

Monitoring Local Bus Service Tenders in England

Final Report 2004

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1. Introduction

BACKGROUND

- 1.1 This report presents the findings of a research study into supported bus services undertaken on behalf of the Department for Transport (DfT) by Atkins Transport Planning. The three-year study was commissioned in 2001.
- 1.2 Local authorities in England (outside London) are able to secure the provision of local bus services that would not otherwise be provided on a commercial basis by bus operators by offering a contract for the provision of the service, in most cases after a competitive tendering process. This mechanism has enabled authorities to ensure that access to the transport system has been maintained and enhanced for a great number of people, particularly those without access to a car living in areas that would otherwise have limited public transport services. Currently around 20% of the total local bus service mileage in England (outside London) is supported by local authorities - the remainder being operated on a wholly commercial basis.
- 1.3 In recent years Government has substantially boosted funding available to authorities through the Urban and Rural Bus Challenge process and the Rural Bus Subsidy Grant (RBSG). The annual cost of supporting tendered local bus services in England (outside London) in 2002/03 was £260 million.
- 1.4 Enabling local authorities to continue providing supported services remains a key element of the Government's 10-year strategy for transport. However, after a number of years of relatively stable prices the cost of supporting local bus services has been increasing in recent years and is a concern. As in all areas of public sector procurement there is a need to ensure that value for money is being achieved and that funding is allocated in a way that best serves policy objectives.
- 1.5 Atkins Transport Planning has, on behalf of the DfT, been reviewing how local authorities procure their tendered bus services with a view to establishing best practice and better understanding the key drivers of cost increases and how these might be best managed. The research undertaken has sought to identify how value for money could best be achieved in the very wide range of different local circumstances under which supported local bus services are needed.

Structure of the Report

- 1.6 Following this introductory section, the remainder of the Report is structured as follows:
 - ◆ **Section two** gives an overview of the objectives of the study and the methodology employed;
 - ◆ **Section three** details the trends in prices and the number of bids for local bus tenders across England and with further detail for the south east;
 - ◆ **Section four** provides an interpretation of the reasons for the observed trends; and
 - ◆ **Section five** provides conclusions.

LOCAL BUS TENDERING

- 1.7 Outside London, services are deregulated and around 81% are provided commercially. In London the market is regulated and TfL plans and funds the entire network.

Objectives for the Tendered Network

- 1.1 The aims of providing tendered bus services could, for example, include any or all of the following:

- ◆ Social inclusion/exclusion;
- ◆ Traffic reduction (to achieve or exceed Road Traffic Reduction Act obligations);
- ◆ Encouragement of particular developments or patterns of development;
- ◆ To provide wider travel choice or travel opportunities;

In response to environmental concerns;

- ◆ To reduce, the resources required in health, education or social services;
- ◆ To assist other policy options, for example the promotion of tourism; and
- ◆ To comply with Government policy or legislation.

- 1.2 In many cases, however, the local authority simply endeavours to maintain the pre-existing level of service, offering out to tender commercial services that are deregistered. This has become increasingly more important as the levels of commercial deregistration have grown. The south east has, perhaps, suffered more than most other regions with the financial failure of operators leading to inevitable commercial deregistrations. In the last two years, Staines-based independent bus operator White Rose ceased trading with the loss of three commercial routes which have had to be rescued, in the short term at least, by Surrey County Council. This followed shortly after the failure of two other Surrey operators, Tillingbourne and Surrey Bus.
- 1.3 As the price of tenders has risen and as a number of the large bus operating groups have sought to improve their operating margins, the ability of local authorities to pursue an automatic replacement policy has been severely tested. It has, therefore, been necessary to determine if there have been changes in the criteria used by the local authorities, or if they have simply altered the threshold levels.
- 1.4 The introduction of Rural Bus Grant has had a marked impact on the provision of tendered bus services and it has been necessary to determine to what extent it has affected the policies of the various local authorities.
- 1.5 Consideration has also been required as to the local authorities' bus strategies and their fit with the criteria used for determining the tendered service network.
- 1.6 Outside of London the 19% of services not operated commercially are supported by Local Authorities, to meet social needs. With the exception of small contracts below a specified limit, these are tendered, either for individual routes or parts of them.

- 1.7 Methods used to secure socially necessary services through tendering vary greatly between local authorities.
- 1.8 Most local authorities maintain a list of parties interested in bidding for bus services through the tender process. A number of authorities will send all tender specifications directly to these operators, others will contact them to establish which tender specifications they are interested in receiving. On occasions notices will be printed in the local and/or trade press inviting companies to tender for services.
- 1.9 The package of services offered for tender varies between authority and between tender. Some authorities tender in batches, others tender for individual contracts and some for an entire geographical area. A number of authorities try and bundle a number of individual services together to make a days work for a vehicle.
- 1.10 Tender specifications tend to outline the service timetable, days of operation, vehicle size and any other vehicle specification such as whether seatbelts are required or whether the vehicle should be low floor. Some tender specifications invite tenders on a number of different variations or on a number of different vehicle types.
- 1.11 Operators can submit alternative timetables on most occasions if they believe it provides a better service, or fits with their existing work schedules. They are also able to submit a 'package' bid, submitting one price for a number of tenders.
- 1.12 There is a great deal of variation between authorities in the financial type of tender. Some authorities tender on a cost basis and others on a subsidy basis. A number of authorities invite operators to submit a price based on either cost or subsidy and some require a price to be submitted for both.
- 1.13 When tenders are returned to the local authority they are opened and all bids are recorded. The bids are considered in terms of best value and quality of service. In general the operator which submits the lowest tender is awarded the contract, although this is not always the case. Where there are questions about an operator's reliability or their ability to deliver all aspects of the tender specification then the contract will not be awarded to them.
- 1.14 There are instances where no tenders are returned or where all tenders which are returned are too high or do not meet the specification. On such occasions the tender may be re-issued or the local authority might negotiate with the operators who have submitted bids to secure a service.
- 1.15 Some authorities award an annual price increase on contracts once awarded whilst others do not. Some authorities only increase the price if the operator applies for their annual increase. The amount of the increase is often in line with inflation.
- 1.16 Local Authorities generally have penalties for poor performance on contracts. For extremely poor performance the contract can be terminated. Annex A provides examples of the types of penalties for poor performance.
- 1.17 The length of tenders varies between authority and between contracts. Contracts are generally awarded for up to five years. There are occasions where local authorities will extend contracts rather than re tendering them and there are occasions where

contracts are let on an emergency basis to cover for a service which has been terminated at short notice, for example.

- 1.18 Tenders are issued for a wide variety of services including conventional bus services, demand responsive services and for some contracts shared taxi services are required. Tenders are also issued for school and social service contracts, although they have not been considered in this study.
- 1.19 The size of the contract varies from a variation to an existing route, through a single journey or infill services to frequent services operating daily. The quality of vehicle also varies greatly. Some contracts require modern low floor vehicles; others specify a maximum age whilst a significant number will accept any vehicle regardless of age.
- 1.20 The tendering system used by local authority does not exclude smaller, independent operators and significant numbers of contracts are held by small independent operators and not by the big groups.

OVERVIEW

- 1.21 Buses are a key element in public transport provision with some 81% of all local bus mileage in 2002/03, outside of London, provided on a commercial basis by a wide range of bus operators. This figure compares with around 84% throughout the previous decade. The remaining mileage, however, is secured through the tendering process and there has been some very real concern in recent years that following a protracted period of falling prices, in real terms, there is now an opposite trend of real increases in tender prices. There is also concern that coupled with this trend, the number of bids for tenders is also reducing.
- 1.22 Information compiled by National Statistics indicates that the cost (in 2002/03 prices) of purchasing non-commercial bus services in England (but excluding London) grew from £208 million in 1997/8 (the last year in which the reducing trend was observed) to £268 million in 2001/02, an increase of some 28%, although this does include additional funding for Rural Bus Subsidy Grant (RBSG). Excluding this additional funding the increase was around 7%, although this is a real terms increase. In the same four-year period, local bus service fares, overall, saw increases substantially above the retail prices index whilst the volume of passenger journeys fell by just under 5%. A slight reduction in funding, to £263 million was seen in 2002/03.
- 1.23 Average operating costs showed consistent real-term decreases following deregulation in 1986 and this trend continued until 1999/2000. In 2000/01 the first increase of over 6% was noted in Great Britain as a whole; a similar figure was seen in English Shire counties and a slightly higher increase in the metropolitan areas. A further 3% increase in operating costs, in real terms, is noted between 2000/01 and 2001/02. A further increase, but only around 1% was then experienced between 2001/02 and 2002/03.
- 1.24 The Government's 10-year Transport Plan, published in July 2000, sets out a long-term investment programme for delivering the aim of a modern, integrated transport system, raising standards of quality, accessibility, safety and reliability whilst reducing congestion and environmental impacts. The provision of bus services is key to ensuring that this vision is achieved and, whilst capital investment in improved

infrastructure through Local Transport Plans is likely to assist commercial operators to provide additional and improved commercial services, particularly where bus priority measures are put into place, tendered services will remain an important feature of local bus services. Real term increases in tender prices will clearly not help in these aims, particularly if that trend is set to continue into the future as operating costs continue to show a reversal of their previous downward trend.

- 1.25 The Environment, Transport and Regional Affairs Committee, in their report of July 1999, was concerned that anti-competitive practices might be having some effect on tender prices, whilst acknowledging that higher operating costs were a major influence. They were particularly concerned that rising tender prices would have major implications for the achievement of the Integrated Transport White Paper's objectives.
- 1.26 Research on bus tenders undertaken in 1999 concluded that prices were rising and that the main reasons for increases in tender prices included:
- ◆ increasing staff costs, reflecting driver shortages;
 - ◆ increasing vehicles costs;
 - ◆ a more commercial approach to tender bidding by some operators;
 - ◆ reduced patronage on some services;
 - ◆ the spending boost produced by the introduction of Rural Bus Grant exacerbating staff and vehicle shortages; and
 - ◆ tendering practice which allows, in some cases, early termination of contracts by operators who, then, seek to regain the contract at a higher price.

GLOBAL AND EXTERNAL TRENDS

Bus Patronage

- 1.27 The numbers of people using local bus services has an obvious impact upon the levels of commercial operation. For many years there has been a steady decline in bus patronage across the UK, although in more recent years there have been indications that this is levelling off; in some cases, notably in London, the trend has reversed and increased passenger volumes have been noted.
- 1.28 Between 2001/02 and 2002/03 an overall increase in passenger journeys of 2.6% was experienced in England, including London. The highest increase, of 7.5%, was noted in London and the biggest reduction in passenger numbers, at 3%, was noted in the South East excluding London (referred to throughout this report as the South East). London has seen consistent increases in passenger numbers since 1998/99. Over the same period outside of London there have been fairly consistent reductions in passenger numbers.
- 1.29 Over the fifteen year period from 1987/8 (shortly after deregulation) to 2002/03 London has seen a 28% increase in passenger journeys; the metropolitan areas have seen a 34% reduction in passenger journeys; and the shire counties have seen a 22% reduction in passenger journeys.

1.30 Figure 1.1, below, shows the trend in patronage for local bus services in England since 1987/8.

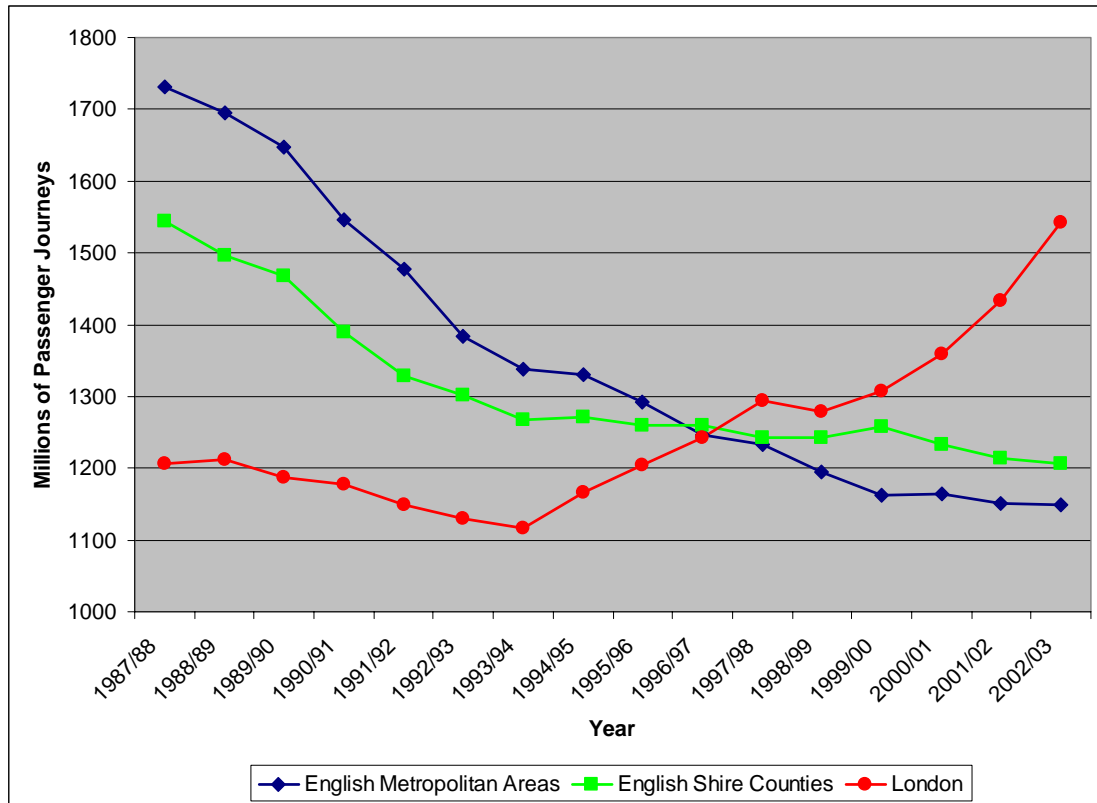


Figure 1.1 – Local Bus Services – Passenger Journeys by Area 1987/88 – 2002/03

- 1.31 Comparisons between the trends in patronage, the trends in passenger receipts and the trends in the number of kilometres operated are interesting in that whilst there is some correlation, it is not exact, possibly due to the time lags involved in customers making choices consequent upon fares or service changes.
- 1.32 The year on year trends in patronage are shown in Figure 1.2. London continues to show strong patronage increases (4.0% in 2000/01, 5.5% in 2001/02 and 7.5% in 2002/03) whilst both the English metropolitan areas and shire counties have seen small patronage falls fairly consistently in recent years (reductions of 1.5% and 1.3% respectively in 2001/02, but only 0.7% and 0.1% respectively in 2002/03). As noted above the south east region suffered the biggest fall in patronage during 2002/03.

