Buses Bill – franchising and partnership improvements – secondary legislation

Department for Transport

RPC rating: fit for purpose

Description of proposal

The proposals will provide additional partnership options and franchising powers to local transport authorities (LTAs), with the aim of encouraging the operation of more effective local bus markets. The impact assessment (IA) updates the primary legislation IA to take account of the specific details in relation to processes that will be defined in secondary legislation. As such, the majority of the IA is the same as the IA that previously received a green-rated RPC opinion (RPC-3178(2)-DFT - attached). The changes will enable certain types of partnerships to operate on individual routes, clarifying administrative responsibilities for Transfer of Undertakings – Protection of Employees (TUPE) requirements, and extending the notice period before companies can withdraw services.

The IA also uses updated evidence, for example in relation to the values of time, in calculating the expected impacts on business. These changes do not have a material net effect on the impacts that will count towards the business impact target.

Impacts of proposal

The updated IA includes additional actuarial costs for local government as a result of Transfer of Undertakings – Protection of Employees (TUPE) requirements relating to occupational pensions – estimated to be between £4,000 and £13,000 per local authority area entering into enhanced partnership agreements.

The updated evidence used leads to smaller than modelled impacts in the form of reduced fares for bus companies as a result of the introduction of franchising. As a result, the pro-competition elements are now assessed as having an equivalent annual net direct cost to business (EANDCB) of £36.2 million, instead of £37 million as assessed in the primary stage IA. The calculation of the net cost to business from the pro-competition elements of the proposal are discussed in more detail in the attached opinion for the primary legislation.

As set out in the previous opinion, the costs and benefits of the elements of the proposal that are considered as qualifying regulatory provisions for the business impact target are materially the same, with an EANDCB of -£1.0 million. These arise due to the efficiency benefits enabled by the enhanced partnerships provisions.

Quality of submission

The IA accompanying the primary legislation included an appraisal of the expected impacts of the policy, including the elements that were to be set out in secondary legislation. As such, the single IA provided a sufficient assessment of the effects of the range of secondary legislation that would be required to implement the primary legislation. The provision of an updated IA to reflect the subsequent changes and additional detail is an example of good practice in relation to the appraisal of primary and associated secondary legislation.

The EANDCB figures confirmed here update the figures confirmed in the previous opinion. The EANDCB figure from this opinion should be used for business impact target reporting purposes.

Small and micro business assessment

The IA provides a clear discussion of the challenges smaller businesses might face in competing for franchises. The Department has also set out how it proposes to mitigate the impacts on smaller businesses, in particular through requirements on LTAs to design franchising processes in a way that considers the needs of and implications for smaller businesses.

Departmental assessment

Classification	Qualifying regulatory provision (OUT) with some non-qualifying elements(pro competition)
Equivalent annual net cost to business (EANCB)	-£1.0 million (qualifying regulatory provision - final estimate) £36.2 million (non-qualifying elements - pro-competition – final estimate)
Business net present value	-£304 million
Societal net present value	£510 million

RPC assessment

Regulatory Policy Committee

Classification	Qualifying regulatory provision (OUT) with some non-qualifying elements (pro competition)
EANCB – RPC validated[1]	-£1.0 million (qualifying regulatory provision) £36.2 million (non-qualifying elements - pro-competition)
BIT score – RPC validated[1]	-£5.0 million
Small and micro business assessment	Sufficient

Michael Gibbons CBE, Chairman

[1] For reporting purposes, the RPC validates EANCB figures to the nearest £100,000.

Previous RPC opinion

Buses Bill – franchising and partnership improvements

Department for Transport

RPC rating: fit for purpose

The IA is now fit for purpose as a result of the department's response to the RPC's initial review. As first submitted, the IA was not fit for purpose.

Description of proposal

The proposals will provide additional partnership options and franchising powers to local transport authorities (LTAs) with the aim of encouraging the operation of more effective local bus markets. They have two main elements:

1. The **enhanced partnership provisions** will enable LTAs and operators to form a statutory partnership to develop and deliver a bus strategy and network plan collectively. The Department expects this to resolve some of the issues with the current partnership provisions, for example by enabling LTAs to ensure registration conditions are consistent with the agreed network plan.

