

COMPETITION AUTHORITY



Comments on the Report on the Regulation of Bus Services Outside the Greater Dublin Area for the Department of Transport

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EXECUTIVE SUMMARY

This submission comments on the Report on Regulation of Bus Services Outside the Greater Dublin Area, produced by Steer Davies Gleave in association with Fitzpatrick Associates (the “SDG Report”). The Authority supports the Minister’s review of the regulation of the public transport sector generally and welcomes the opportunity to comment on the SDG Report.

The principles of better regulation suggest that Government intervention in markets can be justified if it corrects market failure in a proportionate manner. Market failure can occur in markets where there are information failures, externalities or where firms have significant market power. There may also be a valid public policy rationale for intervention in markets such as equity etc.

The potential for market failure exists in the provision of public bus services typically because of externalities (e.g. congestion) and the possibility for information failure (e.g. ensuring safety and co-ordination problems). Given these potential market failures, it is not apparent that there has been any benefit to consumers, or the economy in general, from introducing barriers to entry and creating a monopoly.

Creating this degree of market power in the bus sector does not rectify the other potential problems but rather creates additional market failure associated with monopoly. It also erects a considerable barrier to entry in an industry that has very little (if any) scale economies and low sunk costs.

In the case of inter-regional (long-distance) services, the existence of market failure is less apparent and the proportionate regulatory response is likely to be more light-handed. Experience abroad has shown that countries have benefited from liberalising these markets. Recent research noted in the SDG report shows that deregulating inter-regional services can lead to a 50% increase in passenger trips.

In fact, many countries, including those that rely on social partnership models, are liberalising inter-regional bus service markets. Non-exclusive licences are used in inter-

regional markets in Norway, Finland and Italy and free-market competition in used in Britain, New Zealand and Sweden. Denmark also plans to implement free market competition and it has been proposed in Canada.

It is disappointing that this trend does not appear to be recognised in the SDG report. It is also worrying that the arguments made against recommending such a change are not well grounded. It is noted in the SDG report that Ireland compares favourably with the handful of comparator case studies on inter-regional services and, thus, the report suggests that it would be better not to liberalise. Apart from the small sample size of the case studies, this fails to consider the counterfactual that Ireland would most likely perform even more impressively if open competition were to be introduced.

In terms of regional services, a more liberal regime would improve the situation by further facilitating competitive entry. This approach would also highlight areas where public service obligations may be required. Local authorities (who are most likely to be informed) should have a role in identifying such services and organising the tendering to get the service delivered at a minimum cost. In doing this they could obtain guidance from the transport regulator. The submission argues against the suggestion in the SDG report that there be transport regulators appointed at a regional level.

In urban (provincial city) markets the externalities and co-ordination problems are such that there is a stronger case for intervention. However, as with other markets, any intervention should be proportionate and should not unnecessarily restrict competition. In line with experience elsewhere, the introduction of controlled competition is likely to satisfy both of these concerns.

Therefore, allowing open competition in bus services would appear to be the best approach unless specific reasons can be put forward for introducing controlled competition (which appears to be the case in urban bus transport markets) or where a particular public service obligation has been identified.

This submission supports the introduction of a single national transport regulator that would deal with all urban, regional and inter-regional public transport issues (including

taxis etc.). This will lead to significant cost savings and would minimise the potential for any one group to capture the regulator. Unlike the case of the aviation regulator, it is hoped that the regulator will have to duty to promote competition where it is in the public interest to do so.

Summing up, there is an emerging consensus that the current regulatory regime needs to be overhauled so as to address the expanding needs of consumers. Consumers require a more responsive, efficient and more integrated public transport system. It is well recognised that competition can play a major role in delivering these benefits to consumers.

The EU has expressed a desire to put the consumer at the heart of EU transport policy. The Lisbon Agenda included a call on Member States to introduce more competition in order to deliver a more efficient and consumer responsive public transport. The Competition Authority supports this process.

Change can bring difficulties for some small groups. However, the failure to embrace the necessary changes imposes ongoing costs on the wider society and also brings about the possibility that change will arrive abruptly through the Court system. The taxi example is instructive in this regard. It is better, therefore, to engage constructively in the change process, which will be to the benefit of Irish society generally.

1 INTRODUCTION

The Competition Authority welcomes the opportunity to comment on the Report on Regulation of Bus Services Outside the Greater Dublin Area, which was produced by Steer Davies Gleave in association with Fitzpatrick Associates (henceforth the SDG Report).

This submission is structured as follows. In Section 2 the principles of better regulation are briefly outlined. These are then applied to the bus transport sector outside the greater Dublin area. Section 2 concludes with a short summary of the main points in the Competition Authority's Transport Study as they apply to bus transport outside Dublin. Section 3 examines the SDG Report and highlights that much of the evidence presented supports the Authority's views expressed in the transport study. Section 4 evaluates the conclusions of the SDG Report. The submission concludes in Section 5 with some final comments.

2 PRINCIPLES OF BETTER REGULATION

Generally, markets work to ensure that the products that people want are produced. Competitive markets make supply more responsive to fluctuations or changes in consumer demand. An important benefit is that this makes the impact of good and bad decisions more obvious and allows errors to be corrected quicker. This encourages efficiency and innovation.

2.1 Why Regulate?

Markets may not always function properly and may not produce the best outcome. Where there is market failure state intervention may sometimes be justified. Market failure can occur for a variety of reasons including:

- the existence of market power;
- externalities or public goods; and

-
- information failures.

2.1.1 Market Power

Some parts of public utility industries, such as gas and electricity, constitute natural monopolies. Some form of intervention may be required to prevent abuse of market power. A sectoral regulator who determines the prices and other conditions surrounding access to the monopoly infrastructure is the conventional policy response. In this way market power can be controlled in an *ex ante* manner. Airports, the rail network and ports are good examples of natural monopolies in the transport sector.

More generally, market power is controlled generally in an *ex post* manner through the enforcement of competition rules.

2.1.2 Externalities and Public Goods

Externalities cause private and social costs and benefits to diverge, thereby distorting price signals. This results in the market producing too little of a good or service that has external benefits or, conversely, the market will overproduce goods and services that produce external harm. Private cars produce negative externalities in terms of increased congestion, pollution etc. that the car owner does not bear. A best policy response to these issues is congestion charging and taxation on petrol. In relation to goods or services that have positive externalities, a best policy response is to provide subsidies so that the market produces a greater amount of these goods or services.

A public good is a good that can be provided to more people at no extra cost. For example, all seafarers can enjoy the benefit of a lighthouse. In common with a positive externality the market system will under provide public goods. Therefore, public funding or production of a good may be justified.

2.1.3 Information Failures

For markets to function efficiently consumers must be able to make informed choices. If both parties to a transaction have very different information on issues such as quality,

safety etc. this may cause markets to fail. These types of problems can prevent markets for some types of goods and services from existing.

2.1.4 Public Policy Rationale for Intervention

In addition to market failures, governments may intervene in markets for equity or distributional issues. Redistribution measures invariably involve some efficiency costs, although the overall impact of delivering greater equity may be positive. If the burden is placed on other users through cross-subsidisation, a distortion is created in the market under consideration. Typically, less is purchased of the non-subsidised good or service with an inflated price whereas more of the subsidised good or service is purchased than would otherwise be the case. If such interventions are financed out of general taxation this generally has a less distorting effect on the economy. Such trade-offs should be explicit to allow for such choices to be based on an accurate estimate of the actual costs involved.

2.1.5 Rent-seeking

Sometimes governments intervene in markets even though there is no evidence of market failure or no sound public policy basis for so doing. It may do so in response to ‘rent seeking’ by pressure groups. Pressure groups are likely to try and conceal their true objectives by couching arguments for Government intervention in terms of market failure or on some other laudable public policy ground such as equity. Such behaviour misallocates resources within the economy at a cost to many to the substantial benefit of a few and results in certain market participants earning returns that far exceed what is justified by their productivity.