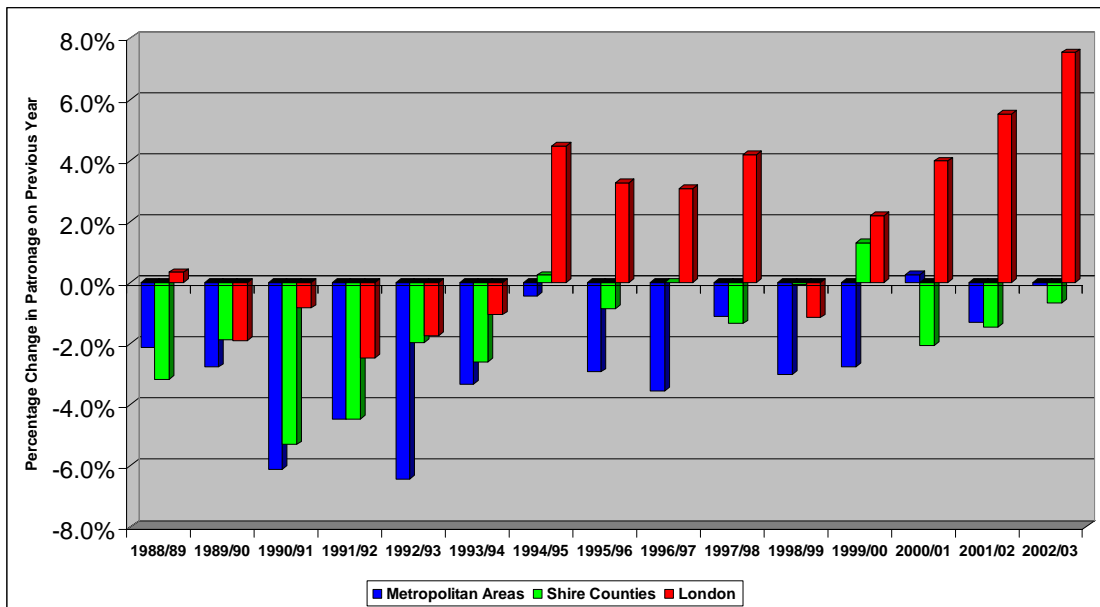


Figure 1.2 – Year on Year Change in Local Bus Patronage

Local Bus Service Kilometres Operated

1.33 Figure 1.3, below, shows trends in commercial and subsidised local bus kilometres.

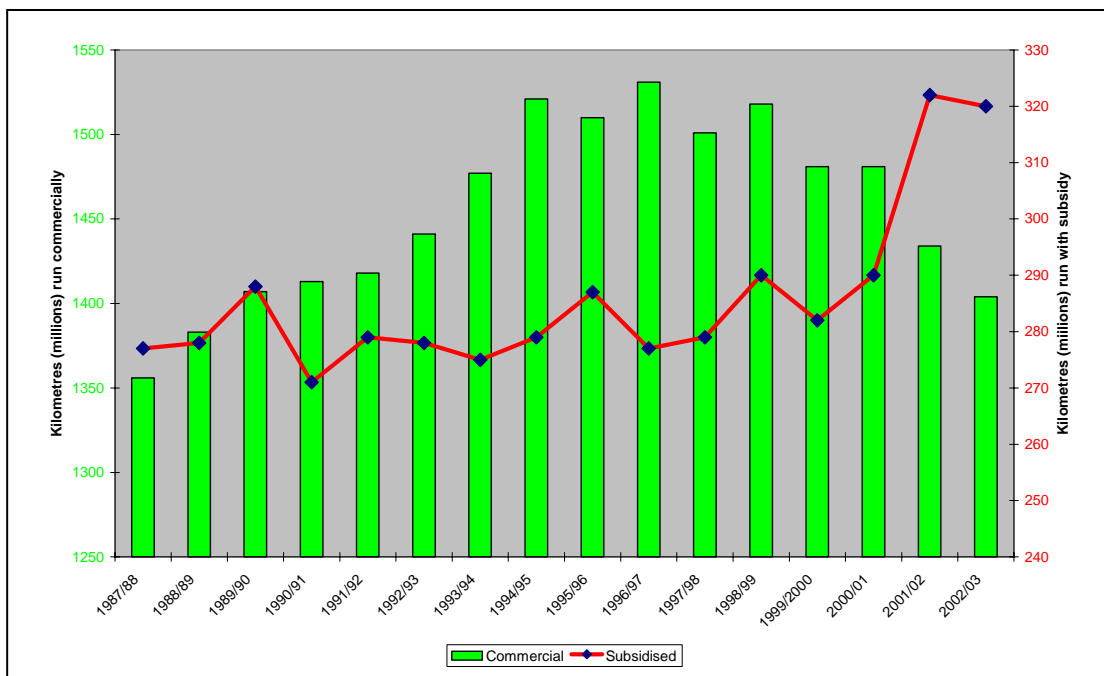


Figure 1.3 – Commercial and Subsidised Local Bus Service Kilometres Operated in England (excluding London) 1987/88 – 2002/03

- 1.34 Between 1987/8 and 2002/03, local bus kilometres operated in England (excluding London) have risen overall by some 5.6%. The total of 1724 million kilometres in 2002/03, however, shows a reduction of 1.8% on the previous year. The highest level of kilometres operated (1808 million) was achieved in 1998/99, that being the highest level achieved in more than two decades.
- 1.35 In the same period, commercial operations have grown by some 3.5% whilst the level of subsidised kilometres has increased by slightly more than 15.5%. A large element of this increase can be attributed to the introduction of Rural Bus Subsidy Grant but, nonetheless, the increase of 10% between 2000/01 and 2001/02 is significant, and particularly compared to a 3.1% reduction in commercially operated kilometres over the same time period. The level of subsidised kilometres did fall slightly (less than 1%) between 2001/02 and 2002/03 whilst commercially operated kilometres reduced by 2%. Commercially operated kilometres are, however, still at a higher level than at any time during the 1980s.
- 1.36 The level of commercial operation as a percentage of the total has reduced across this period, currently standing at 81% against a maximum 85% over the period.

Local Bus Service Support

- 1.37 Figure 1.4 shows the level of support in 2002/03 prices for local bus services since 1987/8. As shown, the overall level of public support for local bus services declined sharply after deregulation in 1986 and continued to fall until 1997/8. Subsequently there have been steady and quite sharp increases in the level of support, particularly when the additional Rural Bus Subsidy Grant (RBSG) and Rural Bus Challenge (RBC) are included. There was, however, a small reduction in the overall level of public support, both in absolute terms and per subsidised vehicle kilometre, between 2001/02 and 2002/03.
- 1.38 At 2002/03 prices, support for local bus services in England outside of London stood at £577 million in 1985/86, immediately prior to deregulation, and then fell steadily to a low of £208 million in 1997/8. Concessionary fares support has remained fairly constant with a total of £312 million paid in 1985/86 and £321 million in 2002/03 (at 2002/03 prices). Bus Service Operators Grant (BSOG), the replacement for Fuel Duty Rebate (FDR), has seen an increase over the same period from approximately £235 million to £378 million, an increase of 60%.
- 1.39 There is a broad correlation between the support for local bus services and operating costs. Operating costs declined steadily between 1985/86 (following deregulation) and 1999/2000; subsequently, however, there have been significant increases of 7% between 1999/2000 and 2000/01 and 3% between 2000/01 and 2001/02. The increase between 2001/02 and 2002/03 is much smaller at less than 1%. This would tend to suggest that operators were, generally, passing on the benefits of reduced operating costs to the local authorities either because of competitive pressure or for other business reasons. The reason for the uplift in tender prices occurring prior to increases in operating costs is, however, of interest although may well reflect an acknowledgement amongst operators that the efficiency gains that had been wrought subsequent to deregulation and privatisation were becoming exhausted.

1.40 The levels of local bus service support for England, but excluding London, are indicated in Figure 1.4 overleaf, as are operating costs.

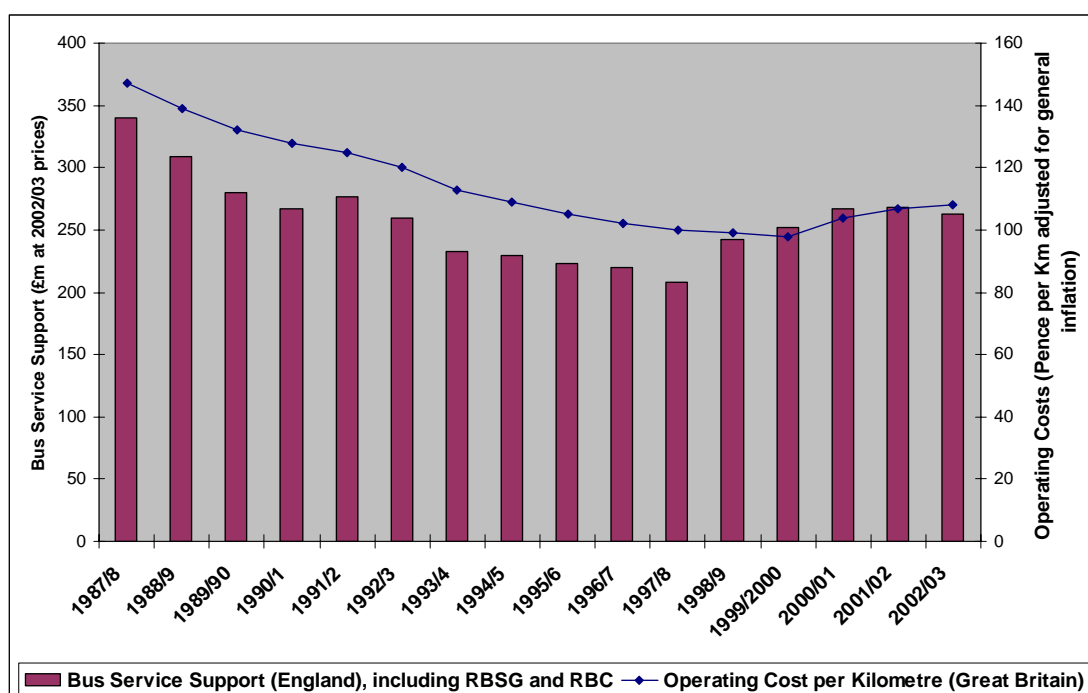


Figure 1.4 – Bus Service Support in England, excluding London 1987/8 – 2002/03 (2002/03 Prices)

1.41 The average subsidy per subsidised bus service kilometre exhibits similar trends, with consistent year on year reductions up to and including 1997/8, with increases from then until 2000/01. There was then a near 10% reduction between 2000/01 and 2001/02, due primarily to an increase in subsidised kilometres with only a marginal increase in the amount of subsidy paid. A small reduction in subsidy per kilometre is shown between 2001/02 and 2002/03. The average subsidy per kilometre, including RBSG and RBC, as at 2002/03, is still no higher than that in 1998/9, even though the overall level of support is higher. Despite recent increases the average subsidy per kilometre in 2002/03 stood no less than 33% lower than in 1987/88. This is shown in Figure 1.5, overleaf.

1.42 However, care is needed in interpreting this trend information, for a number of reasons. Firstly, some of the costs included under bus service support include some infrastructure schemes (bus stops etc), special needs services, special projects and information provision. It is likely that these elements have increased less than bus tender contracts. Secondly, there will be a national tendency for high cost per kilometric services to be dropped in favour of cheaper services. Thirdly, it is likely that the additional supported bus network that has been added in recent years comprises routes that cost less per kilometre to subsidise. This will include rural services funded through the RBSG (which although potentially high cost per passenger are likely to be lower cost per bus kilometre and run over longer distances compared to urban services). It will also include services which are commercial deregistrations – services which by being only just non-commercial are likely to be relatively low in terms of cost per bus kilometre.

- 1.43 It is likely, therefore, that the trend in bus subsidy per kilometre masks an underlying cost increase in providing supported local bus services.

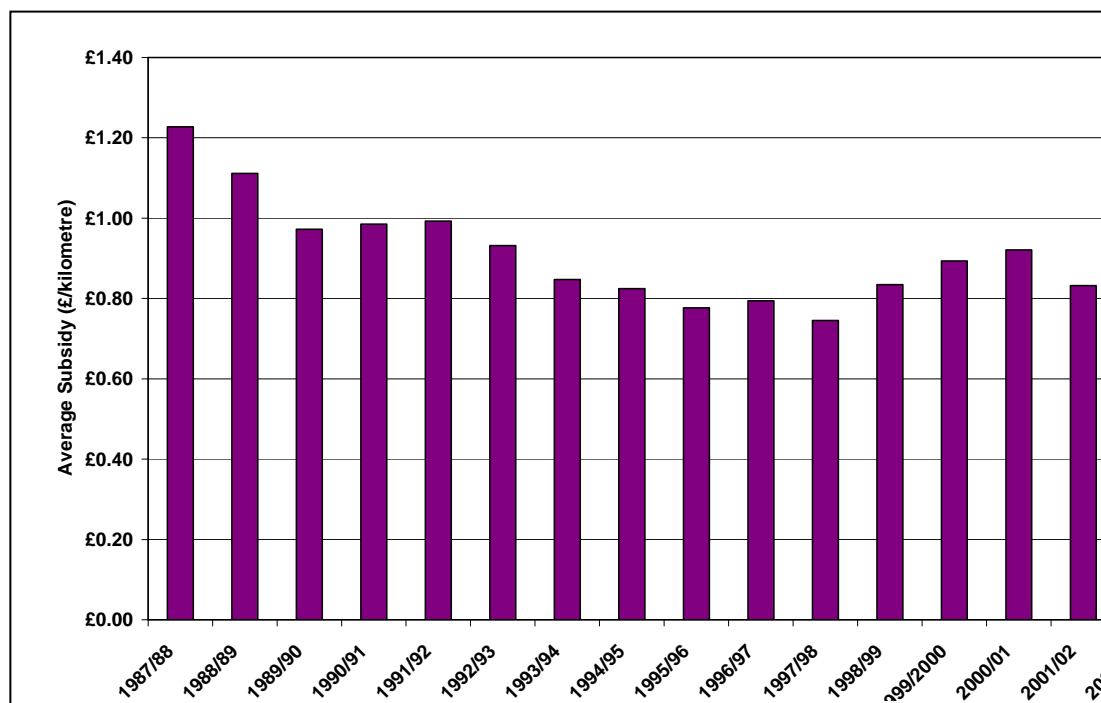


Figure 1.5 – Average Bus Service Subsidy per Subsidised Kilometre, England (excluding London) 1987/88 – 2002/03 (2002/03 Prices)

Operating Costs

- 1.44 Operating costs per kilometre in England (excluding London) in the period 1985/86 to 2002/03 have decreased by no less than 41%. Costs were reducing until 1999 when there was an increase in operating costs per vehicle kilometre. The increase in 2002/03 over 2001/02 was less than 1%.
- 1.45 Operating costs in London, although much higher per kilometre than elsewhere, show a similar pattern. The increase in 2002/03 as compared to 2001/02 was 11.5%
- 1.46 Figure 1.6 illustrates the operating costs per vehicle kilometre for Great Britain as a whole, these being broadly similar to England, excluding London.

