



MINISTRY OF TRANSPORT

## **Response to Issues Paper**

# **Review of Fares for Metropolitan & Outer Metropolitan Bus Services from January 2010 - proposed changes to IPART's fare setting approach**

**New South Wales Ministry of Transport  
June 2009**

# Contents

---

1.	Is it reasonable for IPART to focus on the four largest contract regions as the foundation for estimating the costs and benefits of bus services?.....	2
2.	Should IPART consider a broader set of contract regions in its review of the costs and benefits of bus services? If so, which additional contract regions should IPART include? .....	3
3.	What is the appropriate length for the fare determination?.....	3
4.	Is it better to align the end of the bus fare determination with the end of the CityRail determination, so that fares for both modes can be considered together in 2012?.....	3
5.	Are IPART's proposed assessment criteria for the review reasonable? Should IPART reconsider the criteria, or prioritise them differently? .....	3
6.	What is the most appropriate approach for setting the value of the initial capital base in the four largest contract regions?.....	4
7.	What is the appropriate rate of return to allow on regulatory assets in the four largest contract regions?.....	4
8.	What is the appropriate average remaining life for regulatory assets in the four largest contract regions?.....	4
9.	Is it appropriate to determine the share of costs to be borne by taxpayers based on the external benefits approach? What are the advantages and disadvantages of this approach? .....	5
10.	Are there other external benefits of bus services that IPART should take into account?.....	5
11.	How should IPART take into account the external benefits of bus services that cannot be quantified?.....	5
12.	Is it appropriate to determine the share of costs to be borne by taxpayers based on an optimisation approach? What are the advantages and disadvantages of this approach? .....	6
13.	How should IPART take account of the likely implications for affordability and patronage in its fare decisions? .....	6
14.	Should Newcastle fares be harmonised with fares in the other bus contract regions? If not, what justification is there for a separate fare structure? .....	6
15.	What will be the increase in demand for bus services of the next five years?.....	6
16.	What factors are likely to have the largest impact on bus use?.....	7
17.	Are recent increases in patronage likely to be a good indicator of patronage changes over the next five years? Why or why not? .....	7
18.	Is a flat flagfall and a per kilometre charge that reflects the fixed and variable costs of providing bus services the most appropriate fare structure?.....	7
19.	Under what circumstances should passengers only pay a single flagfall charge when using more than one bus service to complete a journey or multiple transport modes? Given the limitations of current ticketing technology, how could this be achieved on buses? .....	8
20.	Is the current aggregation of ticket sections appropriate? Should more or less ticket types be introduced to better reflect a consistent flat flagfall and per kilometre charge?.....	8
21.	Should all bus passengers travelling more than 16+ sections (24 kilometres) be charged the same fare? .....	8
22.	What factors should IPART take into account when considering the social impact of fare options on bus passengers?.....	9
23.	Are there any other factors IPART should take into account when considering the environmental impact of bus fares?.....	9

**1. Is it reasonable for IPART to focus on the four largest contract regions as the foundation for estimating the costs and benefits of bus services?**

The Ministry has some core concerns about this proposed approach both in terms of the estimation of both total and efficient costs and external benefits.

In particular, Sydney Buses' four contract regions may not be representative of the cost structure of the industry as a whole (even though it is conceded that Sydney Buses forms a substantial part of the total industry).

Each operator in metropolitan and outer metropolitan Sydney faces different operating circumstances. For example, Sydney Buses operates in relatively dense urban areas which affects its revenue and cost profile compared to operators servicing more expansive but lower density areas. Patronage levels on STA services are relatively high per km and trips tend to be shorter with a greater turnover (or churn) for each kilometre travelled. By contrast, private bus operators, especially those in outer suburbs, typically carry fewer passengers but over longer distances.

Moreover, Sydney Buses operates in congested areas which typically affects running costs (eg fuel consumption when idling, gearbox wear and tear etc.), and Sydney Buses' contracts with the Ministry of Transport reflect these additional costs, and which do not generally apply to private operators. However private operators face different cost drivers to Sydney Buses (eg fuel consumption for extra distance travelled and dead running, wear and tear on tyres etc.).

