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FRAMEWORKS FOR OUR NETWORKS: A REVIEW OF PUBLIC TRANSPORT SERVICE CONTRACTS IN AUSTRALIA AND NEW ZEALAND



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FOREWORD

ALLENS

The past two decades have seen major change in public transport in Australia and New Zealand. Rapid population growth and urbanisation have contributed to unprecedented demand for public transport. Structural reforms within government and the broader economy and accelerating technological change have also had a significant impact on the public transport networks in Australia and New Zealand over this period. At the same time, both countries have moved progressively to a governance model for public transport where there is a clear separation between the authority that oversees the development and delivery of the relevant system, and the operator that manages the system and provides passenger services on a day-to-day basis. Although many public transport systems remain government-owned and operated, this reform has facilitated the steady growth over the same period in private sector operation of all modes of public transport services in Australia and New Zealand, from train and light rail to bus and ferry services.

The movement to this governance model for the delivery of public transport services in Australia and New Zealand has not been without controversy, but experience has shown that the reforms have led to significant benefits, including improved performance outcomes and enhanced customer satisfaction, as well as improved efficiency and productivity, resulting in cost savings and consequent benefits for taxpayers. That said, there is no single form of public transport service contract between a transport authority and a transport operator which guarantees a successful outcome. Instead, each contract needs to be carefully structured and designed for the relevant transport network and the policy priorities and objectives of the government of the day. Based on the benefits realised so far, we anticipate the trend toward private sector operation of public transport services in Australia and New Zealand will continue well into the future, and the contractual models under which the services are provided will continue to evolve.

As a leading international law firm, Allens has a long and proud heritage of shaping the future for our clients, our people and the communities in which we work. Our market-leading infrastructure and project financing teams are no exception. These teams advise across the full lifecycle of transport infrastructure and service delivery projects, and play an active role in the development of the markets in which we operate. As we approach our 200th year, we have grown to offer our clients a worldwide network, with 40 offices across 28 countries, through our global alliance with Linklaters. We are privileged to hold some of the world's longest ongoing client relationships, stretching back more than 170 years, and to be trusted with their 'first-to-market' and marketchanging transactions.

With the release of this report in collaboration with UITP Australia New Zealand, our aim is to inform future policy development in the transport sector by providing governments and industry participants with a comprehensive review of the range of public transport service contract models currently in use in Australia and New Zealand, and to provide a useful resource for those directly engaged in contract development and design.



Paul Kenny Partner Allens



Penny Alexander Partner Allens

UITP AUSTRALIA NEW ZEALAND

This report is the result of months of hard work and dedication by our member, Allens. In particular, I wish to thank Partners Paul Kenny and Penny Alexander for their contribution to what will no doubt become a foundational document for all matters related to public transport contracting going forward. I'd also like to thank the public transport authorities across Australia and New Zealand for all participating in the review process. The report offers a comprehensive overview of the Australian and New Zealand markets and jurisdictional arrangements. In undertaking this research, we knew the report would meet a long-standing need to capture and analyse publicly available contract information and that the scale of such an undertaking was why it has not been done before. It is an invaluable resource and record of how public transport service provision is regulated and delivered in our region at the present time and will inform future decision making.

2020 was a challenging year for the public transport sector (and many others) with the global, ongoing disruption of COVID-19. Public transport service contracts have provided the frameworks for the ways in which operators and authorities have persisted in providing safe, efficient and reliable services to the community. We must safeguard our public transport services as the backbone of mobility in our cities and towns, to ensure a future of good air quality and low congestion.

Many jurisdictions globally and locally are reviewing their commercial models and in many respects COVID-19 has accelerated the need to evaluate our frameworks to ensure they provide optimal arrangements for our networks going forward. Understanding the commonalities of jurisdictional approaches to public transport contracting will no doubt aid those who are seeking to review and improve those contracts, help inform the appropriate policy settings for government and drive overall improvements in the passenger experience.

The public transport sector has always been one of innovation and rapid change, moving people and simultaneously being driven by the evolution of the societies in which our networks operate. More than ever, our contracts need to be agile to keep up with a range of factors including changing government priorities and protecting the commercial interests of private operators. This report will give readers a broad knowledge of the mechanisms available to future-proof public transport service contracts against unknown events and prepare for the trials and opportunities presented by climate change, new technologies and population growth. Indeed, these challenges may require investment and change, but they can also be viewed as the chance to innovate and find new ways to collaborate, generate revenue and serve people who need and choose to use public transport.

I'm certain UITP Australia New Zealand members will find this report useful and hope it will enable them to not only improve the design and management of contracts and assist operators in their delivery of world-class public transport services, but also to approach contracting with innovation and creativity to continue to meet the needs of our communities well into the future.



Michelle Batsas Executive Director UITP Australia New Zealand

ACKNOWLEDGEMENTS

We would like to thank the following public transport authorities, and the individuals mentioned, for their time reviewing and providing comments on this report. Their comments were very helpful in making the report as comprehensive and accurate as possible. However, we note that the content of the report, including descriptions of the contracts reviewed and the opinions expressed,

Auckland Transport

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South Australian Department for Infrastructure and Transport

Fergus Gammie Adelaide Rail Transformation Program Director

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Transport Canberra

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Tasmanian Department of State Growth

Kim Harris Principal Contracts Officer, Passenger Transport

Transport for New South Wales

Jenny Birch Director, Metro Bus and Ferry Service Delivery have not been endorsed by any of the people who provided comments or the organisations they represent. The content of the report is entirely the responsibility of the authors.

We would also like to thank the Allens team that assisted with the research for the report and the UITP Australia New Zealand team that assisted with its preparation.

Victorian Department of Transport

Kha Truong Executive Director, Commercial Strategy

Northern Territory Department of Infrastructure, Planning and Logistics

Greg Turner A/Director Passenger Transport

Greater Wellington Regional Council

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EXECUTIVE SUMMARY

Although public transport service contracts need to be designed to meet the unique circumstances of each contract, the goal of this report is to both highlight the commonalities between existing public transport service contracts across Australia and New Zealand and emphasise some of the varied approaches taken to address issues arising from the rapidly changing public transport landscape. The intention is to inform future policy development in the sector by providing governments and industry participants with a comprehensive review of the range of public transport service contract models currently in use in Australia and New Zealand, and to provide a useful resource for those directly engaged in contract development and design.

1.1 CONTEXT

Over the past two decades Australia and New Zealand have moved progressively to an institutional and governance model for public transport where there is a clear separation between transport authorities and transport operators. A corollary has been the increasing use of public transport service contracts as the primary means of regulating the relationship between the two. Contracts are, of course, an essential requirement for private sector provision of transport services, but there are also many instances in which contracts govern the relationship between transport authorities and public sector operators.

In broad terms, public transport service contracts represent the outcome of a series of choices about the numerous variables that make up the structure and design of the contract. These choices are influenced by the commercial and policy objectives set by government for the particular transport service, as well as the governance and institutional environment in which the contract will operate.

While Australia and New Zealand leverage a variety of models of public transport service delivery, in recent years there has been a distinct trend towards opting for a franchising model. This report is based on a review of publicly available service contracts across all Australian states and territories and the cities of Auckland and Wellington in New Zealand. The contracts reviewed are listed in Table 1.

Table 1: Contracts reviewed

- Auckland Bus Services
- Auckland Metro Rail
- Capital Metro Light Rail
- Gold Coast Light Rail
- Melbourne Bus Franchise
- Melbourne Bus Services
- Melbourne Rail Franchise
- Melbourne Tram Franchise
- Newcastle Integrated Services
- Paramatta Light Rail
- Sydney Bus Services1
- Sydney Ferry System
- Sydney Light Rail
- Sydney Metro Northwest2
- Wellington Bus Services
- Wellington Metro Rail



¹ The review is based on the Region 6 Bus Service Contract.

² When the Sydney Metro City & Southwest project is completed it will operate as a single end-to-end metro system with the existing Sydney Metro Northwest network. At that time the Sydney Metro City & Southwest Project Deed will, in effect, replace the current Sydney Metro Northwest Project Deed and apply to services across the whole of the network. Accordingly, for the purposes of this report they are treated as a single service contract, and the report is based on the existing Sydney Metro Northwest Project Deed.

