallen from 250m per year to a low of 170m and recovered slowly to current levels of 250m per annum. Although part of this decline can be attributed to reasons summarised by Cox (see quote above) part of the decline must be attributable to services failing to match the travel needs of the community.

CityRail's return to the current usage level was achieved through massive track and carriage investments (notably the Eastern Suburbs and East Hills lines and Tangara carriages). However, where the CityRail system meets transport needs, a growth rate equal to or greater than population growth should have been achieved (ie 425m journeys per annum). Future growth may occur following the opening of the Merrylands - Harris Park 'Y Link'. Given that growth has not matched expenditure, further expenditure on massive rail capital works programs to stimulate patronage growth may represent inefficient spending by government.

The current recovery in utilisation, with a 2.7% growth in patronage, is an encouraging reversal that the Tribunal will continue to monitor. However, whether a continuation of this modest growth justifies further heavy rail solutions is problematic.

Scope for innovation in the provision of services

The capacity of CityRail to innovate is largely restricted by the fixed nature of the network.

Both the SRA and the STA are attempting to improve transport services for major and sporting events in preparation for the logistic enormity of Olympic related events. These occasions offer both authorities an excellent opportunity to illustrate their performance to infrequent public transport users and quality of services should be paramount.

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90 Cox, Wendell. Urban Transport: From Theory to Reality. Paper to the Transit New Zealand Land Transport Symposium, Wellington. August 1991, p 1.

The Tribunal notes concern expressed within submissions that CityRail's maintenance program has involved lengthy sectional shutdowns which have diminished the public's perception of the reliability of weekend services. Periods of service disruption require significant planning to ensure minimal customer inconvenience. Few service monopolies utilise lengthy sectional shutdowns to facilitate maintenance. Where possible, priority should be given to ensuring continuity of rail services.

Existing rail assets are fixed by route. Nevertheless, innovation is possible to optimise services through carriage, timetable, frequency and by origin-destination variations. The limited length of some station platforms prevents the use of longer peak trains, say 10 or 12 carriages at peak times.

The STA has far greater freedom to ensure the alignment of its services with the transport needs of the community. Both routes and schedules should be surveyed, refined and updated continually to reflect changes in community needs. The STA is currently experimenting with flexible 'set downs' and smaller 'nipper' buses.

In respect of ferries, dedicated loading infrastructure on STA vessels and wharves may limit the flexibility to utilise smaller vessels.

It is critical that future capital programs assess the adaptability of transport infrastructure to ensure assets can be utilised in a changing environment.

5.3 The relevance of fares

A recent report on the impact of fare changes on the patronage of Sydney's public transport (by Professor David Hensher of ITS) has found that large increases or decreases in fare levels are largely irrelevant.[91] Other factors, such as speed of service and convenience are more significant.

The report suggests that:

- commuters are generally less sensitive than non-commuters to fare changes to the equivalent ticket type and mode
- sensitivity within a market increases from a single ticket through to multiple-trip tickets.

Consumers' reaction to fare increases will affect whether revenue will increase or decrease. If a small increase in the fare causes many consumers to stop using a service, the overall result may be a decline in revenue from that service.

The travel decisions of regular users of transport services, ie those who purchase multi-trip tickets, are more sensitive to fare changes. It is possible that a small increase in the fare available to a regular user could cause a decline in demand large enough to reduce overall revenue from that fare. However, this would be unlikely for a small change. While some people would transfer to other tickets (such as single cash tickets) there could also be a reduction in the overall use of public transport.

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[91] Hensher, D and Raimond, T. Evaluation of Fare Elasticities for the Sydney Region, January 1996. The Tribunal has published a summary of the Institute of Transport Studies paper which is available to any interested parties (Research Paper No 7 *Estimation of Public Transport Fare Elasticities in the Sydney Region*).

