



MINISTRY OF TRANSPORT



Rural & Regional Bus Reform Consultative Taskforce

August 2006

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EXECUTIVE SUMMARY

The Minister for Transport, the Hon. John Watkins MP, established a joint Ministry of Transport / BCA Rural and Regional Bus Reform Taskforce in January 2006 to provide advice on recommendations from the Unsworth Review of Bus Services (February 2004) relating to rural and regional bus services.

Specifically the Taskforce was requested to develop options for the implementation of the Government's reform of bus services.

The Taskforce identified three major work streams of funding, contracting and service planning. A working group was established for each area to undertake research and detailed discussion of relevant matters in developing these options.

As it is expected that reform of rural and regional bus services will take some years to complete, the Minister also asked the Taskforce to consider what interim measures could be put in place to assist the sustainability of the bus industry and help maintain essential public transport services.

Recommendations from the Working Groups:

1. Trial three funding model options, evaluate trial results and determine the most effective funding model for rural and regional areas.
2. Review existing Minimum Service Level Policy and establish appropriate service levels for rural and regional areas
3. Develop a revised contract, incorporating the preferred funding and service planning approaches identified in the trial that will achieve the Government's objectives of continuity of service, value for money and the ability to purchase responsive services on behalf of the community.
4. A simplified revised contract be adopted for single, isolated bus operators.
5. A service planning trial be undertaken in the Tamworth area to further inform the process of establishing appropriate network development strategies, service policies and responsibility for service planning functions.
6. The following timetable for the reform process is proposed:
 - Oct 06 – June 07: Trial funding models
Develop standard contracts
Establish network service policies
 - July 07 – August 07: Evaluate funding model trials
 - Sept 07 – Nov 07: Finalise standard contracts
Determine reform roll-out program
Determine any transition requirements
 - January 08: Commence the roll-out of reform of bus services in rural and regional NSW

Recommendations for Interim Measures

The Ministry considers that relief from average age provisions and category shift should be provided on the following basis:

1. Relief from average age provisions to be provided for a period of up to 3 years for smaller operators who can average bus age over no more than 2 vehicles. Relief will only be available where the original vehicle is retained and the safety and reliability of the vehicle is assured through compliance with accreditation and RTA inspection requirements. An application for relief must be lodged.
2. Relief from decreased contract payments arising from a decrease in contract category of non-commercial contract holders be provided through a phased reduction in contract payments over a two year period for those operators whose total contract payments from the Ministry reduce by more than 10% per annum. This relief be limited to variable costs of operation where the purchase price of the bus has been recovered by the operator through prior contract payments.

The Taskforce has recommended relief from increased costs of fuel.

3. Relief from increasing fuel prices be made available to commercial operators through indexation payments.
4. That the Minister consider interim relief for non-commercial operators for increased fuel consumption provided the industry is able to quantify the impact of additional consumption.

Transition Issues

The Taskforce believes that only minimal changes are likely to be required for school bus operators holding a small number of contracts and operating in more isolated areas.

However, a key issue will be coordinating the services of operators who interact with other operators and reorganising the delivery of services in implementing a “network” approach.

The Government has consistently stated since 2004 that its preference is for current contract holders to have the first opportunity to negotiate a new contract if they wish to remain in the industry. Nevertheless, it is recognised that operators will make their own business decisions as reform rolls out and arrangements should be put in place to address them. In the event that operators wish to exit they will have the opportunity to sell their assets in accordance with the “Tingle” amendment.

The BCA has proposed that where an operator may be able to achieve efficiencies by buying out another operator, that the Government continue to pay to the purchasing operator, for a specified period, an equivalent sum that would have been payable to the exiting operator. After the specified period any efficiency savings would accrue to the Ministry. Under this proposal the purchasing operator is responsible for paying the outgoing operator with the Tingle amendment regulation remaining as a safety net.

1. BUS REFORM IN RURAL & REGIONAL NSW: OVERVIEW

1.1 What is bus reform?

To date, the process of “bus reform” in rural & regional NSW has been about looking at the way the State plans, funds and contracts for bus services to see what, if anything, can be done better.

Bus services are an essential public service. Under the *Transport Administration Act* 1988, it is the responsibility of the Director-General of the Ministry of Transport to ensure safe, adequate, and efficient public transport services are delivered to the community within the available funding resources. This is set out in s38 of the Act.

In rural & regional areas, private bus operators provide these services to the community on Government’s behalf. That is why bus operators provide services under contract to the Ministry of Transport.

In rural & regional communities, these contracts are worth more than \$230 million a year in Government subsidies provided through payments under the School Student Transport Scheme (which provides free transport to and from school for eligible students) and the Half Fare Concession Scheme (which allows eligible beneficiaries to travel on half the full fare).

Because of the levels of funds involved, as well as the importance of these services to the community, the Government needs to make sure that:

- The arrangements for bus services are transparent, accountable and deliver value for money.
- Bus services are viable and sustainable.
- The community is getting the best possible services for the funds the taxpayer is providing, with the guarantee of continuity of essential services.

These are the key objectives for rural & regional bus reform and will result in the Government being a more informed purchaser of services.

Bus Reform has been approached in 3 stages:

- Sydney Metropolitan area;
- Outer Metropolitan area; and
- Regional and Rural NSW.

In recognition of the different operating environment in rural and regional NSW, bus reform in rural and regional areas has been approached differently. This reform will cover a range of operators from single bus / single contract holders operating in isolated areas through to larger operators with multiple contracts and larger fleets in regional centres.

To ensure the best outcome from the reform process a consultative approach has been adopted involving industry in determining options for reform and gathering information from service providers and the community through forums held in certain regional areas.

Trials of funding models will be conducted and assessed in determining the most appropriate arrangements and a review of contractual mechanisms is to be undertaken to ensure the most appropriate approach (or approaches) are developed.

As it is expected that bus reform in rural and regional areas will take some years to be finalised, a number of interim measures are being recommended to sustain the industry prior to the roll-out of bus reform.

1.2 What does bus reform mean for...

...the community?

