

The Independent Competition and Regulatory Commission is established under the *Independent Competition and Regulatory Commission Act 1997* (ICRC Act). The Commission's functions are set out in section 7 of the ICRC Act

The Commission is made up of three Commissioners:

Paul Baxter, Senior Commissioner
Robin Creyke, Commissioner
Peter McGhie, Commissioner

The Commission's reports and inquiries are public, except where the Commission assesses some information as being confidential. All publicly available information may be accessed in hard copy at, or available from, the Commission. The Commission maintains a website (www.icrc.act.gov.au) to assist access to a range of documents and other information. The Commission can also be contacted electronically at icrc@act.gov.au.

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Foreword

The Minister for Urban Services has issued a reference for the Commission to inquire into and determine a direction for ACTION prices for the period commencing 1 July 2003 and ending on 30 June 2006. This Issues Paper is the first step in determining a price for ACTION services for the three year period.

The Commission is releasing the Issues Paper to stimulate debate about the issues involved in the provision of public transport through the ACTION network that impinge upon the cost of those services to the users of public transport. The Commission is aware that many people will have views about the issues raised in the paper and encourages submission of those views to the inquiry. The inquiry will involve responses in writing to the Issues Paper and later to the Draft Report and, possibly, an opportunity to make submissions orally to a public hearing.

The Commission's timetable for the inquiry, at this stage, is found in the table below:

Table 1: ACTION price inquiry timetable

Issues Paper released	16 December 2002
Submissions on the Issues Paper close	24 January 2003
Draft Report of the Inquiry released	21 March 2003
Public Hearing	Early April 2003
Submissions on the Draft Report close	24 April
Final Report released	16 May 2003

Submissions on the Issues Paper, or at later stages of the inquiry process, should be provided in writing or electronically. Written submissions can be either mailed to the Commission at PO Box 975 Civic Square ACT 2608 or delivered to the Commission offices at level 7, Eclipse House 197 London Circuit Civic. Submissions made electronically should be directed to the Commission at icrc@act.gov.au, or ian.primrose@act.gov.au.

For information about the inquiry please contact Ian Primrose, Chief Executive Officer, on 62050779, by email to the address above or by fax to 62075887.

Documents relating to the inquiry will be available on the Commission's website at icrc.act.gov.au, at the Commission's offices or may be mailed or faxed to you.

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Introduction

In May 2001, the Commission issued a price direction for ACTION for 2001-02 and 2002-03 which provided for a small real increase in fares in the first year and for a CPI adjustment in the second year. The Commission decided not to make a three-year direction because of several changes which were pending and which were expected to have a potentially significant impact on the future performance of ACTION.

Over the past 18 months, the environment in which ACTION operates has changed:

1. In January 2002, ACTION was established as a statutory authority and became subject to the corporate governance requirements of the *ACTION Authority Act 2001*.
2. Fares policy for school transport services has changed twice. At the time of the Commission's last price direction, the then government decided to remove fares for school students to be effective from September 2001. This policy operated until reversed by the incoming government in December 2001. Also, when school fares were re-introduced, a single-zone fare was applied rather than the earlier two-zone fare.
3. A single zone fare structure was introduced for all ACTION services from July 2002.
4. ACTION and the Department of Urban Services (DUS) signed a five-year contract in December 2001 for the provision of an agreed network of bus services in the ACT.
5. Discussions have been held between ACTION, DUS and Treasury on a new funding model for ACTION services. However, the nature of an appropriate funding model, which should underpin this contract, is still the subject of deliberations by the parties.
6. A number of strategic planning initiatives have been undertaken since the Commission's last price direction, reflecting the broader environment in which public transport policy should be made.

In this changed environment, the Commission is required to make a price direction on ACTION fares for the triennium beginning 1 July 2003. As indicated in the ministerial instruction of 11 September 2002, the direction "should consider current and projected patronage trends and any noticeable trends flowing from the previous 1 July 2002 fare increase and the introduction of single zone flat fares".

Patronage Trends and Fares

In previous price directions, the Commission was concerned about the lack of evidence submitted to it to indicate the effect of fare changes on patronage levels. Different views had been expressed to the Commission – on the one hand, that the “captive” nature of bus passengers in the ACT suggested that the effect of modest fare increases on patronage numbers would be small and, on the other, that fare increases were intrinsically inequitable and that passenger numbers were materially affected by even modest changes to fares.

According to ACTION's 2002 Annual Report, adult and concession passenger boardings fell in 2001-02 during a period when fare increases were constrained to no more than CPI adjustments. With the introduction of a single zone fare structure in July 2002, the Commission understands that recent data suggest that non-student passenger numbers have increased. The Commission at this stage is uncertain, to what extent these changes in patronage are affected by changes in fare levels or changes in fare structures. Interestingly, the change to a single zone fare structure represents an increase in fares for passengers who were one-zone passengers and a significant reduction in fares for passengers who were all-zone passengers. The Commission was advised that the majority of passengers fell into the one-zone category, and it is they who are now incurring fare increases in excess of CPI.