2.1.6 The Costs of Intervention

Government intervention may not always be capable of effectively addressing problems of market failure. Thus, evidence of market failure is a necessary but not sufficient condition for government intervention. It needs to be established that state intervention is likely to improve matters. Similar arguments apply where intervention may be justified on grounds of public policy. Many public policy problems do not have a perfect solution.

The challenge for policymakers is to find the option that contributes most to overall welfare. In some instances the appropriate solution may be to do nothing. Also the market may itself rectify an apparent market failure so that regulatory intervention is not necessary, an example is the provision of insurance services. This highlights the need for detailed analysis to identify both the precise nature of the perceived problem and the most effective way of addressing it.

2.2 Towards Better Regulation

Following the OECD's Regulatory Review Report of Ireland (April 2001) the Department of An Taoiseach is currently overseeing work on a national policy statement on better regulation. An important part of this process will be the work on developing best practice Regulatory Impact Assessments (RIAs) that are designed both to assist policymakers in deciding when to intervene and in what manner intervention is best implemented.

Undertaking a RIA exercise will improve the transparency of the policymaking decision process as well as government accountability, and ultimately, produces better regulation. To carry out a proper RIA the following the following steps will need to be taken:

- enumerate the public policy issue that is to be tackled;
- identify alternative options (including the default options which is choosing not to regulate) to achieve the desired policy change;
- ensure that a meaningful consultation exercise takes place;
- identify the most efficient policy option, including any alternative to regulation; and
- determine whether the benefits justify the costs.

An important principle of better regulation is that the need for regulation should be continually reviewed on a periodic basis to ensure that existing regulations continue to serve the public interest in a proportionate manner.

2.3 *Better Regulation Applied to Bus Transport Outside Dublin*

The motivation for regulation in the bus transport sector relies on the presence of specific market failures.

2.3.1 **Market Power**

Market power currently enjoyed by Bus Éireann arises from a legal monopoly. Specifically, Bus Éireann has market power in almost all of its urban centres outside the greater Dublin area, in certain areas for regional travel and it could potentially have a position of dominance in relation to inter-regional bus transport. Market power is likely to explain why a company has little incentive to reduce price, improve quality, increase route frequency, offer new routes or introduce new technology such as GPS systems¹, etc.

The market power enjoyed by Bus Éireann cannot be justified by a natural monopoly argument. SDG state in paragraph 6.7 (when looking at industries that have a natural monopoly element to them) that “it is difficult to see an equivalent in the bus industry, with the possible exception of bus stations in congested cities²”. The Report also mentions that many studies consider that there are very little, or non-existent, scale economies in the bus industry and concludes that the bus sector is not a natural monopoly (paragraphs 6.8 – 6.10). Therefore, regulation that forces the market to be supplied by just one player is not justified and may prevent the market from attaining a more efficient structure.

The bus industry is also marked by very low sunk costs, as the main capital item is buses, which SDG notes are widely available to buy and sell on reasonably liquid secondary markets³. This means that entry barriers would be low if entry were not

¹ In contrast, GPS systems have been introduced into the taxi market in Ireland with considerable success.

² This is the view taken in the UK where the 1985 Transport Act mandates access to bus stations. Although some countries do retain public ownership of these assets, overall the practice elsewhere is not so clear. Nonetheless, access to bus stations may act as a considerable catalyst to entry from smaller players. It is unlikely to deter large-scale players from seeking to build their own stations that are optimised to their own particular needs.

³ SDG Report, Paragraph 6.50.

prohibited by regulation. Bus Éireann's position of market power is underpinned by such regulations.

The SDG Report notes that mergers in the bus sector are largely motivated by concerns to protect (or enhance) market power. Thus, competition authorities have looked with a jaundiced eye on mergers in this sector. Attempts at monopolisation by mergers in the UK have been frustrated both by regulatory action and by new entry⁴.

2.3.2 Externalities and Public Goods

In contrast with the use of large numbers of privately owned vehicles, mass transit services involve lower burdens in terms of congestion, pollution and other negative externalities. This means that using mass transit services is relatively beneficial to society compared to many other modes of transport.

Mass transport helps to alleviate road congestion, particularly in urban centres. People who never use public transport benefit from this in a manner that is not captured by the market system. Thus, absent government intervention, public transport will be under-provided relative to the level that would be most beneficial to society. Thus, there is a market failure that needs to be addressed, particularly in urban areas.

People who are not regular users obtain a benefit from the existence of public transport, which is keenly felt on days when their normal means of transport fails. People would under-declare their valuation of the option of having a bus service (i.e. they would free-ride on normal users) so the government may have to intervene to ensure a sufficient amount of mass transport is provided.

In addition, there is what can be termed the "return externality". The provision of capacity at off-peak times (late night buses for instance) induces more people to travel to partake of business and leisure activities.

⁴ SDG Report, Paragraph 19.42. Further details on UK bus merger case can be found in the OFT report, The Effectiveness of Undertakings in the Bus Industry, OFT Research Paper 14, December 1997. This report outlines various measures that were imposed upon dominant incumbent operators, including control of prices and frequency of service control

In all of these cases, government subvention to bus companies to increase their level of service can be beneficial. However, it is important to stress that these externalities do not warrant the introduction of a monopoly. The most proportionate response is to provide subvention to all bus companies on a non-discriminatory nature. Currently, such intervention is done under the auspice of the rebate schemes available only to licensed operators.

2.3.3 Information Failures

Information failures are normally associated with buyers and sellers having different information. In this context, government intervention can be justified by the fact that the consumer of a service may not know whether or not they are obtaining an adequate and safe service. Similarly, co-ordination failure may be a result of a lack of information.

Safety is a potential information failure because consumers cannot know the quality of drivers and buses. Without appropriate safety regulation, competition could result in a “race to the bottom” in terms of quality. This failure justifies the role that governments play in relation to both driver licensing and in vehicle testing. It is open to the State to impose higher burdens on operators who wish to benefit from State subvention. The State can, in a system where any reputable company can obtain a licence for services, impose licence conditions in relation to safety. Failure to adhere with these should result in the suspension or revocation of the licence.

Another potential information failure in relation to bus transport relates to consumers being able to make informed choices. Bus transport customers, particularly in urban areas, often need to be able to plan complex, irregular journeys which may need to be facilitated by the central managing of information. The ability of customers to obtain such information and the ability of passengers to inter-change readily between services is a considerable benefit. To facilitate such complex journeys it is important that a system of integrated ticketing be initiated. Integrated ticketing may not occur due to a co-ordination failure. It is also not obvious that private firms (whose products may even be complements) will be able to agree on the modalities that would be required to implement

a sustainable system of integrated ticketing. In any case, such an agreement might produce anti-competitive effects that outweigh its benefits⁵.

Depending upon the degree of market failure, this type of failure could potentially be addressed by ensuring ticketing integration is a pre-requisite for competitive entry or by introducing some form of central planning, particularly in urban networks. Although a monopoly structure could potentially address this issue, this has not occurred to any significant degree in Ireland.

2.3.4 Public Policy Rationale for Intervention

In bus transport the main public service issues are⁶:

- Regional issues; and
- Equity and distributional issues.

Regional issues can be addressed by options such as providing subventions or tendering for services that are clearly identified as not being commercially viable, that fulfil some explicit regional policy requirement.

Equity and distributional issues can be addressed by providing targeted assistance to those identified as in need. Currently, assistance is provided by issuing free travel passes to groups such as pensioners, ensuring reduced fares for school children and providing low-floor buses for people with disabilities. Financial support in relation to these features is given directly to Bus Éireann and licensed operators.