For the community, bus reform aims to ensure that essential public transport services are maintained and that the Government has the ability to purchase the right mix of services.

Bus reform is also about ensuring that the community is properly consulted before service changes are made. While some operators do this well, the Government believes this needs to be a contractual obligation because the services are so important to the community. By updating service level policies, changes can be made to provide a reasonable level of access which reflects local requirements.

The Government is not making changes to the eligibility requirements of the SSTS and, of course, any changes to services will need to take into account distance and travelling times for school students.

Bus reform also means access to a better range of concessions. Following the first phase of the bus reform program: the Review of Bus Services in NSW undertaken by the Hon Barrie Unsworth (the Unsworth Review) - the Government agreed to look at expanding all day travel under the \$2.50 Pensioner Excursion Ticket (PET) to larger country towns. In metropolitan Sydney and outer-metropolitan areas, bus reform has meant half fare concession travel for university students – not just for travel to and from classes – and other improvements.

...taxpayers?

For taxpayers, bus reform is about making sure that the arrangements for the delivery of essential public transport services deliver value – in terms of the amount that is being paid for an appropriate service to be delivered. Revised service level policies will take into account the differing needs in communities across NSW, while ensuring the sustainability of services is also considered. The reform will ensure NSW gets value for the funds it is currently providing for bus services.

... bus operators?

Bus reform is about making the best use of available resources to deliver better services to the community. This may involve reorganisation of services where there are currently inefficiencies, such as overlap or duplication.

Funding arrangements will be reviewed to ensure that cost inputs accurately reflect operating costs and anomalies in the existing arrangements are considered – such as the treatment of “average age,” the impact of “category shift” and the failure of the current system to take into account the impacts of different operating environments (like unsealed roads).

The aim is for viable, sustainable bus services with fair and reasonable remuneration for all bus operators.

1.3 The process to date

The Rural and Regional Bus Reform Consultative Taskforce

With new contracts in place in each of the 15 metropolitan Sydney contract regions, and negotiations under way for the 10 outer-metropolitan regions – Newcastle, Wollongong, the Central Coast, the Blue Mountains and the Lower Hunter – in early 2006, the Deputy Premier and Minister for Transport, the Hon John Watkins MP, established the Rural & Regional Bus Reform Consultative Taskforce to progress rural & regional bus reform.

The role of the Taskforce is to:

- drill down into the issues raised by the Unsworth Review and ensure that the nature and extent of any problems is fully understood;
- develop and make recommendations to the Minister on the different options for improving the planning, funding and contracting of bus services; and
- identify the interim arrangements that should apply prior to the full roll out of bus reform where flaws in the existing arrangements are creating serious viability problems for some operators.

In undertaking this role, the Taskforce has been required to consult with members of the industry and the community and report to the Minister, in August 2006, on reform options that may be trialled.

The Terms of Reference for the Taskforce are at Attachment A to this report.

Membership of the Taskforce

The Taskforce has members from the industry's peak body, the Bus and Coach Association of NSW (BCA) and the Ministry of Transport.

BCA members of the Taskforce are:

- Darryl Mellish, the BCA's Executive Director;
- Peter Ferris, Chair of the BCA's Rural & Regional Reform Board Committee and CEO of the Buslines Group);
- George Tisse, Chief Executive Officer of the Busways Group, representing larger operators;
- Peter Jones, Director of Jones Brothers in Bathurst and Lithgow, representing medium sized operators; and
- Ian Templeman, who operates five "non-commercial" contracts in West Wyalong, representing small operators.

From the Ministry, Taskforce members are:

- Deborah Sutton (the Taskforce Chair) and Catherine Reilly who are Principal Policy Officers in the Ministry's Bus Reform team;
- Phil Sullivan who manages the Transport Operations Division's Northern Office in Newcastle;
- Lyall Kennedy, Director, Network Development, head of the Ministry's Network Development team; and
- Mark Brimfield, Senior Project & Liaison Officer with the Local & Community Transport team.

Three Working Groups looking at funding, service planning and contracting options have provided information to the Taskforce.

1.4 Activities of the Taskforce and its Working Groups

The Taskforce

In accordance with the requirements of its Terms of Reference, the Taskforce held monthly meetings between February and July 2006, with special meetings scheduled for 9 May 2006 and 16 June 2006 to discuss the interim relief measures that might be implemented while bus reform is rolled out.

The Taskforce convened three meetings outside of Sydney and took that opportunity to hold information sessions about bus reform for bus operators and members of the community prior to the meeting. These information sessions were held in the regional areas of Nowra (March), Mudgee (May) and Tamworth (June). Issues discussed at these forums are detailed in section 1.5 below.

The Working Groups

- **The Funding Model Working Group**

The role of the Funding Model Working Group has been to assess the existing "commercial" and "non-commercial" funding models, identify the problems with those arrangements and develop practical, workable solutions.

As part of this process, two Risk Workshops were held with bus operators – one in Sydney in April and one in Wagga Wagga in May. These Risk Workshops aimed to:

- identify the key risks involved in running a bus business (such as patronage, operational costs and capital risk); and
- consider which party to the contract (the Ministry or the bus operator) is best placed to manage those risks.

The risk assessment process formed part of the research that has been undertaken to inform the Taskforce. It is important to understand what areas of risk the industry and Government faces and the impact of those risks. This information will assist in identifying options for alternative funding models and determining areas requiring interim arrangements.

Work to date has indicated that the industry has a clear view of the risks it is willing to bear, assuming service planning guidelines are flexible, while the Government will finalise its position in light of the funding model trials.

This work was used to help develop different options for funding bus services:

- a Gross Cost model where all risk lies with Government, and which is a revision of the “non-commercial” or Pricewaterhouse Coopers (PwC) model;
- a Net Cost model, which is similar to the existing “commercial” funding model,
- and
- a Risk Sharing model which is a hybrid of the Gross and Net Cost models.

Trial of these alternative funding models will test the suitability of both the current and alternative models in sustaining the industry and dealing with the identified risks.