1.2 GOVERNANCE AND INSTITUTIONAL ARRANGEMENTS

The governance and institutional framework in which public transport service contracting arrangements sit plays an important role in determining how readily services can be brought within a contracting model, as well as the form and content of the contracts themselves.

Diagram 1 shows the four typical arrangements for how transport authorities delegate and regulate dimensions of transport operations, including by public sector provision and through private operators.

Diagram 1: Governance and institutional arrangements - Framework

Oversight by Transport Authority

Administrative regulation Contractuo		l regulation 🔶	
Direct provision	Public	operator	Private operator
Model 1 • Services are provided directly by the Transport Authority	 Model 2 Services are provided by a public sector agency subject to administrative oversight 	Model 3 • Services are provided by a public sector agency subject to contractual oversight	Model 4 • Services are provided by a private sector operator subject to contractual oversight

Although the reality is somewhat more complicated than this, at a very general level it is fair to say the evolution of governance and intuitional arrangements in Australia and New Zealand over the past two decades, consistent with other comparable jurisdictions internationally, has been a move from the left to the right across the continuum, away from Model 1 and towards Model 4.

1.3 DESIGN VARIABLES

The report identifies 10 design variables which are considered most significant in terms of the relationship between contract design and achievement of the transport authority's objectives for the contract. They are also the variables most likely to be relevant across all jurisdictions. Table 2 provides an overview of the design variables examined in the report and the ways in which these design variables are addressed in the suite of service contracts reviewed for the purposes of the report.

	5
Design variable	Analysis
Contract term	Selecting the duration of a service contract is a matter of carefully balancing a range of competing considerations, including the impact on incentives to invest in longer-term solutions and capital, ability to forecast patronage and revenue, ability to implement policy, cultural or operational change, and procurement model and market considerations. The service contracts reviewed typically have a term of between 8 and 15 years, with longer terms evident in PPP contracts. Short term priced extensions at the option of the transport authority are common, and longer-term unpriced extension options based on performance are evident in some contracts. Many contracts provide the transport authority with a right to terminate the contract early without cause, but with this right constrained by an obligation to compensate the operator.

Table 2: Overview of design variables

Design variable Analysis



The service model refers to the scope of the services provided under the contract, including the operator's responsibilities with respect to passenger services, infrastructure maintenance and renewal, and vehicle maintenance and renewal. Design of the service model can be a material factor in determining the quality and reliability of passenger service outcomes. A variety of factors will influence the approach to service model design, including the perceived implications of the service model for customer experience, the governance and institutional framework, the regulatory environment, policy and political preferences concerning the scope of delegation of transport authority functions, and the implications of the service model for the market's response to the opportunity where a competitive procurement process is involved.

Revenue model



The revenue model refers to the treatment of farebox revenue derived from the provision of passenger services, as well as the treatment of revenue that can be generated from commercial opportunities associated with the use of transport assets, such as advertising on vehicles and at stations and stops. Most service contracts reviewed operate as gross cost contracts, where farebox revenue is retained by the transport authority and the operator is paid a service fee based on the cost of providing services. The position in relation to advertising and other commercial revenue is more varied, but it is common for contracts to permit operators to earn commercial revenues with the consent of the transport authority, and on the basis that the revenue will be shared with the authority.

Performance regimes



Performance regimes are designed to incentivise the performance outcomes the transport authority is seeking, give operators a greater stake in the system and help to ensure alignment between the objectives of the transport authority and the relevant operator. The key performance indicators and other performance regime metrics are typically focussed on service punctuality and reliability, customer experience and asset management. In all contracts reviewed, incentives and penalties are capped to manage the risk assumed by both the transport authority and the operator. The regimes also allow for adjustments in circumstances reasonably beyond the operator's control, such as weather events, special events, public emergencies and road congestion.

Service change regime

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The service change regime refers to the mechanisms in the contract that deal with the transport authority's need to make changes to the services, including timetable changes and the addition and cessation of services. There are two principal elements that need to be addressed when changes need to be made to the passenger services the operator is contracted to provide, as distinct from general contract variations. The first relates to the process for making service changes and the second concerns the financial implications of the service change. The contracts provide varying degrees of prescription as to the basis on which price adjustments are to be determined, ranging from 'pre-priced' service kilometre or hourly rates to detailed methodologies for determining the 'net financial impact' of the change.

Risk allocation



Risk allocation is a very broad topic, and there will be different risk categories depending on the service model. This report focusses on two key risk issues – the allocation of revenue risk and operating cost risk. As a general principle, optimal risk allocation seeks to assign project risks to the party in the best position to control them. The party with greatest control of a particular risk has the best opportunity to reduce the likelihood of the risk eventuating and to control the consequences if it does. Most service contracts assign revenue risk to the transport authority and cost risk to the operator. However, in many cases there is a degree of risk sharing – eg through patronage incentives in the case of revenue risk and cost pass throughs (typically for fuel costs and changes in law) in the case of cost risk.

Design variable	Analysis
Network integration	Network integration refers to the way in which the contract addresses the operator's engagement in network-wide functions. The contracts reviewed for this report typically include express obligations on operators to support the broader network in key areas such as ticketing, system integration and planning, and other network-wide functions and activities such as marketing and passenger information. However, the review found considerable variation in the approaches taken between jurisdictions.
Projects regime	A common feature of transport networks in Australia and New Zealand today is the prevalence of major network extensions and augmentations. The discussion of projects regimes in the report refers to contractual provisions that deal with new investment in the network. This may be investment by the operator at the instigation of the transport authority, or investment by the authority which requires the cooperation of the operator. The need to facilitate network development, as well as to manage the disruption to existing services that major projects inevitably cause, has led a number of Australian jurisdictions to include detailed regimes governing project planning and development in their service contracts. Regimes of this kind have not been incorporated in New Zealand service contracts to date, which rely instead on general contract variation clauses.
Financial security	Financial security arrangements are an important feature of public transport service contracts. Such arrangements are designed to address a number of risks faced by the transport authority, including the risk of non-performance of the operator's obligations under the contract and the risk of the operator becoming insolvent. The package of financial security arrangements varies across the contracts reviewed, with a 'belts-and-braces' approach preferred in some jurisdictions and a more selective approach adopted in others. Typical financial security arrangements include requirements for the provision of performance bonds, minimum capital requirements, restrictions on engaging in other activities and the provision of securities over the assets of, and shares in, the operator.
End of term arrangements	End of term arrangements refer to the provisions in the contract governing the retendering of the right to operate the services upon expiry of the contract and transition to a new operator, including provisions governing the transfer of assets and employees to a successor operator and obligations to facilitate the retendering process. A robust contractual framework governing the expiry of the service contract is critical both to the successful transition out of the current operator and the successful commencement of the new service provision arrangements. End of term arrangements need to focus on ensuring that all necessary staff, assets and knowledge are transferred or otherwise made available to the successor in the most efficient manner and so as to ensure continuity of passenger services and otherwise minimise operational and reputational risk to the transport authority.

1.4 TRENDS ANALYSIS AND CONCLUSIONS

The trends outlined in this report are likely to see the continued evolution of public transport service contracts to address new issues arising across each of the key design variables and in response to changes to the environment in which public transport services are provided. Changing attitudes and preferences in relation to risk transfer, an increasing focus on contractual relief for unanticipated events (such as the current pandemic), and a continued focus on major project delivery and management of disruption are all issues of particular significance in the current environment. Broader trends and developments will also impact these regimes going forward. These include:

- The changing nature of public transport and the services it provides, which will require service contracts that define an appropriate service model and integrate on-demand services with traditional forms of public transport.
- Innovations such as 'Mobility as a Service', which will require the respective roles of transport operators and authorities to be defined in pursuing innovation and flexibility for technological change to be implemented by operators in partnership with government.
- The need to develop mechanisms that acknowledge and facilitate change as governments continue to invest in major new transport infrastructure, including through more collaborative governance mechanisms and mechanisms that provide the operator with a stake in successful project outcomes.
- The likelihood that governments and transport authorities will look to innovative pricing solutions, such as road pricing and variable pricing for public transport, to reduce congestion and address network capacity constraints.
- The continuing focus on environmental sustainability, and the consequent need for service contracts to support measures such as the move to zero emissions bus fleets, use of renewable energy and obligations or incentives for energy and fuel efficiency.
- Recognition of the power of data to optimise transport systems and understand customer behaviour, which means the collection, storage, sharing and use of data will remain a prominent issue moving forward, and will be reflected in obligations under public transport service contracts in addition to legislative and regulatory settings.