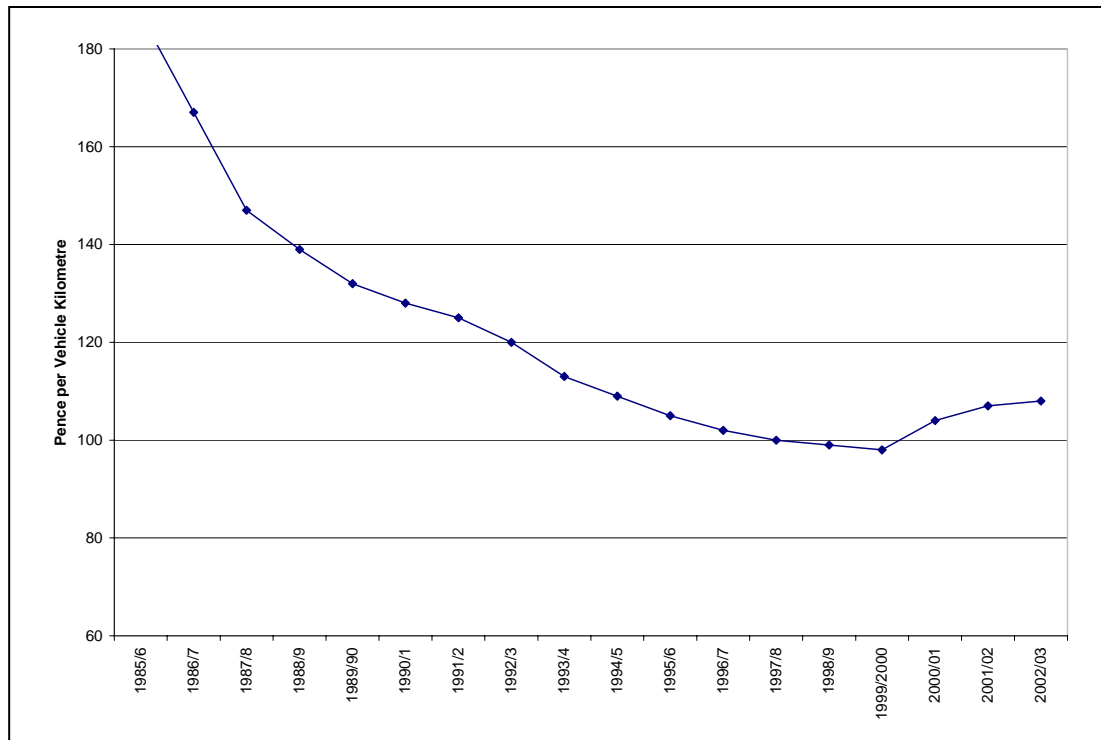


Figure 1.6 – Operating Costs per Vehicle Kilometre (Great Britain) 1985/86 – 2002/3 (2002/03 prices)

- 1.47 Figure 1.7, indicates the relative levels of bus service support, concessionary fares payments and BSOG payments for England as a whole. It can be noted that the overall levels of payment in each of these three categories of 'support' are converging to similar levels.

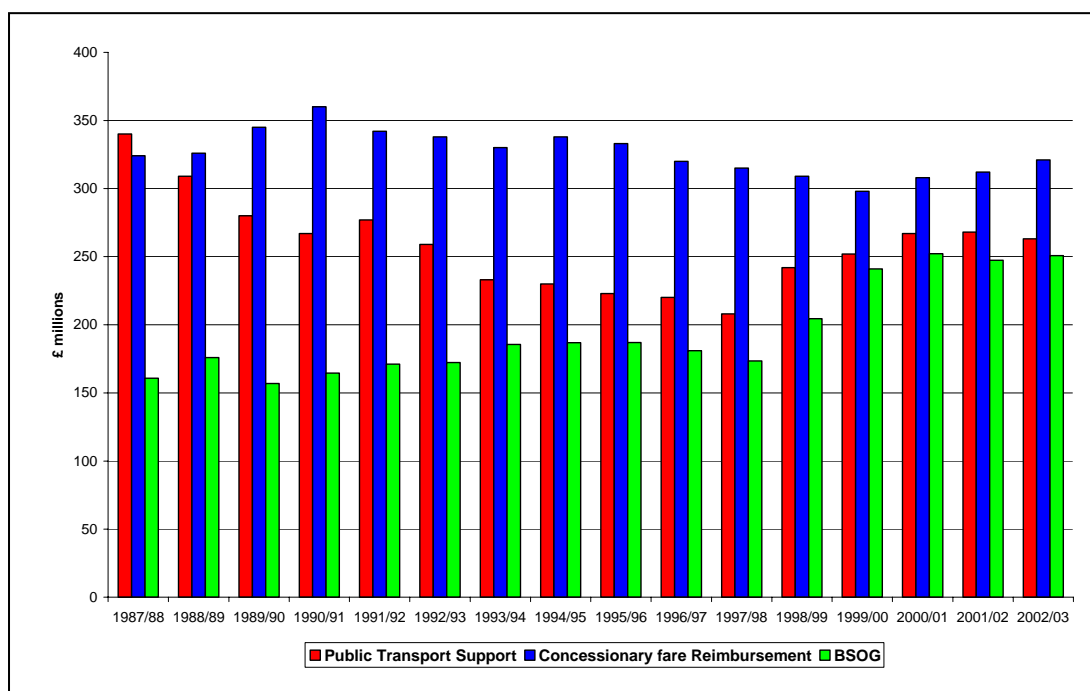


Figure 1.7 – Bus Service Support (England) 1987/88 – 2002/03 (2002/03 prices)

The Cost to the Consumer

- 1.48 The cost of public transport for the user will have an impact on the level of use made of public transport which, as already indicated, will have a longer-term impact upon the levels of commercial operation. Indeed, far more important than the actual costs are the perceived and the relative costs.
- 1.49 Taking 1992 as a base year, both bus and rail fares have risen substantially above the general level of inflation as well as substantially ahead of the general costs of private motoring.
- 1.50 Since 1992, rail fares have increased by more than 44% whilst bus fares have increased by 43%. This is in contrast to the general cost of motoring which has risen by less than 30%.
- 1.51 The 43% increase in bus fares needs to be set against average operating costs having fallen substantially in real terms and it is an interesting contrast to the usual explanation of rises in bus fares as being because of general increases in operating costs.
- 1.52 In all cases, as the general level of inflation has fallen in recent years, so have the increases in bus and rail fares. Figure 1.8, however, clearly indicates a growing 'gap' between the costs of motoring and public transport.

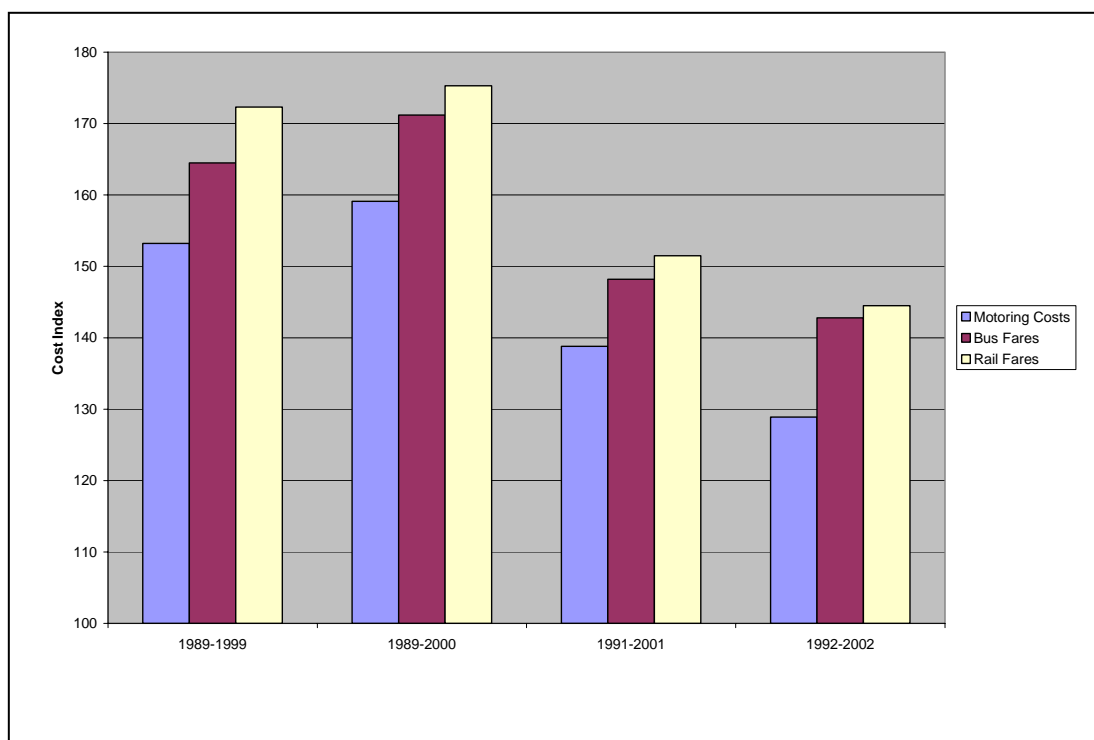


Figure 1.8 – Motoring and Public Transport Cost Indices over Selected 10-year Periods

Trends in Journeys, Kilometres Operated and Public Transport Support by Local Authority Type

- 1.53 Figures 1.9-1.11 indicate the different trends in passenger journeys, kilometres operated and public transport support in the English metropolitan counties, the English shire counties (including, in this case, unitary authorities) and London.

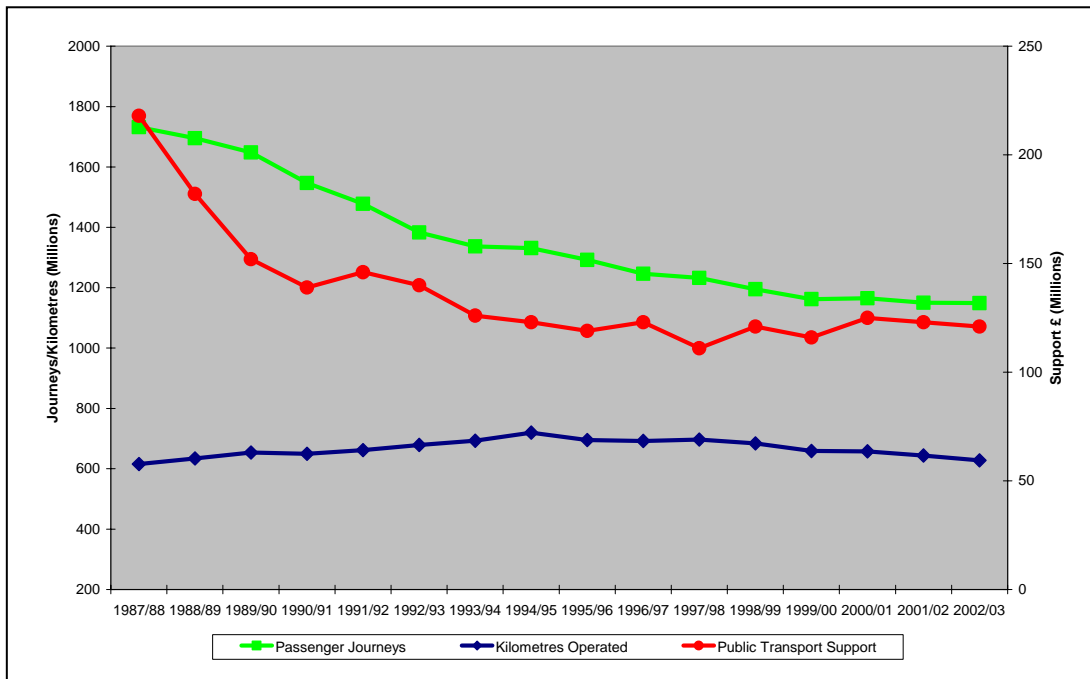


Figure 1.9 – Comparative Indicators 1987/88 – 2002/03: Metropolitan Counties (2002/03 prices)

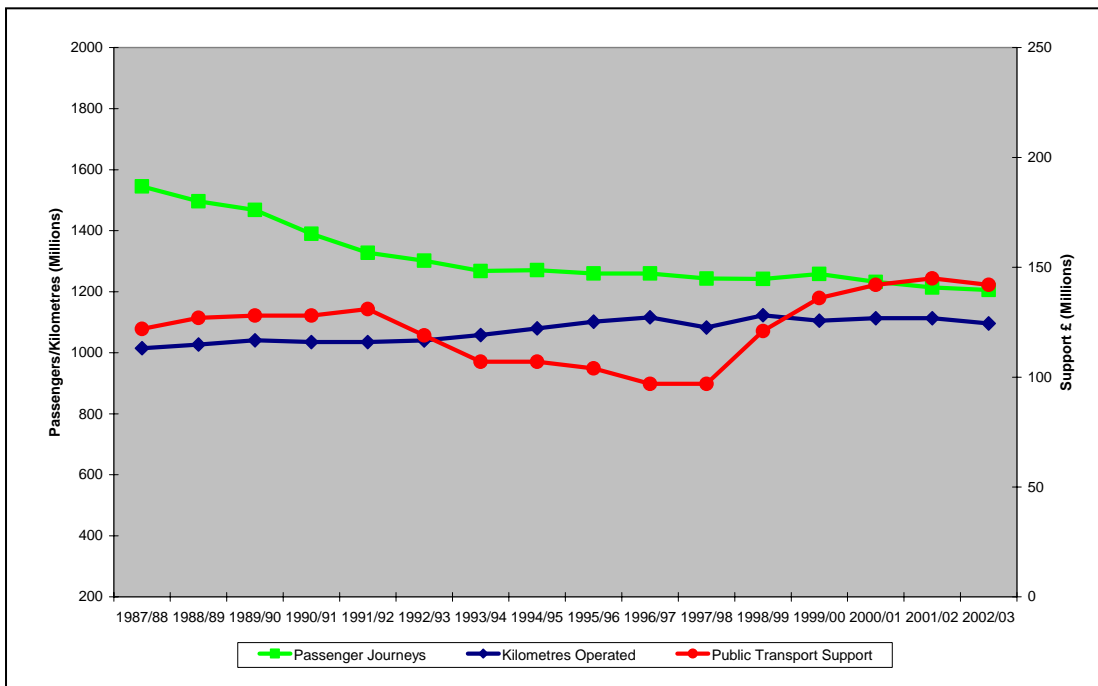


Figure 1.10 – Comparative Indicators 1987/88 – 2002/03: English Shires and Unitaries (2002/03 prices)