Conversely, the travel decisions of users of cash tickets are less sensitive to the level of fares. People purchase multi-trip fares because they are cheaper per trip, quicker, and more convenient than buying a number of single fares. Hence, multi-trip tickets have higher elasticities. This is partly due to their higher dollar value. This implies that increases in multi-trip fares are more likely to result in mode transfer than a similar proportionate increase for the single ride fares. Thus, the impact on the market at the margin is greater. This has strong implications for fares policy. For example, increasing the price of a single ticket offers higher revenue growth prospects with smaller losses of patronage for similar percentage increases in weekly tickets, TravelPasses, and TravelTen tickets.

Hensher's study supports the Cox theory that transport fare levels are largely inelastic, ie following changes to fares, usage changes are minimal within a given range. This view conflicts sharply with comments from Clean Air 2000 calling for reductions in fares to increase patronage and, hence, reduce air pollution.

5.4 Other pricing mechanisms

The NRMA survey reports that the best ways to reduce car usage are to improve public transport and to reduce the cost of public transport.[92] Reducing the cost of public transport can occur through efficiency improvements which reduce the cost of public transport relative to that of the car or through higher government subsidies. The question is whether these measures are effective.

This report has addressed the potential for improving efficiency. The Tribunal has also pointed out that competition for government funding is intense and funds available are limited. If public transport is to compete with the car, other pricing mechanisms need to be considered which would shift the cost of car travel closer to its true economic cost.

Prices and levies can be effective instruments for achieving environmental policy objectives. In principle, prices and levies should cost in externalities, but if price is inelastic, little impact will occur, ie people are prepared to pay to pollute rather than to alter their patterns. An important issue in the pricing of public transport is whether prices should be adjusted to match the possible underpricing of the use of the road system by private vehicles. Underpricing of car use arises because the full costs of environmental damage and congestion impacts of road use are not properly considered. When instruments such as pricing and levies are used it is important that they be able to achieve their required goal.

Road pricing

Underpricing of urban road usage has often been cited as a possible reason to price public transport below full cost recovery. For the reasons stated by Cox (Section 5.1), this is unlikely to be effective. Consideration of the proposed linkage between road pricing and public transport pricing requires assessment of:

- the extent to which road usage is underpriced
- the future role of efficient road user charges
- the impact of road user charges and public transport fares on transport patterns.

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92 op cit, p 7.

In the interim report the Tribunal notes that a study commissioned from ACIL Economics and Policy[93] suggests that a system of comprehensive road user charges is unlikely to be implemented and may also be inappropriate. This view is founded on recognition of the diversity of road users and their willingness or otherwise to pay for improved road services such as reduced congestion. While some may be prepared to pay a substantial toll to reduce journey time, others may value the reduction in journey time at less than the cost of the toll. ACIL suggests that a diversity of options, including slower, less direct ‘free’ routes, and more direct, faster tolled routes may be a more appropriate response. However, a study by the Victorian EPA blames high speed travel for adding $415m to environmental costs.[94] On the other hand, tollways lead to smoother driving with a net saving of $106m.

WSROC is concerned that the Tribunal may have dismissed road pricing as an option.

> “Whilst it is acknowledged that such an approach would be difficult to promote, there is still a case to be made for exploring it further. WSROC has always opposed the use of discriminatory and inefficient use of tolls on selected roads, but more sophisticated methods of road pricing are becoming available.”[95]

WSROC believes that if road pricing mechanisms are not available, other forms of charging such as increased CBD parking fees will need to be considered.

Parking charges

For many public transport is much dearer than car travel. For people who already own a car, the running costs of car use are less than the purchase price of a public transport ticket. In addition, there is the flexibility and convenience of car use. Once car travellers arrive at the end of the journey, there is often no additional cost for parking. This is particularly relevant in suburban areas where parking costs may be avoided. In these circumstances public transport is unable to compete with the car.

In the CBD, parking costs represent a real cost to car travellers.

This may seem to imply the need to charge for parking at urban centres and industrial parks. The Tribunal is concerned that this approach has implementation problems (eg increased parking in nearby streets) and is uncertain that this would really achieve any significant change in choice of transport mode.