In relation to financial assistance, the Government must decide to whom subsidies should be provided, consumers or producers. This typically depends upon the costs of

⁵ The test for this is formalised in Section 4(5) of the Competition Act, 2001.

⁶ In the SDG Report much mention is made of Universal Service Obligations (USOs) in the bus transport market. USOs normally relate to obligations to supply a given level of service to everyone in society. Sometimes this is mandated to be provided at a uniform price. An example is the provision of electricity. Almost everyone is supplied with this service and is charged at the same rate without regard to substantial differences in costs. A more appropriate notion in the case of bus transport is that of public service obligations, where it is not intended that all persons be supplied with the service without regard to cost. This is the case in relation to natural gas in the State. However, once a household is capable of being supplied, some obligations may be put on the company in terms of service quality, prices, etc.

administering any funding. For instance, it may be simpler to subsidise a bus company directly to service a specific area where there is a large number of disadvantaged consumers. Alternatively, it may be more straightforward to provide specific individuals with assistance if they are dispersed across a large area and cannot be easily differentiated from other users. Either of these options allows market failure to be addressed without introducing a monopoly structure.

2.4 The Competition Authority's Transport Study

A number of the issues concerning the regulation of bus services outside Dublin were considered by the Competition Authority in our study of the public transportation sector released in 2002. The terms of reference for the transport study were:

“to undertake a study and analysis of the licensing restrictions and other barriers and restrictions to entry into the rail and bus passenger transport market within the State, and their impact on delivery of passengers by intercity rail, intercity buses and urban buses.”

The study made a number of observations, which remain pertinent. These include the fact that benefits that could easily have been provided in terms of service integration and co-ordination have not been exploited. Given the majority of public transport services are provided by CIÉ subsidiaries, a high level of integration would be expected between its services – however, considerable scope remains for further co-ordination. Sufficient integration could be provided in a more liberalised environment if a regulator specified it as a prerequisite for entry.

In relation to buses, the Authority found that Bus Éireann did not require a license to operate. Moreover, the Government is simultaneously shareholder, regulator and policymaker in public transport services. This would appear to be the type of environment in which regulatory capture is very possible. Other issues the study raised included:

- a lack of transparency regarding Government subsidies as well as a lack of access to these subsidies;

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- a lack of access to bus stations, although it was not clear whether stations would constitute essential facilities under competition law (this would need to be done on a case-by-case basis); and
 - entry (in terms of the number of firms) had been largely confined to remote regional areas not served by Bus Éireann.

Regarding SDG's Report, the following conclusions in the Authority's transport study are pertinent.

- Regulation should be minimal, proportionate, linked to clearly defined objectives and located as close as possible to the market regulated. The regulatory function should also be separate from the operation of services.
- If state ownership or control of transport companies is to be continued, the rationale for such ownership should be clearly set out.
- The development of the market for road passenger transport by bus/coach in the State has been inhibited by regulatory practices, which have resulted in limited competition in many circumstances.
- It is not clear that any form of restrictions on the licensing of bus operators, other than those required to ensure the safety of passengers, is required in the inter-regional market.
- Consideration should be given to the horizontal separation of Bus Éireann – for instance, into urban, inter-regional and regional services – to avoid the risk or perception of cross-subsidisation. This would also improve cost accounting.
- Claims for subsidies should be rigorously evaluated, since experience in other industries has shown that not all such claims are justified. The introduction of competition should help identify which routes or services are genuinely loss-making and which are profitable (i.e. this would reduce cross-subsidisation)
- The organisation of school bus services should be re-evaluated, competition could be promoted by offering contracts on a regional basis.

3 THE SDG REPORT

The terms of reference for the SDG Report was to produce recommendations for a regulatory framework, which meet the objectives of the State's public transport policy⁷. The specific objective of the study was to produce recommendations for a regulatory framework that will:

- promote the provision of high quality services to customers in terms of price, frequency, reliability and comfort;
- ensure transparency as to the value for money being obtained and the services being provided in return for State subsidy; and
- provide for appropriate integration of public transport services (i.e. integration of bus services and integration between bus and rail services).⁸

Before proceeding the submission presents some background information and context that set the stage for the detailed examination of the SDG Report.

3.1 *Background to the SDG Report*

In this section a brief overview of the bus transport sector in the State is provided, along with developments at an EU level and the issues raised by the recent Nestor Court case.

3.1.1 **Bus Transport in the State**

A brief description of bus transport outside of Dublin is included in Appendix One. This description includes information from the Household Budget Survey, Bus Éireann's annual accounts and the SDG Report itself.

To summarise, it is apparent that Bus Éireann is the main player in the three markets identified. Although it faces some competition in the inter-regional market, the level of competition varies significantly across different routes. With respect to funding, Bus Éireann has received grants, which have usually more than compensated its loss-making

⁷ <http://www.transport.ie/transport/index.asp?lang=ENG&loc=469>

⁸ Terms of reference as stated in the tendering document for the study.

activities. However, in 2001 Bus Éireann operated at an overall loss after receiving a State grant, despite the fact that the amount of these grants have steadily increased over the previous five years.

3.1.2 EU Developments

The Commission's White Paper, European Transport Policy for 2010: Time To Decide, states that consumer oriented service will shape the Commission's suggested policy towards transport over the next decade.

Closely related is the process of liberalisation of the mass transport sector supported by the European Council. At the Lisbon summit in March 2000 (where the EU set out an agenda to become the most productive economy in the world), the European Council asked Member States to speed up the liberalisation of the transport sector.

In September 2000, the Commission submitted a proposal for a Regulation concerning public service requirements and the award of public service contracts in passenger transport by rail, road and inland waterways⁹. The Commission's objectives in relation to this proposal were:

- to stimulate more efficient and attractive public transport through the use of controlled competition and other measures; and
- to promote legal certainty for authorities and operators.

A Commission survey of 30 large cities in the EU found that those using controlled competition attracted the most new passengers and achieved the best financial performance. The current draft of the Regulation would allow exclusivity up to a maximum of 8 years in the bus sector.

In framing the proposed Regulation the Commission stressed that competition principles should apply generally. Recitals to the proposed Regulation state that competent authorities should ensure that their actions are in compliance with those rules and principles of the Treaty that aim to ensure equal treatment and fair competition between

⁹ COM 2000/0212

undertakings. It is further stated that “all operators legally established in a Member State be guaranteed effective access to the public transport market of that State in a transparent way and without discrimination.”

The Commission further noted that as Community competition law is increasingly applied to the public transport sector many issues are likely to become contentious, particularly exclusivity. The Commission notes that the Courts are considering some cases in the area. Thus, the Commission’s view was to adopt the current proposed Regulation as the alternative would be reform based solely on the basis of Court judgements.

3.1.3 The Potential for Legal Action

The Commission’s draft Regulation explicitly proposes to manage the transition rather than wait for the Courts make a determination. The recent experience of the taxi market, where the vested interests resisted all but the most limited liberalisation, is salutary in this respect.

An appetite for competition challenge from private operators is seen in the recently settled Nestor Case, about which considerable confusion still exists. Following initial court hearings, a settlement was reached. With its consent, the case against Bus Éireann was struck out. The Irish Independent reported (25 October 2001) that 19 licences were subsequently awarded to Nestor to run daily services between Galway, Dublin and Dublin Airport.

3.2 *The Methodology Used in the Report*

The terms of reference stipulate a number of tasks to be undertaken by the consultants. They can be summarised as:

- to identify distinctive segments of the bus market;
- to provide an economic analysis of options for future regulation of the market segments identified (setting out the anticipated advantages and disadvantages of

each, having regard to the objectives of the public transport policy and the specific objective of the study);

- to investigate the effectiveness of regulatory frameworks based on case studies;
- to consult interested parties (a list of parties to be consulted was provided); and
- to make final recommendations.