Components of each of these funding model options may be modified in testing the different approaches. Further information about these funding model options is set out in Section 5 of this report.

It is proposed that each of these funding model options be assessed through a series of desktop (paper-based) trials over the period from October 2006 to 30 June 2007. These trials would help determine which model or models deliver a viable, sustainable bus industry as well as the best possible value for Government funds.

The final configuration of any funding models adopted will take into account the party best placed to manage that risk which will include consideration of the extent of risk that the industry can sustain and the level of risk premium the Government can justifiably pay.

Membership of the Funding Model Working Group

The Funding Model Working Group comprises representatives from the BCA and the Ministry.

BCA members are:

Darryl Mellish, Executive Director of the BCA;
Frank D'Apuzzo, Managing Director of the Buslines Group;
Luke Gray, Managing Director TITLE, of Surfside Buses; and
George Tisse of the Busways Group.

Ministry members are:

Deborah Sutton (Chair) and Catherine Reilly from the Bus Reform team; and
Pat Murphy Manager, Financial Management Analysis and Reporting from the Ministry of
Transport

SAHA International was appointed to provide advice on financial issues and to assist with the development of funding model options.

• **The Service Planning Working Group**

The Service Planning Working Group's role was to look at options for improving service planning arrangements.

The key issues in this area are:

- Ensuring the ability to develop a local network of bus services;
- Providing the community with the ability to be appropriately involved in the planning and development of services, including the opportunity for regular review;
- Developing an objective basis for the development of a service level policy, which provides for clear and realistic expectations of the services to be delivered and recognises both actual and potential demand;
- Reviewing existing Service Level Policy and establishing appropriate service levels for rural and regional areas;
- Ensuring the most effective use of capital and recurrent funding by minimising overlap and suplications and provides the ability to target resources; and
- Determination of the most appropriate parties to undertake service planning, taking into account resources available, skills, local knowledge, risk exposure and incentive.

A key issue for the Working Group has been the consideration of arrangements where a series of services are provided by a number of separate operators. Because of the essential nature of these services and the amount of funding involved, it is recognised that a framework will need to be developed that enables a review of all services that feed into a common area. Contract mechanisms will then need to be developed to ensure ongoing coordination of services. To this point, the Working Group has focussed on route and school services, but future work will look at the relationship between bus operations and the community transport task.

The Tamworth area has been identified as a suitable location to investigate different strategies as it involves a mix of commercial operators and non-commercial operators with different levels of interaction.

It is proposed to examine how a network would be developed which recognises the different travel needs to and from rural areas, villages, surrounding towns and the regional centre. By doing this in Tamworth, this exercise would be undertaken in

conjunction with the trial of different funding models. This will also emphasise the strong link between service planning responsibility (at both “strategic” and “tactical” levels) and the risk and incentives in the funding arrangements.

This also provides the opportunity to undertake a transport needs survey of the community to identify the current and potential role of bus services in the catchment area of a regional centre, involving business, educational, health and recreational travel. A similar activity was undertaken in Warrnambool in association with the Victorian Bus Industry, which identified a number of measures which could be considered including service issues (frequency, span and coverage), marketing and regulatory reform to increase flexibility with which services can be made available.

It is expected that arrangements for “stand alone” school services, which have little or no interaction with other transport services, will remain largely in their current form.

Membership of the Service Planning Working Group

The Service Planning Working Group is comprised of 9 members :

- Lyall Kennedy (Chair) with Stephen Timbrell and Christine Hall (both senior officers in the Ministry’s Network Development team), Mark Brimfield from Local & Community Transport Division and Phil Sullivan from the Ministry’s Operations Division.
- Darryl Mellish, Richard Rowe (Busways), Peter Ferris (Buslines), Paul Crompton (Nariki P/L T/A Cromptons Bus Service).

• The Contract Working Group

The “Commercial” and “Non-Commercial” contracts were introduced in 1990. In some areas, such as renewal, the contract terms are prescribed under legislation and are very specific. In other cases, these contracts provide a general framework of the rights and obligations of the parties. As a result there are no direct contractual obligations:

- to consult with the community when designing and implementing services and service changes;
- to regularly review service specifications;
- which define reporting requirements;
- to address performance issues, apart from termination; and
- to ensure continuity of services.

Under the existing bus service contracts these matters have been left to resolution through separate ad hoc arrangements between the industry and the Government.

While the major contract development work will occur when the funding and service planning arrangements are confirmed, the issues discussed to date include:

- a) provisions that ensure that the community has an appropriate level of input into the way services are designed, developed and delivered. This means appropriate consultation prior to service changes and proper information once the decision has been made.
- b) an appropriate contract term - taking into account issues such as incentives to develop the network, administrative efficiency and changing demographics – and appropriate “end of term procedures, balancing the flexibility to respond to changing circumstances (e.g. demand or public policy), the certainty required for capital investment and competition policy requirements.
- c) Clearly defined procedures for dealing with contract variations, to enable the Government to seek changes and the operator to seek appropriate compensation for any additional obligations.
- d) A graduated “cure’ regime to enable contract breaches to be identified and addressed by the operator in the first instance, with termination maintained only as a last resort.
- e) Mechanisms for ensuring continuity of essential services which reflect the essential nature of these services, as well as operating realities such as the size and location of the business.
- f) Reporting and performance requirements which balance the need for accountability for publicly funded services with administrative efficiency and take into account other reporting obligations (such as accreditation)

Membership of the Contract Working Group

The BCA's members on the Contract Working Group are Darryl Mellish, Executive Director of the BCA; Ian MacDonald, Executive Assistant, BCA; Stephen Rowe from the Busways Group; Adam Seckold from the Buslines Group (Now departed); Peter Jones of Jones Brothers; and Jim Kellam of Kellams Bus Service.

The Ministry is represented by Deborah Sutton and Catherine Reilly (Chair) from the Bus Reform team; Christine Hall from Network Development; and Phil Sullivan from Transport Operations.

Legal firm Baker & MacKenzie has been retained to provide advice on legal issues and help develop new contracts.