Petrol levies

The CSCTG proposes charging motorists through a levy on fuel sold at urban service stations.[96]

Such a levy has some benefits as it can be charged according to usage. However, the central argument against fuel levies is that they do not affect where the fuel is used. For example, someone who lives in the outer suburbs of Sydney would pay the same levy but could use the petrol to drive into the country while his neighbour may travel into the CBD by car.

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93 ACIL Economics and Policy Pty Ltd, *Road Pricing: Finding the Problem,* GPT Research Paper No 4, September 1995.
94 Environment Protection Authority. *Victorian Transport Externalities Study*. May 1994.
95 WSROC, submission to Tribunal, April 1996, p 3.
96 CSCTG, submission to Tribunal, April 1996, p 9.

A concern with petrol levies may rest with the distributional effects on car owners. The incidence of the levy would be the same on all car owners, irrespective of income, or indeed it could be regressive.

Still, the environment may benefit by increasing the differential in price between leaded and unleaded fuel.

5.5 Transport and urban planning

Complex linkages exist between the provision of transport infrastructure and the urban development it is intended to service. The provision of transport infrastructure may influence the shape of urban development. For example, rail services to the Blue Mountains and Central Coast have stimulated the development of these regions and similarly the northern suburbs of Sydney developed along the North Shore rail line. However, public transport also follows and serves urban development.

Clearly, other factors have a more substantial impact on urban development.

Chief among these are individuals' lifestyle preferences. Many people seeking open space prefer private vehicles as a means of transport. Together these have fostered the patterns of dispersed development which may prove inimical to an increase in the role of mass public transport.

The Tribunal notes that Sydney's sprawling development pattern and uneven access to transport limits utilisation of public transport services. Overcoming these limitations is inherently difficult and may not improve patronage. However, the Tribunal recognises that its determination has the potential to shift users between public transport and other modes of transport.

Travellers are interested in getting from one place to another quickly and conveniently. They are attracted by service that is nearby, frequent, quick and takes them where they want to go. People will be diverted from the automobile only by a public transport system that duplicates the flexibility and service of the automobile. Mode is not important. Mobility, safety and convenience are.

Sydney's transport systems must cater for an enormous range of trips made by individuals for a variety of purposes between locations all over the urban area. Peoples' priorities for features such as cost, speed, comfort, safety and flexibility vary too.

The Clean Air 2000[97] report indicates that in some areas there are large proportions of people who work in the area in which they live. For example, 65 per cent of people live and work in the west compared to 50 per cent living and working in Warringah. Under these circumstances it is difficult for public transport to compete with cars.

Considerable planning attention has focused on methods of increasing housing density, while retaining enjoyable living environments, allowing people to live closer to their work, travel less and for shorter periods. The need to consolidate development is best illustrated by Sydney's deteriorating road traffic congestion. Property valuation places a premium on proximity to good public transport with land values being correlated to the layout of the

[97] NRMA Clean Air 2000 Project Team *Shaping Sydney's Transport - a framework for reform. Discussion Paper.* March 1996, p 12.

CityRail network. Residents within walking distance (2 km) of rail stations comprise over 60 per cent of CityRail's clients. Increasing housing density in outer suburban areas within walking distance to the rail network may reduce road congestion to the benefit of the community.

The proximity of workplaces in relation to public transport is also critical to reducing car usage. Whilst decentralisation of workplaces to suburban and regional centres may provide some relief on CBD bound arterial roads, most popular decentralised locations have poor public transport. The recent popularity of suburban based 'business parks' requires better planning as the majority of these parks are not served by public transport. This means travel by private vehicles is the only choice.

The Tribunal supports planning measures which maximise the use of existing public transport services to and from new residential and commercial developments.

5.6 Environmental issues

In the interim report the Tribunal discussed environmental issues and the environmental benefits of public transport. However, submissions from the Western Sydney Regional Organisation of Councils (WSROC)[98] and Nature Conservation Council (NCC)[99] suggest that the Tribunal has not fully investigated the environmental benefits of public transport. WSROC is concerned that the Tribunal's estimate may be too conservative.

