Implementation of the Public Transport Operating Model update

JULY 2012

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Key points

- New legislation is being enacted to implement the Public Transport Operating Model (PTOM).
- The intent is to incentivise the delivery of effective public transport services to communities, grow patronage, maximise farebox revenue, and improve commerciality.
- A partnership approach between operators and regions (including regional councils, unitary authorities and Auckland Transport) is essential.
- Units, which are the building blocks of the network and services, will be defined in regional public transport plans (RPTPs).
- Regions need to consider the implications of PTOM now, and if necessary, change their strategic public transport planning and procurement approach in consultation with the NZ Transport Agency (NZTA).
- The NZTA is developing policies and procurement requirements – from now on all new bus and ferry contracts must be aligned to the PTOM approach.

Introduction

PTOM, announced by the government in March 2012, is a combination of planning, funding and procurement tools all aimed to improve the efficiency and effectiveness of public transport for New Zealanders. PTOM is intended to build long-term partnerships between regions and bus and ferry operators, which will incentivise the delivery of effective public transport services to communities. A bill to enact PTOM is likely to be introduced to parliament before the end of calendar year 2012. The aim of PTOM is to grow patronage with less reliance on public subsidies. It has two key objectives:

- To grow the commerciality of public transport services and create incentives for services to become fully commercial, and
- To grow confidence that services are priced efficiently and there is access to public transport markets for competitors.

PTOM has been developed by representatives from the public transport sector as part of a review of the Public Transport Management Act 2008. While the Ministry of Transport will manage legislative change, the NZTA will review its policies and procurement requirements to implement PTOM. Regions need to review their public transport planning policies and procurement approach in order to implement PTOM. They can implement the model ahead of legislative change if they wish, with approval from the NZTA.

Metro passenger rail will be incorporated into the legislation, but Cabinet is yet to decide which components of PTOM will apply to rail.

Purpose

This update provides information to regions about the new PTOM. It is intended to provide interim guidance before legislation is finalised, NZTA procurement rules are updated, and formal guidance is produced.

In the absence of such guidance, regions whose bus service contracts expire within the next two years need to review this update and contact NZTA regional staff to discuss how best to incorporate PTOM into their planning and procurement practices. This is because current NZTA procurement rules are not necessarily consistent with the planned PTOM changes and the NZTA must ensure that any new contracts entered into by regions are aligned with the new approach.

Strategic context has changed

PTOM is a strategic change in the way public transport is planned and procured. It provides an opportunity for regions to work in partnership with operators to achieve improved competition and value for money outcomes that may not previously have been possible, while improving the effectiveness of services delivered to communities. Over time all regions are expected to review their procurement strategies to incorporate PTOM requirements. Such reviews are consistent with the NZTA's *Procurement manual*.

The change will be less significant for smaller regions with limited public transport networks and services. Regions that have recently completed tendering service contracts may not need to incorporate PTOM elements in their procurement strategies in the short term. However these regions should still consider the benefits of PTOM components such as partnership-based contracts and joint annual business planning.

New aspects to be considered

All regions will need to consider the new environment in their procurement strategies. These are the key changes, which will be set out in the legislation and NZTA *Procurement manual* and tools:

Regional public transport plans

- The RPTP defines a region's public transport network. Any services not included in the RPTP will be exempt services.

Units

- All public transport services identified in a RPTP will be allocated into 'units.'
- A unit will be no smaller than a full route but may include multiple routes and will include all timetabled services for a route.
- Each unit will be provided under contract to the regional council and operated as a single marketable whole.
- Units will either be tendered on the open market or negotiated with incumbent operators of those services.
- Some units will be fully commercial and will operate without a subsidy (but be eligible for concessionary fare payments). These units will still be under contract. Others will have varying levels of subsidy determined by their commerciality.

Contracts

- Tendering will be designed to the greatest extent possible to enable new entrants to participate in the market.
- Contracts will include a sharing of financial risk and reward.
- All operators with a contract will have exclusive operating rights in the unit (or units) for the duration of that contract.
- Joint annual business planning for units between operators and regions to support stronger partnerships.

Performance indicators

- Key performance indicators designed to grow patronage and farebox revenue will be agreed.
- There will be more transparency about operator and regional performance through the key performance indicators and better availability of information about fare revenue and patronage.

Impact on procurement

NZTA will update its *Procurement manual* and tools to be consistent with PTOM prior to the legislation coming into force in 2013. In the meantime, regions planning to tender service contracts need to consider the implications of contract types and contract lengths on their future implementation of PTOM. The process for regions implementing components of PTOM ahead of legislative change may involve working with NZTA to arrange exemptions from the current rules or approval of components, as they develop a procurement procedure.

Progressive roll out

The implementation of PTOM will gather pace following the passing of the legislation. Prior to that time a number of regions will be implementing PTOM, including letting contracts that incorporate aspects of the model. The NZTA regional offices will work with regions in developing their PTOM processes and welcome early contact. The NZTA will consult with regions and industry groups such as the Bus and Coach Association as it develops policies and guidelines.

Next steps and timeframes

- All regions assess their public transport procurement strategies in light of PTOM (now).
- Consultation on draft NZTA policies, for example risk and reward, group tenders and benchmarking (September–December 2012).
- Regions implementing PTOM ahead of legislation, work with NZTA to arrange procurement approvals (September–December 2012).
- NZTA *Procurement manual* and tools updated (first half 2013).
- Legislation becomes operational (second half 2013).

Further information on the key components of PTOM

The main components of PTOM are summarised below. These are based on the cabinet paper and the work of the Core Working Group. They will be implemented via legislation, regional planning and contracting processes, the NZTA's *Procurement manual* and tools, and partnerships between operators and regions.