Sydney Buses, as the largest operator over 4 contract regions (as well as 1 contract in the Hunter), may also enjoy some economies of scale not experienced by some smaller bus operations. These benefits are potentially enhanced because Sydney Buses is also a part of the wider Government sector, and may have different commercial imperatives. However being part of the Government sector also brings certain costs that might not be part of the costs of a private entity.

Similarly, the positive externality benefits of bus services, may differ considerably between regions. For example, outer urban services have a very different passenger profile and journey purpose.

Again, having regard to the difficulties outlined in the Issues Paper a combination of regions should be selected that represents a more accurate reflection of the total population.

It is also acknowledged that in taking a more representative sample commercial confidences may need to be protected. Aggregating data across a range of operators may also assist in this regard.

**2. Should IPART consider a broader set of contract regions in its review of the costs and benefits of bus services? If so, which additional contract regions should IPART include?**

It is recommended that as many operators as practical be incorporated, and that the data be aggregated. It is particularly important that operators with contrasting operating conditions to Sydney Buses be included with the objective of building a fully representative sample of the industry as a whole.

**3. What is the appropriate length for the fare determination?**

The Ministry notes IPART's proposal to adopt a multi-year price path approach to bus fares.

If IPART adopts such an approach, there is clearly some benefit to replicating the path applied to rail, which would provide a level of operational and budgetary certainty as well as greater fare certainty to passengers over the determination period. It also avoids the need for annual, resource intensive fare processes.

However, this approach should not preclude the need for an adjustment of the price path at any time during the multi-year period should there be a major change to relevant forecast operating costs (e.g. fuel), patronage or the economic climate (affecting the cost of funds and rate of return), or Government policy.

The determination should also leave open the prospect of adjustments needed to fare structures to transition to an electronic ticket.

**4. Is it better to align the end of the bus fare determination with the end of the CityRail determination, so that fares for both modes can be considered together in 2012?**

If a multi-year price path is adopted by IPART, the Ministry believes there is value in the exploring the merits of aligning of bus and CityRail fare determinations (as stated above). Possible benefits include:

- Allowing transport agencies to pool resources in fare determination processes, and co-ordinate the implementation of fare changes;
- The application of consistent economic parameters and
- Facilitating the fare determination of multimodal products such as the Travelpass.

**5. Are IPART's proposed assessment criteria for the review reasonable? Should IPART reconsider the criteria, or prioritise them differently?**

The Ministry generally supports the criteria as set out in **Box 3.1**. However it makes the following clarifications:

- In its submission to the IPART draft fare determination for Rail in 2008, the NSW Government clearly emphasised the need for all fare determinations to give proper consideration to social and environmental impacts, including local demographics and capacity to pay. These same concerns are again raised in relation to bus fares.
- Optimal use of bus services (Paragraph 1) should be a reference to the optimal use of both current bus services and those currently planned to be provided by the Government.
- As the fare structure (and total fare revenue) will impact on both the quantum and identification of future services and investment, an additional criterion for consideration may be to “support the provision of additional services and capital investment in bus services.”

**6. What is the most appropriate approach for setting the value of the initial capital base in the four largest contract regions?**

The Ministry supports a consistent basis being adopted for asset valuation with other regulated utilities. It also supports the inclusion of existing assets at valuation – on the basis that they generally have a significant ongoing market value.

However, the Ministry is sensitive about the potentially significant impact that different valuation methodologies may have on the level of efficient cost – and potentially fare levels and would therefore request discussions with IPART during the course of the review as actual valuations are derived.

**7. What is the appropriate rate of return to allow on regulatory assets in the four largest contract regions?**

The Ministry agrees with the Weighted Average Cost of Capital (WACC) approach to determine the appropriate return on assets. The Ministry would also draw attention to the rates utilised in the bus service contracts.

**8. What is the appropriate average remaining life for regulatory assets in the four largest contract regions?**

Determination of the remaining life of buses is an important component cost of bus services. The Ministry intends to work closely with IPART to ensure that the replacement of capital over the life of the assets under IPART’s fare setting approach is consistent with the bus service contracts. In the bus service contracts held with the Ministry, assets are depreciated over a time frame of 15 years, although the current maximum vehicle age under the (O)MBSC is 25 years.