Utilisation of urban public transport services is a critical component of current government initiatives to reduce air pollution. The Tribunal acknowledges the comments of the Clean Air 2000 Taskforce regarding the need for greater equity of access to public transport services to sustain the current quality of life for all Sydney residents.

Recommendation
The Tribunal proposes to research further the environmental and social benefits of providing public transport.

5.7 Adding value to the transport businesses

Opportunities to 'add value' to existing assets and services may play an important role in improving the financial viability of public transport.

Increasingly, the STA has attempted to tap the tourism and recreational market on a commercial basis. Examples of this include the 'Explorer' bus service, Airport Express buses, and ocean and harbour ferry cruises. CityRail and the STA offer joint ticketing arrangements with major tourist attractions such as Australia's Wonderland and the Taronga Park Zoo.

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98 op cit, p 3.
99 NCC, submission to Tribunal, April 1996, p 1.

Further scope may exist to add value through strategic alliances with other businesses or government agencies. This will require a broad vision of the role of public transport services. There will be a need for pluralism and clever solutions in the design of partnerships. One benefit of this may well be greater integration of transport facilities into the community. There may be wide-ranging opportunities for integration which could include:

- co-location of railway/bus stations with shopping centres or fast food outlets
- joint ventures in parking stations
- sale of rail tickets by newsagents
- provision of services by small, private rail and bus operators.

5.8 Community education

NCOSS[100] and the NCC[101] are critical of the Tribunal for not adequately addressing community education in the previous reports.

NCOSS believes community education is extremely important for several reasons. Some people are not aware of the direct or indirect costs of running a car. This means that people are likely to make ill-informed decisions about which mode of transport to use.

While endorsing these concerns about the importance of community education, the Tribunal believes fuller awareness may do little to alter usage which is driven by self-interest.

People who rarely, if ever, use public transport often have false impressions of standards. Public transport will be more popular if the community is consulted and involved in planning and design.

The NCC and NCOSS have urged the Tribunal to recommend the introduction of community education programs. The Tribunal believes that it is making a considerable contribution to community education through its public processes. Much is dependent upon the groups themselves.

> "Community groups have a crucial role to play in community education and consultation, and it is important that they are resourced to do so effectively."[102]

The Tribunal considers that there is still more work to be done on public transport for Sydney. This work needs to go beyond fares. The analysis currently being undertaken by the NRMA Clean Air 2000 Project Team is an important contribution. The Tribunal plans to undertake a study which will complement this work and will include:

- strategies to improve public transport and understanding of its environmental impacts
- methods of providing transport services cost effectively.

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100 NCOSS, submission to Tribunal, April 1996, p 17.
101 op cit, p 4.
102 op cit, p 17.

Recommendation
In recognition of the need for continuing public education, the Tribunal proposes to undertake a study of transport priorities for the year 2000 and beyond.

5.9 Form of regulation

The Tribunal's legislation requires it to consider a range of factors in regulating prices such as those for urban public transport. These factors can be broadly grouped as:

- consumer protection
  - ⇒ fares, fare structures and standards of service
  - ⇒ general price inflation
  - ⇒ social impacts of decisions
- economic efficiency
  - ⇒ greater efficiency in the supply of services and the use of resources
  - ⇒ impact of another organisation's activities
  - ⇒ the need to promote competition
- financial stability
  - ⇒ rate of return on public sector assets
  - ⇒ impact on borrowing, capital and dividend requirements
- environmental and other standards
  - ⇒ protection of the environment by appropriate pricing policies
  - ⇒ consideration of demand management strategies
  - ⇒ standards of quality, reliability and safety.

The Tribunal is required to balance issues of consumer protection, economic efficiency and financial stability against the requirements of environmental and other quality standards. While, in many respects, these goals may support each other, there are also important areas of conflict and tension.

In public transport there is a substantial overlap between the Tribunal's role and that of the policy agencies. While commercial objectives have become increasingly important for the transport operators, the financial transfers from the government reflect the government's strong interest in 'purchasing' particular outcomes including reduced environmental impacts, improved transport access, and assistance for targeted community groups. As noted in previous reports, the task of the Tribunal in balancing these factors will be made easier when further improvements in the clarity of funding arrangements can be achieved. This may assist in clarifying the relationship between the pricing decisions of the Tribunal and the policy and funding decisions of the government.

