Purpose of report:

- To inform members of:
  i) the interim findings and proposed remedies of the Competition Commission’s review of the local bus market
  ii) the Department for Transport’s enhanced payments for Bus Service Operators Grant

Recommendations:

The RTF is asked to:
1. consider the implications of the Competition Commission’s proposed remedies
2. note the Department for Transport’s enhanced BSOG payments

1 Introduction

1.1 The purpose of this note is to inform the RTF of the interim findings and proposed remedies of the Competition Commission’s review of the local bus market and the Department for Transport (DiT) announcement about enhanced payments for Bus Service Operations Grant (BSOG).

1.2 The governing legislation that de-regulated and privatised the provision of bus services is the 1985 Transport Act, which gave bus operators the freedom to decide the routes and times of the services they wish to provide and the level of fares they charge. Under competition legislation bus operators are not able to talk to each other in order to co-ordinate routes, timetables or fares although there is some relaxation in respect of ticket interavailability between bus companies. Outside of London, which was not considered in the Commission’s review, the role of County and Unitary Local Transport Authorities (LTAs), and metropolitan Integrated Transport Authorities (ITAs) is to consider the need to provide services where they are not provided commercially. This position has been left largely unchanged by successive revisions to the 1985 Act (in 2000 and 2008), although these did create some additional powers.

1.3 In January 2010 the Office of Fair Trading (OFT) referred an investigation into the supply of local bus services to the Competition Commission. In Spring 2010 they sent a questionnaire to bus operators and LTAs/ITAs to seek their views about the local bus market, which many of the LTAs in the Eastern region responded to. Section 2 of this report sets out the provisional findings and proposed remedies in the Commission’s interim report, together with the views of RTAs in the Eastern region. With regard to these, it should be noted that there are very different experiences and views on what the current legislative framework has delivered which means that generic responses on the broad conclusions of the Commission may not be wholly representative of the position within individual or adjacent authorities.

1.4 Fuel Duty Rebate (FDR) was initially paid to operators of registered local bus services under the Finance Act 1965. This was replaced by the Bus Service Operators Grant (BSOG) in 2002, and was extended to cover refunds of the Fuel Duty to a wider range of community transport service operators. Operators have to apply for the rebate to
the Department for Transport (DfT), who check their eligibility, and the DfT refund a proportion of the fuel duty every quarter, adjusted at the end of each year to reflect actual service operation. Until 1994 the level of FDR was 100%; it remains at this level for buses running on bio-fuels, but is buses fueled by diesel and other fuels. Under last autumn’s Comprehensive Spending Review, the grant will be maintained at current levels until 2012 and then reduced in phases between 2012 and 2015. The total reduction will be 20%, although the DfT has recently published incentives to increase BSOG and these are considered in Section 3 of this report. The impacts of reduced funding through for example reductions in fuel duty will result in higher fares, service cuts and pressure on LTA contract budgets.

2 The Competition Commission review of the local bus market

Background

2.1 In early May 2011 the Commission published a report on its provisional findings. The Commission found that there are certain features of the local bus market that prevent, restrict or distort competition and have a detrimental impact on customers. They concluded that the five largest operators (First, Arriva, Stagecoach, Go-Ahead, and National Express) provide 69% of local bus services, and that the following factors inhibit or prevent new entrants or expansion of the existing local bus market, and thus reduce constraint from potential competition:

- Significant on road competition leads to network instability, with frequent registration fare and service changes. This competition often results in one of the operators exiting from the market and deters new passengers and confuses existing passengers.

- New entrants sometimes have difficulty accessing privately owned bus stations and can sometimes have difficulties in developing new bus depots.

- Incumbent operators can have an advantage in that they are likely to already provide an existing network of services. They can also benefit when multi-operator network tickets are inferior to their own network tickets. A substantial proportion of trips are made using multi-trip tickets.

- Partnerships between operators and LTAs/ITAs do not cause an adverse affect on competition, although Concessionary Fares schemes can encourage higher fares and the low number of operators in some areas can, along with the design of the Tenders, restrict competition for services supported by LTAs/ITAs.

- The great majority of urban areas have not experienced any large scale entrants in recent years. Risks and costs are likely to increase with the scale of entry.

2.2 The responses to the Commission’s interim report needs to balance the issues related to barriers to entry for new operators with the ticketing frameworks and strategies already in place. In relation to barriers to entry, there is the need to ensure minimum quality standards which enhance the standing and attractiveness of the bus as a viable mode option, rather than working to the lowest denominator.
2.3 The Commission has, for the moment, ruled out price controls and selective divestment of local bus operators. However alongside their provisional findings they published a number of possible remedies. During May 2011 they consulted on these measures to “open up markets” by tackling the aforementioned factors which can hinder competition. These remedies include:

- Restrictions on aggressive behaviour, such as over bussing, aimed at reducing a rival’s ability to compete.
- Measures to increase the number of multi-operator ticket schemes ensuring they are effective and attractive.
- Ensuring fair access to privately owned /managed bus stations for all operators.
- Recommendations to LTAs on the circumstances in which to pursue Quality Contracts, or franchising in areas most affected by competition, and how to use other powers e.g. Quality Partnerships to promote competition or “improve outcomes to local consumers”.
- Recommendations to the DfT to update its best practise guidance on supported services and to LTAs to follow this guidance.
- Measures to make more information available to LTAs and potential suppliers on the performance of supported services.