The terms of reference also provide a list of evaluation criteria: economic performance, productivity and patronage, fares, value for money, service quality, integration, social cohesion, dealing with change, economic development, environmental criteria, and availability and quality of data.

3.2.1 Analysis of the Evaluation Criteria

Many of these criteria are directly associated with the benefits normally associated with competition. In the bus transport sector, competition can deliver improved economic performance, higher productivity and patronage (relative to previous trends), value for money in fares (including the reduction of cross-subsidisation), improved service quality, more innovation, and could ensure that bus transport plays a role in making Ireland a more productive society. Many of these benefits are evident in the case studies selected in the SDG Report.

Furthermore, more appropriate, proportionate regulation of the competitive process could deliver better ticket integration, social cohesion, quality data and provide environmental benefits.

3.2.2 Case Studies

Case studies can be useful in identifying different institutional frameworks and their likely pitfalls. They can assist in understanding the incentives created by a particular regulatory framework and are helpful for designing a corrective mechanism. However, case studies do not necessarily provide a robust basis upon which to draw general conclusions.

A thorough analysis of more empirically based analysis is generally more helpful in analysing the main drivers of changes and underlying general findings, as such analysis is

less prone to case specific factors. Much of the relevant literature investigates the efficiencies in the production of bus services under different regulatory frameworks. A more extensive examination of some of the relevant literature is included in Appendix Two.

3.2.3 Consultation

The principles of better regulation focus on the benefits of wide consultation. However, if consumers and private bus operators have not been fully consulted, as seems to be the case with the SDG Report, it is unlikely that the full range of views can be considered. Moreover, consumers' responses to surveys may be conditioned by low expectations of current services. Indeed, a group rarely contacted in this area is those who do not use buses (for example, those who have already switched to other modes of transport). The perspective of these groups would also provide important insights into consumer behaviour.

3.3 *Commentary on SDG's Analysis*

In examining SDG's analysis certain themes emerge. These are dealt with in the following section.

3.3.1 The rationale for State ownership and/or control should be clarified

The potential conflict of interest arising from the fact that the State acts as regulator, shareholder and policy maker in public transport services and the importance of transparency and accountability in this area are highlighted as key issues in the Report (paragraphs 1.10 and 4.1). Any conflict of interest is a concern because it could increase the likelihood of regulatory capture of the Department by the main operator. Evidence of this includes the strong criticism by private operators of licensing procedures, both in

terms of time taken to receive a decision and the lack of transparency regarding the criteria used to award a license¹⁰.

3.3.2 The use of State funding should be clarified

A number of comments in the Report support the view that there is not enough transparency with regards to the funding of the Government's public transport social objectives. For instance, the Report states that Bus Éireann receives funding to meet "public service obligations" that appears to related to maintaining regulated bus fares rather than any explicit service requirements¹¹. This lack of immediate connection between the subvention and specific public service obligations means that the subvention may be used for purposes for which it was never intended, including lowering fares on routes where Bus Éireann is facing competition.

Of the €29m that Bus Éireann paid for 208 buses in 2001, €6.5 million came from the State via the National Development Plan, equivalent to approximately 46 buses (paragraph 4.22). However, Bus Éireann claimed that the Government had initially agreed to provide funding for 148 buses, leaving Bus Éireann to fund the remainder out of reserves and increased debt.

The use of subsidies should also be rigorously evaluated because experience in other industries has shown that not all claims for subsidies are justified. Therefore, the production of proper regulatory accounts by all firms that receive public money to meet public service obligations is important in maintaining public and business confidence in the system.

3.3.3 Potential integration benefits of a monopoly have not been fully realised

The Report provides some examples of a lack of integration between Bus Éireann's services. In particular, paragraphs 13.6 and 13.7 detail specific integration issues, such as

¹⁰ SDG Report, Paragraph 3.5. It would been useful for the Report to provide further details regarding the licensing process and to have elaborated on the criticism of the licensing regime emanating from private operators.

¹¹ SDG Report, Paragraph 4.8.

a lack of co-ordination between routes and a lack of integration between urban bus services and inter-regional/regional bus services, in Limerick and Galway.

3.3.4 Benefits of increased competition and market liberalisation

The Report provides evidence that where competitive entry has been facilitated via market liberalisation, markets have developed to consumers' benefit as well as, in some cases, to reduce the need for state assistance. This is consistent with the general findings of the Authority's Transport Study, these being that the regulatory regime has inhibited the development of the bus transport sector in Ireland, and that regulation should be minimal, proportionate and linked to clearly defined objectives. The relevant case studies refer to the three markets defined earlier. In relation to urban markets, the findings include:

- Various studies of Denmark, Norway and Sweden have suggested that tendering in urban networks have reduced operating costs by 12 –35 percent in real terms between the mid 1980s and the mid 1990s (paragraph 13.12);
- Tendering out five year contracts for urban areas in New Zealand has brought about improvements including a six percent increase in the number of trips between 1990 and 1998 (box, page 132);
- In Cambridge, England, Stagecoach re-launched its local network and generated a 25 percent year-on-year increase in patronage (paragraph 16.10).

In relation to regional markets, the findings include:

- The threat of tendering has been used to negotiate for efficiency improvements and cost reduction in Norway. This has brought about significantly lower costs in real terms (box, page 62);
- In Finland (a country with similar population patterns to Ireland) the majority of bus services outside the main cities are privately provided without significant subsidy (paragraph 14.3).

In relation to inter-regional services, there may be no need to restrict the licensing of operators other than to ensure safety standards. Evidence supporting this approach includes:

- White (1999) and ECMT (1999) suggest that deregulating inter-regional services can lead to increases in demand on competed inter-city coach routes of up to 50 percent (paragraph 6.55);
- Non-exclusive licences are used in the inter-regional markets in Norway, Finland and Italy and free-market competition is used in Britain, New Zealand and Sweden. Denmark plans to implement free market competition and it has been proposed in Canada (paragraph 18.5).

SDG comments suggest that although deregulation in Britain is often criticised, this liberalisation may have actually reversed negative trends in bus transport in these countries. In particular, the report mentions:

- Since deregulation, bus-kilometres outside London and the other metropolitan areas, have increased by over 30 percent (including an eight percent rise in the last 10 years) compared with a 18 decrease in kilometres in the ten years immediately prior to deregulation (paragraph 6.57);
- Although regional bus patronage outside London and the other metropolitan areas falling 16 percent between 1990/91 and 2000/01, it had fallen by 30 percent over a comparable period prior to deregulation, 1975 to 1985/86. Furthermore, deregulation was successful in achieving the Government's stated aim of reducing the level of subsidy provided for bus services¹² (paragraph 6.63).

The SDG Report also expresses doubt that equivalent subsidy reductions could have been achieved under alternative regulatory models without similar declines in patronage.

¹² In relation to the often-mentioned instability in services in the UK it is notable that in at least one it was the predatory actions of the incumbent that was responsible for instability in services. The OFT investigated and found that the incumbent had taken anti-competitive action. See The Effectiveness of Undertakings in the Bus Industry, OFT Research Paper 14, December 1997.

Scotland is an interesting country for comparison given its similarities with Ireland. Of relevance is:

- The case study of the Highlands notes urbanised areas have seen improved frequencies and significantly reduced journey times, whilst services in rural areas have been maintained with improved reliability (chapter 8);
- There was a “massive” increase in inter-regional services in the five years following deregulation (paragraph 19.9);
- The National Federation of Bus Users consider deregulation delivers important benefits to consumers in terms of higher frequencies, lower fares and faster journey times (paragraph 19.49).