In reviews of other industries, the Tribunal has sought to:

- regulate through reference to benchmarked efficient costs while recognising the practical constraints on the pace at which efficiency gains can be achieved
- set an overall cap on revenues, or set average prices which:
  - ⇒ are consistent with financial sustainability
  - ⇒ provide strong incentives for agencies to improve efficiency
  - ⇒ provide considerable scope for agencies to restructure individual prices in accordance with the principles established by the Tribunal and subject to specific side constraints which the Tribunal may set on specific services.

The Tribunal will apply this broad approach to the transport sector. However, the Tribunal considers that further work may be required following this review before it can establish a medium term revenue or price path.

In setting overall revenue or price targets, the Tribunal will need to have regard to the level of funding the government may wish to provide for the achievement of specific goals and environmental impacts. However, in regard to the latter, price appears to be a relatively insignificant reason to shift between modes of transport.

An important issue in monopoly regulation is setting prices to achieve flexible, commercial price setting that is responsive to customer preferences and market pressures.

In this context the DoT has noted that:

> "Care needs to be taken to ensure that price regulation does not become price determination as:
> - this reduces the commercial flexibility of the service providers (in fact it means that there is no commercial flexibility)
> - it cancels any incentive for service improvements and creates every incentive for service deterioration (through a cost cutting campaign)
> - it removes commercial responsibility from the service providers, leaving nobody accountable for transport services
> - it discourages competition in markets and erects a high barrier to entry
> - it places too heavy a burden on the price regulator to assess the multiplicity of markets, and market responses, within transport
> - it virtually eliminates price as a mechanism for clearing the market."[103]

The Tribunal is aware of the potential problems outlined by the DoT. These problems are most acute where the operators face the greatest competition from other modes. At present, the Airport Express and Explorer services are exempt from the Tribunal's regulation. The scope for further exemptions of services of certain fare types needs to be examined. The Tribunal will seek to set an overall cap on average fares, and establish principles for restructuring fares. It may, also, set some constraints on maximum increases for particular services or ticket types.

Regulatory caps based on the recovery of efficient costs have the merit of encouraging the service provider to improve efficiency and provide better price signals to consumers. In the case of rail, some prices, such as those for outer metropolitan and inter city services, are a very long way below actual costs. Indeed, for those services, fares appear to be well below fully distributed efficient costs[104]. A reference point for prices based on such costs may be meaningless and futile in this situation.

In these circumstances, the meaning of efficient costs needs to be carefully considered. It may be possible to establish a hierarchy of efficient costs which includes:

1. the average short run avoidable costs of the service provided
2. the efficient fully distributed costs for the lowest cost alternative (eg road coaches instead of inter urban and inter city services)
3. the average long run avoidable costs of the service provided (this includes capital costs specific to the service in addition to the costs included in 1).

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103 Department of Transport, *Response to the GPT's Paper, Fair Fares: the Issues*, 1995, pp 5-6.

104 Fully distributed efficient costs refers to a long run estimate of all costs assuming best practice industry benchmarks are achieved. This includes proportional allowances for corporate overheads and the like.

At a minimum, prices should exceed short run avoidable costs. The efficient costs of alternative modes may also provide a suitable intermediate reference point. This is not to imply that the lowest cost alternative should always be chosen. However, incorporation of the lowest cost mode as a pricing reference point may encourage careful consideration of the relative merits of different modes and an assessment of customers' willingness to pay for higher standards of service.

5.10 Conclusion

Public transport is desirable for social and environmental reasons. Not everyone uses public transport. However, the community would be better off if more people used public transport. People will not be coerced into public transport, they have to be attracted; the car remains a formidable competitor.

In making their transport decisions people have to consider the fare to be paid, the cost of travelling by car and the quality of service afforded by each potential mode of travel.

