

Review of fares for private ferries in NSW from 2 January 2007

Report to the NSW Minister for Transport

Transport - Report
December 2006

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1 INTRODUCTION AND OVERVIEW

The Independent Pricing and Regulatory Tribunal of New South Wales (the Tribunal) has completed its 2006 review of fares for private ferry services regulated under the *Passenger Transport Act 1990*. Based on this review, it makes the following recommendations to the Minister for Transport on the maximum fares private ferry operators can charge for these services from 2 January 2007.

1.1 Overview of recommendations

The Tribunal recommends that private ferry fares be increased by 5.8 per cent before rounding. This recommendation will result in a maximum fare increase for an adult ticket of 30 cents on almost all private ferry routes, and an increase of 50 cents on one route after rounding, as shown on Table 1.1 below.

Table 1.1 Tribunal's recommended maximum private ferry fares from 2 January 2007 (\$ Adult Ticket)

Operator	Route	2005/06 actual fares	2006/07 fares (after rounding)	Absolute change
Central Coast Ferries	Woy Woy-Empire Bay	5.80	6.10	0.30
Church Point	Scotland Island-Morning Bay	5.90	6.20	0.30
Clarence River Ferries	Illuka-Yamba	5.70	6.00	0.30
Cronulla-National Park	Cronulla-Bundeena	5.00	5.30	0.30
Dangar Island	Brooklyn-Dangar Island	5.00	5.30	0.30
Matilda Cruises	Circular Quay-Darling Harbour	5.70	6.00	0.30
	Circular Quay-Lane Cove	5.70	6.00	0.30
Palm Beach	Palm Beach-Mackerel and the Basin	5.90	6.20	0.30
	Palm Beach- Ettalong Wagstaffe	8.50	9.00	0.50

To assist it in making future recommendations, the Tribunal also recommends that each private ferry operator be required to provide it with additional information on changes in its costs for four cost items (labour, fuel, insurance and interest), the proportion of its total costs that each of these cost items represents, and its service quality.

1.2 Overview of Tribunal's rationale for these recommendations

In making its recommendation on fare increases, the Tribunal considered the change in private ferry operators' costs since the last fare review in 2005, the scope for the private ferry industry to improve its productivity, and the other matters it was asked to take into account (see Chapter 2). The Tribunal notes that its recommended fare increases are larger than those it determined in 2005. However, it considers these fare increases are reasonable given the significant fuel cost increases experienced by private ferry operators over the last year.

The Tribunal rejected the private ferry industry's proposal that either:

- fares for services provided by high-speed operators (Matilda Cruises and Palm Beach) be increased by 8.5 per cent and those for low-speed operators be increased by 5 per cent, or
- fares for all private ferry services be increased by 7.5 per cent.

In the Tribunal's view, the proposal to allow differentiated fare increases for high and low-speed operators was too complex, and placed too much emphasis on one item in the cost index - fuel - the price of which varies considerably over even a short period of time. This view is consistent with the Tribunal's decision to reject Sydney Ferries Corporation's proposed differentiated fare increase for its Manly services and to increase all fares by a consistent percentage, as part of its 2006 determination on Sydney Ferries' fares. In addition, the proposal to increase fares for all services by 7.5 per cent was not justified by the information provided by the private ferry industry.

The Tribunal has again included a recommendation detailing the information it requires from private ferry operators to enable it to undertake a robust investigation. The Tribunal appreciates that many private ferry operators are small businesses that may not possess sophisticated data recording and management systems. However, the Tribunal considers that its information requests are reasonable: all operators are likely to collect and record information on their costs, revenue, patronage and service levels. Therefore, as part of next year's fare proposal, the Tribunal expects the industry to provide it with actual cost and revenue data for each operator for the two most recent years. The Tribunal will also request information on any fuel relief payments made by the Minister of Transport to the private ferry operators to ensure this revenue is taken into account in next year's fare review.

Finally, as in previous years, the Tribunal questions the need for private ferry fares to be regulated. While the Tribunal considers its information requirements to be reasonable given the form of regulation, the current form of regulation does place a burden and cost on the industry, stakeholders and the Tribunal which needs to be weighed against the size of the industry (valued at \$4 million¹), its economic importance, and the impact of deregulation. In addition, most operators face competition from other modes of transport for their services. For example, the operators on Sydney Harbour must compete with Sydney Ferries, and other operators face competition from land transport, water taxis and commuter dinghies. Use of their services is also often discretionary in nature, such as trips by holidaymakers and other tourists. Given the above, a rigorous regulatory regime for fares may not be required and the Tribunal considers that price monitoring is a more appropriate form of government oversight for the private ferry industry.