A further study, not referred to in the Report, by the TAS Partnership Ltd (2000)¹³ found that bus kilometres travelled increased by an average of one percent per annum in the ten years to 1998. It also found that demographic trends such as population decline, fewer children and increased car ownership can explain reduced bus use (which has declined mainly in urban areas that experienced industrial decline). Overall the study showed that profitability has increased and smaller operators have emerged as niche providers in more remote areas in response to withdrawal by larger operators.

3.3.5 Points of dispute

There are some specific points raised in the SDG Report that raise concern. Specifically:

3.3.5.1 *Potential benefits of liberalisation to Ireland*

The Report suggests that the benefits of liberalisation could be negated if private operators currently providing a service in regional areas where Bus Éireann does not, move to servicing more lucrative opportunities after liberalisation (paragraph 7.19). However, if the original route was profitable prior to liberalisation, it would remain so and thus an incentive to provide the service would still exist. Should there be a severe

¹³ Development Department Research Programme Research Findings No.115, Trends in the Local Bus Market, by TAS Partnership Ltd for the Scottish Executive, www.scotland.gov.uk/cru/resfinds/drfl15-00.asp.

shortage of bus service resources, this concern could be valid, however, as the Report notes, buses are readily available, meaning such a shortage is extremely unlikely. Moreover, if an opportunity is more lucrative elsewhere this would suggest that the total benefits to consumers of providing this service elsewhere is larger than the benefit to existing consumers. If this was not the case, the amount the operator could receive from consumers elsewhere would not be likely to exceed the amount gained from the original consumers, providing no incentive for the operator to move the service.

The Report states that Bus Éireann has experienced consistently higher patronage growth in inter-regional services than the companies investigated in the case studies (paragraph 21.3). It also notes that the per capita use of inter-regional services in Ireland is much higher than in areas covered by the case studies, although it fails to account for the possibility of specific factors that may relate to the Irish market, such as the relative lack of train services. SDG conclude that “it would be unwise to take action which could destabilise the network or undermine passenger confidence”. Such an assertion fails to fully consider the counter-factual case of deregulation of inter-regional services. Deregulation of these services has produced significant benefits everywhere, and it is very likely that the Irish performance could be even more of an outlier if inter-regional services were deregulated.

3.3.5.2 *The use of Tampere, Finland, as a case study*

The Report mentions the case of Tampere in Finland (chapter 14) as a good example of a public sector monopoly provider. It is noted that customer levels of satisfaction are reasonably high. However, patronage has fallen by over 33 percent in the last 20 years. Although demographic trends could influence these figures (no evidence is provided), it is not clear that this should be considered as an unqualified success. It may well be that by only surveying remaining customers, the opinions of the significant numbers who have abandoned their services altogether, perhaps because of dissatisfaction, are being ignored.

3.3.5.3 *Cross-subsidisation*

The Report does not appear to acknowledge the costs of funding public service objectives by internal cross-subsidisation¹⁴ and instead appears to support the continued existence of charging prices above the competitive market level for some consumers. However, using revenue collected from general taxation is typically regarded as a more efficient approach¹⁵. This is because cross-subsidisation distorts consumers purchasing decisions and can also allow inefficient entry, that is entry can occur in the profitable segment of the market, even though a new entrant may have higher costs than the incumbent. Additionally, entry may be desirable in the loss-making segment of the market, but cross subsidies may make it unprofitable and thus unattractive for new entrants, even though the new entrant may be more efficient and may therefore be capable of providing services in the loss-making segment of the market at lower cost than the incumbent. Cross subsidies can, therefore, create potentially large welfare losses and could even serve to reduce, rather than increase, service provision.

4 COMMENTS ON THE CONSULTANTS' CONCLUSIONS AND RECOMMENDATIONS

The SDG Report advocates the establishment of a new regulatory system with a number of market specific measures. This submission focuses on the most contentious competition issues raised in the Report.

¹⁴ See SDG Report, paragraphs 6.58, 7.20, 18.13, 18.16, 24.27 and 24.28. The Report refers to the introduction of competition on profitable routes as “cherry-picking” and appears to consider this a negative effect. However, competitive entry on these routes that results in reduced prices would be beneficial to consumers and, therefore, highly desirable.

¹⁵ A rare exception to this general approach is if there are network externalities. In this situation, an existing consumer may benefit from an additional consumer using a service. Therefore, charging the first consumer an additional amount to “subsidise” an additional consumer may more accurately reflect the benefits that accrue to each consumer.

4.1 *Comments on the SDG's' Overall Conclusions*

The overall conclusions refer to a number of general public transport objectives as a justification for regulation, public service obligations and public funding for some bus services.

The SDG conclusion that the nature of the regulatory regime is not the primary influence on service provision but rather that it is the level of public subvention that is critical, is not well established. For example, our examination of the inter-regional market suggests that free entry with quality controls and without any subsidy will deliver a much better service than currently exists. It is striking in the case studies that in contrast with Bus Éireann other comparator companies received no operational deficit funding, did not receive any fuel duty rebates (or substantially lower rates of rebate) and they did not receive capital grants.

A related point is the claim that Ireland performs poorly in terms of supporting bus services in provincial areas. A clearer demonstration of this, when consideration is taken into account of the supports that the Expressway services receive, would have been useful. It appears that there is a cross subsidy of regional services by inter-regional services (whose case for receiving subvention is considerably weaker on public service grounds). This has the potential to distort competition in both regional and inter-regional markets.

The SDG report comes to the conclusion that there is “ a need for a more transparent system, so that public service obligations are consistently defined, and that the cost of meeting them is explicitly recognised¹⁶.” This can be achieved in a more liberalised environment where companies that receive subventions (after having been selected by a tendering process) would be required to keep separated accounts. This would make explicit where subvention was required and where any potential cross subsidy arises.

The Report notes that the market may fail to deliver the socially desirable levels of service in provincial areas. Certainly, this is likely to be true in certain circumstances.

¹⁶ SDG Report, Paragraph 24.9.

However, these facts need to be established on a case-by-case, service-by-services basis. In absence of regulatory barriers to entry, the lack of a particular service is likely to show that no one is able to provide the service on a purely commercial basis. This may, in turn, justify the need for public funding. However, it first needs to be established that the market will not deliver the service. This may require some experience with a much more liberalised regime than the current one.

4.2 Comments on the Proposed Regulatory Structure

The Report recommends the establishment a two tier regulatory system comprising of:

- A central body called the National Passenger Transport Authority, independent of the Department of Transport which would address policy matters of national nature, including administration of concessionary travel, allocation of public funding based on the assessment of the population transport needs; and
- Two Regional Passenger Transport Offices (RPTOs) that would be responsible for implementing policy, taking into account the relative costs of serving the need of the population.

The Report also proposes that the Department of Transport would remain responsible for setting the overall framework within which the regulator would operate. The Department would also be responsible for safety and financial standards for bus operators. There is confusion as to where the exact responsibility for policy would lie, as the SDG report seems to suggest a general policy role for the NPTA. It is standard practice for the Minister to retain this role in the standard Minister-regulator relationship.

If functions that are currently provided by other Government Departments are to be moved to a body such as the NPTA it is imperative that the costs and benefits of this are assessed. For instance, in terms of having the data available to implement a concession scheme for older persons the existing Government department is likely to have a considerable advantage in terms of systems etc. Similarly, moving the processing of rebates from the Revenue Commissioner's and the school schemes from Education would

be problematic. Such tasks are not the core competency of most regulatory bodies and would require substantial duplication of systems that currently in existence elsewhere.

It would be optimal to ensure that the body that dealt with public transport in the GDA was also involved in looking at the transport systems of the provincial cities. The issues considered would be identical. In line with best international practice it would be useful to consider integrating the regulation of other public service vehicles such as taxis etc. into the same office. Many of the issues are similar and the wider role would both save costs and lower the probability of regulatory capture.