1.5 Consultations and Submissions

Issues raised in the forums held in Nowra, Mudgee and Tamworth as well as submissions received by the Taskforce are summarised below.

There was, as might be expected, some common issues that were raised in all forums. There was also quite a considerable divergence of opinion on some of those issues.

- **Average Age**

“Average age” is calculated, for “commercial” contracts, based on the average age of the vehicles used to provide the services at any time in the life of the contract.

For non-commercial operators, average age is calculated across the life of the contract and the age of the bus used to provide the services may not exceed an average of 8 years for a Category 1 or 2 vehicles and 12 years for Category 3 and 4 vehicles.

This means that, depending on the age of a vehicle at the commencement of the contract, a Category 1 or 2 bus may be up to 12 years of age before it must be replaced and a Category 3 or 4 bus may be up to 17 years before it must be replaced.

For “commercial” operators, the average age of vehicles used to provide the services must be less than 12 years at any given time in the life of the contract.

The Unsworth Review flagged the fact that average age requirements appeared to impact inequitably on smaller operators and questioned whether it was a suitable proxy for the safety and reliability of bus services. This was repeated by some sections of the industry.

Other sections of the industry, however, have argued strongly that “average age” is not a problem when operators properly understand the provisions of the contract and adequately plan the replacement of their vehicles.

- **Category shift**

For non-commercial bus operators, payments are based on the category (i.e. size) of bus needed to provide the services, which establishes the capital payment and the payment for running costs.

“Category shift” takes place when student numbers increase or decrease over a given threshold. For Category 4 buses, the minimum student number is 42, for Category 3 buses the maximum number of students is 41 and the minimum 26, while Category 2 buses carry a maximum of 25 and a minimum of 12.

If student numbers fall or rise beyond these bands, the capital and operating payments are varied accordingly. An annual survey is undertaken in March to determine the number of students using the service.

Operators in areas in which there are declining populations, in particular, expressed concerns about the impact on their ongoing viability because of their increased exposure to the risk of “category shift.”

- **Differences in operating environments**

A consistent issue raised by operators in rural & regional areas was the need for new funding arrangements to take into account additional costs associated with operating in remote locations, particularly the wear and tear on vehicles operating on unsealed roads and the higher costs of fuel (because of higher distribution costs).

- **Service reorganisation and who is best placed to deliver the services?**

It is accepted that there is at least some degree of inefficiency in the existing arrangements, with overlap and duplication between school services especially around the larger regional centres.

“Commercial” contractors have exclusive rights to pick up passengers in their contract areas. This means that the “non-commercial” bus, bringing school students in from out of town, are unable to pick up students along their route once the non-commercial bus is inside the town boundary. This results in multiple buses operating in the same area.

Non-commercial school services have been developed individually by the Ministry in response to particular demands which do not necessarily take into account adjoining services.

Like the Sydney metropolitan area, inefficiencies also exist where multiple “commercial operators” service a single area. Pickup / set down restrictions operate as a result of exclusive rights for each of the operators.

This results in services necessarily run by each operator rather than sharing the service responsibility and operating as a more efficient network.

- **Private vehicle conveyance**

In submissions to the Taskforce and the Ministry, some operators commented on issues with the Private Vehicle Conveyance (PVC) scheme, under which families who do not have access to a bus service receive a subsidy to help meet the costs of transporting their children to school.

They have indicated that, in some instances, the cost of PVC would exceed the cost of providing a bus service or varying an existing service.

The Ministry has commenced a review of the PVC Scheme. The BCA provided a copy of its Submission to that review to the Taskforce.

Other Issues Raised During Consultation:

- **Fuel Prices**
Impact of fuel prices on viability;
- **Interim Contracts**
Issuing of interim contracts in the lead up to bus reform;
- **Unpaid Kilometres in Non-commercial Contracts**
Unpaid kilometres in non-commercial contracts after contracts change hands;
- **SSTS Administration and Schools**
Administrative effort in SSTS reporting, especially in obtaining information from schools;

- **Increased Compliance Administration and Costs**
Increasing compliance requirements such as accreditation, impact of reform, safety management systems, drug and alcohol testing, WorkCover and fuel rebate schemes.
- **Goodwill**
Government policy approach on goodwill;
- **Asset Control (Access)**
Concern over control of assets;
- **Service Planning**
Concern over what will be a contract area and what services will be required;
- **Lead Entities**
Concern that the metropolitan lead entity approach would apply across the state;
- **Community Transport Services**
Questions concerning the interaction between Community Transport and the bus industry.
- **Access to Accreditation Training**
Concerns over access to accreditation training.

1.6 Working Group Recommendations

1. Trial three funding model options, evaluate trial results and determine the most effective funding model for rural and regional areas.
2. Review existing Minimum Service Level Policy and establish appropriate service levels for rural and regional areas
3. A simplified contract be adopted for small, isolated bus operators.
4. Develop a revised contract, incorporating the preferred funding and service planning approaches identified in the trial that will achieve the Government's objectives of continuity of service, value for money and the ability to purchase responsive services on behalf of the community.
5. Undertake a service planning trial in the Tamworth area to further inform the process of establishing appropriate network development strategies, service policies and responsibility for service planning functions.
6. The following timetable for the reform process is proposed:

Oct 06 – June 07:	Trial funding models Develop standard contracts Establish network service policies
July 07 – August 07:	Evaluate funding model trials
Sept 07 – Nov 07:	Finalise standard contracts Determine reform roll-out program Determine any transition requirements
January 08:	Commence the roll-out of reform of bus services in rural and regional NSW

2. INTERIM ARRANGEMENTS PENDING RURAL AND REGIONAL REFORM

Given that it is expected reform of rural and regional bus services will take some years to complete, the Minister asked the Taskforce to consider what interim measures could be put in place to assist sustainability of the industry and thereby assist in continuity of services.

Areas initially identified as causing financial distress in the industry are:

- Average age.
- Category shift.
- Fuel indexation for commercial operators.

2.1 Average Age

Operators must comply with the average age requirements which have been adopted as a proxy measure for safety and reliability.

