

Summary:

Market oriented contracts for purchase of public transport services in Nordland County

The Institute of Transport Economics (TOI) has been engaged by Nordland County and the Federation of Norwegian Transport Companies, Nordland branch, to participate in the process of designing new contracts for the purchase of public transport services in Nordland County. Our work has been centered around these main issues:

- ?? A discussion of different elements to be part of the contract. We have in particular discussed in what way the contract can regulate the distribution of responsibilities and risk between the authorities and the operators.
- ?? A discussion of the revenue potential in the county. We have evaluated in what ways it may be possible to increase the demand for public transport in the county, and what means the authorities and the operators have to achieve this.

Our project has been carried out by an examination of the contracts used today for public purchase of transport services from the operators. We also examine alternative types of contracts. We have interviewed important actors in the county administration as well as with the operators in the county. We conclude our report by giving advice about what kind of contract would be the best choice for the county, considering

- ?? the aims for public transport in Nordland,
- ?? international experiences with different types of contract for public transport,
- ?? and finally weaknesses in the model currently in use.

This summary will only report the main conclusions of our work, not the totality of our evaluation.

Introduction to Nordland County

Nordland County is situated in the north of Norway. It is one of the largest counties in Norway measured

in square kilometres. The county is densely populated. The largest towns in the county are Bodø, Harstad and Mo i Rana. Apart from these, the population is for the most part situated along the coast in smaller towns or villages.

The modes of public transport in Nordland are by train (one line going through the length of the county and another line from the city Narvik and into Sweden), by boat and bus. This report concerns with public transport by bus, which constitutes the largest part of public transport in the county.

There are ten bus operators in the county. They all operate on area concessions, and the relationship between the authorities and operators are regulated through four-year net contracts.

We have examined some key figures for the bus industry in the period from 1995-2000. This shows that the total production of kilometres was at the same level in 2000 as it was five years previously. The number of passengers has been stable throughout the period. The revenues have decreased in the period, while the cost level has increased. From this we conclude that the fares have been low. The fares have been set by the authorities.

Future contracts for public transport in Nordland County

Aims

The County Council has outlined some goals for public transport in Nordland. We consider these goals to be extremely important for the choice of means. The means (such as contracts) must be chosen in a way that they reflect and help fulfil these ends. The aims are

1. a more market effective public transport
2. a stronger degree of customer orientation in public transport

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3. more market responsibility to the operators in the county.

Experiences with different kinds of contracts

Incentive based contracts are increasingly used, in Norway as well as in Europe. It is appropriate to say that conditions for public transport have been in constant change for a longer period of time. This has led to a stronger focus on

- ?? The customer. Evaluations of customer satisfaction are used as parameters in quality contracts. When responsibility for revenues are turned over to the operator, the operators customer orientation is likely to increase.
- ?? Responsibility for revenues and market. The responsibility is moved from the authorities to the operators to achieve higher quality public transport and an increased interest in customer satisfaction in the operating companies.

The legal and institutional environment for public transport has changed over time. In its turn, this constitutes new requirements for both operators and the authorities. Lately competition for contracts in public transport has become an important subject, according to the Draft Regulation on action by Member States concerning public service requirements and the award of public service contracts in passenger transport by rail, road and inland waterway, from the EU Commission.

Weaknesses in the contract currently used in Nordland County

We point to four elements as the main weaknesses in the contract used in Nordland County today.

1. The "Alfa-model". This is a model used in many Norwegian counties to calculate the operators assumed cost level, based on data from reference counties. Data from several counties constitutes a reference cost level. The counties themselves have cooperated in designing the model. The model works well as an instrument for budgeting. However, it is not a good tool for determining marginal costs. The model does not take account of the differences between the operating companies to a sufficient degree.
2. The county administration and operators have agreed on certain minimum levels of revenue that the operators must acquire during the contract period. These minimum levels have been quite steep compared to average Norwegian passenger growth – an average growth in passenger

transport of 2,8 % is required. Only two out of ten operators have succeeded in acquiring these levels of passenger growth. Those who did not make it must in terms of the contract cover the deficit themselves.

3. Quality. In the contract there is a description of what kind of quality related work should be done by the operators and the authorities during the contract period. Some quality measures are described, and it is also suggested in the contract that a quality handbook should be made in cooperation between the operators and the authority. However, our opinion is that this is not a sufficient obligation in order to achieve a higher level of quality. There is also a lack of precise requirements. The words used in the contract are "ought to" and "should", instead we suggest the use of the stronger terms "must" and "shall".
4. Distribution of responsibilities. In the current contract the division of responsibilities are quite clear. The final responsibility for approval of several important factors (fares, fare structure) belongs to the authorities. From this we conclude that the responsibility for the market actually belongs to the authorities.

Recommendation

Our general conclusion is that the authorities in Nordland County should co-operate with the operators in designing and establishing a quality contract for public transport in the county. We also recommend that the subsidy is made dependent on a certain level of quality and customer satisfaction achieved by the operators.

The arguments for suggesting a subsidy dependent on the operators goal attainment, are found in the following characteristics of such a contract.

- ?? Operators are given responsibility for revenues stemming from the customers they are actually serving.
- ?? Operators are given an increased responsibility for the tactical level (planning, fares, vehicles and services).
- ?? The authorities are given an opportunity to put stronger requirements on financial performance and competition in the agreement between the two parties. A threat of competition must be established and maintained within the whole contract period.
- ?? The authorities will define the economic incentives in the contract.

We recommend that the clause on 2,8% average passenger growth is abolished in the new contract. By using a net contract (as the County Council has decided), transferring responsibility for the market to the operators and introducing a quality contract and a subsidy dependent on results in the market, the operators will have a stronger financial incentive than they have in the current contract. The clause is simply not needed.

Subsidies dependent on certain levels of achievement by the operators will decentralize responsibility for the market, under the assumption that the operators are the ones to know the market best. This implies that the operators must have more freedom to operate freely in the market, to a larger extent than they have with the current contract.

The establishing of this kind of contract and relationship between the authority and the operators is complex. We suggest that the new contracts should be designed in a close cooperation between the parties.

Potential revenues in Nordland County

An important issue in the relationship between the authorities and the operators in Nordland is to what extent the operators are collecting all potential revenues in the county.

We have debated this issue at length with both the operators and the authorities, and we do not wish to enter into a discussion on where more money can be made in Nordland. Our experience from similar projects in similar counties suggest that *creativity in planning public transport* is of vital essence. The question of exploiting the potential for revenues in the densely populated areas in Nordland must concern level of service and the use of alternative kinds of vehicles. Introduction of smaller vehicles will lead to a higher frequency and thus an increase in the number of passengers. To get maximum effect out of the potential market it is necessary to address the ability, will, efforts and degree of freedom to be creative in planning public transport. This goes for the authorities as well as the operators.