The regulator should also have a duty to support competition and should have to conduct regular reviews to see if interventions remained necessary. In this manner, the regulator should overtime end up only dealing with issues where the market fails to deliver what society needs and with clearly defined public service obligations.

It is not clear why the role of implementing policy in a regional context could not be achieved in a less cumbersome manner than having two RPTOs. Many of the needs at a regional level are much more likely to be known at a much more devolved level. It is likely that a structure such as that proposed would rely to a large extent on the basis of suggestions of local authorities etc. Thus, it is likely that having RPTOs is likely to be overly bureaucratic. It may be better to have local services devolved to local government, with clear guidelines of what their role is to be being given by the national transport regulator.

4.3 Comments on the Recommendations for Specific Markets

4.3.1 Inter-Regional Network

The SDG conclusions and recommendations on the inter-regional routes cause concern. The statement that:

“It is important, from the perspectives of social cohesion and regional economic performance, that these social benefits are not sacrificed in the pursuit of

theoretical benefits of open competition, which may prove short lived or serve narrow sectional interests¹⁷.”

fails to square with the facts as presented by SDG. Abroad there are very few (if any) public service obligations imposed on inter-regional routes. The SDG case studies show that they mostly are run on a commercial basis in an open market framework. The benefits of this model on inter-regional routes were noted in Section 3. Moreover, competition is normally associated with enhanced consumer welfare, whilst the absence of competition (where it might otherwise exist) is normally associated with serving narrow sectional interests. The fact that numerous countries have moved to a deregulated regime and that more are planning to do so shows that the benefits of competition in inter-regional services are becoming more recognised.

Consistent with the approach of undertaking a regulatory impact assessment, it is useful to investigate other options that could address any properly identified market failures. For instance, the provision of an integrated system to facilitate multi-leg journeys and public of information may be best left to the operators to organise, subject to compliance with competition law. Furthermore, no evidence was presented on the proportion of travellers on inter-regional buses that would require such a facility.

SDG propose the set up a company, *Expressway Management Company*, independent of Bus Éireann. This company would issue service licences but not own or operate services directly. Instead, the company would contract with Bus Éireann and as SDG put it “potentially” with other independent operators for specific services. Private bus companies could also choose to operate independently, outside of the Expressway system. In addition, this company would manage infrastructure such as bus terminals, and would “manage and promote an integrated national network with through ticketing and co-ordinated services, building on the current Expressway base.”¹⁸.

Where services are profitable and where there is already an element of competition, it is unclear what market failure is being addressed by this proposal. Thus, no convincing

¹⁷ SDG Report, Paragraph 24.26.

¹⁸ SDG Report, Paragraph 24.30.

argument is advanced for such a regime. For example, the Dublin-Galway route has three operators and there is no indication that this has adversely affected the provision of other inter-regional services. Barrett (2000) reported that Bus Éireann's fares on the Dublin-Galway route were considerably lower than on the Dublin-Cork route where it faced no competition. Similarly, there is no indication that competition from "travel clubs" has undermined the Expressway network.

According to SDG, all of Bus Éireann's Expressway routes are profitable and "travel clubs" and private licensed inter-regional routes are also likely to be profitable given that they receive no State subvention. In effect, a semi-competitive market has emerged and no convincing reason has been put forward for trying to reverse this trend. There appears to be no valid reasons for not regularising the situation in respect of "travel clubs" and permitting full competition.

Furthermore, the proposal could impact negatively on incentives to enter the market. The position of the Expressway Management Company could act as a deterrent to new entry. Therefore, significant regulatory oversight would most likely be required, as this company could be in a position to take advantage of a high degree of market power.

The Report envisages that one of the functions of the Expressway Management Company would be to coordinate timetables with a minimum gap of 15 minutes between departure times. The purpose being to avoid buses racing each other to bus stops along a route to pick up passengers. However, it is not clear that such behaviour would be witnessed on inter-regional routes, as it is unlikely to be economically viable to run parallel services. Commercial sense is likely to drive bus operators to operate services at reasonable intervals, as this is likely to maximise patronage for both operators, as is shown in Oldabe (1998)¹⁹.

In light of the Commission's thinking in framing the new regulation, consideration must be given to how robust such a system would be to legal challenge under competition and other grounds.

¹⁹ Local Bus Deregulation and Timely Inability, Discussion Paper EI/21, London School of Economics, 1998.

4.3.2 Urban (Provincial City) Network

The SDG Report recommends that operators should deliver urban services on the basis of exclusive franchise contracts awarded after a competitive bidding process. The consultants envisage that the contracts would be management contracts and state that “there are clearly benefits from having urban networks planned as a single entity”²⁰. While this statement may be true, further investigation is required to establish it conclusively.

The Report also states:

“[D]esired standards of service for each city should be specified by the National Passenger Transport Authority in light of local land use and transport strategy”²¹

It is not entirely clear who should organise the provision of these services. Bus services are of local interest and there may be strong advantages in decentralising the decision making at a local level either to local authorities or an association of local authorities. SDG noted that there might also be operational synergies as the relevant local authorities are often responsible for traffic management. An important theme in devolving power to local authorities is that proper guidance is given from the centre and that consistent and fair procedures are followed.

There may be a concern about the small size of many private operators that would appear to preclude them from taking on a franchise for a city and arguably limits the potential for “competition for the market”. However, this view is based on experience under the current regime. Barriers to entry into the bus market are actually very low and competition/controlled competition will allow the most efficient private operators to expand readily.

If SDG’s proposal is implemented particular attention should also be paid to contract length, as this can operate as a barrier to entry. The EU rules will only specify a maximum duration. It is always open to the Minister to choose a shorter contract term, if

²⁰ SDG Report, Paragraph 24.43.

²¹ SDG Report, Paragraph 24.50.

he so wishes. Specific contract terms are also critical in ensuring that operators have incentives to extend services, operate efficiently and innovate. Contract monitoring and enforcement is also important.

SDG also outlines some concerns, in particular that the relatively "small scale and limited number of opportunities in Irish provincial cities may deter foreign bidders, given the time required to understand the bidding process and relevant legislation"²² and that it "is conceivable that few companies would pre-qualify and Bus Éireann could emerge as the sole bidder for the city contracts"²³. These comments are unfortunate as they could send negative signals to potential entrants and are based on speculation.

To further facilitate entry it may be necessary to re-allocate a number of vehicles previously provided to Bus Éireann free-of-charge under the National Development Plan. Several transfer schemes are possible including free redistribution, hire and purchase or direct sale.

The recommendation that there be accounting separation of urban services from Bus Éireann is to be welcomed. This measure would provide greater transparency and would dramatically reduce the opportunity to cross-subsidise.

4.3.3 Regional Services

SDG's view on regional services is that the principal choice is between exclusive area contracts and a liberalised form of licensing, with support for non-commercial activities provided on a route specific basis. SDG come down on the side of "a liberalised licensing regime, short of full deregulation, could offer the best of both worlds."²⁴

The SDG Report also indicates that more subsidies per head are needed for local regional services than for urban services²⁵. However, many regional services are currently provided without subsidy. Rather than assuming the need for subsidisation,

²² SDG Report, Paragraph 24.54.

²³ SDG Report, Paragraph 24.56.

²⁴ SDG Report, Paragraph 24.62.

²⁵ It is not clear whether SDG are referring to subsidy per head of population in an area or subsidy per head of user.

funding requirements should be assessed on a case-by-case basis. Indeed, a period of open competition would identify routes that did not require subsidy. Routes that local interests (the local authority perhaps?) thought might be socially beneficial could be put out to tender (with the firm requiring the smallest subsidy winning).