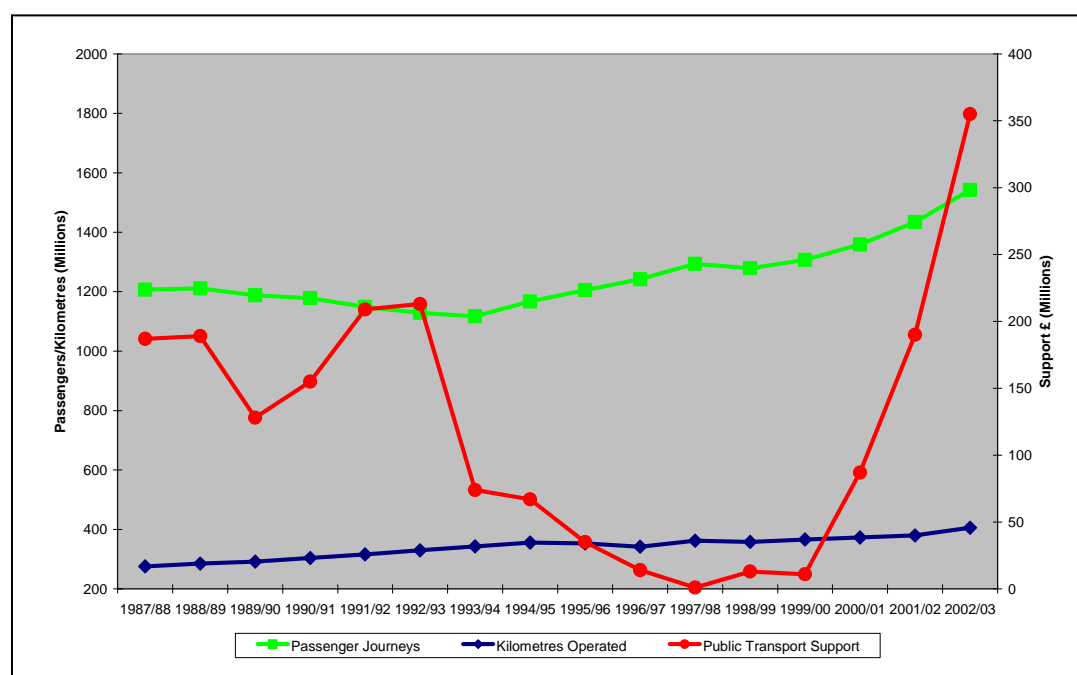


Figure 1.11 – Comparative Indicators 1987/88 – 2002/03: London (2002/03 prices)

- 1.54 The decline in passenger journeys is most pronounced in the metropolitan counties, whilst London shows consistent increases in the last ten years.
- 1.55 Levels of support have risen quite dramatically in London with an increase of 90% comparing 2002/03 with 1987/88. In the metropolitan counties support has actually reduced by 45% whilst the shire counties and unitary authorities show an increase of 16%.
- 1.56 A comparison in support levels between 1981/82 and 2002/03 is, however, interesting. Over that period, support in the metropolitan counties has reduced by 75% and in the shire counties by 24%; the figure for London shows an increase of 22%.
- 1.57 The number of kilometres operated is relatively consistent over the same period in the metropolitan and shire counties, however in London there has been an increase of nearly 50%.

LEGISLATION

- 1.58 The following section provides a brief summary of current legislation relating to the bus industry.

The Legislative Framework

- 1.59 The operation of **local bus services** (see panel for definition) in England is determined by the 1985 Transport Act as amended by the Transport Act 2000. The

provisions of the Act became effective from October 1986 from which date the bus industry in Great Britain¹ is generally referred to as having been "deregulated".

- 1.60 The Act introduced competition into the supply of bus services. Typically, the competition in the supply of bus services brought about by the Act is referred to as "on road" - in that it is based upon operators competing in the open market for passengers with the freedom to operate whatever services they wish, subject to holding an Operators Licence and registering the particulars of services with the relevant area Traffic Commissioner.
- 1.61 Since private sector operators focus on providing services on a strictly commercial basis, provisions exist for **Local Transport Authorities (LTAs)** - see panel for definition - to directly support non-commercial services. The Act places a duty on LTAs to secure the provision of appropriate public passenger transport services to meet public transport requirements where those services would not otherwise be available. These are generally referred to as **secured** or **supported** bus services (see panel for definition).

Key Definitions

- ◆ **Local bus services** are defined in Section 2 of the 1985 Transport Act as:

services where passengers are carried at individual fares and where it is possible to both board and alight within 15 miles.
- ◆ **Local Transport Authorities (LTAs)** (as defined by the Transport Act 2000) refers to those authorities in England (outside Greater London) who have a statutory duty to prepare a Local Transport Plan (LTP) and are required to make an assessment of requirements for supported services and meet the identified requirements. This comprises:
 - County Councils and Unitary Authorities; and
 - Passenger Transport Executives (PTEs) on behalf of Passenger Transport Authorities in Metropolitan Areas.

District Councils can also secure local bus services but they are not required to make an assessment of local requirements². Different rules apply in Scotland, Wales and Northern Ireland. However, many of the elements of good practice may still be applicable.
- ◆ **Secured or supported** bus services are defined as those local bus services procured by local authorities under the 'The Service Subsidy Agreements (Tendering) Regulation 1985 (SI 1921)', 'The Service Subsidy Agreements (Tendering) (Amendments) Regulations 1989 (SI 464)' and The Service Subsidy Agreements (Tendering) (England) (Amendment) Regulations 2004 (SI 609) of the 1985 Transport Act.

- 1.62 The Act also obliges LTAs who wish to subsidise local bus services to go to open competitive tender and to determine which tender to accept solely by reference to what, in their view, is the most cost effective and economic application of the funds

¹ The 1985 Act did not apply to Northern Ireland.

² District/ Borough Councils within PTE areas may not secure services.

available for such subsidies. This ensures that there is "off road" competition for the supply of local bus services when such services are not commercially provided by operators through the mechanism of "on-road" competition. There is, though, the scope to let a restricted number of contracts without the need to competitively tender - the so called *de minimis* provisions. The Transport Act 2000 introduced a duty for LTAs to have regard to the interests of the public and operators when inviting and accepting tenders for subsidised services.³

Bus Industry Structure

- 1.63 The 1985 Transport Act also fundamentally altered the structure of the bus industry and the operators themselves.
- 1.64 The 1985 Transport Act led to the privatisation of both the National Bus Company (NBC) and Scottish Bus Group (SBG), in each case the individual operating units being sold separately. It also saw municipal and PTE operators being put at arms length from the local authority.
- 1.65 Following a number of years of rapid and ongoing change, the industry has tended to consolidate into a number of major groups. These include Arriva, First Group, Go Ahead, National Express and Stagecoach who are all publicly quoted and whose interests include bus and rail operations both in the UK and overseas. The number of municipal (arms-length) companies has reduced to less than twenty. The major groups, as well as some smaller groups including Blazefield Holdings and Yorkshire Traction, provide well over half of all local bus services in Great Britain
- 1.66 Relatively unchanged, however, is the very large number of much smaller operators who continue to provide school buses, many rural services and, in some cases, urban services. In Great Britain, 68 per cent of PSV operators are small fleet operators with five or fewer vehicles.

1998 COMPETITION ACT

- 1.67 The 1998 Competition Act (see panel) has a particular bearing on the provision of supported services in two respects:
- ◆ the requirement it places on authorities' tendering practices to ensure that competition is not inhibited; and
 - ◆ the restriction it places on co-ordination of ticketing and services - though this applies across both the commercial and supported networks.
- 1.68 It is noted that bus operators have taken the Competition Act very seriously and are very wary of breaching any of its provisions. In the context of bidding for supported services many operators seek reassurance from the tendering authority that the contract is not in breach of competition rules.

³ This duty is broader than that originally included in the 1985 act which required LTAs not to inhibit competition between operators as a result of providing service subsidies.

The **1998 Competition Act** specifically prohibits:

- ◆ agreements between undertakings, decisions by associations of undertakings or concerted practices which have the object or effect of preventing, restricting or distorting competition in the United Kingdom; and
- ◆ conduct by one or more undertakings which amount to the abuse of a dominant position in a market in the United Kingdom.

The Act provides a non-exhaustive list of agreements and conduct to which the prohibitions apply and includes:

- ◆ directly or indirectly fixing purchase or selling prices or any other trading conditions; and sharing markets or sources of supply; and
- ◆ sharing markets or sources of supply.

These two have particular relevance to the bus industry in terms of providing a co-ordinated services and ticketing.

- 1.69 The following sub-sections present a summary of the implications of the Act for supported services along with guidance now available from the Office of Fair Trading (OFT).

The Competitive Tendering Process

- 1.70 Ensuring that there is competition in the supply of local bus services is fundamental to the deregulated environment brought about by the 1985 Transport Act as amended by the Transport Act 2000⁴.
- 1.71 LTAs are required to ensure that, by supplementing the commercial network with supported services, the "on-road" competitive market between operators is not distorted or undermined.
- 1.72 Furthermore, authorities are required, through their procurement strategy, to ensure that fair and equitable "off-road" competition for supported service contracts is maintained and encouraged in a manner which aims to achieve best value for money for the budget being spent. As discussed above, the procurement strategy must also be compliant with EU Directives.
- 1.73 Because of the complexities of the Competition Act and the ramifications for LTAs (and operators) if supported services are found to have been specified and procured in breach of the rules, the Transport Act 2000 introduced the "Competition Test".

⁴ The 2000 Transport Act revoked the original requirement of the 1985 Act for authorities to behave "so as not to inhibit competition" when tendering for non-commercial services and replaced it by a duty to have regard to the interests of the public and of operators when making when inviting and accepting tenders for subsidised services (see below). Nevertheless, the interpretation of the requirements of the 1998 Competition Act remains important in letting contracts for supported services.

- 1.74 The OFT has provided guidance⁵ on applying the "Competition Test" to the process of identifying and then procuring supported local bus services in assessing whether would adversely affect competition.
- 1.75 LTAs are encouraged to use the Test themselves to subject proposals for supported services⁶ to scrutiny to see if the conditions apply. Under the new legal exception regime, the OFT does not grant decisions in respect of notifications of proposals. If a proposal passes the Test, then there is no need to inform the OFT. The OFT is available to give advice if LTAs are unsure if their scheme meets the criteria under section 9 of the Competition Act, but the advice is not a decision (i.e. it is not binding on the OFT).

⁵ Guidance on the Competition Test" (OFT393), October 2003 , available at www.of.gov.uk

⁶ The Competition Test was also developed to enable an assessment to be made of statutory Quality Partnerships and Quality Contracts that are included in the Transport Act 2000.

The Competition Test

If a scheme (a proposal for a supported bus service) is considered likely to have an adverse effect on competition it will need to satisfy the **Competition Test**. The Test recognises that even if a scheme has a significantly adverse effect on competition, this may be justified if the scheme produces certain benefits, and is 'proportionate'.

Justification for a scheme exists if it:

- ◆ Secures improvements in the quality of vehicles or facilities used for or in connection with the provision of local services, by, for example:
 - by specifying newer vehicles with wheelchair access or low- or flat-floor buses, providing better access for disabled passengers and passengers with children; or
 - providing bus stops that give electronic real-time information; or
- ◆ Secures other improvements in local services of substantial benefit to users of local services, by, for example:
 - providing more reliable services possibly at greater frequency; or
 - providing greater inter-modal integration of services; or
 - providing journey time savings; or
- ◆ Reduces or limits traffic congestion, noise or air pollution, by, for example:
 - requiring the introduction of vehicles that produce fewer emissions; or
 - achieving increased public transport usage

Where a scheme has or is likely to have a significant adverse effect on competition, but can be justified, the adverse effect on competition must be '**proportionate**' to the achievement of the justification. Where a scheme meets the first or second justification (above), the OFT will adopt a two-stage approach:

- ◆ First, it will balance any benefits to passengers against the detriment to competition. Accordingly, a significantly adverse effect on competition may still be considered proportionate if the benefits produced for passengers outweigh the detriments to competition, so that, overall, passengers or the wider general public are better off;
- ◆ Secondly, it will consider whether those parts of the scheme which result in a significantly adverse effect on competition are necessary to achieve the justification(s).

The OFT is not likely to consider that the elimination of all competition will be proportionate. It is possible that a scheme may meet more than one of the justifications: for example, an improvement in the quality of bus services may also benefit the public at large, by encouraging increased use of public transport, and consequently reducing pollution and improving air quality. Where a scheme meets the third justification, the OFT will assume that the benefits of the scheme to passengers or the public outweigh the detriment to competition, unless there is evidence to the contrary. However, it will still be necessary for an LTA to demonstrate that the restriction is necessary to achieve the third justification.