 A renewed focus on the impact of unforeseen events such as the COVID-19 pandemic, which will require provisions that allow for flexibility to respond in line with government policy and priorities whilst mitigating the revenue and cost impacts on private operators.

Each of these trends is having, and will continue to have, an impact on public transport service contracts and the sector more broadly.

Our aim with this report is to highlight the commonalities between existing public transport service contracts as well as identify some of the varied approaches taken to address issues arising from the rapidly changing public transport landscape. Governments and industry participants alike will need to be mindful of continuing developments in the sector as they consider how service contracts can be designed, negotiated and implemented in a way that achieves the multiple policy objectives of governments under a commercial and contractual model that remains attractive and sustainable for transport operators. The purpose of this report is to provide a resource that we hope will be useful for those involved in contract design and development to assist with that process.



2 INTRODUCTION

Historically, public transport has been seen as a government responsibility – one of state and territory governments in Australia and regional governments in New Zealand. However, governments in Australia and New Zealand are increasingly looking to the private sector to develop and operate public transport systems.

Over the past two decades Australia and New Zealand have moved progressively to an institutional and governance model for public transport where there is a clear separation between transport authorities and transport operators. A corollary has been the increasing use of public transport service contracts as the primary means of regulating the relationship between the two. Contracts are, of course, an essential requirement for private sector provision of transport services, but there are also many instances in which contracts govern the relationship between transport authorities and public sector operators.

Public transport service contracts play an important role in helping governments achieve improved performance outcomes. Well-structured and carefully designed service contracts can be a critical factor in promoting an increased focus by transport operators on customer service. Not only does this lead to enhanced customer satisfaction, improved efficiency and greater productivity, but also cost savings and consequent benefits for taxpayers regardless of whether the transport operator is publicly or privately owned.

While Australia and New Zealand leverage a variety of models of public transport service delivery, in recent years there has been a distinct trend towards opting for a franchising model. In franchising models, private operators deliver public transport services and oversee day-to-day operations whilst the government retains ownership over the public transport infrastructure and makes strategic decisions about network planning, timetabling and fare pricing.

This report comes at a particularly active time in the ongoing evolution of this trend. Greater Wellington Regional Council completed the franchising of the Greater Wellington metro rail service in 2016. The Victorian Government completed a comprehensive renegotiation of franchise contracts for the Melbourne train and tram networks in 2017. In mid-2018, Queensland's Department of Transport and Main Roads (DTMR) through its public transport division, TransLink, completed the execution of new bus service contracts in South East Queensland. At the same time it commenced the procurement process associated with Regional Urban Bus contracts, which were all executed in early 2019. DTMR is currently overseeing the procurement process for the Stage 3 extension of the Gold Coast Light Rail by a private consortium. Transport for NSW achieved financial close on new contracts for the City & Southwest extension to Sydney Metro in December 2019. The Public Transport Authority in Western Australia recently completed a major retendering of three Transperth bus service contract areas, representing 27% of its bus service network.

The South Australian Government announced the award of a franchise contract for the operation of Adelaide's metropolitan train network in September 2020, and service delivery by the new operator commenced on 31 January 2021. Auckland Transport has announced the refranchising of the Auckland train network. The procurement process is underway and expected to be completed or well advanced by the end of 2021. Transport for NSW has also announced a three-year program to procure metropolitan bus services for Sydney. This will involve the franchising of Regions 7, 8 and 9, which are currently under public sector operation by State Transit. The Victorian Department of Transport has indicated its intention to conduct a refranchising of the Melbourne bus franchise, which covers roughly 30% of Metropolitan Melbourne bus services.

In addition, the commercial and contractual models for public transport provision continue to evolve internationally, with the current COVID-19 pandemic placing considerable stress on public transport networks both financially and from an operational perspective. The UK Government's announcement in September 2020 that it intends to end the current franchising model is especially significant in this respect, and the outcomes of the Williams Rail Review's 'root and branch review' of rail franchising will be of great interest both to policy makers and transport sector participants.³

It is accordingly an opportune time to survey current contracting practice.

2.1 THE SUITE OF CONTRACTS REVIEWED IN THIS REPORT

This report is based on a review of publicly available service contracts across all Australian states and territories and the cities of Auckland and Wellington in New Zealand. The contracts reviewed are listed in Table 3, and further details in relation to each contract are contained in Schedule 1.

³ The Williams Rail Review was announced by the United Kingdom Government in September 2018. Details of the review can be found at <u>https://www.gov.uk/government/</u> <u>collections/the-williams-rail-review</u>

Table 3: Contracts reviewed

- Auckland Bus Services
- Auckland Metro Rail
- Capital Metro Light Rail
- Gold Coast Light Rail
- Melbourne Bus Franchise
- Melbourne Bus Services
- Melbourne Rail Franchise
- Melbourne Tram Franchise
- Newcastle Integrated Services
- Paramatta Light Rail
- Sydney Bus Services⁴
- Sydney Ferry System
- Sydney Light Rail
- Sydney Metro Northwest⁵
- Wellington Bus Services
- Wellington Metro Rail

This suite of contracts provides a rich source of data in relation to current policy and practice in Australia and New Zealand concerning public transport service contracting. The contracts reviewed include heavy rail, light rail, bus and ferry services. They also include both PPP contracts (under which the operator is responsible for the design, delivery and financing of new transport infrastructure), and service contracts for the operation of existing services using existing transport infrastructure.

The distinction between PPP contracts and pure service contracts is an important one in defining the scope of the review. There is a wealth of commentary and guidance materials on PPP contracting, including the National PPP Policy and Guidelines as endorsed by Infrastructure Australia and the state, territory and federal governments in Australia.⁶ This report does not seek to address the design, delivery and financing of new transport infrastructure – its focus is on public transport service provision regulated through service contracts. Accordingly, the review of PPP contracts is focused

on those provisions dealing with the operation and maintenance phase of the project and not the project delivery phase.

2.2 LIMITATIONS ON THE REVIEW

There are number of limitations on the review that need to be borne in mind. The most important is that the report is based solely on publicly available information. While many jurisdictions have policies in place that require publication on the internet of material government contracts, this is not universally the case. The report relies on the published versions of contracts in those jurisdictions which have adopted a policy or practice of publishing their contracts.

A second and related limitation is that in many cases the published versions of the contracts have been redacted to remove information deemed confidential or commercially sensitive. This is generally financial and pricing information, but also sometimes includes risk allocation, performance metrics and other details.

Thirdly, while those jurisdictions that publish their contracts do so routinely in relation to the originally executed versions of the contracts, this is not always the case in relation to amendments and modifications. Accordingly, it is not possible to be certain that the contracts reviewed are fully up to date.

Finally, while the majority of the contracts reviewed were executed contracts, the Auckland Bus Services contract was a template contract which formed the base for bespoke contracts with individual operators.⁷

Despite these limitations, the report provides an informative and reliable overview of current policy and practice. The aim of the report is to identify common themes and issues derived from a review of the contract suite as a whole rather than to provide a record of the specific positions reflected in individual contracts.

2.3 POLICY AND PRACTICE AT A POINT IN TIME

As alluded to above, the report comes at a time of highly active engagement by transport authorities with public transport service contracting. In particular, the franchising of rail services in Adelaide represents a major milestone in the evolution of the franchising model, as does the development of a wholly new network under private sector operation in the form of Sydney Metro. Similarly, the refranchising of rail services in Auckland will present an opportunity to learn from the successes

⁴ The review is based on the Region 6 Bus Service Contract.