The remainder of this section considers the issues relating to these remedies.

Restrictions on aggressive behaviour by bus operators

2.4 The Commission found that very few routes overlap substantially with the route of a competing operator. This would appear to be the experience of most LTAs in the Eastern region. The Commission suggests introduction of a legally binding Code of Conduct to ensure that operators do not practice exclusionary behaviour so that competition is sustained more often, and to restrict large incumbent operators from increasing service frequencies, reducing fares or other exclusionary measures. It is the view of the LTAs in the Eastern region that, where such behaviour is evident, amendments to legislation that provides a robust and enforceable system would be welcomed, and that the Traffic Commissioner is best placed to regulate such activity. However, a standard set of rules to regulate such behaviours is unlikely to be able to take into account the differing demands and needs of local services.

Increase number of multi-operator ticket schemes that are effective & attractive

2.5 The Commission sought views on the area of coverage of multi-operator ticketing together with the management structure of such schemes (statutory schemes run by the LTA, operator-run schemes or schemes run by a third party with cooperation from bus operators). The view of LTAs in the Eastern region is that multi-operator ticketing schemes may be successful in urban areas where there are already multiple operators along sections of route or there is an opportunity for significant market growth allowing new entry and expansion of the supply side of the market, thus encouraging competitive activity. In terms of the management structure, schemes led by the LTA or Operator are preferred.

2.6 The Commission’s proposed multi-operator ticketing remedies refer to “common standards in technology”, which implies their view is that any such schemes should be based around a “Smartcard” system. However it may take some time to implement due to the costs of technology and administration of “smartcard” schemes. Conflicting ticket machine systems may also necessitate the purchase and installation of new systems and discourage smaller operators from participating. Where routes are already operationally marginal these additional costs, should an operator be compelled...
to participate, may actually lead to a contraction of the market and dilution of any existing competition. A paper based ticketing system with revenue based on the principle of “sitting where it lies” could be implemented relatively quickly and provide a “quick win” to benefit the local community. However such schemes have been challenged by OFT on the grounds they could conflict with the Ticketing Block Exemption or other rules. The LTAs have recommended that, as part of its review, the Commission should recommend to Government what legal changes are necessary to minimise the barriers faced in the introduction of such schemes and to ensure that they can be implemented successfully and effectively.

2.7 The Commission’s review found that even where a multi-operator ticket does exist, large incumbent operators can still gain competitive advantage by pricing their own tickets at a significant discount and failing to market the multi-operator ticket. The Commission’s reference to larger operators having discounted ticketing products in the market place which may not be offered or viable for new entrants means, by implication, either potential greater support for new entrants or upward adjustment of existing fares which will not be in the interest of customers. The proposals to make these tickets more attractive to passengers include Conditions relating to their area and time of use so they are no less attractive than those of the individual operators, and to specify a maximum premium. The experience of LTAs in the Eastern region is that the price of multi-operator tickets would depend on the price and profit margin of the participating operators; there are some cases of significant variation in price differential between two local operators particularly for period return tickets, and also the operational profit margin would need to be set at the highest level to ensure adequate returns. In these circumstances, any restrictions on multi-journey tickets offered by individual operators would not be in the interest of the travelling public if the purchase of a multi-operator ticket is not required for their journey. As the Commission found little evidence of competition on routes, just because a multi-operator ticketing Scheme is in operation doesn’t mean that the multi-journey tickets of individual operators should be restricted. It is unlikely that most operators would wish to withdraw current ticket offers and it is difficult to see how this could be enforced without inhibiting competition between operators.

2.8 Other factors that will need to be taken account of include the range of tickets (day return, weekly, other period returns), the point of sale (on-bus, ticket machines, retail sales through paypoint etc) and concessions. In relation to the last of these, a particular issue is the fact that different operators have different upper age limits of a Child. Whilst there is no legal compulsion on bus operators to provide any young persons concession at any time, the variation in upper limits of a Child’s age, this could make it difficult to get operators to agree to introduce multi-operator tickets for children, and with some LTAs having schemes for 16-19 year olds, could mean that there is a “gap” for those operators services where the upper age limit for a child is less than 16. To make the operation of multi-operator ticketing schemes easier to implement, it would be helpful if the Commission could recommend a standardised upper age for a child of 16. However some LTA in the Eastern region are concerned this could lead to operators withdrawing existing child concessions.