Local Authority Duties and Responsibilities

- 1.76 With the exception of local authorities being responsible for providing school transport under the 1944 Education Act, it was not until the Local Government Act of 1972 that local authorities were required to 'co-ordinate' the provision of public passenger transport, although that duty had been placed on PTEs under the 1968 Transport Act.
- 1.77 Under the 1985 Transport Act, given that bus services had been deregulated, a duty was placed on PTEs and local authorities to secure the provision of appropriate public passenger transport services to meet public transport requirements where those services would not otherwise be available.
- 1.78 The Act also obliged local authorities who wish to subsidise local bus services to go to open competitive tender and to determine which tender to accept solely by reference to what, in their view, is the most cost effective and economic application of the funds available for such subsidies. There was also a duty not to inhibit competition between operators as a result of providing service subsidies.
- 1.79 The competitive tendering regime for non-commercial services remains unchanged, although the scope of tendering has increased with the provision of specific subsidies such as the Rural Bus Grant.
- 1.80 The 1985 Transport Act was not any more specific in the ways in which determination of 'appropriate public passenger transport services to meet public requirements' might be achieved. It was also not specific in the way in which tendering should be conducted, the result of which is that each local authority tends to operate in a slightly different way. Some local authorities prefer net cost tenders whilst other prefer gross cost tenders; the length of contracts can also vary substantially.
- 1.81 The competitive tendering regime has led to some instability in the supply of bus services. In some cases, operators have sought to 'de-register' a commercial service in the hope that funding for its continuation would be forthcoming. If unsuccessful, however, in securing the contract, they sometimes then indicate their 'willingness' to continue commercial operation or, in other cases, then register a commercial operation in competition with the tendered service. Examples of this practice are, however, becoming less common.
- 1.82 The main result of the introduction of competitive tendering was a substantial reduction in the level of support required for bus services, despite the increased level of operation (see paragraph 10.13). For Great Britain as a whole, the level of support required fell from £1,113 million in 1984/5 to just over £400 million in 1989/90. There have, subsequently, been further dramatic falls although costs are now beginning to rise.
- 1.83 Concessionary fares, typically for the elderly and disabled, have been provided by local authorities for many years, with a rapid expansion of schemes in the early 1970s. The Transport Act 1985 introduced a more consistent approach to operator compensation for participating in schemes, on the basis of revenue foregone, however the powers remained discretionary and, therefore, wide variations existed

and district authorities were not obliged to offer concessions. The cost of local bus concessionary fares schemes has, in real terms, fallen fairly consistently in the last ten years from £516 million in 1990/91 to £443 million in 1999/2000.

- 1.84 The Transport Act 2000 has, however, introduced minimum standards for concessionary fares schemes. In England this comprises a 50% reduction on full standard adult fares for men and women aged 60 and over and the disabled (excluding weekday morning peak periods).
- 1.85 The Act also imposes a number of other duties and responsibilities on local authorities in terms of public transport. It defines authorities which are to be local transport authorities, namely councils of counties and unitary authorities in England, principal councils in Wales and Passenger Transport Authorities (PTAs). It imposes a duty on those authorities to prepare and publish a Local Transport Plan setting out their policies for the promotion of safe, integrated, efficient and economic transport facilities in their area, and to develop a bus strategy for carrying out their bus functions. The Local Transport Plan replaces the Transport Policies and Programmes brought in under the 1972 Local Government Act. A similar regime also exists in Scotland.
- 1.86 An important change brought about by the Transport Act 2000 is the revocation of the requirement for local authorities to behave “so as not to inhibit competition” when tendering for non-commercial services. This is replaced by a duty to have regard to the interests of the public and of operators when making and varying Quality Partnership schemes, ticketing schemes and when inviting and accepting tenders for subsidised services.
- 1.87 Specific details with respect to Quality Bus Partnerships, Quality Contracts and ticketing schemes are also contained within the Transport Act 2000 and these are described more fully in the following sections.
- 1.88 New guidance has also been issued on the **second round of Local Transport Plans (LTP2)**. As noted above the Transport Act 2000 requires all local transport authorities to prepare a Bus Strategy, as part of that authority's LTP. Guidance for LTP2⁷ identifies that the Department considers it essential for the development of a Bus Strategy to be fully integrated within the wider local transport strategy/LTP process, so that LTPs can demonstrate the full contribution of buses to the delivery of better transport outcomes for the 'Shared Priorities' - congestion, pollution, accessibility and road safety. It is noted that LTP2 guidance identifies local bus patronage as a mandatory for performance monitoring.

Quality Bus Partnerships, Quality Contracts and Ticketing Schemes

- 1.89 The concept of Quality Bus Partnerships (QBPs) has been in existence from the mid 1990s and, generally, involves one or more bus operators and one or more local authorities (district, county, unitary, principal councils or PTAs) agreeing a partnership. The operator(s) agree to provide a certain standard of service, usually through the introduction of low-floor buses, whilst the authority agrees to provide

⁷ Full Guidance on Local Transport Plans, Second Edition, Department for Transport, December 2004 available on www.dft.gov.uk

some infrastructure improvement, such as bus priority or improved shelters/waiting arrangements, to assist the operation. Such schemes have been non-statutory.

- 1.90 The Transport Act 2000 allows for statutory schemes, the principal difference being that they would be enforceable at law. The facilities to be provided under a scheme must include facilities at specific locations along bus routes, or prospective bus routes, which bus operators can use. Information facilities, often included as part of non-statutory schemes, may not be included if the authority has already determined that these must be provided throughout their area as part of provisions in the act relating to information provision. Standards may then be imposed upon operators, but these specifically must not include service frequencies or timings.
- 1.91 A statutory scheme requires formal consultation with operators and interested parties and once in operation must remain so for at least five years.
- 1.92 Quality Contracts differ from Quality Partnerships in quite fundamental ways. Sections 124 to 134 of the Transport Act 2000 enable local authorities, either alone or jointly, to make a Quality Contract (QC) scheme provided that they are satisfied that it is the only practicable way to implement their bus strategy or strategies.
- 1.93 Under a QC scheme, the authority will determine what local services should be provided in the area concerned and to what standard. Contracts would then be let with bus operators, granting them exclusive rights to provide services to the authority's specification. The contracts may last for no more than 5 years.
- 1.94 If a QC scheme is implemented, the standard provisions of the 1985 Transport Act would no longer apply. Operators would not be able to register any service wholly within the QC area for commercial operation. For that reason, full consultation is required and a scheme could not come into operation for at least 21 months after it is made.
- 1.95 Sections 135 to 138 of the Transport Act 2000 empower local transport authorities, alone or jointly, to set up ticketing schemes, whereby operators of local bus services are required to make and implement arrangements to accept each other's tickets or provide integrated ticketing in ways specified in the scheme.
- 1.96 In making a scheme, the local transport authority must be satisfied that it is in the public interest and helps to implement the bus strategy.
- 1.97 Some operators are already involved in area-wide ticketing, although as already noted the provisions of the Competition Act have stifled developments, but they cannot be compelled to do so. If a scheme is made, operators will be compelled to participate if they wish to provide local bus services in the area.

RECENT LEGISLATIVE CHANGES

- 1.98 Since the changes contained within The Transport Act 2000, there have been three significant changes in legislation which governs the bus industry. The first change relates to service registrations and the second to Bus Service Operators Grant (formerly Fuel Duty Rebate). The final change relates to *de minimis* service provision.

Service Registrations

- 1.99 As part of the proposals in the 1999 consultation document 'From Workhorse to Thoroughbred: A Better Role for Bus Transport' two important rules have been changed for the registration of local bus services.
- 1.100 The period for registration of a new service or the alteration of an existing service was extended from a 42 to a 56 day period. Reasons for the change include that it allows bus operators less opportunity to make changes to local bus services, which can confuse and deter passengers. Further it allows local authorities more time to provide accurate passenger information.
- 1.101 The other change was to abolish the 'five minute rule' which allowed operators to change the timing of individual buses by up to five minutes either side of the time quoted without informing the Traffic Commissioner.

Bus Service Operators Grant

- 1.102 Eligibility to receive Bus Service Operators Grant has been extended to include a wider range of community transport operators.
- 1.103 The Bus Service Operators Grant (England) Regulations 2002, which came into force on 1st May, set down the range of services operated under a permit under section 19 of the Transport Act 1995 which are newly eligible to receive the grant.
- 1.104 Eligibility to receive the grant has been extended to a range of non profit making community transport services operated in England under a permit under section 19 of the Transport Act 1985. These services do not follow a fixed route and timetable and are for use by particular categories of passengers, rather than the general public.
- 1.105 The regulations provide that the newly eligible services are those used wholly or mainly by:
- ◆ those aged sixty or over;
 - ◆ disabled persons;
 - ◆ those on income support or job seekers allowance; and
 - ◆ those who are socially excluded by reason of unemployment, poverty or other economic factors, homelessness, geographical remoteness, ill health, religious or cultural mores, or who believe it would be unsafe to use other public transport.
- 1.106 Additionally, in February 2004, new regulations were introduced that enable demand responsive and flexible services to also qualify for BSOG⁸. This does have a direct impact on supported services in that it better enables LTAs to replace conventional supported services with flexible services, particularly in rural areas.

⁸ These regulations were amended by the Bus Service Operators' Grant (Amendment) (England) Regulations 2004, Statutory Instrument 2004 No. 9.

PROVISIONS FOR *DE MINIMIS* CONTRACTS

- 1.107 *De Minimis* contracts have played an important role in the tendering process. *De Minimis* rules/exceptions to the Service Subsidy Agreements (Tendering) Regulations enable authorities, under certain circumstances, to let supported services without having to go through competitive tender.
- 1.108 The rules governing *De Minimis* contracts have been amended on a number of occasions, most recently by the Service Subsidy Agreements (Tendering) (England) Regulations 2004⁹ which came into force on 1st April 2004. Detailed guidance on the application and interpretation of the rules is available on the DfT's website¹⁰.

⁹ http://www.dft.gov.uk/stellant/groups/dft_localtrans/documents/page/dft_localtrans_028602.hcsp

¹⁰ www.dft.gov.uk

2. Study Objectives and Methodology

OBJECTIVES OF THE RESEARCH

- 2.1 The overarching objective of the research was to improve the understanding of the reasons for changes in the prices of supported local bus services. The research was required to be more broad-based and to determine not only the explicit reasons for change, but also the underlying and determinant factors.
- 2.2 The findings have informed the development of Good Practice Guidance for tendering authorities to ensure best value in their procurement of non-commercial bus services.
- 2.3 Specific objectives of the research included:
- ◆ Monitoring of all English local authority tender prices and number of bids per contract over a three year period between 2001 and 2003;
 - ◆ Highlighting of trends in tender prices;
 - ◆ The determination of explicit reasons for any changes in tender prices and further analysis through case studies to understand the underlying changes in the market;
 - ◆ Monitoring of local authority responses to changes in the tendered bus service market;
 - ◆ Analysis of local authority criteria used to determine the costs and benefits of individual bids including contractual requirements;
 - ◆ Reporting on the objectives being pursued by local authorities in determining their tendered network and how this fits with other public transport policies, strategies and expenditures;
 - ◆ Monitoring the reaction of operators to the changing market;
 - ◆ Analysis of changes to local authority budgets and expenditures;
 - ◆ Determining the impact of best value reviews and the level to which local authorities are pursuing cross-cutting analysis; and
 - ◆ Analysis of the ongoing commercial changes to local bus service networks and the responses of local authorities and other operators.

STUDY METHODOLOGY

- 2.4 Given that there are a large number of local authorities involved in tendering for local bus services and a much larger number of individual operators bidding for the various contracts, the data collection exercise has been a challenge.
- 2.5 Our intention, throughout, has been that the data collection be achieved through close co-operation with the tendering authorities, the bus operators as well as other interested parties including the Association of Transport Co-ordinating Officers (ATCO), the Commission for Integrated Transport (CfIT) and the Audit Commission.

- 2.6 The level of co-operation received was not as high as had been anticipated; however, a significant amount of information has been received.
- 2.7 In order to consider all relevant tenders and all relevant issues, the starting point was to build a database in which records could be maintained of all local bus tenders for the 87 English tendering authorities. The overall intention was to keep the database as simple as possible to allow continued and timely updating as well as rapid analysis at high and low levels.
- 2.8 Source data included the following:
- ◆ Tendering authorities' tender documents;
 - ◆ Tendering authorities' tender policies and procedures;
 - ◆ The local authority bus strategy (within the Local Transport Plan);
 - ◆ Atkins and ATCO commissioned surveys;
 - ◆ Local authority and operator detailed interviews;
 - ◆ Trade press; and
 - ◆ Traffic Area 'Notices and Proceeding' to provide a useful back-up to monitor changes to bus services.

Ensuring 'Like for Like' Comparisons

- 2.9 In order that 'like-for-like' comparisons can be made some measure of resource requirements has been necessary. Where the tendering authority did not provide any indication of resources, it was necessary to use a proxy measure, in most cases an approximation of the 'bus hours' required – that is, the number of hours an operator would need to consider for costing purposes to operate the contract as specified.
- 2.10 A further level of analysis in the database, therefore, considers either:
- ◆ Miles/kilometres;
 - ◆ Bus hours; or
 - ◆ Some other proxy measure or estimate where neither of the above is available.

DATA COLLECTION

- 2.11 The volume of data required meant that it was necessary to visit individual authorities in order to collect data on all existing tenders, as well as those pre-existing such that ongoing comparisons could take place.
- 2.12 In order to keep the database up to date the various authorities were asked to include Atkins on their circulation list for new tenders and to inform us of the details of the contract if and when the tender was let.
- 2.13 Visits were arranged to a number of authorities to collect data on existing, and expired contracts where appropriate. A number of authorities sent details of their existing contracts by post, which was very helpful in the data collection process.

- 2.14 Not all information was available for all contracts but where possible the following information was acquired:
- ◆ Copy of contract timetable;
 - ◆ Cost of contract (existing and when contract let);
 - ◆ Type of contract (e.g. cost or subsidy);
 - ◆ Date of commencement and expected expiry of contracts;
 - ◆ Vehicle specification details (size and type – low floor etc);
 - ◆ Mileage and/or operating hour details per contract;
 - ◆ Details of bids received;
 - ◆ Details of previous contract if appropriate (including price).
- 2.15 In addition a copy of the Conditions of Contract and Bus Strategy was acquired whenever possible.
- 2.16 The initial intention had been that the database would hold at least an 85% sample of all contracts. In the event, however, the database holds a sample of around 40% of all contracts. This figure is likely to be representative and provides a good spread of authority types across the various regions.

DATABASE

- 2.17 A database has been compiled for all contract and new tenders for which data was obtained.
- 2.18 The information contained in the data base is as detailed below:
- ◆ Contract number;
 - ◆ Start and finish date;
 - ◆ Annual hours and annual miles;
 - ◆ Vehicle size;
 - ◆ Contract type;
 - ◆ Price when awarded and current price of the contract being replaced;
 - ◆ Package or single bid;
 - ◆ Operator;
 - ◆ Days of operation;
 - ◆ Service type;
 - ◆ Number of bids;
 - ◆ Highest, middle and lowest bids;
 - ◆ Successful operator; and
 - ◆ Whether or not the contract was let.

LOCAL AUTHORITY SURVEY

- 2.19 A Local Authority survey similar to the annual survey undertaken by ATCO was undertaken in both 2002 and 2003. Responses to this were poor with less than 50% of authorities responding. Many authorities commented that they had insufficient resources to complete the surveys and that those resources that were available were better employed in the tendering process itself.
- 2.20 There was some understandable frustration on the part of the Local Authorities at the time period for the Atkins and ATCO survey being different. However, as the ATCO survey covers a period from October to September and our project requires reporting in a financial year this was considered necessary.