¹ CVA submission, 10 August 2006, p 8.

1.3 Structure of report

This report explains the Tribunal's recommendations in detail, including why it reached its decisions and what those decisions mean for private ferry operators and their customers. It is structured as follows:

- Chapter 2 outlines the context in which the Tribunal undertook its fare review, and process it followed
- Chapter 3 focuses on the changes in private ferry operators' input costs and productivity that provided the basis for the Tribunal's recommended fare increases
- Chapter 4 discusses the range of other matters the Tribunal considered in formulating its recommendations.

2 CONTEXT AND PROCESS FOR TRIBUNAL'S REVIEW

In November 2002, the then Minister for Transport asked the Tribunal to investigate and report on fares for private ferry services regulated under the *Passenger Transport Act 1990* on an annual basis, up to and including the 2007/08 financial year. The terms of reference require the Tribunal to consider the cost of providing the services concerned, the standards of quality, reliability and safety of these services, the need for greater efficiency in the supply of services, and a range of other matters (see Appendix 1).

In undertaking its 2006 review of fares for private ferry services, the Tribunal has taken each of the matters included in the original terms of reference and the then Premier's letter into account. The Tribunal's review process included conducting public consultation and undertaking its own analysis. Its consultation included:

- inviting the Commercial Vessel Association of NSW (CVA) - the body which represents the private ferry industry for the purposes of the fare review - to provide a submission detailing its pricing proposals, and publishing this submission on its website
- inviting other interested parties to respond to the CVA's submission and publishing their submissions on its website
- holding a public hearing on 20 October 2006 and inviting the CVA and Matilda Cruises to participate in a roundtable discussion on relevant issues (see Appendix 2 for a list of attendees and their affiliations).

The Tribunal has made its recommendations on fare changes in accordance with section 9(1)b of the *Independent Pricing and Regulatory Tribunal Act 1992* (the IPART Act).

3 CHANGES IN OPERATORS' COSTS

The key issue the Tribunal considered in its review of private ferry fares was the change in the costs private ferry operators incurred in providing these services in 2005/06. To calculate the extent of this change, the Tribunal first determined the weighted average change in operators' input costs. The Tribunal then determined that labour productivity gains of 0.5 per cent were achievable and adjusted the operators' wage costs accordingly. The outcome of this labour productivity adjustment was that the overall weighted average increase in operators' costs was reduced by 0.1 per cent, from 5.9 to 5.8 per cent.

The following sections discuss the Tribunal's considerations in relation to the change in operators' input costs and productivity performance, and set out its recommendations on fare increases for 2007 and the information it requires for private ferry operators for the next fare review.

3.1 Change in operators' input costs

As it did in the 2005 review, the Tribunal used its index of operators' input costs, known as the Commercial Vessel Association Cost Index (CVACI), to calculate the weighted average increase in operators' costs for the 2006 review. Given the nature of the industry – particularly its relatively small size and the fact that many of the operators are small businesses – this index is simple. It consists of five items that reflect the key costs of the industry. These include wages, fuel, insurance, interest and other. 'Other' costs include those of repairs and maintenance, depreciation, berthing/mooring, advertising and motor vehicles.

The cost data used in the cost index was supplied by the private ferry industry, through the CVA. The Tribunal verified the reasonableness of this cost data prior to its inclusion in the cost index. In addition, it made one substantial change to the cost index, by fixing the relative weightings of the items in the index.

In previous years, the relative weightings of the items in the cost index have fluctuated from year to year (see Table 3.1). As a result, the index has reflected both changes in the price of each input cost item, and changes in quantity of each item operators have used. These yearly fluctuations have enabled private ferry operators to fully pass through any cost increases they incur to customers, regardless of whether these costs were efficient. The Tribunal considers this approach is unsatisfactory and that private ferry operators must be provided with an incentive to seek efficiency savings.