Access to privately owned/managed bus stations and depots

2.9 It is unfortunate that the findings relating to access to bus stations and depots are considered in the same section of the report as the issues associated with each are very different. The experience of LTAs in the Eastern region is that there are few privately owned/managed bus stations. Whilst there may be a case for ensuring equitable access to publicly owned or funded bus stations/interchanges, where an individual operator has invested in depot, we consider it is generally unreasonable to enforce sharing those facilities with other operators.
Advice to LTAs/ITAs on when to use Franchising or other Powers

2.10 The Commission proposes a Franchising remedy in areas “where competition is weak and is not delivering benefits to customers”, and particularly in larger urban areas that have a complex network structure where large numbers of passengers will use multiple routes. In particular the PTEs in the main Metropolitan areas have welcomed the Commission’s Franchising proposals. The experience of London suggests that franchising incurs significantly higher levels of public subsidy, since operators transfer a proportion of risk on to the authority, and under a franchise system it is likely that a few large scale operators will dominate. The LTAs in the Eastern region believe that Franchising is welcomed in large urban conurbations and in areas such as Hertfordshire where towns are close to each other, as it would result in competition for the market rather than competition in the market. However such a model would be unsuited to rural transport provision.

2.11 The Commission is also seeking views on what changes could be made to other models. With regard to Quality Contracts, it should be noted that bus operators do not favour them. There are no Quality Contracts currently in operation, although proposals are currently being developed in some areas. LTAs and ITAs have to show that Quality Contracts are proportional to the level of public interest involved and find this difficult to demonstrate. With regard to the Partnership approach, the view of some LTAs in the Eastern region is that a partnership approach would not increase competitive activity but would instead stabilise the market by ensuring that there is not over supply. This in itself may be advantageous to the travelling public, particularly if a multi operator ticketing scheme is run in such partnerships.

Tendering for supported services

2.12 The Commission proposes that the DfT should update its guidance on the tendering for supported local bus services. Overall it concludes that the “market for tendered bus services works well in most instances”. It indicates that more bids for supported services are likely to be received if LTAs specify longer contracts (up to 8 years), and allow both minimum subsidy (operator keeps the revenue) and minimum cost contracts (LTA keeps the revenue) as each operator has different preferences. However the Commission acknowledges that “there are good reasons for LTAs adopting a particular approach to the design of a contract” that does not maximise competition. The experience of LTAs in the Eastern region is that most do not experience problems with the level of competition for contracts and the consequential impacts of cost and service delivery.

2.13 The Commission also proposes that bus operators should be obliged to hand over revenue information about Tendered bus services to LTAs, and considers that this will also encourage greater competition in Tendering for supported.

Other issues

2.14 In a competitive environment, and at a time when both LTAs and bus operators are experiencing cuts in funding, it would be advantageous if competitive restrictions could be viewed in a different light, particularly where this would be a benefit to the local community. For example, in the context of service frequency, an indirect result of directly competing routes is that two operators running a half hourly frequency could time their buses to run at similar times. In the interests of passengers, under these circumstances it would be appropriate if the Commission set a principle that more even headways should be provided between the two operators, resulting 15 minute headway rather than two 30 minute headways in the above example. However whilst this is desirable from a transport planning viewpoint, the operators counter argument is that they find certain timeslots more attractive than others and would wish to operate the most profitable services only.
3 DfT changes to Bus Service Operators Grant (BSOG)

3.1 In its response to the Comprehensive Spending Review last Autumn, the coalition Government announced a 20% reduction in Bus Service Operations Grant in 2012. The DfT subsequently announced two incentives for operators to increase their BSOG rate:

i) an 8% increase if they have operational “Smartcard” systems and
ii) a 2% increase if they use Automatic Vehicle Location systems.

3.2 These incentives require bus operators to provide data from smartcard and AVL systems to the LTAs should they request. If the operator does not provide the agreed data to the LTA, then they risk losing the enhanced BSOG payments.

3.3 The DfT has set out minimum requirements of information from smartcard and AVL systems. They also encourage LTAs to enter into a data sharing agreement with the bus operators, which can include any other information on local services. The LTAs should treat any information as commercially confidential, and must seek agreement of the operator to publish any data and only publish data at an aggregate level.

4 Conclusion

4.1 It is interesting to note that the Commissions findings relate principally to how the existing local bus market can be “fine tuned” to encourage more Competition and remove any barriers. One of the conclusions was that Operators see their biggest threats from rival operators and not from car users, although many operators deny this. However operators need to be persuaded of the benefits of growing their market, rather than poaching it from each other. In this respect, it is important to note that, particularly in relation to personal and workplace/commercial travel planning initiatives, bus operators will have an important role to play, and this is not even recognised in the Commissions provisional findings.

4.2 The main conclusions that can be drawn from the assessment of the Competition Commission’s proposed remedies are that the Commission should:

- extend the scope of multi-operator ticketing to include paper ticket based schemes with revenue distributed on the principle of “sitting where it lies”, and recommend to Government what legal changes are necessary to minimise the barriers faced in the introduction of such schemes and to ensure that they can be implemented successfully and effectively
- recommend a standardised upper age for a child of 16 for all bus operators
- recommend to Government the legal changes to competition law to allow even headways between, for example two operators, resulting a 15 minute headway rather than two 30 minute headways.

4.3 These, and other points outlined in Section 2 above, have already been made by some of the LTAs in their responses to the interim findings and proposed remedies of the Commission’s review.

4.4 Notwithstanding the positive impact of enhanced BSOG payments set out in Section 3. Members attention is drawn to the impacts of reduced funding resulting in higher fares, service cuts and pressure on LTA contract budgets.