⁵ When the Sydney Metro City & Southwest project is competed it will operate as a single end-to-end metro system with the existing Sydney Metro Northwest network. At that time the Sydney Metro City & Southwest Project Deed will, in effect, replace the current Sydney Metro Northwest Project Deed and apply to services across the whole of the network. Accordingly, for the purposes of this report, they are treated as a single service contract, and the report is based on the existing Sydney Metro Northwest Project Deed.

^{6 &}lt;u>https://www.infrastructure.gov.au/infrastructure/ngpd/index.aspx</u>

^{7~} We understand from Auckland Transport that the executed contracts contain few variations to the template.

and failures in other jurisdictions. At the time of writing, the Adelaide and Auckland procurement processes are underway but incomplete and Perth's re-tender of 27% of its Transperth bus services has recently been completed.⁸ The Sydney and Melbourne bus franchising procurements are at an early stage.

This report necessarily reflects policy and practice at a point in time. There will always be new themes and trends emerging. The report seeks to capture these to the extent possible. More importantly, however, it aims to provide a framework for consideration of service contracting which can be reviewed and updated periodically as new contracts are entered into and made public.

2.4 STRUCTURE OF THE REPORT

Following the Executive summary in Chapter 1 and this introductory Chapter 2, the report begins in Chapter 3 by providing an overview of the institutional and governance arrangements for public transport services in Australia and New Zealand. As explained in Chapter 3, an understanding of the institutional and governance framework is an essential part of the context for understanding the approach taken to contracting in each relevant jurisdiction. Chapter 4 of the report then describes the key design variables which need to be addressed in developing public transport service contracts. These comprise:

- Revenue model
- Performance regimes
- Service change regimes
- Risk allocation
- Network integration
- Projects regimes
- Financial security
- End of term arrangements

These key design variables form the basis of analysis undertaken in the report of the contracts forming the review suite. Sections 5.1 – 5.10 of the report discuss each design variable by outlining its key features and summarising its treatment in the contracts reviewed, identifying common themes, approaches and issues.

Chapter 6 provides a brief summary of conclusions, focussing on current and future trends in the public transport sector and their implications for service contracts.

Details of the service contracts reviewed for the purpose of the report are set out in **Schedule 1**, while **Schedule 2** provides a list of useful resource materials.

- Contract term
- Service model



8 The Adelaide rail franchise contract was awarded to Keolis Downer in September 2020, but provision of services will not commence under the contract until the end of January 2021.

3 GOVERNANCE AND INSTITUTIONAL ARRANGEMENTS BY JURISDICTION

Critical to examining public transport service contracting arrangements is the governance and institutional framework in which they sit. This plays an important role in determining how readily services can be brought within a contracting model, as well as the form and content of the contracts themselves. A variety of governance and institutional arrangements exist in Australia and New Zealand.

The role of the transport authority

Two key concepts in describing public transport governance and institutional arrangements are those of the 'transport authority' and 'transport operations'.

The transport authority sits at the centre of the framework. This is the entity with responsibility for making strategic decisions about public transport planning and for ensuring the provision of public transport services to the community. The transport authority may be a

government department or a separately constituted authority with delegated responsibility from government or, in some jurisdictions, a combination of both.

Transport operations can be provided and regulated by the transport authority in several different ways. The key dimensions are:

- whether the services are provided directly by the transport authority or by a separate body supervised by the authority;
- whether the transport authority's oversight of operations is regulated through administrative arrangements or by contract; and
- whether the services are provided exclusively by a public sector agency or are procured through a contestable process in which private sector operators can bid for the right to provide services.

Alternative combinations of these three dimensions lead to four typical governance and institutional arrangements, as represented in Diagram 2.

Diagram 2: Governance and institutional arrangements - Framework

Administra	Administrative regulation Contractual r		l regulation
Direct provision	Public	operator	Private operator
 Model 1 Services are provided directly by the Transport Authority 	Model 2 • Services are provided by a public sector agency subject to administrative oversight	Model 3 • Services are provided by a public sector agency subject to contractual oversight	Model 4 • Services are provided by a private sector operator subject to contractual oversight

Oversight by Transport Authority

The first model (Model 1) is shown to the left of the continuum. Services are provided directly by the transport authority and oversight of service provision is dealt with through internal administrative arrangements within the authority. Second from the left shows the second model (Model 2), where services are provided by a separately constituted public sector agency and the relationship between the transport authority and the operator is regulated through public sector administrative arrangements. This might be through the transport portfolio legislative framework or other less formal inter-agency arrangements. In the third model (Model 3), services are provided by a separately constituted public sector agency, but the relationship between the transport authority and the operator is regulated through an explicit service contract. Finally, to the right of the continuum, in the fourth model (Model 4) services are

provided by a private sector operator appointed through a contestable procurement process. The relationship is regulated by a service contract between the transport authority and the operator, negotiated as part of the procurement process.

Although the reality is somewhat more complicated than this, at a very general level it is fair to say the evolution of governance and intuitional arrangements in Australia and New Zealand over the past two decades, consistent with other comparable jurisdictions internationally, has been a move from the left to the right across the continuum, away from Model 1 and towards Model 4.

This high-level framework is used to provide an overview of the governance and institutional arrangements in each of the Australian and New Zealand jurisdictions which are the subject of this report.

3.1 AUCKLAND

Auckland Transport is the transport authority in Auckland. Auckland Transport is a 'Council-Controlled Organisation' of Auckland City Council. As a Council-Controlled Organisation under the *Local Government Act* 2002 (NZ), Auckland City Council has the responsibility to appoint at least 50% of the board of directors or trustees of Auckland Transport.

Auckland's public transport system compromises heavy rail, bus and ferry services under the 'AT Metro' brand.

Heavy rail services operate over four lines with 41 stations. The network will be expanded in 2024 with the completion of the City Rail Link project, which will add a 3.45km twin tunnel underground rail link and two new

underground stations, as well as upgrades at Britomart and Mt Eden Stations. Heavy rail services are provided by a private operator, Transdev Auckland, under contract to Auckland Transport.

Bus services in Auckland are provided by private operators under contract to Auckland Transport. These services are provided in five separate bus regions. Similarly, ferry services to Whangaparaoa Peninsula, Waiheke Island, Rakino Island and Beachlands are provided by four private operators under contract to Auckland Transport.

A future light rail network comprising two major lines is also planned for Auckland.

Diagram 3: Governance and institutional arrangements - Auckland

Transport Authority: Auckland Transport



3.2 AUSTRALIAN CAPITAL TERRITORY

Transport Canberra, which is a division of the Transport Canberra and City Services Directorate of the ACT Government, is the transport authority in the Australian Capital Territory (ACT).

Public transport services in the ACT comprise bus services and a light rail service operating from Gungahlin to the City in Canberra. There are ten rapid public transport routes in Canberra (nine serviced by buses and 1 via light rail). The Rapid network is supported by a series of local and feeder services which connect the suburbs with the major transport corridors and key activity centres. The light rail service, operated by Canberra Metro Operations (CMET), commenced operation in April 2019 and currently comprises a 12km route serving 13 stops from Gungahlin to the city centre. Transport Canberra is in the process of planning for Stage 2 of the Canberra Light Rail Network.

Bus services are provided directly by Transport Canberra. The light rail service is provided under a PPP contract between the ACT Government and a private sector consortium.

Diagram 4: Governance and institutional arrangements - Australian Capital Territory

Transport Authority: Transport Canberra

Administrative	e regulation ————————————————————————————————————	ontractual regulation	
Direct provision	Public operator	Private operator	
• Buses (Transport Canberra)		• Light rail (Canberra Metro)	

3.3 NEW SOUTH WALES

Transport for NSW (TfNSW) is the lead transport authority in New South Wales. TfNSW is established as a statutory body under the *Transport Administration Act 1988* (NSW) and is managed and controlled by the Secretary of the Department of Transport.