**9. Is it appropriate to determine the share of costs to be borne by taxpayers based on the external benefits approach? What are the advantages and disadvantages of this approach?**

The Ministry agrees with IPART's proposition that the external benefits approach is a useful tool for determining the taxpayer's contribution to public transport, when considered appropriately with a range of other factors.

However, it should not be determinative. In theory, fares could continue to be reduced until the benefit generated for the community from using additional bus services is less than the economic cost of service provision (and other smaller costs including the impact of taxation etc.).

However, this theoretical limit may never be reached because of absolute constraints on the capacity of the system, which are particularly relevant during peak periods. The Ministry of Transport is able to work with IPART on identifying and analysing these constraints for consideration as part of the review.

Finally, any calculation of external costs and benefits invariably comes with a degree of uncertainty and subjective judgement and, depending on the methodologies employed and the underpinning assumptions, the value of external costs and benefits may vary significantly.

As such, the Ministry supports the proposed approach providing externalities are not given undue weight relative to other factors, ensuring a reasonable fare outcome from both the perspective of passengers and the community as a whole.

**10. Are there other external benefits of bus services that IPART should take into account?**

"Agglomeration benefits", though difficult to quantify, should be an external benefit that IPART considers. It recognises the important role that public transport plays in delivering a productive and growing economy as well as intrinsic benefits to society as a whole, in particular:

- Helping create a larger and deeper labour market,
- Helping to broaden the customer base for businesses,
- Providing greater potential for learning, information exchange and knowledge sharing.

**11. How should IPART take into account the external benefits of bus services that cannot be quantified?**

Valuation of agglomeration benefits will require some consideration of the economic contribution and value of major commercial hubs in the Greater Metropolitan Region (Sydney's Global Arc, Parramatta etc.) and how that may

be affected if bus services were not provided. Discounting the value of calculated benefits may be appropriate given the uncertainties in valuation methodology and underlying assumptions.

**12. Is it appropriate to determine the share of costs to be borne by taxpayers based on an optimisation approach? What are the advantages and disadvantages of this approach?**

The Ministry believes that IPART's proposed optimisation approach is a useful tool to help IPART determine appropriate fare levels, providing benefits are not given undue weight relative to other factors. However, as noted above the economic benefits will be impacted by the constraints on the bus system to deliver the level of service demanded given the level of fare subsidy.

**13. How should IPART take account of the likely implications for affordability and patronage in its fare decisions?**

Given the current economic climate, and in light of previous representations made by the NSW Government, it is requested that IPART carefully consider the impact of any fare increases on passengers' ability to pay.

Whilst this consideration inevitably includes a broad range of measures, the Ministry requests that specific consideration be given to the demographic profile of bus passengers and the proportion of the household budget that the cost of bus transport likely occupies.

**14. Should Newcastle fares be harmonised with fares in the other bus contract regions? If not, what justification is there for a separate fare structure?**

The implementation of bus fare harmonisation was driven by the NSW Government's bus reform initiative across metropolitan and outer metropolitan Sydney. During this process a decision was taken to leave time-based fares operating in Newcastle, an arrangement reflected in the current bus operator contract covering service delivery and funding arrangements.

The NSW Government has not at this point sought to extend fare harmonisation to the Newcastle contract region, and has not requested IPART to make such a determination. .

Consideration of Newcastle fares should take place in the context of the delivery of the electronic ticketing system.

**15. What will be the increase in demand for bus services of the next five years?**

Forecasting bus patronage is difficult and even more so in this current climate of economic uncertainty. The Ministry's Transport Data Centre will work closely with IPART to set patronage forecasts that are reasonable for the purposes of the fare determination.

**16. What factors are likely to have the largest impact on bus use?**

Broadly speaking, key factors affecting bus patronage tend to be:

- employment growth;
- service quality (e.g. frequency, reliability and journey time); and
- the cost and attractiveness of competing modes, being mainly private motor vehicle and to a lesser extent, trains (in areas serviced by both rail and bus).

**17. Are recent increases in patronage likely to be a good indicator of patronage changes over the next five years? Why or why not?**

It is important to distinguish patronage changes brought about by different causes, rather than relying on one simple indicator (e.g. the economy or fuel prices) to forecast future patronage.