Travellers do not fully realise the full economic cost of travelling by car and undervalue its cost. Pricing mechanisms which place a per unit of travel value on the car may improve this.

Planning and urban transport are interrelated. Urban planning should maximise the use of existing public transport. New release areas should include adequate public transport options to encourage use of public transport.

Community education is a key component of any attempt to increase use of public transport. Many groups have a role to play. For its part, the Tribunal will continue to place information before the public which increases community awareness and permits a rational discussion of the transport alternatives.

Attachment 1 Terms of Reference

Review of the Pricing Policies of Government Agencies supplying Public Passenger Transport Services

Pursuant to Section 11(1)(b) of the Government Pricing Tribunal Act, 1992, the Tribunal will conduct a review of the pricing policies of public passenger transport services which are provided by the State Rail Authority and the State Transit Authority.

The review (Matter No. SRI/95/1) will examine the pricing of government monopoly bus, ferry and train services which have been declared in the Government Pricing Tribunal (Passenger Transport Services) Order 1992, No. 3.

Terms of Reference

The review of prices and pricing policies will consider:

1. The cost of providing the services and the scope for greater efficiency in the supply of the services including comparisons of costs with best practice public and private sector operators in Australia and overseas.

2. The protection of consumers from abuse, in terms of price or standards of service, which may result from inappropriate use of a dominant market position.

3. The evaluation of alternative structures and levels of fares, having regard to: the relative impacts on users; the interrelationships between travel modes (particularly any impact on road use); and environmental costs and benefits.

4. The scope for integration of services and fares between travel modes, including possible integration with private transport operators.

5. Economic, social, urban development, land use and environmental impacts that may arise from any program of fare restructuring, and any other costs and benefits of such restructuring.

6. The importance of community education about pricing relationships between cars, private buses and government transport and the relationship between pricing and budget expenditures on transport.

7. The impact on pricing policies of: borrowing, capital structure, rate of return on assets and investments, dividend or subsidy requirements, and the impact of any need to renew or increase relevant assets.

8. The impact of national competition proposals on the matters under terms of reference 1 to 7, and the form and extent of price and access regulation having regard to developments at the national and state levels.

Requirements under Section 13(1)c

Under Section 13(1)c of the Government Pricing Tribunal Act 1992 the Premier has requested the Tribunal to consider the following matters when making its investigations:

1. The relationship between the pricing of public passenger transport services provided by government agencies and those which are provided by non-government suppliers, including an evaluation of the efficiency and service quality of the benchmark presently used by the Department of Transport both for setting STA fares and for determining Social Program Contributions.

2. The financial flows to government-agency provided and private-sector provided public passenger transport services arising from government social policy programs, and the general principles that should apply to pricing social equity services in public passenger transport.

3. The relationship of government funding for public passenger transport to funding for other transport modes.

4. The operation of the Countrylink rail passenger service. This part of the Inquiry is to commence after publication of the Draft Final Report covering urban passenger transport.

Attachment 2 LIST OF SUBMISSIONS

Organisations and individuals who made submissions to the Inquiry are listed below. This list includes submissions on the Issues Paper and on the Interim Reports. A summary of submissions on the Interim Reports was published in the 1996/97 Determination Report *Public Transport Fares from 7 July 1996*.

Action for Public Transport
Australian Quadriplegic Association

Beale, P
Beeney, A J
Blue Mountains Commuter and Transport Users Association
Bower Cards
Bus & Coach Association (NSW)

Caldwell, Robert
Castle, W & D
Central Sydney Community Transport Group
Centre for Microeconomic Policy Analysis - University of Sydney
Chapple, Jack S
Coalition of Transport Action Groups Incorporated
Combined Pensioners & Superannuants Association of NSW
Commuter Council
Council of Retired Union Members Associations of NSW
Council of Senior Citizens
Council of Social Service of NSW
Council on the Ageing
Craig, William