Public transport services in New South Wales comprise metropolitan and regional heavy rail, light rail, bus and ferry services and are provided by a mix of public sector and private sector operators. TfNSW has also trialled various on-demand models, including ebikes, bus on demand and ferry on demand.

The public sector services are provided by separately constituted public sector agencies. These comprise:

- Metropolitan rail services, provided by Sydney Trains;
- Rregional rail services, provided by NSW TrainLink; and
- Metropolitan bus services in Sydney's north western suburbs, eastern suburbs, lower north shore and northern beaches (Regions 7, 8 and 9), provided by the State Transit Authority

These services are managed under contracts with TfNSW. In the case of bus services the contracts cover the delivery and performance of services as well as payment, while for Sydney Trains and NSW TrainLink, funding is managed through administrative processes rather than by contract.

Services provided by private operators are provided under contract to TfNSW. These services include the new Sydney Metro Northwest, Sydney Light Rail, Paramatta Light Rail, metropolitan bus services across 11 regions (other than Regions 7, 8 and 9), outer metropolitan bus services and all rural and regional bus services. Current planning envisages a significant expansion of the Sydney Metro network, including extensions to City & Southwest and Sydney Metro West. The Sydney Ferry System contract, comprising nine routes, is also provided by a private sector operator, Transdev Sydney Ferries, under contract to TfNSW. Manly Fast Ferries is also a key public transport service providing commuter capacity as a high frequency, fast ferry service between Manly and Circular Quay. For the most part these services have been procured through a contestable procurement process or in accordance with existing contractual extension or augmentation provisions.⁹ In late 2019, the NSW Government announced that private sector operators for bus regions 7, 8 and 9 would also be sought through a contestable procurement process. That process was originally planned to be completed by the end of 2020, but due to the COVID-19 pandemic the process has been delayed and staggered.

In Newcastle, operation and maintenance of public transport is delivered by the private sector under a multimodal contract – the Newcastle Integrated Services contract. Under this contract, Newcastle Transport, which is currently operated by Keolis Downer Hunter (trading as Transport for Newcastle), operates and maintains the light rail, bus and ferry networks. The Newcastle light rail consists of six stops along a 2.7km track, the bus network consists of approximately 21 routes, and the ferry travels between two terminals along the Hunter River.

Diagram 5: Governance and institutional arrangements - New South Wales

Transport Authority: Transport for New South Wales

	Administrative regulation	Contra	ctual regulation
Dire	ect provision	Public operator	Private operator
		 Metro rail (Sydney Trains) Regional rail (NSW TrainLink) Sydney buses, regions 8 & 9 (State Transit) 	 Sydney Metro Northwest (Metro Trains) Sydney light rail (Transdev) Sydney ferries (Transdev Sydney Ferries) Sydney buses, excl. regions 7-9 (various operators) Outer metropolitan buses (various operators) Rural and regional buses (various operators) Rural and regional buses (various operators) Parramatta light rail (Great River City Light Rail) Newcastle multi-modal services (Keolis Downer Hunter)

⁹ Outer metropolitan and rural and regional bus services have not been competitively procured.

3.4 NORTHERN TERRITORY

The **Public Transport Division**, which is a division of the Northern Territory Transport Group of the Northern Territory Government, is the transport authority in the Northern Territory.

The Northern Territory public transport system comprises bus services in and around Darwin and Alice Springs, and ferry services from Darwin to Mandorah and to the Tiwi Islands.

In Darwin, buses are provided by private operators, Buslink and Territory Transit, under contract to the Northern Territory Government under the 'Darwinbus' brand. Services are also operated under the Darwinbus brand to surrounding areas such as Humpty Doo.

In Alice Springs, buses are provided by Buslink and other private operators under contract to the Northern Territory Government.

The ferry services from Darwin to Mandorah and the Tiwi Islands are operated by Sealink NT under contract with the Northern Territory Government.

Diagram 6: Governance and institutional arrangements – Northern Territory



Transport Authority: Public Transport Division for Northern Territory

Ferries (SeaLink)

3.5 QUEENSLAND

The Department of Transport and Main Roads (DTMR) is the transport authority in Queensland. DTMR is responsible for all facets of road, rail and public transport in Queensland. Public Transport is managed by DTMR's TransLink Division (TransLink). Unlike Transport for NSW and Transport for Victoria, TransLink is no longer a separate statutory agency since being reintegrated into DTMR in 2012. Formal statutory responsibility sits with the Director-General of DTMR.

Public transport services in Queensland comprise heavy rail, light rail, buses and ferries, and are provided by a mix of private and public sector bodies at state and local council government levels.

Metropolitan and regional rail services are provided by Queensland Rail, a statutory authority established under the *Queensland Rail Transit Authority Act 2013* (Qld). Queensland Rail discharges its statutory functions through its wholly owned subsidiary, Queensland Rail Limited. Queensland Rail provides both metropolitan rail services through its Citytrain services and regional rail services through Travel and Tourism services. Queensland Rail's services are delivered under a Train Service Contract managed by DTMR. The Citytrain network consists of over 152 stations across 13 lines, and caters primarily to commuter passengers in south-east Queensland. The regional network consists of over 5,700km of track and eight rail systems, and caters to long distance passenger services as well as freight. A new 10.2km rail line from Dutton Park to Bowen Hills, including four new stations, is currently being developed and is due to be completed in 2024.

Light rail services in the Gold Coast region are provided under a PPP arrangement with the state by a private consortium, GoldlinQ Pty Ltd, under contract to DTMR. The light rail system (G:link) consists of 20km of duplicated track, including 19 stations on one single line. A new Stage 3, 6.6km extension with eight new stations will extend the system to Burleigh Heads, with a further Stage 4, 14km extension to Coolangatta Airport being planned after the extension to Burleigh Heads is completed.

Bus services in South East Queensland are provided by the Brisbane City Council (trading as Transport for Brisbane) and 13 private bus operators, delivering 17 separate service contracts. Similarly, TransLink also manages 16 private bus operators delivering 18 separate service contracts in Regional Queensland. A new Brisbane Metro bus system is contemplated which will consist of two lines covering 21km linking Brisbane's outer suburbs with the CBD.

The Brisbane ferry services (CityCat and City Ferry) are operated by a private operator, Transit Systems (SeaLink),

under contract to Brisbane City Council. Other ferry services in Queensland are operated by private operators under contract to DTMR and operate on a variety of different subsidy regimes ranging from agreed cost to simplified concessional reimbursement regimes.

Diagram 7: Governance and institutional arrangements - Queensland

Transport Authority: Department of Transport and Main Roads (DTMR)

Administrative re	egulation →	Contractual regulation
Direct provision	Public operator	Private operator
	 Metro rail (C Regional rail (Tourism) South East Q buses (Transp Brisbane) 	 itytrain) Gold Coast light rail (GoldlinQ) (Travel and Metro buses (various operators) Regional buses (various operators) Brisbane ferries (Transit Systems) Other ferries (various operators)

3.6 SOUTH AUSTRALIA

The **Department for Infrastructure and Transport (DIT)** is the transport authority in South Australia. Public transport services are managed and overseen by the South Australian Public Transport Authority, which is a division of DIT. Like Translink in Queensland, it is not a separate statutory agency.

Public transport services in South Australia comprise heavy rail, light rail, buses and ferries. The services are provided by a mix of public and private sector operators.

Metropolitan rail and light rail services have until recently been provided by Adelaide Metro, which is a business name of DIT. The heavy rail network comprises six lines covering 132 km of track and 88 stations. A single 33-stop light rail route runs 16.5km from Glenelg to Hindmarsh. In mid-2019, the South Australian Government announced its intention to contract out heavy and light rail services through franchising arrangements. Following a tender process, in September 2020 the government announced that the new contract for the Adelaide metropolitan heavy rail network had been awarded to Keolis Downer, which will operate the network from the end of January 2021.

New contracts for Adelaide's bus and light rail services were awarded to private sector operators in March 2020. Three of the bus services contracts were awarded to Torrens Transit, and one bus services contract was awarded to each of Keolis Downer and Busways South Australia. The contract for services on the light rail network was awarded to Torrens Connect, a joint venture between Torrens Transit, UGL Rail Services and John Holland. The bus and light rail services contracts were scheduled to commence in July 2020.