CASE STUDIES

- 2.21 In order to better understand particular aspects of the tendering process under different local circumstances a number of case studies were undertaken.
- 2.22 Case study findings informed the development of good practice guidance and are reported separately.

3. Trends in Prices and Bids

3.1 In this section the results of the research undertaken with the co-operation of the various local authorities and the questionnaire returns are described.

TRENDS IN LOCAL BUS TENDER PRICES

3.2 The tables below provide details of average changes in tender prices, regardless of contract length and, therefore, nominal, based on the following:

- ◆ Analysis of the bus tender database (as described in Chapter 2) for tenders let in the financial years 2000/2001, 2001/02 and 2002/03;
- ◆ Analysis of responses to the Atkins local authority questionnaire survey for the financial years 2001/2002 and 2002/03; and
- ◆ Analysis from the ATCO local authority questionnaire survey for the years 1998 - 2003.

Table 3.1 – Trends in Local Bus Tender Prices: Bus Tenders Database

	2000/01	2001/02	2002/03
Percentage Change in cost of supported bus services awarded through tender in a given year relative to the previous year according to the price per annual timetabled hour ¹¹	9%	11%	13%
All Authorities			
Percentage Change in Price for 'Like for Like' Local Bus Tenders ¹²	16%	18%	(a)
All Authorities			

Table Notes: (a) Insufficient data

¹¹ Analysis achieved by comparing change in cost of bus tenders awarded in target year with those awarded in the previous year, using cost per annual bus hour operated as the indicator of tender price. Cost per annual bus hour is defined as the annual tender price on award divided by the estimated number of timetabled hours operated by a tendered service in a year.

¹² Analysis of 'Like for Like' achieved by comparing change in cost of bus tenders awarded in the target year against the current price of the tender being replaced. This analysis compares only those contracts in the database that have been replaced by identical or similar contracts. It compares the price on tender award with the price immediately prior to award (the "current price").

Table 3.2 – Trends in Local Bus Tender Prices: Local Authority Questionnaire Surveys

Percentage Change in Price for 'Like for Like' Local Bus Tenders ¹³								
	Atkins (a)	Atkins (a)	ATCO (b)	ATCO (b)	ATCO (b)	ATCO (b)	ATCO (b)	ATCO (b)
	2001/02	2002/03	1998	1999	2000	2001	2002	2003
Shire Counties	25.2%	15.0%	16.3%	16.1%	17.8%	23.2%	20.8%	16.4%
Metropolitan Areas	(c)	(c)	9.0%	8.1%	7.7%	10.5%	(c)	11.4%
Unitary Authorities	5.7%	15.3%	2.4%	18.3%	13.4%	23.9%	15.1%	8.2%
All Authorities (d)	18.5%	18.6%	11.8%	17.0%	16.7%	20.9%	19.6%	15.0%
Annual increase in Retail Price Index ¹⁴	1.8%	2.7%	n/a	n/a	n/a	n/a	n/a	n/a
Inflation (RPI) over preceding 4 years	9.5%	9.9%	n/a	n/a	n/a	n/a	n/a	n/a

Table Notes: (a) Relates to financial year April - March inclusive

(b) ATCO Price, Expenditure and Competition Survey 2003. Relates to October-September period inclusive - the year quoted defines the year the survey was undertaken, thus 2000 relates to the period October 1999 to September 2000.

(c) Sample size insufficient

(d) ATCO survey results for all authorities include Welsh and Scottish councils

3.3 The analysis of data from the database of bus tender information is constrained by the ability to make genuine 'like for like' comparisons. The first of the analyses shown in Table 3.1 looks, for contracts awarded in a given year, at how the cost of purchasing a unit of bus service provision - an annual timetabled bus hour – has changed from contracts awarded the previous year. It will therefore combine the effect of procuring new or differently specified services as well as the replacement of existing tenders.

3.4 The second analysis method shown in Table 3.1 compares the new tender award price with the current price - i.e. the price of the contract immediately prior to being re-awarded¹⁵. In principle this gives a better 'like for like' comparison. It is noted that the analysis is affected by changes in tender specification that may have been introduced when the new contract was awarded. In analysing the information, however, those tenders known to be different on new award have been excluded. However, obtaining the detailed information on such changes was difficult and, as a result, the changes reported may understate or overstate the actual tender price increases.

¹³ The Atkins survey asked authorities to provide information on local bus contracts that had been renewed in the financial year in question.

¹⁴ Source: Office of National Statistics: CHMK, All items excluding mortgage interest payments

¹⁵ In the majority of cases the current price is the award price plus any inflationary increases awarded over the life of the contract.

- 3.5 The questionnaire survey data specifically focuses on replacement of existing contracts and is, to a degree, also a 'like for like' comparison. However, it is considered likely that respondents will not always have explicitly excluded contracts where changes in specification have occurred on re-tendering. It may also be likely that respondents did not factor in any in-built inflation adjustments included in existing contracts when comparing with replacement contracts. On balance it is considered that the survey responses could slightly overstate the change in tender prices.
- 3.6 Table 3.3 gives a breakdown of average tender duration, derived from the database.

Table 3.3 – Local Bus Tender Contract Lengths

Length of Contract	% of Contracts in Sample
Up to 12 months	4%
13-24 months	15%
25-36 months	14%
37-48 months	35%
> 48 months	33%

- 3.7 The contracts will have been previously let at some point within the last five years - the average from Table 3.3 is 3.9 years. The prices of a tender being renewed after a period of 3-5 years will therefore be likely to reflect inflation over the previous contract period.
- 3.8 Whilst there are variations in the findings from the three data sources the evidence the evidence clearly shows that bus tender prices have been increasing at a rate significantly greater than the Retail Price Index (RPI).
- 3.9 The variability in the survey data given the sample sizes and, particularly, the limited amount of time series data means that is difficult to draw firm conclusions on trends. The database and survey information suggest that price increases over the last four or so years have been running at between 15% and 20% for 'like for like' service replacements. While the latest ATCO (2003) figures seem to suggest that price increases are now declining, there is insufficient data available to identify this as a trend.

KEY DETERMINANTS

- 3.10 The overall figures and those for the different authority types do mask significant variations both between authorities and between contracts in individual authorities.

Variations by Contract Type

- 3.11 Table 3.4 presents results from the bus tender database, looking at the change in tender prices according to the price of procuring an annual timetabled bus hour through newly let contracts in a particular year. The table also shows the different proportions of minimum cost and minimum subsidy contracts.

Table 3.4 – Breakdown by Tender Type

Tender type	99/00	00/01	01/02	02/03
Minimum cost - increase in tender price	-	8%	7%	21%
Minimum subsidy - increase in tender price	-	2%	-1%	0%
Contract type not known	-	31%	17%	10%
Increase – all contract types	-	9%	11%	13%
Minimum cost % of all minimum cost and minimum subsidy contracts	78%	85%	72%	69%

- 3.12 This suggest that price rises for Minimum Costs contracts have been greater than those for Minimum Subsidy contracts. This conclusion is backed up when the tender database is examined on a true 'like-for-like' tender replacement basis, though sample sizes are smaller.
- 3.13 Drawing conclusions from the analysis of contract type is complicated by the treatment of revenue. In minimum subsidy contracts the revenue is taken by the operator; in minimum cost contracts revenue is taken by the local authority. Thus, changes in revenues need also to be taken into account in assessing the trends in minimum cost contracts. Given that in many areas revenues have been either constant or declining (due to falling patronage) it would be reasonable to conclude that the net effect on local authorities of minimum cost contracts is an above inflation cost increase. For minimum subsidy contracts – though recognising the smaller sample size on which the trend is based – the evidence suggest that price rises have been less.
- 3.14 Analysis of the number of bids received for each of the two contract types is shown in Table 3.5.

Table 3.5 – Trends in the number of bids received by Tender Type

Tender Type	99/00	00/01	01/02	02/03
Minimum Cost	3.1	3.1	2.8	2.7
Minimum Subsidy	3.7	3.5	3.3	5.0

- 3.15 This suggests that more bids are received for minimum subsidy tenders than for minimum cost. It is also noted that minimum subsidy contracts tend to be let in urban

areas where services are more likely to be closer to being commercial and where operators have greater potential to increase revenue and support their commercial networks than in rural areas. This could be expected to influence price increases.

- 3.16 The evidence also suggests that the trends in price changes are dependant upon whether the contract is for a whole service, an infill to an existing commercial service, or for other journeys.¹⁶ As with the majority of tenders, there are wide variations between the price changes. Table 3.6 below summarises the evidence from the database.

Table 3.6 – Breakdown by Service Type

Service type	00/01	01/02	02/03
Complete service	5.5%	6.6%	-4.5%
Infill service	(a)	63%	50%
Various other journeys	21%	5%	-13%

Table Notes: (a) insufficient data

- 3.17 Overall there appears to be evidence that the price increases have been lower for whole service contracts where the operator has an element of ‘control’ over the product. There is also evidence that price increases for single journeys are also lower than average, often because the particular journey ‘fits’ with the operator’s schedules and loss of the contract would not yield a significant operating cost reduction. The highest price increases appear to be for infills. It is also noted that the number of bids received for tenders is highest for complete services. Over all years the average number of bids for complete service contracts is 3.5. For infill services it is only 2.9, whereas for various other journeys it is 2.6. In general, it would appear that cost increase pressures are less severe on tenders for complete services.

Variations by Contract Length or Size

- 3.18 The tenders and contracts reviewed include short length, less than one year contracts (often for seasonal services or in the case of emergency), as well as those for one, two, three, four, or five years duration. Most local authorities have policies of letting contracts for between three and five years, although in many cases ongoing commercial deregistrations have significantly impacted upon the tender programme resulting in ‘non-standard’ contract lengths.
- 3.19 Analysis of the tender database suggests that the lowest annual equivalent price increases have been experienced on contracts let for 3 or 4 years. The highest annual equivalent price increases tend to be for 2-year and 5-year contracts.
- 3.20 In terms of the size of contracts, some of the highest percentage increases are found on small contracts of up to £20k per annum value, although the overall effect on a local authority’s budget is consequently relatively small. However, whilst increases in

¹⁶ Infill journeys are defined as journeys operated with support on a commercial service. Other journeys are a contract is made up of journeys from more than one service.

excess of 20% are very few on contract values above £100k per annum, there are isolated examples. Between the range £20k to £100k per annum contract value, the variations are little different at any point on the scale.

Variations by Time of Day and Day of Week

- 3.21 Analysis has been carried out on the trends in tender prices where contracts are for specific times of the day or on different days of the week. In some cases, often on larger contracts, local authorities tender separately for evenings, Saturdays and Sundays, although the individual tenders may form part of a comprehensive batch.
- 3.22 There had been a preconception that annual equivalent price increases for evenings and weekends might be rather higher than for other times of the day or week, particularly given the increasing difficulty in the recruitment of staff willing and available to work 'unsocial hours'. The evidence shown in Table 3.7 (from the database) suggests that the lowest price increases occur on all day services - whereas highest price increases occur on early evening, early morning and peak journeys. In the case of peak hour services the operator requires a bus in the fleet to undertake the journeys in question. It is likely therefore that such contracts will carry a full share of overhead costs, whilst marginal costing principles might be applied to contracts which do not require a peak vehicle.

Table 3.7 – Breakdown by Service Time of Day

Service type	00/01	01/02	02/03
All day	5.0%	0.1%	-8.0%
Evening	8.5%	38.4%	(a)
Interpeak	-4.4%	5.2%	(a)
Early morning	17.2%	27.0%	(a)
Peak	4.5%	19.2%	11.1%

Table Notes: (a) insufficient data

TRENDS IN THE NUMBER OF BIDS

- 3.23 Table 3.8 presents an analysis from the bus tender database of the number of bids received for invitations to tender for supported services.
- 3.24 Over the period considered, the average number of bids received for local bus service tenders in England, excluding London, has remained broadly constant. It is emphasised that the database represents bus tenders that have been let and therefore excludes from the calculation of the average those that have not been let because no tenders have been received. The changes between authority types and years are, overall, marginal and not statistically different given the variability in the data. There is no evidence to suggest that the reduced number of bids has led to any variation in the rate of increase in tender prices.

Table 3.8 – Trends in the Number of Bids Received for Local Bus Tenders - Bus Tender Database

Authority Type	99/00	00/01	01/02	02/03
Shire Counties	3.2	3.6	3.0	3.5
Metropolitan Areas	3.2	3.1	3.1	3.1
Unitary Authorities	2.5	2.9	2.3	2.4
Total	3.2	3.2	3.0	3.0

3.25 Information on number of tenders received is also available from the local authority questionnaire surveys, though noting that this includes, in the calculation, the average where no bids are received. This is shown in Table 3.9. This broadly confirms the analysis from the database.

Table 3.9 – Trends in Local Bus Tender Prices: Local Authority Questionnaire Surveys

	Average Number of Tenders Received per Contract						
	Atkins (a) 2001/02	Atkins (a) 2002/03	ATCO (b) 1999	ATCO (b) 2000	ATCO (b) 2001	ATCO (b) 2002	ATCO (b) 2003
Shire Counties	2.6	3.0	3.1	2.9	3.0	3.2	3.0
Metropolitan Areas	(c)	(c)	2.3	2.5	3.1	(c)	2.6
Unitary Authorities	2.3	2.4	2.7	3.0	2.8	2.6	2.8
All Authorities (d)	2.4	2.7	3.1	2.9	2.9	3.0	2.8

Table Notes: (a) Relates to financial year April - March inclusive

(b) ATCO Price, Expenditure and Competition Survey 2003. Relates to October-September period inclusive - the year quoted defines the year the survey was undertaken, thus 2000 relates to the period October 1999 to September 2000.

(c) Sample size insufficient

(d) ATCO survey results for all authorities include Welsh and Scottish councils

3.26 The evidence suggests that the number of bids received in Metropolitan areas, as compared to Shire counties is rather lower primarily because a larger percentage of tenders, given the overall size of the contracts, receive only one bid.

Regional Variations

3.27 Initial research suggested that there were no significant regional variations in the numbers of bids received. Both the questionnaire and our own research, however, now indicates that the number of bids received in the south east is significantly lower than for England as a whole in the shire counties. The figure for unitary authorities is similar and, indeed, slightly higher than for England as a whole.

- 3.28 Available evidence, however, suggests that factors other than lower levels of competition for contracts, are leading to higher than average price rises in the south east.