Average age requirements are set out in Section 1.5.

The Ministry understands, from representations made from individual operators, that “average age” requirements impact most heavily on small bus operators, especially one bus operators or operators who hold a small number of contracts with a mix of Category 1/2 and 3/4 vehicles. This is because they have nothing to “average” against so the average age of their vehicles used to provide the services is, in effect, the maximum age.

In considering any changes, safety and reliability impacts are critical. The Taskforce identified a number of initiatives that will increase safety of vehicles which have been implemented since average age was introduced in 1990.

These measures include:

- More stringent operator accreditation requirements, which include a formal Safety Management System;
- Increased compliance requirements under the RTA Heavy Vehicle Inspection Scheme;
- Commercial incentive to maintain buses to achieve eligibility for the Fuel Tax Credits Scheme

Furthermore, reliability reporting measures are expected to be introduced in the contract.

The Ministry has always been prepared to conduct viability assessments where operators are facing serious viability concerns. Where this is caused by the requirement to meet average age requirements, the Ministry has been prepared to consider giving operators – large and small – relief from those requirements for a reasonable period of time. These arrangements will continue to be available, and the Ministry will assess applications on a case-by-case basis.

The Ministry's view is that the inability to "average" their fleet means that smaller operators are disadvantaged under the PwC's depreciation payments and are, therefore, more likely to be experiencing financial viability issues.

As a result the Ministry believes it is appropriate to provide relief from complying with average bus age requirements to small operators who can demonstrate compliance with other existing safety and reliability measures.

To be eligible, it is proposed that operators make a written application to the Ministry providing details of their fleet and demonstrating their inability to take advantage of fleet age averaging.

Because average age has been adopted by the Ministry as proxy for vehicle safety and reliability, it is proposed that operators seeking interim relief from their average age requirements – whether on equity or hardship grounds – must also demonstrate that they are meeting all accreditation obligations relating to vehicle maintenance.

Recommendations:

1. That the Minister consider targeted "average age" relief for replacement of buses to operators who can average bus age over no more than 2 vehicles.
2. Provide a period of up to 3 years extension of time to replace the existing contract bus.
3. Relief be made available only for existing buses. No relief to be provided where existing bus is replaced with a second hand bus.
4. Operators seeking relief must lodge an application with the Ministry of Transport outlining the following:
 - Grounds on which relief is sought: eg
 - i. Financial distress being suffered (if any);
 - ii. Whether interim contract arrangements are causing any difficulties;
 - iii. Whether bus reform is causing concerns of contractual uncertainty;
 - iv. Whether volatility of the contract category is expected to require bus replacement within the period for which relief is sought;
 - v. Seeking equity with larger operators on the basis that the bus is safe, reliable and not yet reached the end of its useful life.
 - Period of relief sought
 - Compliance with all accreditation requirements to date of application
 - Copy of last HVIS inspection report
5. The Ministry to develop a standard application form covering these aspects.

2.2 Category Shift

As noted previously in this report, category shift takes place when student numbers rise or fall, changing the payments that affected “non-commercial” operators receive for the provision of the services.

The BCA has raised this as a serious issue for all operators – large and small – and is arguing for relief to be applied “consistently and equitably” across the industry.

Options discussed at the Taskforce included a “parachute” or phased reduction in payments over a period of two years.

To understand the nature and extent of the problem, the Ministry undertook a preliminary analysis of changes in bus category resulting from the 2006 survey using contracts managed by the Ministry’s Northern Office.

The results were as follows:

- 40 operators were affected by a total of 47 changes in category. In other words, some operators experienced more than one change. One operator, holding two non-commercial contracts but no commercial contracts, experienced a decrease in categories in both contracts.
- A drop in bus category impacts most on single bus operators. For example, an operator who went from a Category 3 to a Category 2 bus experienced a \$23,994 (or -21% change) in revenues on a total contract value of \$109,391. Approximately 80% of the reduction in payments related to the change in the capital payment, with the balance the different between the service payments.
- The 11 single “non-commercial” contract holders in the sample experienced total revenue losses of between 13% and 22%.
- In contrast, the one operator in the sample who held both a single “non-commercial” contract and a “commercial” contract experienced a -22% revenue change on the “non-commercial” contract and a -3% change overall.
- Operators with two “non-commercial” contracts (and no “commercial” contracts) experienced overall revenue falls of between 4% and 6% when they went down one category in one of their contracts while for “non-commercial” operators with three contracts the total decrease in revenue was 2%.
- For “non-commercial” operators with multiple contracts, the picture is somewhat different. One operator, holding 12 “non-commercial” contract experienced a loss of less than 0.25% in total revenues when shifting from a Category 4 to a Category 3 bus in one of their contracts.
- Finally, operators with a large number of both “commercial” and “non-commercial” contracts experienced losses of less than 0.1% of total revenues across all contracts.

It is noted that some operators would choose not to replace a bus if the category went down, in anticipation of either a future increase in vehicle category or in order to maintain flexibility for charter operations.

Recommendations:

As a result, the Ministry believes it is appropriate to provide relief on the following basis:

1. That the Minister consider relief for operators who have experienced a decrease of 10% or more in total contract payments received from the Ministry through a phased reduction of payments over a two year period, provided the bus is replaced.
2. Relief to cover both the capital and operating costs where it is demonstrated that the purchase price of the bus has not been fully recovered through depreciation paid through contract payments.
3. No relief proposed for increased category shift – operators may make application for special consideration to the Ministry, as has already been stated in other forums.

2.3 Fuel Indexation for Commercial Operators

The Bus Industry Cost Index (BICI) is used to adjust the fares that are applicable to “commercial” contract holders.

In the early years of the BICI the percentage movement was calculated by looking at the fuel prices 12 months apart. More recently the average price over the full year has been calculated and compared with the average for the previous year to arrive at the percentage increase.

The movement of fuel prices is just one of the measures that go into the BICI. Fuel is about 12% of the basket of costs and wages are just over 50%.