Regional bus services are the subject of 28 contracts with private operators.

A passenger ferry service is operated between Cape Jarvis and Kangaroo Island by a private operator (Kangaroo Island SeaLink Pty Ltd) under contract with DIT.



Diagram 8: Governance and institutional arrangements - South Australia

Transport Authority: Department of Infrastructure and Transport (DIT)

Administrative regul	lation	Contractual regulation
Direct provision	Public operator	Private operator
 Metro rail (Adelaide Metro) (pre January 2021) 		 Metro rail (Keolis Downer) (post January 2021) Adelaide light rail (Torrens Connect) Metro buses (Torrens Transit and Australian Transit Enterprises) Metro buses (various operators) Ferries (Kangaroo Island SeaLink)

3.7 TASMANIA

The Department of State Growth (DSG) is the transport authority in Tasmania. Contracts with operators are entered into by the Secretary of State Growth in accordance with the *Passenger Transport Services Act* 2011 (Tas).

The Tasmanian public transport system comprises metropolitan and regional bus services, and a ferry service between the Tasmanian mainland and Bruny Island.

Bus services in the urban centres of Hobart, Launceston and Burnie are provided by Metro Tasmania Pty Ltd (Metro). Metro is a state-owned company established pursuant to the *Metro Tasmania Act* 1997 (Tas). Metro's shareholders are the Minister for Infrastructure and Transport and the Treasurer. The *Metro Tasmania Act* was amended in 2018 to allow Metro to operate public transport services in addition to those provided by road, such as ferry services. However, to date, Metro remains an operator of bus services only.

All other metropolitan and regional bus services in Tasmania, as well as the ferry service to Bruny Island, are provided by private sector operators under contract to DSG.

Diagram 9: Governance and institutional arrangements - Tasmania

Transport Authority: Department of State Growth

Administrat	tive regulation Contractual	regulation
Direct provision	Public operator	Private operator
	 Hobart, Launceston and Burnie buses (Metro Tasmania) 	 Other metro buses (various operators) Regional buses (various operators) Ferries (SeaLink)



3.8 VICTORIA

The Department of Transport (DOT) is the transport authority in Victoria. However, certain transport authority functions are carried out by Transport for Victoria (TfV), which is a statutory body established under the *Transport Integration Act 2010* (Vic). TfV has primary responsibility for the procurement and operation of public transport services, while DOT is responsible for strategic policy and planning.

Public transport services in Victoria comprise metropolitan and regional heavy rail, light rail and bus services and are provided primarily by private sector operators engaged under contract to TfV.

Metropolitan rail and light rail services are provided under franchise agreements with Metro Trains Melbourne and Yarra Trams, respectively. Melbourne's metropolitan rail network consists of 16 lines and 222 stations along 430 km of track, and is currently being extended via the Metro Tunnel Project which will introduce 9 km of rail tunnel and five new underground stations. Melbourne's light rail network consists of 24 routes and over 1700 stops along 250km of track. Metropolitan bus services are provided under several different contract types. A franchise agreement with Transdev accounts for approximately a third of the metropolitan bus network. The balance of the metropolitan network is divided into 15 regions, each of which is separately contracted by TfV to private operators under ten-year or seven-year contracts. Rural and regional services are provided under approximately 35 contracts with private operators.

The exception to private sector operation is regional rail services, which are provided by V/Line Corporation (V/ Line), a separately constituted public sector agency. Victoria's regional commuter rail network consists of 14 lines across Victoria. The V/Line services are regulated under a partnership agreement between V/Line and TfV. V/Line leases and maintains over 3,520km of rail track for use by commuter services and freight rail operators.

Diagram 10: Governance and institutional arrangements - Victoria

Administrative regulation Contractual regulation Direct provision Public operator Private operator • Regional rail (V/Line) • Melbourne rail (Metro Trains) • Melbourne light rail (Yarra Trams) • Melbourne bus franchise (Transdev) • Other Melbourne buses (various

Transport Authority: Department of Transport

3.9 WELLINGTON

Greater Wellington Regional Council (GWRC) is the transport authority in Wellington.

Wellington public transport services operate in accordance with the Public Transport Operating Model (PTOM) comprised of heavy rail, bus and ferry services grouped under 18 contractual units and operating under the 'Metlink' brand.

Heavy rail comprises five rail lines operating over 154km and 53 stations in one PTOM unit. The service is provided by a private operator, Transdev Wellington Limited, under contract to GWRC and Greater Wellington Rail Limited (GWRL). Transdev Wellington subcontracts Hyundai Rotem Company as the vehicle services subcontractor. Transdev also contracts KiwiRail to provide carriage locomotives and/or shunt services on the Wairarapa line.

operators)

operators)

Rural and regional buses (various

Bus services are provided by private operators contracted to GWRC. There are over 100 bus routes grouped into 16 PTOM where each unit is the subject of a separate contract. There are currently four operators engaged under these contracts, comprising Tranzit Group, NZ Bus, Mana Coach Services and Uzabus.

Two harbour ferry services (the City Cat and Cobar Cat) run commuter services between Days Bay, Queens Wharf and Seatoun under one PTOM unit. These services are contracted by GWRC to a private operator, East West Ferries Ltd.

Car Pty Ltd, which is a wholly owned subsidiary of the Wellington City Council (a separate entity to GWRC).

A funicular also runs between the central city and Kelburn. It is owned and operated by Wellington Cable

Diagram 11: Governance and institutional arrangements - Wellington

Transport Authority: Greater Wellington Regional Council

Administrative regulation		Contractual regulation
Direct provision	Public operator	Private operator
	• Funicular (Wellington Cable Car)	 Wellington rail (Transdev and Kiwirail) Buses (various operators) Ferries (Fast West Ferries)

3.10 WESTERN AUSTRALIA

The Public Transport Authority (PTA) is the transport authority in Western Australia. The PTA is a statutory authority established under the Public Transport Authority Act 2003 (WA) which is managed by a Managing Director, reporting to the Director General of the Transport Portfolio, who also manages the Department of Transport, Main Roads WA and the Portfolio Strategic Projects Office. The Department of Transport's key focus is providing strategic transport planning and policy across public and commercial transport systems in Western Australia, whilst the PTA's focus is delivering new public transport infrastructure and providing passenger transport services.

The WA public transport system comprises metropolitan and regional heavy rail services, metropolitan and regional bus services, dedicated school bus services, regional coach services and passenger ferry services.

All metropolitan public transport bus, train and ferry services operate on a fully integrated basis under the Transperth banner which is a business name of the PTA. Transperth Train services are predominately provided by PTA staff, although some major functions are outsourced,

including above-rail and below-rail maintenance. The metropolitan rail network comprises five lines of more than 180km of track and 72 stations. Transperth bus services are provided by three bus service contractors, Swan Transit (Transit Systems/SeaLink), Transdev and Path Transit (Keolis Downer), operating 11 contract areas, which are retendered on a rolling basis approximately every two years. The Transperth bus network operates approximately 1,450 buses covering 292 standard bus routes and 293 dedicated school routes. Transperth ferry services operating between Perth and South Perth are also provided under contractual arrangements with a private operator (Captain Cook Cruises/SeaLink).

Regional intra-town passenger services are delivered by the PTA under the Transwa banner which is also a business name of the PTA. The regional rail network operates across four routes and road coaches operate over 29 routes, serving more than 240 regional locations.

Regional Town bus services are also administered by the PTA under contractual arrangements with private operators. They operate under a general TransRegional banner (eg TransBunbury) in 14 major regional towns.

Diagram 12: Governance and institutional arrangements – Western Australia

Transport Authority: Public Transport Authority

Administrative regulation		lation	Contractual regulation
	Direct provision	Public operator	Private operator
	Metro rail (Transperth)Regional rail (TransWA)		 Metro buses (Path Transit, Swan Transit and Transdev) Regional buses (various operators)

Perth ferries (Captain Cook Cruises)

4 OVERVIEW OF KEY DESIGN VARIABLES

In broad terms, public transport service contracts represent the outcome of a series of choices about the numerous variables that make up the structure and design of the contract. These choices are influenced by the commercial and policy objectives set by government for the particular transport service, as well as the governance and institutional environment in which the contract will operate.