Variations by Contract Type

- 3.29 Evidence, both for England as a whole and specifically in the south east, suggests there are no significant variations by contract type, with the obvious exception of ‘*de-minimis*’ contracts which, by their very nature, are not subject to competitive tender.
- 3.30 The change in rules with respect to ‘*de-minimis*’ contracts is likely to see an increase in their numbers. Overall, the proportion of contracts let as ‘*de-minimis*’ is similar in the south east as compared to England as a whole. This is both in terms of the number of contracts and the vehicle kilometres operated.
- 3.31 A comparison of the percentage of all contracts that were let as ‘*de-minimis*’, is shown in Table 5.10.

Table 3.10 – Percentage of ‘De-Minimis’ Contracts

	Atkins (a) 2001/02	Atkins (a) 2002/03
Shire Counties	22%	21%
Metropolitan Areas	(b)	(b)
Unitary Authorities	28%	25%
All Authorities	25%	22%

Table Notes: (a) Relates to financial year April - March inclusive

(b) Sample size insufficient

- 3.32 In England as a whole the early research suggested that there are slightly more bids for RBSG tenders than for more conventional local bus tenders. We have not continued this area of the research in detail, however that trend appears still to be present. This appears to be because many RBSG contracts require fewer vehicles and, therefore, smaller operators are able to submit bids. By complete contrast, however, in the south-east there are rather fewer bids for RBSG contracts. Initial indications suggest that because the larger operators suffer comparatively greater staff recruitment and retention difficulties than elsewhere, they are less likely to bid for ‘non-core’ work. There are also, compared to elsewhere in England, rather fewer smaller operators and, therefore, the number of bids is reduced. The number of bids for RBSG contracts in the financial year 2001/02 is shown in Table 3.11.

Table 3.11 – Trends in the Number of Bids Received for RBSG Services

	Atkins(a) 2001/02	Atkins(a) 2002/03
Shire Counties	2.9	2.7
Metropolitan Areas	(b)	(b)
Unitary Authorities	2.4	2.3
All Authorities	2.7	2.5

Table Notes: (a) Relates to financial year April - March inclusive
(b) Sample size insufficient

Variations by Contract Length or Size

- 3.33 We have found no significant variations in the actual numbers of bids received depending on the length of the contract specified.
- 3.34 There are, however, variations in the numbers of bids received when considering the contract size. Large contracts, in excess of £100k value per annum tend to receive fewer bids than smaller contracts, doubtless because of the level of resources required for larger contracts such that smaller operators may not feel able to bid. The risk element on larger contracts may also be a deterrent to smaller operators.

Variations by Time of Day and Day of Week

- 3.35 In England as a whole there appears to be no particular difference in the numbers of bids received for tenders depending on the time of day or the day of the week.
- 3.36 In the south east, however, there is some evidence that a number of operators tend not to bid for tenders that involve operations, largely or only, outside of the weekday daytime period. The contrast with the rest of the country is probably because of the greater staff recruitment and retention difficulties encountered in the south east. A number of smaller operators are using the 'no shift or Sunday work necessary' message as an incentive for new recruits.
- 3.37 Some operators have said that their decision on whether or not to bid for work at 'unsociable' times depends on the proportion of that work they are currently engaged in since they wish to maintain a 'balance' in the staff roster in order to make jobs attractive to new recruits and to retain existing staff.
- 3.38 It is noted that a number of local authorities let separate contracts for early morning journeys as well as evening and Sunday services. In some cases they may be let at a different time to the daytime element of services. This practice may deter some operators from making a bid since the roster balance might be lost.

THE EFFECT OF COMMERCIAL WITHDRAWALS AND EARLY TERMINATION OF CONTRACTS

- 3.39 In the last two to three years, whilst the overall mileage operated has been stable and, in some cases, even seen increases, there have been some fairly substantial commercial service withdrawals.

- 3.40 The reasons for operators making commercial withdrawals are varied, but the following factors are particularly important:
- ◆ Staff shortages (sometime leading to temporary withdrawals, as in the case of Reading for example);
 - ◆ Increased resource requirements on core routes (often urban or inter-urban) because of increased congestion and the introduction of more rigorous operating standards by the Traffic Commissioner;
 - ◆ Increased resource requirements on core routes because of increased frequencies, sometimes as a result of Quality Partnerships;
 - ◆ Reduced passenger numbers and, therefore, revenues;
 - ◆ Financial pressures because of increasing driver and other staff wages; and
 - ◆ Lack of capital investment leading to some vehicles not being replaced at the end of their useful life.
- 3.41 Commercial service withdrawals have an obvious impact on local authority budgets for revenue support. The questionnaire circulated to local authorities for the financial year 2001/02 specifically requested details of the impact of commercial withdrawals. The net extra cost of providing replacement services totalled £2.2 million for the Local Authorities who responded (40%). In broad terms this translates to some £6 million per annum for England as a whole. In addition, a net extra cost of £1.3 million is reported for replacement contracts let on early termination by the incumbent operator, suggesting, again in broad terms, an additional cost of over £3 million per annum across England.
- 3.42 In many cases, withdrawn commercial facilities are not replaced on a like-for-like basis. If alternative facilities are available within a reasonable distance, the withdrawn services are generally not replaced. Where no alternative facilities are available either reduced frequencies are provided or 'de-minimis' arrangements entered into to divert other commercial facilities.
- 3.43 The net extra cost of commercial withdrawals represents around 4.5% of the total expenditure in the south east for 2001/02. This compares to around 3.4% of the total considering England as a whole. Should the authority choose to continue to support these services then that additional cost is ongoing.
- 3.44 Around half of authorities in the south east, a similar proportion to England as a whole, reported that cuts in existing tendered services have been necessary to meet budgets. Often the cuts are to journeys running outside of the core operating hours of 0800 to 1800, inevitably leading to a deterioration in the overall quality of the network of services.
- 3.45 In those south east authorities responding to the survey, a total of some 7,400 commercial journeys had been withdrawn per week. On a similar gross-up, the indications are that 15,000 or more commercial journeys were withdrawn in the year 2001/02.
- 3.46 The survey for the financial year 2002/03 was less specific in this respect but the majority of responding authorities indicated that the level of commercial withdrawal in that year, whilst still significant, was at a lesser scale. The survey was not repeated

for the financial year 2003/04, however indications are again that the level of commercial withdrawal has, in the majority of cases, lessened.

- 3.47 There have, however, recently been indications that in certain areas, particularly rural areas, further increasing cost pressures are leading to more large-scale retrenchion of networks. The implications of this on bus strategies and LTPs cannot be underestimated.
- 3.48 It is clear that the south east has suffered more commercial withdrawals than any other region. Other authorities surrounding London (in the eastern region) have also suffered large commercial withdrawals.

4. Analysis of Trends

- 4.1 This section provides some generic analysis of the reasons for the recent trends in tender prices and the number of bids received. It follows on from feedback received from operators and local authorities. In this respect, the Confederation of Passenger Transport (CPT) and the individual operators themselves have been especially helpful.
- 4.2 The section is divided into operator issues; contract and local authority issues; competition issues and regulatory issues.

OPERATOR ISSUES

- 4.3 Contact with operators has suggested that the following issues have emerged as determinants in the level of price increase:
- ◆ Pressure on bus operator margins;
 - ◆ Above-inflation wage increases for driving staff;
 - ◆ Driver shortages;
 - ◆ Increased and increasing insurance costs;
 - ◆ Fuel prices;
 - ◆ Increasing congestion, exacerbated by increased Traffic Commissioner attention to reliability;
 - ◆ Increased accidental damage costs on low-floor vehicles;
 - ◆ Increased levels of vandalism, particularly glass etching;
 - ◆ The need to 'catch up' on lost ground; and
 - ◆ Contractual issues.

Bus Operator Margins

- 4.4 It has already been noted that whilst operating costs have only in the last two years started to show increases following many years of quite substantial reductions, bus fares have risen consistently above the general level of inflation suggesting higher profit levels for operators. It is also apparent that overall subsidies and subsidy per kilometre started to increase prior to any discernible increase in costs. Overall this would tend to suggest that bus operators have, for a period at least, sought higher returns and operating margins in their businesses, doubtless because of City pressures.
- 4.5 Indeed, it would be widely recognised that the major groups scored considerable success in the early and mid 1990s in driving down costs, improving revenues and, therefore, achieving higher margins.
- 4.6 Most recently available information from the major bus groups has continued to suggest that operating margins are under pressure. Those for the largest five groups are shown below in figure 4.1.

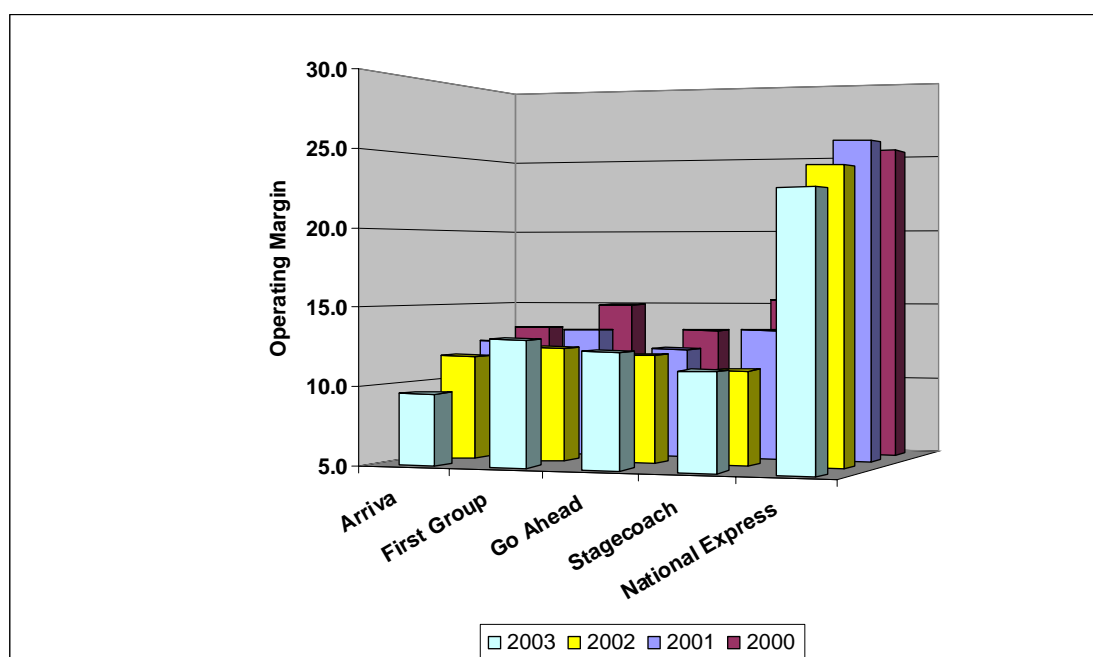


Figure 4.1 – Major Bus Group Operating Margins (%)

- 4.7 All of the five groups have, generally, seen margins reduce year on year between 1999 and 2003 and this follows a number of years of improving margins for most. National Express with limited bus operations across the country, although the major operator in the West Midlands metropolitan area, continues to enjoy the highest margins. First Group, Go Ahead and Stagecoach managed to reverse the trend, slightly, reporting improved margins for 2003.
- 4.8 There are, of course, numerous reasons for margins to be affected, but the fact that the majority of the major groups have suffered similar fortunes does tend to suggest both cost and revenue pressures and it is in the past 3-4 years that those pressures have been passed to the local authorities in terms of increased tender prices.
- 4.9 It is likely that there are time lags between the initial advent of cost pressures and the realisation that the trend is set to continue such that increased prices have to be passed to the customer. It is, therefore, likely that operators have included an element of 'catch up' in their tender pricing to make good previous losses or sub-standard returns. This is not to say that operators have endeavoured to make 'super' profits on contracts, but rather that they have been more realistic in tender pricing. One operator quoted the term '*margin refreshment*' which also includes a 'buffer' to cover for the uncertainty over the life of the contract. Doubtless the 'once bitten twice shy' attitude will be adopted by many operators.

Wage Levels

- 4.10 Quite clearly the most significant cost, driver wage levels for bus staff are increasing well above the general levels of inflation and other wage increases.
- 4.11 National statistics suggest that hourly wage rates for drivers in Great Britain increased by 5% between 2001 and 2002. Feedback from the bus industry suggests

that current wages settlements are running at levels well above this. In some areas, some settlements during 2003 and, indeed, previous years, have been up to 20%.

- 4.12 The major groups have co-operated in this research by providing details of percentage wage increases. Commercial confidentiality needs to be maintained, however we can report that one of the major groups in the south east has seen drivers' pay increases of 8.5% in 2002, compared to 4-5% in operations outside of the south east. Another operator saw wage levels increase by 11% in a 12 month period; this settlement was concluded in order to attract sufficient driver numbers and was based on the recognition of the local 'market rate' for similar employment.
- 4.13 Since drivers' pay often represents around 60% of total costs, a 10% pay increase in one year will impact total costs by well over 5%. In certain areas, particularly those where the public transport market is buoyant (usually urban areas), the business can adapt and commercial operations can be maintained. In other areas, however, marginal or even profitable commercial operations quickly become non-commercial.
- 4.14 Whilst drivers' pay rates have had the greatest impact on overall costs of operation there have also been above-inflation settlements for other grades of staff.
- 4.15 Many smaller operators have, traditionally, relied upon part-time staff to cover peak only operations, often provided directly or indirectly for schools. It is suggested that rates for part-time staff have risen by even higher levels than full-time staff, generally because there are increasing part-time opportunities in businesses such as retail (particularly with the trend to longer hours or 24-hour opening). Tender prices for peak-only operations and schools services, therefore, have risen dramatically.
- 4.16 It is likely that the pressure on drivers wages will continue over the next few years since, whilst compared to other occupations there has been some 'catching up', particularly in the south east, bus drivers wages are, on average, only around 60% of those for all occupations.
- 4.17 Bus drivers tend to be categorised as 'non-skilled' or 'manual' workers; however, even amongst other occupations in this category, drivers' wages have been lagging behind the national trend and it is often the case that other 'unskilled' trades receive supplements for overtime and unsocial hours, something becoming more common in the bus industry, but still far from the norm.