This BICI percentage increase is then applied to the 4 fare scales (Metropolitan, Urban Fringe Country Town and Rural) which are used to generate the operator’s revenue (i.e. for SSTS, half fare reimbursements and as the maximum level for cash fares).

Because of the calculation of the BICI and the way fuel movements are calculated, operators eventually receive the extra costs applicable to fuel increases – although they have to carry the cost increase changes for up to 12 months.

The Ministry has provided relief to “non-commercial” operators through quarterly indexation. Operators providing services under metropolitan and outer-metropolitan contracts receive the benefit of monthly indexation as part of the total contract package.

Recommendations:

1. That the Minister consider expanding fuel relief through fuel indexation payments to rural and regional commercial operators.
2. Any relief paid through fuel indexation be taken into consideration in determining any future back payments arising from IPART recommendations.

2.4 Fuel Consumption for Non-commercial Operators

The industry has identified failure of the PwC model to effectively compensate for increased fuel consumption arising from design enhancements over time. This matter has not been considered by the Taskforce but may be separately considered on direction by the Minister. The BCA has proposed a survey of industry to determine current consumption rates.

This issue will initially be considered as part of the 2006 IPART process. If suitable data is not available in time this issue could be considered by the Taskforce as a potential additional interim measure.

Recommendations:

1. The proposed BCA survey be undertaken and results used to determine the quantum of impact on non-commercial operators.
2. Results of the survey be applied in formulating a recommendation to the Minister for any further relief as an interim measure.
3. Any increase in payments in 2006 arising as a result of IPART's consideration of increased fuel consumption be taken into account in determining any additional relief required

3. RURAL AND REGIONAL ENVIRONMENT

Service providers in rural and regional areas fall into distinct categories according to the size of their business, location of the contract area and the number of bus service contracts they hold:

- Small, single contract holders in isolated areas;
- Small, single contract holders operating into villages and small towns;
- Medium businesses holding either multiple small and / or a medium town contract; and
- Large business operating multiple medium / large contracts.

The following services are currently being provided and will be required to be part of new bus reform contracts:

- Dedicated stand alone school services
- Country Town services
- Village to Town services
- Country Town to Country Town services
- School services feeding into a Country Town

The current funding and contractual models do not recognise these business differences.

The Ministry does not have information about the size of “commercial” fleets in rural & regional NSW, but keeps records of the number of vehicles each operator is accredited to operate in delivering services (whether under “commercial” and “non-commercial” contracts). While some operators will be accredited for more vehicles than they use to provide the services, this information helps provide a snapshot of the industry’s profile.

Table 1: Number of buses for commercial operators

No of buses for which operator is accredited	No of “commercial” operators
1	3
2	4
3	2
4	5
5	5
6	3
7	1
8	3
9	3
10	5
12 - 18	12
20 - 28	9
30 - 37	7
40 - 49	5
50 - 60	4
100 - 120	3
190 – 200	1
350	1

As a rough measure, there 61 rural & regional bus operators that have “commercial” contracts, based on counting operators who trade in different locations but are owned by the same parent company as a single operation. Of these 61 operators, 34 (55%) operate fewer than 10 vehicles and 19 (31%) operate fewer than 5.

A review of the number of contracts held by individual operators also assists in understanding the diversity of the industry.

Table 2: Number of contracts held by individual operators

No of contracts held	No of “commercial” contract holders	No of “non-commercial” contract holders
1	88	443
2	12	143
3	5	63
4	1	30
5	-	17
6	2	12
7	3	12
8	1	9
9	-	4
10	-	7
12	-	6
13-20	-	9
21-29	-	4
27	1	-
53	-	1

Information generated from the review of services in Tamworth undertaken by the Service Planning Working Group revealed that the city of Tamworth has a population of 32,543 (2001 data) with approximately 7557 school students (2006 data) at 21 schools are serviced. Regular passenger and school services are provided through 3 commercial and 21 non-commercial contracts.

A breakdown of these contracts in the Tamworth area is as follows:

- 3 commercial contracts, held between 2 operators, operating wholly within the city boundary
- 3 commercial contracts, held between 2 operators, operating from villages into the city area.
- 21 non-commercial contracts, held between 3 operators, running from rural areas into the city area.
- 23 non-commercial contracts, held between 19 operators, operating wholly outside of Tamworth city, running into smaller villages and towns from rural areas.

OPTIONS FOR REFORM

3.1 Isolated Single Contract Holders

In recognition of the business nature of single isolated school bus service contracts it is considered that just one type of contract for all bus services in rural and regional areas is not appropriate.

For this reason the Taskforce proposes the following arrangements for “stand alone” isolated school bus services:

- a simplified contract reducing administrative burden;
- reduction of planning and reporting requirements;
- review of security arrangements;
- possible first right of refusal for second contract term; and
- revision of existing funding arrangements to ensure sustainability.

3.2 Larger Contract Holders

Reform may involve amalgamation of services where services are provided by a single operator.

Basically contractual reform needs to meet the Government’s core objectives including:

- Ensuring that the community and the Government have adequate input into the design, development and delivery of services.
- Ensuring that there is continuity of essential transport services for the community.
- Improved transparency and accountability under performance-based regular reporting across a range of indicators.
- The ability for Government to purchase services meeting its public policy priorities.

Appropriate funding arrangements will be established to ensure transparency, accountability and sustainability.

3.3 Service Area Networks

Reform in areas currently serviced by multiple operators is expected to require reorganisation of those bus services in order to achieve maximum efficiency.

The framework for an appropriate level of access to service is to be developed. Services provided under existing contracts will be reviewed to determine services that could be provided as an optimal network. It is expected that an optimal network will result in a reorganisation of existing services.

The Ministry’s preference is to work with the industry in developing an appropriate transition plan to achieve network changes.

3.4 Next Steps

- Develop a “stand alone” contract for isolated school services;
- Develop funding arrangements through the conduct and evaluation of the trial; and
- Determine the delivery of service networks through the trial.