Department of Ageing and Disability Services

Environment Protection Authority
Ettinger House Inc

Federation of Parents & Citizens Associations of NSW
Fox, G J

Gobbe, M

Jones, S A

Killeen, Greg

Knowles, Ronald C

Lunsford, Roslyn

Macquarie University
Macquarie University
Matilda Cruises

Mills, R J
Mooney, David

National Federation of Blind Citizens of Aust Ltd
Nature Conservation Council of NSW
NRMA Limited
NSW Department of Transport
NSW Treasury

O'Loughlin, Carolyn

Parker, Alan
Peninsula Public Transport Coalition
PLWHA (NSW) Inc
Prazak, Peter
Public Transport Union

Retired Teachers Association
Richmond, Jonathan E D
Roads and Traffic Authority
Rozelle Balmain Precinct Committee

Smith, Colin
Southern Cross University
State Rail Authority of NSW
State Transit Authority of NSW
Sydney City Council

Taylor, Graeme
The Hills Community Aid & Information Service Inc
The Voice of the Elderly (VOTE) Inc
Total Environment Centre

UAGRP
University of Western Sydney Nepean
University of Wollongong, Associate Professor P Laird
Urban Affairs and Planning, Department of

Vaucluse Progress Association
Veersema, Hans
Voice of the Elderly

Wade-Ferrell, R W
Webster, Joyce
Western Suburbs Commuter Association
Western Sydney Regional Organisation of Councils
Western Sydney Transport Forum
Wilson, R

Attachment 3 PUBLIC HEARINGS AND CONSULTATIONS

Public hearings

Public hearings for this review were held on 23 and 24 October 1995 at the Hotel Lawson, Bulwara Rd, Ultimo. Following release of the six interim reports, public hearings were held on 26 April 1996 at the Hotel Hilton, 259 Pitt St, Sydney. The following organisations were represented at these hearings.

23 October

STA	Mr Lucio Di Bartolomeo Mr Paul Dunn
SRA/CityRail	Mr Len Harper Dr Dick Day
Department of Transport	Mr Alan Coutts Mr Ian Robinson Mr Lindsay Lee
Public Transport Union	Mr Peter Murphy
Directorate on Ageing	Ms Gillian McFee Mr Leo Flynn Mr David Kilsby
Combined Pensioners and Superannuants Association	Mr Bruce Hutton
Unity Action Group for Retired Persons & Voice of the Elderly (Vote)	Ms Phyllis Thompson

24 October

Department of Urban Affairs and Planning	Dr Joan Vipond
	Mr Hugh Smith
Action for Public Transport	Mr Peter Mills
WSROC	Clr Alex Sanchez
	Mr Alex Gooding
Commuter Council	Mr Kevin Parish
Blue Mountains Commuter Association	Mr John Marsh
NSW Council of Social Service	Mr Robert Drake

26 April

STA	Mr Guy Thurston
SRA	Dr Dick Day
WSROC	Mr Alex Gooding
Commuter Council	Mr Kevin Parish
NSW Council of Social Service	Mr Robert Drake

Public access to transcripts of hearings and submissions

Transcripts of these public hearings and copies of all submissions are available for public inspection at the Tribunal's office, Level 2, 44 Market Street, Sydney. Copies of transcripts and submissions may be purchased. Transcripts are also available on computer disk.

Seminars

Public seminars were held on 13 October 1995 at the Metcalfe Auditorium, State Library, Macquarie St, Sydney and on 3 November 1995 at the Holroyd Centre, Merrylands. The following speakers addressed the seminars:

13 October

Professor Tom Parry	Chairman, *Government Pricing Tribunal (now IPART)*
Mr Len Harper	Chief Executive, *CityRail*
Mr Lucio Di Bartolomeo	Chief Executive, *State Transit Authority*
Mr Frank Jordan	Director Economic Strategy, *NSW Treasury*
Mr Charlie Richardson	*Central Sydney Community Transport Group*

3 November

Professor Tom Parry	Chairman, *Government Pricing Tribunal*
Dr Dick Day	General Manager, Planning and Business Development, *CityRail*
Mr Barrie Macdonald	Executive Director, *Bus and Coach Association*
Mr Robert Drake	Deputy Director, Policy, *Council of Social Service of NSW*