The **franchise proposals** have the objective of encouraging competition for the market by replacing deregulated markets with a franchising system for awarding contracts. They will allow combined authorities with directly-elected mayors, and other LTAs with the Secretary of State's consent, to let a franchise, or a number of franchises, to best meet local needs and discharge their statutory functions. The proposals include an 'open access' provision to enable other companies that identify a gap in service provided by a franchise to apply to the LTA to offer an additional service. The franchise proposals are intended to reduce the scope for incumbent operators to behave in anti-competitive ways (for example through effectively creating barriers to entry through unproductive on-road competition).The Department expects the proposals to result in lower barriers to entry to enable a greater range of operators to compete effectively.

Community transport schemes, such as those run on a non-profit basis, will be exempt from the enhanced partnership and franchise restrictions. Due to an ongoing EU infraction case, the Department intends to consult on the definitions and requirements relating to community transport schemes, and will subsequently take forward changes through secondary legislation.

The quality of submission section of this opinion highlights some issues that the Department should address prior to the publication of the impact assessment.

Impacts of proposal

Franchising: costs to business

Where pursued, the Department expects franchising to result in costs to incumbents, for example as a result of reduced fares or requirements to service less profitable routes as part of a more integrated service. It may also result in incumbents being successfully challenged by competitors and losing contracts to serve some routes. The Department, however, also expects there to be benefits for companies awarded franchises, such as increased passenger volumes and reduced costs, for example through reduced on-road competition and LTAs taking over responsibility for marketing of bus services. The Department expects the ‘open access’ provisions to have a small net benefit to business, as a result of increased profits to businesses that are successfully awarded additional contracts.

The most significant costs to business are the estimated reduction in bus company revenue. The Department expects reduced fares as a result of effective franchising to result in a small offsetting increase in bus journeys. The net effect on bus company revenues is expected to be a cost of between £2 million and £15 million each year in each LTA, depending on the size of the LTA. While there is some uncertainty over the take-up of franchising, the Department’s best estimate is that six LTAs will take-up the option, leading to a total reduction in bus company revenue of £256 million over the appraisal period.

The Department expects increased operating costs, including familiarisation, tendering and administration costs of franchising, to be partially offset by reductions in other costs, for example reduced mileage as result of less on-road competition or by enabling investment in improved service quality, such as newer buses, reducing per mile costs. However, these are still expected to result in a total cost of around £59 million during the ten year appraisal period.

The RPC is able to validate the estimated equivalent annual net direct cost to business (EANDCB) of £37.0 million of the franchising proposal, and confirms that this is a result of a pro-competition measure to be considered as a non-qualifying regulatory provision in relation to the government's business impact target.

Enhanced partnerships: benefits to business

The Department expects the enhanced partnership provisions to provide two main benefits to bus companies as a result of more effective planning: improved service quality resulting in an increase in journey numbers, and lower operating costs, for example from more efficient planning reducing costs per mile, although this will be partially offset by administration costs such as the costs of implementation meetings. Using the best estimates for each area, the Department expects the overall the enhanced partnerships proposal to save business an average of £1.0 million each year.

The RPC is also able to validate the EANDCB of -£1.0 million for the enhanced partnership proposals, and that this element should be considered as a qualifying regulatory provision.

Benefits to bus users and wider society

Alongside the assessment of impacts on bus companies, the IA discusses the potentially significant societal benefits of more effective bus services. In particular, the Department expects the proposal to result in significant benefits to bus users, both in terms of reduced fares and improved service quality. Taking the effects of franchising and enhanced partnership together, the Department estimates that the benefit to bus users will be around £860 million over the ten year appraisal period. The Department also expects wider local benefits, most notably from reduced congestion (£51 million over ten years), and changes in government spending and tax receipts, for example through capital investment and reduced fuel duty. The Department estimates the net present value of the proposal to be £546 million over the ten year appraisal period.

Quality of submission

Direct impacts of franchising

The RPC raised a number of concerns as a result of its initial review of the IA. These included the Department's assessment of all the impacts of the proposal as indirect. However, this was not correct as:

- the introduction of franchising, and the costs that will be imposed on business as a result of the restrictions on the deregulated market, is the primary purpose of the proposal;
- the regulation is intended to bite on the bus market, via LTAs, rather than, for example, influencing the market through affecting consumer behaviours in other areas; and
- the changes are intended to directly change prices (fares) and quantity (journey numbers), with bus operators not having any flexibility over the imposition of costs if franchising goes ahead.

The revised IA now correctly assesses the impacts of franchising as direct.