Driver Shortages

- 4.18 Our analysis suggests that the average shortage of drivers on establishment across England is around 10%, although there are significant regional variations. Given this shortage, and combined with other pressures, operators are unwilling to consider bids for tenders outside of their 'core' operations.
- 4.19 Research undertaken as part of the Thames Valley Multi Modal Study suggests that:
- ◆ High employment in the South East places pressure on operators which result in services being withdrawn and/or fares increases;
 - ◆ Acute staff shortages have resulted in emergency timetables being introduced in Basingstoke (October 2000 – April 2001) and Reading (November 2000);

- ◆ Reading Buses have been experiencing staff shortages in excess of 13%; and
 - ◆ Scheduled bus kilometres fell by 9% in the Bracknell Forest area due to acute problems of recruitment and retention.
- 4.20 The Oxford Bus Company was forced to reduce frequencies around 18 months ago because of acute driver shortages; they have, however, restored around half of the frequency and intend to restore the remainder as soon as they are able.
- 4.21 As noted above, this same operator has improved the staffing situation through a recognition that the local 'market rate' has to be paid. The increased costs associated with this, however, are ultimately passed to the customer be it the individual passenger paying an individual fare or the local authority as purchaser of non-commercial services.
- 4.22 Additional demand for drivers which is being seen in many areas, will, inevitably, maintain the pressure on wage levels, operating costs and, therefore, tender prices.

Insurance Costs

- 4.23 In common with the rest of the insurance market, that for buses has seen substantial cost increases over the past two years and the events of September 11th 2001 in the United States led to further cost pressures in this area.
- 4.24 A further reason for increasing insurance costs is the ever more litigious nature of society. Accidents on board buses and with other vehicles are not, in themselves, increasing in numbers, however the number of claims being made is very much higher.
- 4.25 Many operators are looking at insurance premiums up to 30% higher than twelve months ago. Even though insurance represents much less than 5% of total costs, such increases are still significant and will, inevitably, impact upon tender prices.

Fuel

- 4.26 Fuel prices, until the recent 3 months, had fallen both in actual and real terms in the previous eighteen months. The situation is, however, complicated by the fact that many of the major groups have complex hedging arrangements for their fuel purchases. On the positive side, however, this also means that recent increases are unlikely to have a major impact on the overall cost base of operators.
- 4.27 The fuel consumption of new buses is often much greater than those they are replacing. Over recent years vehicles have become more technologically advanced and, often, have also become heavier leading to an increase in fuel consumption. Lower emission standards can, also, adversely impact upon fuel consumption.
- 4.28 All of these factors mean that net fuel costs, although still one of the smaller elements in the cost profile but often around 12% of the total, are likely to take on a greater significance.

Low Floor Vehicles

- 4.29 The introduction of low floor vehicles is also having an impact upon the cost profiles of operators. Whilst the introduction of any new vehicle has a positive effect on maintenance costs, for the early life years anyway, many operators are reporting massive increases in accident damage because of the use of low floor vehicles, often because proper infrastructure is not in place, but also because of the very nature of the vehicles with side panels very close to kerb edges.

Vandalism

- 4.30 Whilst, again, this represents a very small part of the overall cost structure, many operators are reporting increasing levels of vandalism, adding to the overall costs of operation.
- 4.31 Of particular concern appears to be the growing practice of 'window etching' which is leading to greatly increased glass costs.

'Catching Up' On Lost Ground

- 4.32 As already noted, the current cost and margin pressures for operators started around three or four years ago but there appears to have been some time-lag before the actual scale of the pressures has filtered through to the operations themselves. It is likely, therefore, that some operators will be 'making up for lost ground' with current increases in tender prices. This would appear to be particularly relevant in those local authority areas where no annual inflationary uplift is provided for contract prices.
- 4.33 There is also likely to be a tendency to over-compensate and ensure that similar 'mistakes' are not made again.
- 4.34 In terms of wage levels, current settlements are, effectively 'catching up' on many years of below-inflation increases. Whilst actual increases in pay rates for bus staff have an obvious impact, shortages of staff are also likely to put further cost pressures on the operators, not least the cost of recruitment or, particularly, retention.
- 4.35 It is possible, although it is difficult to gather substantive evidence, that operators are using higher tender prices to underpin parts of their commercial core networks. This may be a short-term phenomenon as operators seek to 'catch up' by introducing fares revisions or marketing initiatives. It might also provide a 'breathing space' whilst the future of the commercial network is reviewed and changes made in a more considered way

Contractual Issues

- 4.36 Many operators have expressed concerns about contractual issues, notably:
- ◆ Higher specifications;
 - ◆ Penalty clauses; and
 - ◆ Termination clauses.
- 4.37 Whilst these are also issues for the local authority, many operators are suggesting that the 'red tape' surrounding contracts has become so difficult that some of them no

longer wish to play a role in the tendered market or, if they do wish to play a role, cost into their bids time and effort associated with the administration of the complexities.

- 4.38 Operators have also suggested that an increasing number of schools services are being tendered as local bus services with the attendant higher conditions of contract, leading to higher prices.
- 4.39 It is suggested that some penalty clauses in certain local authority areas are draconian and operators are, therefore, building an element into their bids for tenders to cover possible penalties.
- 4.40 It is also suggested that in cases where the local authority can terminate a contract at short notice, the operators are building in elements of cost to cover a possible termination that leaves them with unavoidable costs in the medium-term.

CONTRACT AND LOCAL AUTHORITY ISSUES

- 4.41 There are a number of issues with respect to contract specifications and the way in which contracts are let that may impact changes in tender prices. Early indications suggest that the following are relevant:
- ◆ Higher specifications for contracts;
 - ◆ Changes to contracts involving network alterations;
 - ◆ Approach to negotiation; and
 - ◆ Size of the tendering authority.

Higher Specifications for Contracts

- 4.42 Our analysis to date indicates that a number of local authorities are now seeking higher specifications in terms of vehicles, staff and other quality factors. Early indications were that higher specifications had not led to tender prices being significantly higher. Whilst we have still not been able to discern any large price increases for higher specifications, the attitude of the industry as noted above suggests that those increases may remain to be seen over the coming months.

Changes to Contracts Involving Network Alterations

- 4.43 Many local authorities when re-tendering will review the content and scope of the contracts and, in a number of cases, make revisions to the network, often involving a reduction in the number of kilometres operated. In many cases this is as a result of a fundamental review and a decision that certain journeys or services no longer meet minimum criteria for the tendered network.
- 4.44 Our research suggests that whilst the local authority then achieves a headline reduction in the tender price, or at least a smaller increase in the tender price, the cost per kilometre operated is often significantly higher. A judgement, then, has to be made as to whether or not better value is achieved. However, it does appear to be the case that some of the journeys or services no longer forming part of the tendered network might, had they been tendered, been provided at little or no additional cost. The network implications are not always, it seems, considered in sufficient depth and

it might be the case that a range of options should be offered out to tender, as is often the case with many contracts.

- 4.45 The ongoing trend for operators to withdraw commercial services will inevitably mean that local authorities are forced to make more fundamental reviews of their tendered service networks and it will become ever more important for authorities to have a sound basis for making decisions on what services they wish to support in terms of best value and social inclusion.

Approach to Negotiation

- 4.46 A number of local authorities, once tender prices have been received, negotiate with the successful bidder to achieve better value. Others, however, do not and it may be that a more pro-active approach to negotiation could achieve better prices across the board. Regulations surrounding the ability of local authorities to negotiate are rather unclear; however, there are no specific inhibitors for negotiation, so long as there are good reasons for doing so and, importantly, that either all bidders are invited to negotiate, or that the lowest bidder is invited to negotiate.

Size of the Tendering Authority

- 4.47 Particularly when considering unitary authorities, there are a number of tendering authorities who have few local bus contracts. Some unitary authorities, the Cleveland area being one example, combine their efforts to achieve better network co-ordination and better tender prices. The complex local authority boundaries in the former county of Berkshire may well create barriers to the implementation of a co-ordinated network and consideration of a joint approach to tendering should be considered. Both Slough and Bracknell Forest have populations only just above 110,000, whilst the remainder of the Berkshire unitaries all have populations below 150,000. This contrasts with Kent which has a population of nearly 1.4 million.

COMPETITION ISSUES

- 4.48 The September 2001 ATCO survey and report suggested that the lack of competition in some areas is a direct cause of increased tender prices. The evidence available to Atkins from our survey and research does not suggest this to be the case and we have consistently found this to be so. We have based this conclusion on the basis that there is no particular evidence that those tender renewals where few bids are received are subject to any higher percentage increases than where larger numbers of bids are received.
- 4.49 Without substantial historical research it is difficult to determine whether or not the initial bid prices for contracts could have been affected by the absence of competition; however, the research does suggest that on relative like-for-like terms, i.e. considering resource inputs, there are no significant differences between bid prices, regardless of the number of bids.
- 4.50 What does appear relevant from our research across England, however, is the emergence of new competition. In cases where contracts have been retendered and a new competitor has emerged, some of the lowest percentage tender price

increases have been noted; indeed, there are many cases where incumbent operators have either not increased the price or have reduced it.

- 4.51 Once competition has become established, operators tend to recognise the tactics of the other competitors and bid likewise.
- 4.52 There is, however, also evidence that new entrants to the market tend to under-price their bids and the instances of contracts being terminated early are much higher where an award has been made to a new or relatively new operator. Any price reductions can, therefore, be fairly short term and then show as very high percentage increases at the next round of retendering, often well in advance of the normal programme.
- 4.53 Competition between the major groups, apart from in isolated cases, is either limited or non-existent. Indeed, the trend not to compete for tenders not within the core operation has grown in the past few years not least because of driver shortages.

REGULATORY ISSUES

- 4.54 It has also been suggested that tender prices and overall tender budget requirements have been increasing because of a tighter regulatory regime on the part of the Traffic Commissioner. A number of operators have been subject to investigation for irregular and unreliable operations, sometimes resulting in large fines or restrictions on commercial activities. Whilst this stricter regime does have customer benefits in terms of ensuring a more reliable service, many operators are concentrating resources on core routes, often increasing resources there at the expense of other routes, to avoid action by the Traffic Commissioner.
- 4.55 In a similar way to higher contract specifications and 'red tape' it is also suggested that many smaller operators are reconsidering whether or not they wish to be in the bus market because of regulatory issues. Many feel that the Traffic Commissioners' timekeeping standards are impossible to achieve. At the same time it is suggested that it is becoming increasingly difficult to obtain test dates for vehicle MOTs whilst the activities of the Vehicle Inspectorate are becoming ever more visible.

5. Conclusions

- 5.1 The research process set out to better understand both trends in prices for local bus tenders in England, the key drivers of price changes and how local transport authorities have responded to the changing conditions.
- 5.2 The headline finding of the research is that tender prices have been rising at a rate greater than the general level of inflation. This has been confirmed by a number of strands of research and analysis: from data gathered over a period of three years on newly let and re-let bus tenders; from questionnaire surveys of local transport authorities (comprising new research undertaken specifically for this study as well as ATCO's annual local authority survey); and from case study evidence.
- 5.3 The evidence available indicates that over the last few years the average price increase for authorities in England letting new tenders (compared to the price of tenders being replaced) was between 10-20%. Taking into account the length of time between initial contract letting and subsequent renewal this suggests inflationary increases significantly ahead of the general levels of inflation. In terms of annual equivalents, this is around 2% ahead of general inflation levels.
- 5.4 Accurately identifying price increases was made difficult by the nature of tendered bus services and the availability of comprehensive data on which to base solid statistical analyses. Although tendered bus services are let and then re-let on a regular basis, on average every 3.9 years, the re-tendering process often results in changes in service specifications, as local authorities' priorities and needs evolve, and in tender outcomes in terms of what operators offer to deliver. As such identifying true "like-for-like" increases in tender prices is exceedingly difficult. Additionally, the research identified that there is significant variation in the way that authorities procure tendered services, for example varying degrees of preference for minimum cost contracts over minimum subsidy contracts, and the price at which tenders are let. Much of the variability is accounted for by the wide range of different types of service and service specifications that make up the overall basket of what are termed tendered services. These range from relatively low-priced infill services, often let for only short periods, to higher priced complete services (or groups of services) very often let for the maximum allowable five years. Thus, while the overall trend identified from the data assembled on newly let and re-let bus tenders was one of increasing price, this masked very significant variability by local authority tendering approach and by type of service being tendered.
- 5.5 A key reason generally considered to be relevant in influencing the increases in tender prices has been the perceived reduction in "off-road" competition for tenders as the bus industry has become increasingly consolidated amongst the large groups. The various sources of evidence assessed did not, however, support this view. Over the last three to four years the average number of bids received per tender has remained reasonably stable at around 2.5 - 3.0. Furthermore, evidence from case studies and dialogue with local authorities indicated that efforts were being made to ensure that services were being put out to tender in a way that would enable some of the very small local operators to compete for contracts with the larger groups. While it is noted that the number of bids received per tender is highly variable, in some cases only one (or sometimes zero) bids were received for tenders, there is no

evidence to support the view that a general lack of competition for contracts is to blame for the overall increase in tender prices.

- 5.6 The increase in tender prices, as indicated by the various sources of evidence assessed, appears to be driven by the underlying operating cost increases faced by bus operators over the past few years. These cost increases, which have been identified elsewhere since they have also affected services operated on a commercial basis, broadly match the increases seen in the prices of tendered services. The direct impact of operating cost increases is, however, complicated by the time lag effect of the tender re-letting cycle. The majority of local authorities apply an annual inflation element such that the price paid to operators after the first year of a contract is increased in line with inflation. The above inflation annual increase in bus operating costs has, it is suggested, forced operators to significantly increase prices, relative to the existing tender price, on tender re-bidding as a means of re-basing to current operating cost levels and allowing for future above inflation operating cost increases. As noted above, tender cost increases also need to be seen in the context of changes in service specifications which have increasingly sought to improve the scope and quality of tendered service provision - for example by ensuring that vehicles meet accessibility standards.
- 5.7 Overall, no evidence has been found to suggest that operators are systematically increasing prices for re-let tendered services for any reason other than in response to operating cost increases or changing contract specifications.
- 5.8 The research has also identified that many local authorities have been forced to re-prioritise funding for supported services as a consequence of tendered service contract withdrawals and commercial service deregistrations. This has placed additional pressure on tendered services budgets and forced a change in approach to replacement service procurement. At this stage it is difficult to assess whether the costs of tendered services have increased in these circumstances because of the change that has occurred in the services being procured.
- 5.9 The research also found that local authorities adopted different approaches in procuring and maintaining their supported networks. It is clear that there are dangers in being overly prescriptive in defining how services should best be procured. All the evidence from case studies and consultation with authorities indicated that knowledge of local networks, passenger demands and local bus operators' disposition and capacity are critical in cost-effectively securing services of an appropriate quality. Nevertheless, a range of procurement methods were identified as representative of good practice. These are set out in a separate "Good Practice Guide".