Public transport service contracts are invariably long and complex documents. The published version of the Sydney Metro Northwest contract runs to over 750 pages, comprising the body of the agreement together with 46 schedules. The published version of the Melbourne Metro Rail Franchise Agreement comprises eight separate modules running to over 1200 pages. The published version of the Wellington Metro Rail contract is over 580 pages in length.

The length and complexity of public transport service contracts reflects the multifaceted nature of public transport service provision and the many elements which need to combine to provide passenger services. These include the availability of relevant infrastructure, the availability of the rolling stock, bus or ferry fleet, service planning and coordination, the operation of scheduled services, the provision of customer information, arrangements for fare collection and enforcement, management of disruptions and management of the interfaces between current operations and major projects being undertaken on the network. The respective roles of the transport authority and transport operator in each of these areas, as well as many others, need to be clearly specified if the contract is to function effectively. In addition, the long duration of many public transport service contracts means they need to be forward looking and flexible so as to be able to accommodate changes to service requirements, changes in government policy priorities and changing consumer preferences.

Table 4 provides an indicative list of the main clause headings likely to be included in a public transport service contract. Some of these can be expected to follow a relatively standard formulation, while others are likely to be tailored to the particular preferences (in terms of policy and practice) in the jurisdiction concerned, as well as the governance and institutional environment.

 Access and Inspections Accreditation and compliance Asset Management Assignment and Change of Control Commercial Opportunities Compensation Events Conditions Precedent 	 Default and Termination Dispute Resolution End of Term Requirements Fares and Ticketing Governance Indemnity and Liability Insurance Intellectual Property 	 Network Services Coordination Objectives Payments Performance Regimes Privacy Projects Regime Records and Reporting Relief Events 	 Safety Security Service Changes Service Requirements Step-in Subcontracting Term Warranties
ConfidentialityData and Systems	 Key Contracts Modifications	 Restrictions on Activities 	

The selection of an appropriate set of design variables for consideration in this report aims to achieve a balance between comprehensiveness and materiality. The report identifies 10 design variables which are considered most significant in terms of the relationship between contract design and achievement of the transport authority's objectives for the contract. They are also the variables most likely to be relevant across all jurisdictions, providing an opportunity for cross-jurisdictional comparisons.

Table 4: Typical service contract clause headings

Each design variable is summarised below and is considered in detail in the following sections of the report.

Contract term	Refers to the length of the initial contract term, whether there are priced or unpriced options to extend the contract, whether the operator can 'earn' an extension based on performance, and whether the transport authority has a right to terminate the contract early in the absence of default.
Service model	Refers to the scope of the services provided under the contract, including the operator's responsibilities with respect to passenger services, infrastructure maintenance and renewal and vehicle (rolling stock, bus, ferry) maintenance and renewal.
Revenue model	Concerns the basis of payment to the operator under the contract, including whether the contract operates as a net cost contract under which the operator is entitled to retain farebox revenue, or a gross cost contract under which the farebox is retained by the transport authority.
Performance regimes	Refers to the mechanisms in the contract designed to incentivise the particular performance outcomes the transport authority is seeking. The review focusses on the existence and nature of regimes addressing punctuality and reliability, customer experience and asset management.
Service change regime	Refers to the mechanisms in the contract which deal with the transport authority's need to make changes to the services, including timetable changes and the addition and cessation of services.
Risk allocation	A potentially very broad area, as there will be different risk categories depending on the service model. For the purposes of this report, the review is focussed on two key risk issues – the allocation of revenue risk and operating cost risk.
Network integration	Refers to the way in which the contract addresses the operator's engagement in network- wide functions such as the provision of transport information, wayfinding signage, marketing, and multi-modal ticketing.
Projects regime	Refers to the nature of any provisions in the contract which deal with new investment in the network. This may be investment by the operator at the instigation of the transport authority, or investment by the authority which requires the cooperation of the operator.
Financial security	Refers to the nature and quantum of mechanisms securing operator performance. These include requirements for the provision of performance bonds, minimum capital requirements, restrictions on engaging in other activities, and the provision of securities over the assets of, and shares in, the operator.
End of term arrangements	Refers to the provisions in the contract governing the retendering of the right to operate the services upon expiry of the contract and transition to a new operator, including provisions governing the transfer of assets and employees to a successor operator and obligations to facilitate the retendering process.

5 ANALYSIS OF KEY DESIGN VARIABLES

5.1 CONTRACT TERM

Selecting the duration of a service contract is a matter of carefully balancing a range of competing considerations.

Longer concessions are often supported on the basis that they provide operators with a better opportunity to achieve organisational and cultural change, and encourage better quality investment by the operator by ensuring the operator does not focus on short-term solutions and returns. Longer concessions may also be justified to support value for money outcomes where new capital investment is required. This is the case under PPP contracts, where the operator is responsible for financing the development of the relevant network, as well as operating and maintaining it. In those circumstances, a longer concession is typically required for the operator to recoup the cost of the development work given that, under a PPP model, service payments typically only commence once the infrastructure delivery phase is complete and operational service has commenced.

However, longer concessions take day-to-day operational control of the relevant network away from the transport authority for a longer period and may constrain the authority's ability to implement policy or operational change, which can be both politically and socially sensitive. Longer concessions may also give the incumbent operator an advantage (real or perceived) in future retendering processes and reduce the competitive pressures felt by the operator which incentivise performance. They can also increase the exposure of the operator to longerterm macroeconomic factors and make it more difficult for them to accurately forecast costs, revenues and risks for bidding purposes. This risk can then end up being passed on to the transport authority, either by way of



risk premia being incorporated in contract payments, or through failure of the contract. This was the case with the initial Melbourne train and tram franchise contracts, where National Express handed back its train and tram concessions only three years into a 15-year contract term, in large part due to overly optimistic patronage and revenue forecasts.

The contract term may also be influenced by the procurement model, with contracts awarded through sole source negotiations or limited tenders likely to be shorter term and with more limited options to extend.

Table 5 below provides a high level overview of key aspects of the contract term provisions in the suite of service contracts reviewed across the dimensions of initial term, options for extension, and rights to terminate early without cause (so-called 'termination for convenience').

Initial term

As Table 5 demonstrates, the initial term of the contracts reviewed ranges from 6 to 20 years. As expected, the contracts relating to PPP projects typically have longer concession terms – 20 years in the case of Capital Metro Light Rail and 15 years for Sydney Metro Northwest, Sydney Light Rail and Gold Coast Light Rail. A key differential amongst the PPP-related contracts concerns the commencement date for the initial term and, in particular, whether the contract term is tied to the date of actual or expected completion of construction, thereby affecting the allocation of delay risk between the parties.

For non PPP service contracts the term is typically between 8 and 10 years. The relatively short seven-year term of the Melbourne Rail Franchise and Melbourne Tram Franchise contracts needs to be understood in context – both contracts were the result of sole-source negotiations with existing operators who secured the right to negotiate the contracts with the transport authority under their previous contractual arrangements. The previous contracts provided for an initial eight-year term with a seven year unpriced option to extend, subject to the satisfaction of performance criteria and the conduct of a good faith negotiation of price and terms.

The Auckland Bus Services contracts have differing initial terms depending on the procurement model applied in awarding the contracts:

 Like-for-like contracts: As part of the transition to the New Zealand Public Transport Operating Model (PTOM) in 2013, from the previous model of operators registering commercial transport services with councils, existing operators were offered a once-only 12-year fixed-term contract. The new PTOM contracts contained an equivalent number of in-service kilometres to those held in existing commercial registrations, in exchange for relinquishing those commercial registrations.