However, SDG recommend a two-phase implementation process. Initially, operators would make offers, or “bids”, outlining their proposed service. If several operators offered overlapping services, the regulator would negotiate a regular service pattern, or reasonable intervals, between services. As was mentioned above this is not likely to be an issue that requires a regulatory intervention. In addition, the operators would have to commit to providing services for a minimum period.

In the second phase, the regulator would put out to tender perceived ‘gaps’ (areas or times where no service is offered on a commercial basis). These “supported” contracts would be allocated on a “net cost” basis.

It is also unclear from the SDG Report what criteria would be used toward both commercial and supported contracts. The commercial contracts seem to be awarded on a “beauty contest basis” with some elements of negotiation. It would likely be much more efficient (in the context of the SDG model) that a competitive tendering system was used. This would ensure efficient delivery and would minimise the scope for legal action by disappointed operators. SDG envisage supported contracts being awarded on a net cost basis. If the SDG suggestion were to be acted upon these should also be tendered for on a competitive basis, with the firm requiring the least subsidy to provide a certain defined level of service winning.

5 CONCLUDING THOUGHTS

The main points in this submission are the following.

Bus transport has no natural monopoly elements. Absent regulatory and legislative barriers, there are no significant barriers to entry. The market system will under-provide public transport due to externalities. Governments intervene by subsidising the supply of

public transport. The market system is not likely to provide sufficient guarantees on safety. This requires that governments regulate both vehicle and driver quality. The market system may not provide sufficient co-ordination and integration in areas where it is critically required such as cities. Thus, a regulator is warranted to ensure that these issues are tackled.

Questions of public service obligation in the transport sector normally revolve around regional and equity/distributional considerations. The provision of public service obligations is best achieved via competitive mechanisms that ensure best value for money.

None of the above provides support for introducing or maintaining a monopoly.

Against this background more and more states are re-defining their role in relation to public transport and moving away from being regulator and main market participant to setting the stage for regulation of the behaviour of independent operators in a competitive environment.

Where appropriate, as with inter-regional services, states are moving to a completely de-regulated regime (apart from controls on driver training and vehicle safety). In other cases, as in cities where considerable benefits from co-ordination exist, the introduction of controlled competition for the right to an aggregation of routes over the medium term is the norm that is being adopted.

There is considerable evidence that such initiatives bring benefits to consumers and society generally in terms of better value for money and improved services (particularly in terms of innovation and the adoption of technology). This submission draws on data contained in the SDG report that supports this view.

There are compelling reasons to completely liberalise the inter-regional bus market. Yet, the SDG report does not favour this option. This submission argues that this is a mistake, which is based on flawed reasoning and a failure to take into account the benefits that are known to have accrued elsewhere. The list of countries that have moved (or are in the

process of moving) in this direction grows annually. The Scandinavian countries, which are noted for their comprehensive public services, are at the vanguard of this movement.

There are also some concerns about the proposed regulatory structure, particularly in relation to the second tier regulators that would operate at a regional level. This is unlikely to be an efficient response as local issues are best tackled at a more localised level. The regulator's office should have responsibility for public transport generally throughout the entire State and should extend to taxis etc. This would lead to significant cost savings and minimise the potential for any one group to capture the regulator. It is hoped that the regulator would have a duty to promote competition where it is in the public interest to do so.

All of these points suggest that the current regulatory regime needs to be liberalised so as to promote competition in the interests of the wider society. This will lead to better services and place the consumer at the heart of transport policy. More and more countries are adopting this agenda in relation to transport. The EU Commission in supporting the Lisbon agenda is proposing to introduce competition/controlled competition to stimulate more efficient and consumer responsive public transport.

Failure to grasp this opportunity for change not only deprives a country's citizens of improved public transport but also runs the risk of the system being overturned by Court action. The example of the taxi market is instructive in this regard, where resistance to all but cosmetic liberalisation was negated by a decision of the Court.

APPENDIX ONE: BRIEF DESCRIPTION OF BUS TRANSPORT OUTSIDE THE GREATER DUBLIN AREA

Spending on buses

The Household Budget Survey shows that spending on buses is strongly associated with income²⁶. Elderly persons predominate in the lowest deciles in terms of income and they obtain free travel (with some restrictions) so there is not a one-to-one relationship between spending and usage at all income levels.

Urban households spent a little over twice that of rural households. This may be due to much better provision of public transport in urban areas alongside with differences in preferences and demographic characteristics, such as car ownership, etc. In any case, 67 percent of all spending on buses came from urban households, most of which can be assumed to be spent on urban bus services.

During the survey period (in 2000) the average Irish household spent the equivalent of €3.29 per week on bus fares. Controlling for household size this equates to about a euro per person per week.

Also notable is that there are currently 583,000 travel passes in existence (this is seen as a over-estimate as some holders would have become deceased) addressing equity and distributional issues. As a result, Bus Éireann, and 118 private bus companies receive payment under the free travel scheme. The cost of the scheme was €42.8m in 1999, €44.8m in 2000 and €46.3m in 2001²⁷.

Bus Éireann output and finances

The submission has compiled some information on Bus Éireann's services from their last five published annual reports.

²⁶ These data are from the Household Budget Survey 1999-2000. The preliminary results are available from the Central Statistics Office at www.cso.ie.

²⁷ The Report notes that the basis for the free travel scheme rests on surveys undertaken in the 1970s (paragraph 4.12).

There is a small increase (six percent) in the number of passenger journeys on Bus Éireann's provincial city services over the five years to the end of 2001. Against the backdrop of the trend in general economic activity during this period this is a small increase. It does correspond, however, into a 32 percent increase in the distance travelled by Bus Éireann's provincial city services. This may reflect an increase in the number of buses being deployed or routes being extended into more remote areas etc.

	1997	1998	1999	2000	2001
Passenger Journeys (in 1,000s)					
Provincial city services	18,938	18,900	18,731	19,156	20,051
Other Scheduled services	18,499	18,610	19,525	21,364	23,729
School Transport scheme	47,761	46,882	45,593	43,797	43,610
	66,260	65,492	65,118	65,161	67,339
Vehicle Kilometres (in 1,000s)					
Provincial city services	5,750	5,856	5,927	7,197	7,593
Other Scheduled services	57,085	58,739	60,605	66,363	70,457

Source: Bus Éireann Annual Reports

Passenger journeys on other services increased by 28 percent over the five years to the end of 2001. This was accompanied by a 23 percent increase in the distance travelled over the same period. Most of these increases have taken place since 1999 and a significant proportion of the increase would appear to be the result of the introduction of a number of new routes (see below). The output of the school transport programme remained relatively stable because of demographic reasons.

Bus Éireann's financial statements over the five years until the end of 2001 show that total revenue rose from €130m to over €227m, with the vast amount of the revenue coming from services other than city services.

	1997	1998	1999	2000	2001
City Services (in €1,000)					
Revenue	14,651	14,798	14,827	20,081	21,918
Deficit before State Grants	-2,930	-3,721	-5,094	-9,741	-16,873
Other Services					
Revenue	115,193	119,216	127,128	182,721	205,875
Surplus/Deficit before State Grants	246	1,168	1,618	-2,523	-18,901

Total Deficit Before State Grants	-2,684	-2,553	-3,476	-12,264	-35,775
State Grant	6,985	7,112	7,379	20,013	30,236
Excess of Grant over Deficit	4,301	4,559	3,903	7,748	-5,538
Source: Bus Éireann Annual Reports					

Over the full range of services provided by Bus Éireann over the five years from 1997 to 2001 the State Grant exceeded the total amount of losses by around €15m. Historically, Bus Éireann have been loss making. Until 2000, the inter-regional and regional services collectively, produced small surpluses. In addition, with the exception of 2001, Government subventions exceeded any operating deficit, i.e. the subvention exceeded the cost of operating loss making or social services. This is important since the only apparent rationale for state transfers is that they are required to fund such services which are considered desirable on public policy grounds.