Pro-competition test

The Department has also now included an assessment of the proposal against the four 'pro-competition' criteria in the Better Regulation Framework Manual. The IA provides specific answers to each of the four questions with the responses summarised below.

The Department's assessment is that franchising will strengthen the ability of a range of operators to compete through removing the barriers to entry that can be created by incumbents' anti-competitive practices. The Department expects the introduction of a tendering and contracting process to lead to a more effective competition process than is currently the case. The Department cites the Competition Commission's 2011 report into local bus markets to highlight the current lack of effective competition in the majority of local markets. Where competition does currently exist, it tends to take the form of on-road competition, which can be costly for operators but without delivering significant benefits for users. In light of this, the Department's assessment is that the introduction of franchising is primarily designed to introduce competition for markets, in order to benefit users. The Department, therefore, expects competition for the market to lead to greater competition overall delivering significant benefits for bus users, and a net social benefit. On this basis, the RPC can confirm the Department's pro-competition assessment of these elements of the proposal.

Other points

Following concerns raised in the initial review, the IA also now:

- discusses the potential costs of cross-border travel between LTA areas where franchising has been taken forward;
- discusses the implications for the Competition and Markets Authority of the statutory consultee function, and
- includes a strengthened small and micro business assessment.

The Department has also amended the post-implementation review plans to reflect that, given the potentially significant costs and benefits of the proposal and its complex nature, a 'high' level of evidence regarding the implementation and effects should be gathered to inform any review effectively.

There are, however, two areas that should be improved further:

Presentation of costs and benefits

While the Department has provided sufficient evidence to support the validation of the EANDCB figure (for better partnerships) and the pro-competition assessment (for franchising), the IA presents the costs and benefits of the proposal in a confusing and counterintuitive manner. For example, the "*significant reduction in operating revenues for bus operators*" is discussed as a net effect of reduced individual fares and an increased number of journeys in the benefits section of the IA (as a dis-benefit), while the administrative costs of franchising are considered as a net effect alongside improved vehicle mileage in the costs section of the IA. This makes it difficult to understand the size and scale of the different elements of the proposal, and could significantly reduce the ability of stakeholders to develop a meaningful understanding of the estimated impacts. The IA should be amended to provide clear information regarding the gross costs and benefits of the elements of the proposal, and not just present net figures.

The additional information provided by the Department, in the 'EANDCB calculator' spreadsheets is important in understanding how the estimates associated with individual LTA areas have been aggregated. The IA should be amended to provide summary details of these estimated costs and benefits at least, rather than just ranges and overall figures. This should include summarising the time profile of the costs and benefits over time during the ten year appraisal period. The detailed modelling in the supporting documents underpins the assessment of costs and supports the robustness of the estimated impacts – ensuring this is reflected better in the IA will improve the quality of the IA.

Potential impacts of 'open access' provisions

The Department's assessment that the open access provisions are consistent with the pro-competition tests is reasonable. However, the IA would benefit from including further discussion on the potential costs to franchise holders. For example, it would appear that they may incur some costs in relation to demonstrating whether a proposed new route would adversely affect their business. It is also not clear whether the franchise holder would be given the opportunity to fill the identified gap, or otherwise respond, in advance of the LTA issuing a permit for the proposed route.

Small and micro business assessment

The Department has improved the small and micro business assessment. The IA now provides a clearer discussion of the challenges smaller businesses might face in competing for franchises. The Department has also set out how it proposes to mitigate the impacts on smaller businesses, in particular through requirements on LTAs to design franchising processes in a way that considers the needs of and implications for smaller businesses.

Departmental assessment

Classification	Neutral (no direct impact on business)
Equivalent annual net cost to business (EANCB)	£0.0 million (initial estimate) -£1.0 million (qualifying regulatory provision - final estimate) £37.0 million (non-qualifying regulatory provision - pro-competition – final estimate)
Business net present value	-£306 million
Societal net present value	£546 million

RPC assessment

Classification	Qualifying regulatory provision (OUT) Non-qualifying regulatory provision (pro competition)
EANCB – RPC validated[2]	-£1.0 million (qualifying regulatory provision)

[2] For reporting purposes, the RPC validates EANCB figures to the nearest £100,000.

Regulatory Policy Committee

	£37 million (non-qualifying regulatory provision - pro-competition)
BIT score – RPC validated[1]	-£5.0 million
Small and micro business assessment	Sufficient

Michael Gibbons CBE, Chairman