Units

All services will be planned as units by the region and identified in the Regional Public Transport Plan. A unit must at a minimum be all services on one route for the full timetable, but can include more than one route where a group forms a marketable whole. All units will have a contract with the region guaranteeing exclusive operating rights, although there may be some crossover of units, particularly on key arterials.

Commercial units

These are units operated without direct public subsidy from the region and the NZTA (excluding SuperGold card and concessionary fare payments). Provided services remain without direct public subsidy, they will not be put out to tender. However, they will still need to meet specific performance measures. Over time the number of commercial units is expected to increase as operators innovate and invest to improve the commerciality.

Tendered units

A portion of the regional network must be competitively tendered – the proportion will be determined by the region through its procurement strategy, influenced by the region's overall commerciality ratio. Tenders will be based on the gross operating cost of the unit. The region will provide recent trend information about the unit to the market as part of the tendering process. Contracts for tendered services will be for nine years, with a re-set of the gross operating cost at six years. This is separate to and different from NZTA indexation adjustments. Tender prices will be used to benchmark prices for negotiated units and re-sets. In smaller regions it is likely all units will be tendered.

Negotiated units (applicable mainly to larger regions)

Units with above average commerciality for the region may be directly negotiated with operators rather than going out to tender. This provides an incentive to improve the commerciality of a unit since, if a service meets the criteria, it will be renegotiated rather than tendered. Negotiated units (including fully commercial units) will have a term of six years. Benchmarking information from tendered units will be used to inform direct negotiations.

Like for like units (applicable where commercial registrations were in place prior to 30 June 2011)

These are a one-off commercial arrangement within a negotiated unit as part of the transition to PTOM. In exchange for relinquishing commercial registrations, operators will be offered negotiated units that contain an equivalent number of service kilometres to those held in existing commercial registrations, with a once-only 12-year fixed term contract.

Exempt services

Commercial services not identified in a regional public transport plan will be exempt services and will not be under contract. Exempt services do not have exclusive operating rights and can set their own fares and timetables. All inter-regional services that drop off or pick up passengers outside the region will be exempt.

Regional public transport plans

These are statutory plans that must be reviewed at least every three years, containing the unit descriptions and policies relating to the provision of public transport services. Regions are responsible for adopting the plan but must engage with operators in developing it, particularly when determining unit design. Plans are publicly consulted on.

Contracts

Contracts should provide a platform for partnership, and will include partnership principles, an agreement for joint annual business planning, updated key performance indicators and financial risk and reward sharing. Contracts should provide incentives for the partners to grow patronage and farebox revenue. In large regions a three-tiered approach is under development. Each of the three contract tiers is described below:

- Regional agreement

A strategic agreement between all operators and the region setting out matters for consistent treatment across the region, for example partnership principles. Any operator who intends to provide services in the region must be a signatory to the regional agreement.

- Partnering agreement

An agreement between an individual operator and the region setting out how they will work together, including aspects such as key performance indicators and reporting requirements.

- Unit agreement

An agreement for an operating unit which will contain details of services, including schedules, route coverage and peak vehicle requirements.

League table (applicable mainly to larger regions)

The league table ranks all units in a region and will be published annually. Initially it will be based just on the commerciality ratio of a unit. After a region has transitioned all contracts to PTOM, a weighted formula that also takes into account the relative increase in patronage will be used. League tables will be used to determine which units will be negotiated and which tendered. League tables are likely to be used in this way only in larger regions, and small and medium regions will only publish the commerciality of units.

Commerciality ratio

The commerciality ratio shows what portion of the costs of running a service are recovered from fare revenue. It is used to determine a unit's placing on the league table and consequently whether it will be negotiated or tendered. The commerciality ratio will also be used to assess the region's network as a whole. The formula for deriving the commerciality ratio is (fare revenue + concessionary fares + SuperGold payments)/(fare revenue + concessionary fares + SuperGold payments + subsidy). The commerciality ratio is similar in concept to the NZTA's farebox recovery ratio.

Benchmarking (applicable mainly to larger regions)

Regions will use tender cost prices from tendered units to determine a suitable benchmark price range for negotiated units and cost re-sets for tendered units. Such information will initially be provided to the region by a neutral third party.

Fare setting

Regions will describe their policy for fare setting, which will apply to all units, in the Regional Public Transport Plan. Operators may set the fares for exempt services.

Information requirements

All units will be required to provide patronage and revenue information to the region and the NZTA. Recent revenue and patronage information for units going out to tender will be disclosed to potential bidders. Revenue information for commercial units will not be made public, unless the service is to go out to tender due to operator withdrawal, or poor performance.

Risk and reward sharing

Risk and reward sharing essentially involves the operator and the region sharing any profits or losses above or below the previous year's revenue. All contracts will contain a risk and reward sharing model, but these may vary in complexity between units, and between regions.

Annual business planning

This is an annual process where the operator of a unit and the region will review the performance of the unit and agree a collaborative business plan to grow patronage and maximise farebox revenue.

Dispute process

Most disputes will be managed through standard contract clauses. In cases where operators consider they have been adversely affected by a region's decision in respect of exempt services or new services, there will be a right of appeal to the District Court.

More information about PTOM, including the cabinet paper and questions and answers, can be found on the Ministry of Transport's website **www.transport.govt.nz**.

Further contact with the NZTA can be made through our regional offices (contact your regional planning and investment manager), and for matters of policy, the national public transport unit (contact Julie Alexander julie.alexander@nzta.govt.nz).