4. TRIALS

4.1 Funding Model Options:

- **Model 1: Gross cost/revised PwC**

The first funding model option is a “gross cost” or “non-commercial” model which aims to address the problems with the PwC model.

- **Model 2: Risk sharing**

Under this model, the risks are shared between Government and the operator.

Most – but not all – costs are covered by direct payments, with the operator carrying a level of revenue risk tied to patronage. It is the midway point in the spectrum of funding model options between the “gross cost” and “net cost” arrangements.

- **Model 3: Net Cost or “commercial”**

The third option is a net cost model, based on a modification of existing “commercial” arrangements.

Under this model, operators are remunerated on a fare per passenger basis. A variant to this model is how the margin should be calculated.

This is the BCA's preferred model for services in larger towns and centres and is dependent on adequate service planning guidelines providing suitable flexibility.

The BCA has been seeking confirmation that a funding model based on “per head fares per boarding” will meet Government's transparency, accountability and value for money requirements. The BCA model also requires “community transport” tasks to be identified and paid for separately.

The Ministry sees no reason why a “commercial” model cannot meet those transparency, accountability and value for money requirements, as long as there is:

- a clear link between costs and fares (and the model assesses the costs of providing the services, not merely the sum of the inputs);
- the margin is commensurate with the real level of risk carried under the contract;
- there is a method for establishing and auditing “actual” SSTS travel and payments are linked to the results of that process. This may include, for example, a survey process under which payments move when recorded patronage has changed outside a certain level of tolerance.
- an appropriate agreed methodology for assessing changes in fare levels.
- A delineation between route and school services and “community transport” services is clearly identified during the trials.

4.2 Trial Methodology

Step One: Understanding Costs.

The first step in developing trials is to understand the costs incurred by individual operators, recognising different costs for the different category of operator dependant upon the size and location of the business.

It is imperative that there is an understanding of costs incurred by operators in order to effectively determine an appropriate level of revenue which covers this cost and allows for a reasonable margin (commensurate with risk exposure)

An option for establishing costs is to survey operators. Issues to be considered with this approach are:

- It is highly dependant on the capability and attitude of individual operators;
- Different operations and business practices between business may impact on the accuracy of data collected. Eg small businesses in particular may not accurately record labour hours;
- Costs recorded on a 'whole of business basis' may not be representative of the entire costs of running a business eg owner manager/ driver/ mechanic. In-house repairs versus outsourced, allocation of depot costs; and
- Gathering of reliable information can be extremely time consuming and require extreme attention to detail

Another option is to adopt a combination of unit costs and actual rates to determine actual cost:

- Some unit rates could be determined through industry averages or research eg. Award rate for drivers, fuel costs; and
- Other rates to be determined through operator survey.

Difficulties in this approach include large quantities of data, a potential level of inconsistency in the costing of expense items by different businesses, accuracies through an "averaging" approach and the degree of cooperation required from operators.

The preferred approach is the combination of unit and actual costs confined to six major areas of expenditure:

- Labour
- Fuel
- Maintenance
- Finance – Depreciation, interest and leasing
- Overhead
- Margin

By confining the areas of expenditure down to six major items the process will be less complex for operators. Operators will be encouraged to provide information on one or more components, with this input used determine the respective unit costs for operators in that particular category – eg small, isolated operator.

The sample size of operators is yet to be confirmed, but is expected to be in the vicinity of 100 service providers.

Step Two: Determining rate per km for each model

Cost components are to be derived through a combination of survey responses from operators and industry research (such as fuel and finance costs) and statutory obligations (such as vehicle registration, award wages, workers compensation insurances and superannuation). Depreciation is to be calculated rather than surveyed.

Once determined, cost components are then to be inserted into each funding model adopted for the trial.

Step Three: Communicating the trial process to operators.

It will be important to work with operators in the selected trial area to ensure there is an understanding of how the trial model would work, including how the rates were developed.

It will also be important to emphasise that there is to be no change to actual payments or actual services as a part of the trial, with the trial purely being a desk top comparison.

Step Four: Evaluation of the Trial Models

Evaluation of trial models is to be undertaken against each of the models as well as against existing funding arrangements. This evaluation involves comparison of costs over both the existing services and any optimised network identified by the Service Planning Group.

5. NEXT STEPS IN THE REFORM PROCESS

5.1 Evaluating the trials and refining the funding model/s

The trials are proposed to run from October 2006 through to June 2007.

During the trial period, evaluation of costs incurred by the operators will occur initially after three months. Should the process need to be refined this will occur at that point prior to the final evaluation of the full trial.

The final evaluation will occur in July – August 2007. The evaluation report will include recommendations for the funding models most appropriate to be adopted for rural and regional bus services, including any refinements deemed necessary from results of the trial.

5.2 Finalise the new contract/s

During the conduct of the funding model trials work will continue in developing the “nuts and bolts” clauses of the contract. Once the funding model evaluation and the service planning framework are completed, final work on the contract can commence.

It is expected that a standard contract will be finalised by November 2007.

5.3 Government approval and roll out of reform

Recommendations on the funding models for bus services in rural and regional areas will be made after the final evaluation of the trials. Approval from NSW Treasury and Cabinet will be required prior to proceeding with the roll-out of reform.

A roll-out program will be developed in consultation with the industry. At the time the roll-out program is developed, any transitional arrangements that might be required will be identified. In particular, the Government does not have a fixed view on how it will continue to consult with the industry in working towards a smooth transition to the new arrangements.

5.4 Transition and Exit Options

The Government has consistently stated since 2004 that its preference is for current contract holders to have the first opportunity to negotiate a new contract if they wish to remain in the industry. Nevertheless, it is recognised that operators will make their own business decisions as reform rolls out and arrangements should be put in place to address them.

The “Tingle amendment”

When the NSW Parliament passed the Bus Reform Act in 2004, the Government agreed to an amendment in the Legislative Council, proposed by the Hon John Tingle, to provide a mechanism for operators who wished to exit the industry.

The so-called Tingle amendment allows an operator who does not wish to remain in the industry to apply to the Director-General to make an incoming operator purchase the outgoing operator’s assets as a requirement of the new contract. The assets would be valued by an independent valuer.