The Commission has expressed concern that more reliable documentation and analysis on this issue was not available. The Commission is pleased that a study is currently underway which is investigating fare elasticities (change in patronage in response to a change in price) for bus passengers in the ACT. The results of this study should provide necessary and helpful data on the impact of changes in fare levels and structures, together with the impact of changes in prices for alternative modes, on ACTION patronage expectations. The results of this study are expected to be available for inclusion in the Draft Report due early in 2003.

New bus timetables were introduced in May 2002. According to ACTION's 2002 Annual Report, the biggest impact of that change was in the Gungahlin area, where an extra 205 services were provided, representing an increase of 15%.

The Commission invites submission on the level of patronage for these new services and the loss of patronage due to services being withdrawn from elsewhere to provide those services.

The Commission has always been made aware of community concern about school student transport. Since the last price determination in 2001, significant changes to the provision of school transport services have been made. The School Student Transport Scheme (SSTS) involved additional services and the abolition of student fares from September 2001. The change of government led, in December 2001, to the re-introduction of student fares,

but on a single zone basis. The Commission understands that the abolition of school fares led to an increase in student passengers and that, despite the re-introduction of fares, school student passenger numbers have remained high.

The Commission invites views about the extent to which the community's concerns about school student transport have been met through the single-zone student fare.

Integrated Land Use and Transport Strategy

Previously the Commission raised concerns about the context in which ACTION bus fares should be assessed. It appeared that, in terms of market activity, ACTION was being judged on its existing patronage numbers but it had little ability materially to increase patronage levels. This may have led to an overly harsh "report card", given that Canberra is a market dominated by the use of private motor vehicles, and there is likely to be a limit to public transport patronage potential. Currently, ACTION's share of total transport trips in the ACT appears to be in the order of 5-6%, and even a 20% increase in activity would have a negligible impact on total transport activity. The Commission noted in previous price directions that there are more substantive policy issues driving the objectives which public transport, including ACTION, should pursue.

The Commission would benefit from comment on those policy issues.

The Commission is pleased to note that steps have been taken in terms of a broader transport focus for the ACT. Planning and Land Management (PALM) is developing a Canberra-wide planning framework to provide the basis of strategic decisions for the next 25-30 years. The framework is called The Canberra Plan and comprises three parts: The Canberra Spatial Plan, The Canberra Economic White Paper and The Canberra Social Plan. As part of this planning framework, the Commission understands that studies are being undertaken to investigate the future of public transport, car parking charges, the costs of private and public transport as well as the fare elasticity study referred to earlier. A number of these studies should be concluded within the inquiry period and will assist the Commission's thinking.

The Commission welcomes contributions from government or the public as to how the proposed role of ACTION in a wider context of land use development and transport services might be taken into account in determining service prices.

Operating Costs

In previous price directions, the Commission noted ACTION's achievements in reducing its operating costs, but it also indicated that ACTION should continue vigorously to pursue efficiency improvements. The Commission notes that ACTION commissioned a consultant (INDEC) to carry out a series

of benchmarking studies. According to ACTION's 2002 Annual Report, INDEC claims that further savings of up to \$2.6 million could be achievable over the next few years. Out of an annual actual expenditure figure of around \$67 million, this proposed efficiency improvement figure only represents 4% of total costs.

The issue with ACTION's operating costs is to establish the difference between its actual costs and what are referred to as efficient costs. The difference between the two is considered to consist of inefficiencies and other costs principally associated with ACTION being in government ownership and over which management may have little control. While the conceptual differences appear straightforward, the Commission is concerned to ensure that the appropriate measures of inefficiencies and costs of government ownership are in place.

The Commission invites submissions on efficiency and cost issues relating to ACTION's structure or ownership.

The Commission understands that there are different opinions circulating in government about what might constitute the costs of government ownership which affect ACTION's total operating costs. There needs to be agreement about those costs so that ACTION has appropriate and achievable cost reduction targets in the short term and over the medium term.

The Commission notes that in previous directions the cost reductions in out years have generally turned out to be less than what was anticipated. The Commission also notes that a new enterprise bargaining agreement is due for negotiation and it is not clear at this stage what the cost implications are for ACTION's budget. The Commission is keen to ensure that, for whatever levels of service are agreed between ACTION and DUS, ACTION provides those services at the most efficient cost.

The Commission would welcome discussion about the role, performance and efficiency of public transport, noting that they are a focus of government attention, particularly in the current debate about an appropriate funding model for government and ACTION.

Government Funding Policy

ACTION is now a statutory authority and obliged, under the *ACTION Authority Act*, to "provide an effective, affordable and accessible public transport network; and without prejudice to the point above, to operate on a sound commercial basis".