Table 3.1 Cost Index – weightings provided by the CVA over the last five years (%)

Index weights	2002	2003	2004	2005	2006
Wages	39.0	45.2	45.0	43.8	28.6
Fuel	13.9	12.1	7.6	9.0	17.5
Insurance	4.2	5.5	8.3	6.2	4.0
Interest	4.5	4.2	3.1	6.5	2.1
Other	38.4	33.0	36.0	34.5	47.7
Total	100.0	100.0	100.0	100.0	100.0

For this reason, the Tribunal decided to fix the weightings of the items in the cost index, so that they remain the same from year to year. This means that any change in the index will reflect changes in the price of the operators' costs only. Fixing the weightings is also consistent with price indexing approach taken by the Australian Bureau of Statistics for measures such as the CPI. The Tribunal proposes to use these fixed weights for the next five yearly reviews. It will reweigh the index after five years to ensure the weightings continue to appropriately reflect the cost structure of the industry.

To determine the fixed weightings, the Tribunal took the weighting of each item provided by the CVA for the last five years (including 2005/06) and calculated the average weighting of each item. It applied these average weightings for the 2006 review. It then used the cost data supplied by the CVA to calculate the percentage increase in operators' labour, fuel, insurance and interest costs since 2004/05. For the 'other' cost item, it used the percentage increase in the price of goods and services within the economy (as measured by the latest Sydney CPI).² This resulted in a weighted average increase in private ferry operator costs in 2005/06 of 5.9 per cent (Table 3.2).

Table 3.2 Weighted average change in operators' costs for 2005/06, as measured by CVACI using fixed weights (%)³

Item	2006 weight	Change since 2004/05	Contribution to Index change
Wages	40.3	3.2	1.3
Fuel	12.0	26.5	3.2
Insurance	5.6	0.0	0.0
Interest	4.1	6.3	0.3
Other	37.9	3.2	1.2
Weighted average change			5.9

The Tribunal notes that for this review, it extended the period over which changes in the cost items were measured to the end of the September quarter 2006. This means that the Tribunal has taken into account the most up to date information when recommending the new fares commencing 2 January 2007. In the past the Tribunal has used financial year cost changes; however, it considers that using the latest data is more appropriate as it is setting prices into the future.

² The change in CPI used in the decision was the All Groups CPI, Weighted Average for Sydney, for the four quarters to the September quarter over the average of the four quarters for the same period of the previous year.

³ Numbers may not add due to rounding.

3.2 Productivity adjustment

Like last year, the Tribunal considers that its recommended maximum fares for private ferry operators should reflect the fact that productivity (defined as output per hour worked) has been rising in the Australian economy for as long as relevant data have been collected. For example, economy-wide labour productivity (measured by the rise in the volume of gross value added relative to total hours worked) has risen at an annualised average pace of 1.6 per cent over the past five years.⁴

The Tribunal acknowledges that there is no specific labour productivity data for the private ferry industry. However, it still considers that labour productivity gains within the industry are achievable. The Tribunal also recognises that the industry may be unable to attain the rate of productivity growth achieved by the Australian economy as a whole. For this reason, in last year's review it applied a conservative productivity adjustment of only 1 per cent to the wages item of the cost index.

This year, the Tribunal sought the views of private ferry operators on the scope for productivity gains within their industry. The CVA claimed that labour productivity improvements are not possible for most employees in the industry because of the small size of operators and that crew requirements are determined by regulation or the market place.⁵ The Tribunal accepts that the nature of the industry means labour productivity gains may be small. But it considers that they are nonetheless achievable, and that users of private ferry services should benefit from productivity gains within the industry through lower fares.

Taking into account all of the above, the Tribunal believes that productivity gains of 0.5 per cent are achievable within the private ferries industry over the coming 12 months. Therefore, it has adjusted the wages cost item in the CVACI by 0.5 per cent to derive an estimate of labour costs for the private ferry industry. As a result of this adjustment, change in the labour cost item since 2005/06 has decreased from 3.2 per cent to 2.7 per cent and the weighted average change in costs decreased from 5.9 per cent to 5.8 per cent (Table 3.3).

Table 3.3 Weighted average change in operators' costs, as measured by CVACI after Tribunal's productivity adjustment (%)

Item	2006 weight	Change since 2004/05	Contribution to Index change
Labour	40.3	2.7	1.1
Fuel	12.0	26.5	3.2
Insurance	5.6	0.0	0.0
Interest	4.1	6.3	0.3
Other	37.9	3.2	1.2
Weighted average change			5.8

⁴ The 1.6 per cent is the annualised 5-year average increase in GDP per hour worked from 2001/02 to 2005/06. Source: ABS *Australian National Accounts National Income, Expenditure and Product*, June Quarter 2006, p 21 Table 3.

⁵ Submission from CVA, 10 August 2006, p 7 and public hearing notes.