For instance, there is a general recognition that the strength of the wider economy has an important role in determining patronage trends.

On the other hand, better network planning, service improvements, additional capacity (including 300 growth buses announced in November 2008), and fare and concession harmonisation can see major increases in patronage on certain routes and in certain contract regions, regardless of broader economic conditions.

The Ministry proposes that IPART work with its Transport Operations Division and Transport Data Centre on any patronage forecasts.

**18. Is a flat flagfall and a per kilometre charge that reflects the fixed and variable costs of providing bus services the most appropriate fare structure?**

The Ministry notes a flagfall and per kilometre distance charge approach was taken by IPART in its Cityrail fare determination for 2009-2012. However, it should be noted that Cityrail fares were already broadly cost-reflective and granular with over 20 distance bands, and as such Cityrail fares were more amenable to such an approach without price impacts on passengers.

Bus fares are less directly cost-reflective, in that fares are currently based on five distance bands, with the majority of passengers paying fares within the first two distance bands. Changing to a flagfall and distance charge model from this relative coarse structure may create immediate price impacts for certain groups of passengers.



The Ministry acknowledges that cost reflective pricing is relevant, from both an economic and equity perspective. It may help inform passengers about the relative cost of their journey compared to other alternatives. It may also help support the viability of future investments.

However the impact of implementing fully cost reflective fares must be balanced against other relevant factors, such as the social and environmental impact of any fare change, and its impact and affordability for users. These factors should be given suitable weight alongside cost reflectivity in any immediate fare determination.

**19. Under what circumstances should passengers only pay a single flagfall charge when using more than one bus service to complete a journey or multiple transport modes? Given the limitations of current ticketing technology, how could this be achieved on buses?**

Bus passengers are allowed to transfer free of charge between buses under restricted circumstances with some operators.

Current ticketing technology means that extended use of transfer tickets (e.g. transferring within a set period after initial ticket purchase) would be difficult to roll out across the entire network, and would require manual proof-of-payment validation by bus drivers or Transit officers, similar to the validation of the Pensioner Excursion Ticket on private buses. There are potential time and resource implications, creating potential audit issues, and slowing boardings for passengers.

The development of an electronic ticketing system means that there is scope to consider these benefits in a future fare reform.

**20. Is the current aggregation of ticket sections appropriate? Should more or less ticket types be introduced to better reflect a consistent flat flagfall and per kilometre charge?**

The Ministry wishes to make the distinction between the introduction of new ticket types and the introduction of new fare gradations on existing tickets. In this context, it takes IPART's comments as referring to the introduction of new fare gradations, e.g. a bus single may have 10 different prices, rather than 5 currently.

There does not appear to be any compelling benefit in altering the current fare arrangement ahead of the implementation of electronic ticketing. The Ministry believes this issue needs to be considered at the appropriate time in the context of the implementation of electronic ticketing.

**21. Should all bus passengers travelling more than 16+ sections (24 kilometres) be charged the same fare?**

The Ministry requests caution if IPART is considering extending fare bands beyond 16+ sections, as presumably this would be the basis for setting higher fares for people who travel further on buses. While this may be proposed in support of the notion of a more cost reflective fare, there are concerns about the impact on longer distance travellers, resulting in less affordable fares for some people. This concern was also reflected in the Government's submission on rail fares in 2008.

As such, the Ministry sees no compelling reason why additional bands should be added beyond 16+ sections, especially ahead of the implementation of electronic ticketing.

**22. What factors should IPART take into account when considering the social impact of fare options on bus passengers?**

This includes, but is not restricted to, consideration of matters such as the demographic profile of bus passengers, the proportion of the household budget that the cost of bus transport likely occupies and Government's ongoing policy to use public transport fares and public transport more generally as a tool of social and economic inclusion. The current economic climate should be an important guiding factor.

In addition, it is important to recognise that longer journey distances carry with them inherent disadvantages for commuters in terms of greater time spent travelling and away from families. These must also be factored into any pricing regime designed to attract more people to public transport.

**23. Are there any other factors IPART should take into account when considering the environmental impact of bus fares?**

The Ministry notes that IPART is intending to have regard to the environmental benefits of bus usage and the Ministry supports this approach.