A close examination of the profit and loss accounts from 1999 to 2001 indicates that a possible explanation for this deterioration is that there has been a substantial increase in expenses associated with fuel (which is to be expected given the extra distances travelled and increased congestion) and also in operating and other expenses (which includes labour costs). The large impact of labour costs and the tight labour market is noted in the SDG Report at paragraph 23.9 where it is stated that labour shortages in 2000/01 drove up costs of contracting out school bus services.

SDG Reports that there are some 1,901 licensed private operators who between them own 4,890 buses. Most of these are very small-scale operations, although the largest operator owns 87 buses. Private bus companies have 571 licensed routes, although as SDG suggests, not all licences may be being used at present.

The market presence of private operators depends on the market being serviced. Different market segments identified by SDG are logical from an operational perspective, but further analysis based on the principles of relevant market definition would be required to carry out a detailed competition analysis of the various markets. These principles are presented in Box Two.

Market players in inter-regional services

The SDG Report notes that since 1987 Bus Éireann Expressway services have grown four-fold and the Report further notes that these routes are wholly commercial on a route-by-route basis. In 1999 profits on the Expressway service amounted to €7.5m. There are currently 184 buses dedicated to the Expressway service, which operates 66 routes. However, this remains insufficient to cater for peak demand and, as a result, Bus Éireann contracts out some of its services to private operators in times of excessive demand. Sub-contracting to private operators normally amounts to 35 buses a day, though this rises to 140 buses at peak times (when Bus Éireann Expressway have 324 buses at their disposal). This is of serious concern as large scale out-sourcing, of the type engaged in by Bus Éireann on its Expressway services, can lead to reluctance on the part of the sub-contractors to employ strategies that attack the position of the incumbent in other areas. This also means that passengers are serviced within the existing timetable rather than new services providing more choice in terms of timetable.

An important group of operators on inter-regional routes are the “travel clubs”. These are scheduled unlicensed services, which carry up to 3,000 to 9,000 people per day depending on the day of the week. SDG estimate that this equates to 1.4-1.6 million trips per annum, which SDG claim equates to 20-25 percent of the volume of Bus Éireann’s Expressway services (implying that Bus Éireann’s Expressway accounts for between 5.6 and 8 million trips per annum). Travel clubs are not eligible for fuel rebates, which puts them *a priori* at a competitive disadvantage to all licensed operators (including Bus Éireann). Nevertheless, a number of these services appear to operate successfully.

Private firms operate 25 daily services from provincial towns to Dublin compared with Bus Éireann’s 66 Expressway routes, although passenger volumes may be lower than on Expressway routes, and some of the daily services may be more appropriately compared with Bus Éireann’s commuter services to Dublin.

Although without further information on the activities of licensed operators other than Bus Éireann it is difficult to estimate market shares, it is clear that private sector operators in the form of both licensed operators and travel clubs account for a significant

proportion of inter-regional bus travel. The position varies between routes, with Bus Éireann facing significant competition in some areas and none on others. For example, Barrett (2000) Reports that there are three operators including Bus Éireann on the Dublin-Galway route, operating a total of 26 services daily, while Bus Éireann faces no competition on the Dublin-Cork route, for example. The reasons for such differences are not clear. Nonetheless, it is clear that Bus Éireann is the largest operator on the inter-regional bus market and, while it faces strong competition on some routes, it is the only operator on many others.

Players in regional services

Up until recently the Bus Éireann's Regional network has been stable. The SDG Report notes that Bus Éireann recently added 42 new regional services (using resources from the school bus fleet). Most of these have lost money in the amount of €2,000-5,000 per annum and Bus Éireann is in the process of removing some of the services. No information was provided in the SDG Report about how long it takes new regional services to stabilise in terms of passenger numbers, which is important to know if we are to make decisions about long-term commercial viability.

The SDG Report notes (in line with the findings in the transport study that “private sector operators are particularly active in this market, despite the absence of financial support.” Slightly less than half of all privately held licences are for regional services. The indications are that many of these apply to routes, which Bus Éireann had chosen not to operate. This may suggest a degree of “cherry-picking” of routes by Bus Éireann.

Urban (provincial city) services

Bus Éireann provides city services in Cork, Limerick, Galway and Waterford. It also provides a small-scale service in places such as Navan, Sligo, Dundalk and Athlone. The SDG Report notes a large improvement in service levels since 1999. Cost recovery on these services is reported at 74 percent. It appears that Bus Éireann has a monopoly in these services with the exception of Galway and Waterford where private sector operators hold 37 licences.

APPENDIX TWO: SUMMARY OF RELEVANT LITERATURE

Kennedy (1995)²⁸ estimated that the cost savings due to the tendering for cost contracts in the London Regional bus routes amounted to some 20 percent. Similar findings are echoed in Glaister (1993)²⁹ which considered bus deregulation in the UK. This research identified key success factors and showed that, as competition for tenders was strong after deregulation, subsidies were rapidly reduced without undue fare increases and without cutting service levels. Coordination of services and integrated ticketing was quickly re-established because of the commercial opportunities. However, despite increased services, patronage did not increase. Initial irregularities and changes in services, combined with poor information and were considered probable explanations. The paper also concluded that the tendering process (competition for short-term monopoly rights) adopted in London has worked well but placed limited pressure on costs. Savage (1993) also had similar findings and noted that innovations in operating practices were introduced after privatisation of the public bus companies in 1986.

Investigating the impact of deregulation in rural bus services, Bell and Cloke (1991)³⁰ showed that relatively little change took place in the short term, but that there was indication that services worsen in the medium and long term. This was attributed to both a reduction in the financial contributions from the local state and a general lack of competition. Examining 62 regional bus companies in Switzerland, Filippini (1992)³¹ found that cost inefficiency could be attributed to a significant degree to the regulatory regime rather than scale of operation.

²⁸ “London Bus Tendering: The Impact on Costs”, Kennedy, David, London School of Economics, *International Review of Applied Economics*; 9(3), 1995, pages 305-17.

²⁹ “Bus Deregulation in the United Kingdom”, Glaister, Stephen, London School of Economics & Political Science.

³⁰ “Deregulation and Rural Bus Services: A Study in Rural Wales”, Bell, P.; Cloke, P., University of Manchester; St David's University College, Wales, *Environment and Planning*; 23(1), January 1991, pages 107-26.

³¹ “Inefficiency in a Regulated Industry: The Case of the Swiss Regional Bus Companies”, Filippini, Massimo; Maggi, Rico; Prioni, Paola; Zurich University, *Annals of Public and Cooperative Economics*; 63(3), July-Sept. 1992, pages 437-55.

Gwilliam and van de Velde (1990)³² reviewed the reform of bus industry regulation for ten Western European countries. They observed a reluctance to accept British style open entry to the industry. This article suggests that the difference in the perceptions of the effectiveness of the competition is explained by the difference in emphasis placed on the use of local political control of the bus industry as an instrument of social and economic policy. In the wider context of urban transportation, Winston (2000)³³ identified entrenched political forces inhibiting constructive change as an explanatory factor for large public transit deficits and severe highway congestion. This position is supported by empirical evidence based on simulations for the United States and the United Kingdom's early experience with privatisation.

³² "The Potential for Regulatory Change in European Bus Markets", Gwilliam, K. M., van de Velde, D. M., Erasmus University, *Journal of Transport Economics and Policy*; 24(3), September 1990, pages 333-50.

³³ "Government Failure in Urban Transportation", Winston, Clifford, AEI-Brookings Joint Center for Regulatory Studies, Working Paper 00-8, November 2000.