The Tribunal will work with the industry over the coming 12 months to gain a better understanding of its recent productivity performance. However, the Tribunal stresses that it will continue to consider productivity performance for all future reviews of the private ferry industry.

While the Tribunal has considered all the matters set out in the terms of reference for this review, in deciding to fix the weights of the cost index and applying a productivity adjustment it was particularly mindful of the need for greater efficiency in the supply of services so as to reduce costs for the benefit of consumers. The Tribunal considers that the 2006 review recommendations will ensure that operators seek out efficiency savings. This will benefit consumers through lower prices in the coming years.

3.3 Recommended fare changes

The Tribunal calculated its recommended maximum fare for each regulated private ferry service by:

- increasing the existing (actual) fares by 5.8 per cent (the weighted average increase in operators' costs as measured by the CVACI and adjusted for productivity gains), and
- rounding to the nearest 10 cents.

Recommendation 1

That maximum fares for adult tickets for private ferry services be increased from 2 January 2007 as shown in the column headed 'Rounded 2006/07 fares' in Table 3.4 below.

Table 3.4 Tribunal's recommended changes to maximum private ferry fares (\$)

Operator	Route	2005/06 actual fares	2006/07 unrounded fares	2006/07 rounded fares	Absolute change	% change
Central Coast Ferries	Woy Woy-Empire Bay	5.80	6.14	6.10	0.30	5.17
Church Point	Scotland Island-Morning Bay	5.90	6.24	6.20	0.30	5.08
Clarence River Ferries	Illuka-Yamba	5.70	6.03	6.00	0.30	5.26
Cronulla-National Park	Cronulla-Bundeena	5.0	5.29	5.30	0.30	6.00
Dangar Island	Brooklyn-Dangar Island	5.0	5.29	5.30	0.30	6.00
Matilda Cruises	Circular Quay-Darling Harbour	5.70	6.03	6.00	0.30	5.26
	Circular Quay-Lane Cove	5.70	6.03	6.00	0.30	5.26
Palm Beach	Palm Beach-Mackerel and the Basin	5.90	6.24	6.20	0.30	5.08
	Palm Beach- Ettalong Wagstaffe	8.50	8.99	9.00	0.50	5.88

3.4 Tribunal's information requirements for the 2007 fare review

For the next fare review, the Tribunal will be requiring private ferry operators to provide the same cost information that supported the derivation of the CVACI in this review (ie, changes in their labour, fuel, insurance and interest costs). In addition, to help increase the robustness of its considerations in relation to cost and other matters relevant to its investigation, it recommends that the Minister for Transport require private ferry operators to provide additional information, as set out below. This information should be provided for each operator, as information aggregated at the industry level is not sufficient for the Tribunal's processes.

Recommendation 2

That each private ferry operator (either directly or through the CVA) be required to provide the Tribunal with the following information for the 2007 fare review:

- *Changes in costs for four cost items: labour, fuel, insurance and interest. This information should cover the two years preceding the fare review. Information on fuel costs should include any fuel relief payments from the Ministry of Transport during 2006/07.*
- *The weight of each of these cost items relative to total costs.*
- *Trends in revenue as a result of the 2007 fare increases and other factors that may have affected patronage and revenue in 2006/07.*
- *Data on service quality and related matters, which are currently supplied to the Ministry of Transport (or any extension to that data that the Ministry might require).*

4 OTHER MATTERS

While key issues the Tribunal considered for this review were private ferry operators' costs and productivity performance, where possible it has also considered the other issues included in the terms of reference for this review. These issues include standards of service quality, reliability and safety, the need for greater efficiency, patronage, environmental and social considerations, and the effect on the level of government funding provided to private ferry operators. The Tribunal's ability to address each of these issues has been restricted by the lack of information provided by the private ferry operators.

4.1 Standards of service quality, reliability and safety

As in past reviews, neither the private ferry operators nor the Ministry of Transport provided data on service quality, reliability and safety. Therefore, the Tribunal was unable to determine how the industry's service performance has varied compared to previous years. Action for Public Transport also noted the lack of information on service standards in CVA's submission. In addition, it highlighted a number of services which were either reduced in frequency or cancelled.⁶

4.2 Need for greater efficiency in supply of services

The issue of efficiency is discussed in Chapter 3.