The Tingle amendment does not, however, allow for a “good will” component in the valuation of these assets.

In discussions with the BCA, the Ministry has agreed that the regulation that will allow the valuer to value the business on a “going concern” or “market value for existing use” basis. This will depend on whether the business as a whole is being sold (in which case a “going concern” valuation is appropriate) or whether some of the assets being used to provide the services, like a bus fleet, are being sold (in which case “market value for existing use” is the appropriate methodology).

There is generally – but not always – a premium for a business sold as a “going concern” or assets sold for existing use. This is because a fleet of buses (for example) will generally be more valuable to a potential purchaser seeking to operate the services as the purchaser does not have to source each bus separately. This also assumes that The vehicles are also available with maintenance records, are registered, roadworthy, and ready to continue to provide services the next day.

Drafting instructions have been provided to Parliamentary Counsel and it is expected that the new regulation will be in force before the end of the year and well before the roll out of rural & regional bus reform.

While the regulation provides the mechanism for valuing assets of an existing operator, the funding arrangements that are to be developed will need to provide a mechanism to ensure the operator purchasing the assets is operating on a viable basis.

The BCA has raised the impact on business viability if operators are unable to recover their investments and has raised concerns that cash-flows may be insufficient to meet financial commitments.

The Government has consistently stated that it is committed to viable contracts but is not prepared to publicly fund business decisions based on the payment of goodwill, instead, exiting operators are being given the first opportunity to negotiate a new contract on transparent commercial terms.

BCA proposal:

The BCA has therefore proposed an alternative mechanism to transition to the reorganised services. The BCA proposal is outlined below.

In considering any approach to the valuation of assets it should be noted that for small, isolated services the treatment of any assets for that service in the event that the service no longer being required will be no different under the reform process than it is now. Operators have entered into current “non-commercial” contracts on the understanding that if student numbers reduce to the point where the service is no longer required then it will be discontinued.

Under BCA’s “commercial” funding model option, an operator may be able to achieve efficiencies by buying out another operator, on the basis that the purchasing operator is guaranteed that the agreed funding for the exiting operator would continue for a specified period to the purchasing operator. After the specified period the savings accrue to the Ministry.

The concept would be for the lead entity to continue to be paid the remainder of the contract at the same rates. The lead entity would then be responsible for paying the outgoing operator, with the Tingle Amendment regulation remaining as a safety net.

6. CONCLUSION

The Taskforce believes the recommendations presented in this report fulfil the requirements as set out in the Terms of Reference.

The Ministry and the BCA believe the Taskforce should continue to:

- guide the development of new funding arrangements, contractual models and service planning policies for rural and regional bus services in NSW; and
- identify practical transition arrangements that will help achieve their smooth implementation.

RURAL AND REGIONAL BUS REFORM CONSULTATIVE TASKFORCE

Terms of Reference

Background

The Minister for Transport, the Hon. John Watkins MP, has agreed to the establishment of a joint Government/BCA Rural and Regional Bus Reform Taskforce. The role of the Taskforce will be to develop principles and options for, and provide advice on, implementation of the recommendations from the Unsworth Review of Bus Services (February 2004) relating to rural and regional bus services.

Reform Objectives

The Government's objective is to develop new contracting, service planning and funding arrangements for rural and regional NSW which provide:

- performance based contracts incorporating a passenger focus, consistent service standards and mechanisms to ensure continuity of essential passenger services;
- transparent funding arrangements that support value for money, proper allocation of risk and a sustainable industry; and
- effective service planning arrangements which reflect local travel patterns, minimise duplication and represent optimal use of the transport funding and assets in each location.

Taskforce Composition and Process

The Taskforce will comprise of up to five representatives from the Ministry of Transport covering its bus reform, network development, operations and community transport divisions and up to five members representing the private bus industry and reflecting the mix of small, medium and large operations in rural and regional NSW. Additional representatives will be co-opted as needed to participate on working groups to address key issues. The Minister will also seek advice from other key stakeholders.

The Taskforce and/or its working groups may meet with key stakeholders, such as operators, relevant government agencies and the Ministry of Transport's Director General, in the course of its deliberations as appropriate. Taskforce meetings will be held monthly. Working group meetings will be held as needed.

Reform Principles

The rural and regional reform process will be underpinned by the principles outlined in the final report of the Review of Bus Services, including the need to:

- ensure the best possible use of the rural and regional bus fleet;
- develop a more equitable, updated funding model that links return to operational effort, provides for a rational, consistent and transparent allocation of risk and does not favour some operators at the expense of

others;

- include requirements for community availability and charge-out rates in contracts; and
- implement a more rational and coordinated approach to service planning.

Terms of Reference

Specifically, the Taskforce will be required to identify options and provide advice in regard to:

- 1) The implementation of contract reform in the diverse environment that encompasses rural and regional bus services.
- 2) Major contract provisions including: service and safety standards (including average age); employment and staffing issues; performance monitoring, reporting and assessment; arrangements for cooperation and integration; requirements in respect of community/charter work availability and working with schools to ensure effective services; contract terms; treatment of assets; continuity of service; and end-of-contract arrangements.
- 3) A new financial model for rural and regional bus services that: properly manages real risk; reflects efficient benchmark costs; links return to operational effort; provides greater equity for contract holders with smaller operations; recognises income from other sources; and establishes a per vehicle kilometre charge for charter and community work.
- 4) Achieving service improvements, better use of available resources, a stronger customer focus, and enhanced fairness and accountability in a cost neutral context.
- 5) Service planning principles and processes to guide service reviews that include community consultation and feedback.
- 6) The strategies and areas proposed for the pilot projects.
- 7) Implementation principles for the roll-out of reforms across country NSW to promote smooth transition, continuity of service and effective contract management.
- 8) Identification of changes, consistent with the broader reform program, that could be implemented in the short term and provide benefits to both the community and industry.

Timeframe

The Taskforce will be required to provide advice to the Minister on the above matters by mid 2006.