The Commission will consider how these objectives might be expressed in the Commission's price direction to ACTION. The Commission has looked at the "commercial fare" concept in previous directions but has had difficulty in defining a useful meaning for the term. There is circularity in the argument which determines a revenue requirement based on an agreed cost base plus

some prescribed return, attributes that cost according to actual passenger numbers, and then claims that the resulting number is the “commercial fare”. ACTION’s business, as confirmed in its contract with DUS, is to provide an agreed network of services. Given the number of passengers involved, the business is fundamentally a non-commercial activity. In other words, commercially reasonable fares could not be set that would generate sufficient revenue to cover operating costs, or provide for asset replacement or return on equity. In contrast, faced with similar circumstances, a commercial operator would either significantly reduce the network of services to reflect passenger volumes, or perhaps provide no services to some locations.

Until now, ACTION’s funding from government has comprised a series of payments which have been described as some kind of community service obligation (CSO), for example, pricing CSOs, service CSOs, concession CSOs, or school services CSOs, together with a general subsidy or injection for operations. Effectively, there was little firm basis for the separation of payments into those categories. The main aim was to identify and fund the deficit or shortfall between ACTION’s costs and farebox revenue.

In the past, the Commission has raised the issue of determining minimum service levels, as the basis for government payments, leaving ACTION with the discretion of providing services above those if it believed that there were financial advantages to do so. Because DUS has contracted ACTION to provide a defined set of services for a five-year period and the average farebox revenue is low, there is a view that rather than revisit the arrangements, and the deficiencies, in the Minimum Service Level Agreement approach, it would be more efficient to develop and implement a new funding model to be agreed between ACTION and the government. The development of such a funding model, would be critical to the Commission developing an appropriate price direction for the next three years.

The Commission would welcome views on matters relating to appropriate way in which public bus transport systems in the ACT should be funded

A Three Year Price Path

In the current direction, the Commission set a price path over two years. In the reference for this price direction the government wishes to have the price path extended to three years. In the past, directions for more than one or two years have been made difficult by a number of issues, including such things as the uncertainty surrounding the structure of ACTION and government policies about the structure of fares for school children and whether there should be one or more fare zones. In determining the appropriate length of the price direction, the Commission will need to consider which period offers the maximum benefits in terms of certainty for ACTION, government and the community and the stability of public transport policy, among other things.

In this inquiry, the Commission is interested in receiving submissions on the appropriateness of a three year price path from July 2003 to June 2006 and matters that should be considered in arriving at a price path extending over a three year period.

Form of Price Regulation

In past price directions for ACTION services, the Commission has set average annual price caps that have allowed flexibility for ACTION to structure their services and actual fare levels to meet the policy requirements of government while at the same time improving service efficiency. The Commission has made recommendations about the adequacy of the cost recovery in different areas of ACTION's operations, recommendations that have been substantially addressed in subsequent reforms to the way in which ACTION has structured actual fares. The Commission has consistently sought greater clarification of the government's objectives for ACTION, in part to provide greater certainty about the costs that ACTION is required to meet and the adequacy of the combination of farebox revenues and payments from the government to meet the total operating costs.

The Commission has sought to retain flexibility for ACTION to set prices in ways that are consistent with achieving its overall objectives as specified by Government, while having transparent arrangements that determine the levels of revenue ACTION can expect from the farebox and government payments.

In setting the level of regulated fares, the Commission can continue to use an average annual fare approach, or it can adopt one of two alternative approaches, namely

- a fare cap for each type of fare charged by ACTION, or
- a revenue cap for the total farebox recovery by ACTION.

An average annual fare cap allows ACTION greater flexibility in the fares that it charges for different services and customer groups. A fare cap on individual type of fare category basis removes this flexibility. A farebox revenue cap would provide a greater degree of certainty as to the level of revenue that ACTION could expect to recover from passengers, but would do so in a way that would potentially require further fare increases should the revenue cap not be achieved.

The Commission would welcome submissions from interested parties as to the appropriate form of regulation that should be used in the next price direction.

Other Considerations

Under the provisions of Section 20(2) Of the ICRC Act, the Commission is required to have regard to a number of other factors when making a price direction. These other factors are:

- protection of consumers from the abuse of monopoly power
- standards of quality, reliability and safety
- principles of ecologically sustainable development
- social impacts of the decision
- considerations of demand management and least cost planning
- the effect of general price inflation over the medium term, and
- any arrangement that a person providing regulated services has entered into for the exercise of its functions by some other person

In addition to those statutory requirements, the Commission is required by the terms of the reference to consider current and projected patronage trends and any noticeable trends flowing from the previous fare increase in 1 July 2002.

The Commission would welcome submissions and comments on any or all of these factors as they relate to the operations of ACTION and the deliberations by the Commission on an appropriate prices direction for bus services in the ACT.