4.3 Patronage

CVA submitted that patronage growth for all but one of the operators is limited. This is because the markets served by the operators are mature and there is limited population growth in the vicinity of the ferry wharves.⁷ Action for Public Transport argued that some patronage growth should be possible and that any increase in fares could reduce patronage and revenue⁸. The Tribunal is also concerned about the potential impact of fare increases on patronage, but it notes that its recommended increases are to maximum fares, and operators have in the past charged less than the maximum. Therefore, the Tribunal is providing the operators with the flexibility to change their fares to suit the individual market conditions up to the maximum levels set out in Table 1.1.

4.4 Environmental and social considerations

In general, the Tribunal considers that ferry services are beneficial to the environment, to the extent that they contribute to net reductions in pollution and congestion caused by private car use. While no information was available to the Tribunal to allow it to give full consideration of the effects of its recommended fare increases on ecologically sustainable development, it considers that given the size of the increases and the characteristics of the services provided, they are unlikely to result in a shift away from ferries to private cars.

⁶ Submission from Action for Public Transport (NSW), pp 2-3, 27 September 2006.

⁷ Submission from CVA, pp 2-3, 19 September 2006.

⁸ Submission from Action for Public Transport (NSW), pp 1-2, 29 September 2006.

The terms of reference require the Tribunal to consider the social impact of its recommendations, which involves considering the impact of the recommended fare increases on customers, and the affordability of private ferry services. However, data on the incomes of private ferry users are unavailable. In addition, ferry operators have not provided data on market segmentation (for example commuters and tourists) and trends in passenger numbers.

The Tribunal considers that any fare increases will have some effect on customers, but this effect must be balanced against industry viability and the ongoing provision of the services.

4.5 Effect on level of Government funding

If the Tribunal's recommended fare increases are implemented, government funding of private ferry operators for the School Student Travel Scheme (SSTS) and half fare reimbursements will increase by approximately \$106,000 in 2006/07 if a full year of reimbursements are made.⁹

⁹ Tribunal's own estimate based on information provided by the Ministry of Transport.

APPENDIX 1 TERMS OF REFERENCE

"I, Bob Carr, Premier, approve, under Section 9(1)(b) of the *Independent Pricing and Regulatory Tribunal Act 1992*, the Tribunal entering into an arrangement with the Minister for Transport to investigate and report on the following matters relating to the private ferry industry:

1. Fares for regular services regulated under the *Passenger Transport Act 1990*.
2. Level of remuneration received from the Government for school student services delivered under commercial contracts.

A final report is to be provided to the Minister for Transport by June each year.

In conducting this investigation, the Tribunal should consider:

- i. the cost of providing the services concerned;
- ii. relativities with the Government owned ferry services, including in terms of service, efficiency, cost and ticketing products;
- iii. the protection of consumers from abuses of monopoly power in terms of prices, pricing policies and standards of service;
- iv. the need for greater efficiency in the supply of services so as to reduce costs for the benefit of consumers;
- v. the impact of pricing policies on borrowing and capital requirements and, in particular, the impact of any need to renew or increase relevant assets;
- vi. the need to maintain ecologically sustainable development;
- vii. the social impact of the recommendations;
- viii. standards of quality, reliability and safety of the services concerned (whether those standards are specified by legislation, agreement or otherwise and any suggested or actual changes to those standards as notified to the Tribunal by the Minister for Transport); and
- ix. the effect of any pricing recommendation on the level of Government funding provided to private operators under commercial and non-commercial contracts.

In conducting the investigation the Tribunal will invite submissions from the private ferry operators, the relevant unions and other stakeholder groups, including user groups."

APPENDIX 2 SUBMISSIONS AND HEARING PARTICIPANTS

The following provided written submissions to the review:

Action for Public Transport
Commercial Vessel Association of NSW
Council of Social Service of New South Wales (NCOSS)

The following organisations and individuals attended the public hearing held at the Tribunal's offices on 20 October 2006.

Representatives of IPART:

Dr Michael Keating AC, Chairman
Mr James Cox, CEO, Full-time Member
Ms Sibylle Krieger, Part-time Member
Ms Fiona Towers, Director, Energy and Transport
Mr Aaron Murray, Program Manager, Transport
Mr Alex Oeser, IPART

Roundtable participants:

Mr David Cribb, Commercial Vessel Association
Mr Anthony Haworth, Commercial Vessel Association/Matilda Cruises
Mr Graeme Taylor, Action for Public Transport
Mr Warren Gardiner, NCOSS

Other attendees:

Mr Andrew Nicholls, Ministry of Transport
Ms Elisabeth Reedy, ITSRR
Mr Paul Trevaskis, Blue Mountains Commuter and Transport Users Association
Mr Allan Miles, Action for Public Transport