- Tendered service contracts: Under the PTOM, a proportion of the public transport network must be competitively tendered. Contracts based on successful tenders will have a term of nine years, to incentivise this mode of contracting.
- Other negotiated service contracts: If an operator meets certain criteria demonstrating above average commerciality for the region, the authority will renegotiate the contract for the service, rather than enter into a tendering process. The availability of negotiated contracts aims to incentivise operators to improve the commerciality of their services. These negotiated contracts have a term of six years; and
- Contracts which are reclassified as a Commercial Unit:¹⁰ Contracts may be re-classified where the farebox revenue was at least equal to annual gross cost for the Unit for the most recent contract year. These contracts will have an initial term of nine years. The longer tenure length for Commercial Units is intended to incentivise operators to become fully commercial.

Options for extension

Most of the contracts reviewed provide for an optional extension to the term of the contract, ranging from six months to six years. Typically, the extension right is exercisable by the transport authority and can be exercised multiple times up to the maximum time period, which has the benefit of giving the authority flexibility in managing a retendering process or to resume public operation at the end of the contract.

Leaving aside the existence of an option to extend, however, there is little commonality amongst the provisions. There is significant variation from contract to contract as to the length of the extension period, the extension mechanism, whether extension is tied to performance and the terms of the extension (including whether the extension is pre-priced or conditional on the operator making a new pricing proposal which is acceptable to the transport authority).

Early termination other than for default

Finally, the majority of contracts reviewed provide for early termination of the contract in circumstances other than simply operator default. In particular, many of the contracts provide the transport authority with the right to terminate without cause (so-called 'termination for convenience') and provide one or both parties with the right to terminate for extended force majeure, and specify the financial consequences of these rights being exercised, including any applicable termination payments.

Under the Newcastle Integrated Services, Sydney Bus Services and Sydney Ferry System contracts, the transport authority also reserves the right to terminate if performance benchmarks are not met, with no termination payment payable to the operator in these circumstances. This approach can be viewed as operating. as an alternative to a shorter initial term with an option to extend.



¹⁰ Under the Auckland Bus Services contract, services are grouped into 'units' of routes. Either the transport authority or the operator may propose to the other party that an existing Unit be reclassified as a Commercial Unit during the term of the service contract. As noted in Table 5 below, the revenue model for Commercial Units is different to non-Commercial Units and operates on a net cost basis.

Table 5: Contract term

Contract	Initial term	Extension period	Extension trigger & is it priced?	Early termination other than for default
Sydney Metro Northwest	15 years from Date for Completion	Up to 2 years	Transport authority can request an extension proposal prior to expiry. The extension proposal must include projected costs/fees. Transport authority has full discretion to accept or reject the extension proposal.	 Transport authority: Convenience Uninsurable risk Unable to reach agreement on an Augmentation Either party: Force Majeure Termination payments differ depending on termination trigger.
Sydney Light Rail	15 years from Date for Completion	Up to 2 years	As above.	 Transport authority: Convenience Uninsurable risk Unable to reach agreement on an Augmentation Either party: Force Majeure Automatic: If a Planning Modification is refused and parties cannot agree on a resolution Termination payments differ depending on termination trigger.
Newcastle Integrated Services	10 years	None	N/A	 Transport authority: If the first 5 years' performance benchmarks are not met Convenience Force Majeure Termination payments differ depending on termination trigger.
Parramatta Light Rail	8 years	Redacted	Redacted	 Transport authority: Convenience Either party: Force Majeure Termination payments differ depending on termination trigger.
Sydney Bus Services	8 years (can be reduced to 5 if performance benchmarks are not met)	None ¹¹	N/A	 Transport authority: If the performance benchmarks as at the end of the first four years are not met Convenience Force Majeure Termination payments differ depending on termination trigger.

11 This is based on the Region 6 contract. Some contracts have a discretionary 1 year extension option.

Contract	Initial term	Extension period	Extension trigger & is it priced?	Early termination other than for default
Sydney Ferry System	9 years	None	N/A	 Transport authority: If the performance benchmarks at the end of the first four years are not met Convenience Termination payments differ depending on termination trigger.
Melbourne Rail Franchise	7 years ¹²	Up to 3 years	At the transport authority's discretion, at least 6 months prior to expiry. Extension is on the same terms and is priced.	 Transport authority: Fundamental Change (in the nature of the Franchise Business or the operating characteristics of the train network, whether due to a change in state policy or otherwise).
Melbourne Tram Franchise	7 years	Up to 3 years	At the transport authority's discretion, at least 6 months prior to expiry. Extension is on the same terms and is priced.	 Transport authority: Fundamental Change (in the nature of the Franchise Business or the operating characteristics of the tram network, whether due to a change in state policy or otherwise).
Melbourne Bus Franchise	7 years	3 years	Automatic extension if performance criteria satisfied. Extension is on the same terms and is priced.	Transport authority: • Convenience If terminating for convenience, the transport authority pays the Franchisee a predetermined termination payment.
Melbourne Bus Services	8 years	2 years	Automatic extension if performance criteria satisfied. Extension is on the same terms and is priced.	Redacted
Gold Coast Light Rail	15 years from Financial Close ¹³	None	N/A	Transport authority: • Convenience • Uninsurable risks Either party: • Force Majeure Termination payments differ depending on termination trigger.

¹² The previous Melbourne Rail Franchise and Melbourne Tram Franchise agreements were for a term of eight years and granted the operators an exclusive right to negotiate a new seven-year agreement if they met certain performance benchmarks.

¹³ Financial Close occurs prior to construction, once the conditions precedent have been satisfied or waived.

Contract	Initial term	Extension period	Extension trigger & is it priced?	Early termination other than for default
Capital Metro Light Rail	20 years from Services Completion ¹⁴	Up to 5 years	Transport authority can request an extension proposal at least 33 months prior to expiry. The extension proposal must include projected costs/fees. Transport authority has full discretion to accept or reject the extension proposal.	 Transport authority: Convenience Either party: Force Majeure Termination payments differ depending on termination trigger.
Auckland Metro Rail	8 years	None; however, has been extended by mutual agreement	N/A	N/A
Auckland Bus Services	12 year fixed term for 'like-for-like' contracts 6 years for any other negotiated service contract 9 years for a tendered service contract 9 years for a service contract for a 'Commercial Unit'	None	N/A	 Transport authority: Insufficient funding Change in law that results in the transport authority being unable to satisfy its legislative requirements through the service contract If terminating for funding or policy constraints, no termination payments are payable by the transport authority. Either party: Force Majeure
Wellington Metro Rail	9 years	Up to 6 years	Operator can request an extension (at least 23 months prior to expiry) where it has satisfied performance criteria across the last 3 years of the initial term. If the Operator does not do so, the transport authority can extend the contract by up to 3 years. Extension is on the same terms and is priced.	Transport authority: • Convenience • Force Majeure Termination payments differ depending on termination trigger.
Wellington Bus Services	9 years (tendered units) 12 years (direct units)	At the discretion of the transport authority	Transport authority can issue an extension notice (specifying the extension period) at least 6 months prior to the initial expiry date, or 3 months prior to the end of any extension period. Extension is on the same terms and is priced.	Transport authority:ConvenienceForce MajeureTermination payments differ depending on termination trigger.

¹⁴ Services Completion occurs once all the Services Completion Criteria have been satisfied (ready for services to commence).

5.2 SERVICE MODEL

The service model refers to the scope of services for which the transport operator has responsibility. Design of the service model can be a material factor in determining the quality and reliability of passenger-service outcomes. In a franchising context, the service model can also be an important factor in determining the market response to the franchise opportunity, both in terms of attractiveness to the market and consortium structures.

Service model components

The potential components of the service model will clearly vary between alternative public transport modes (heavy rail, light rail, bus and ferry), and there is a wide range of activities associated with the provision of public transport services that can potentially be assigned either to the operator or the transport authority, or for which they can have shared responsibility. For the purpose of this report the service model components have been broadly categorised as comprising the following:

Passenger Services	Refers to the operation of the passenger fleet (trains, light rail vehicles, buses, ferries) to carry passengers in accordance with the designated timetable or headway/frequency. Typically, this involves the provision and management of drivers and certain other customer-facing staff, and responsibility (in many cases shared with the transport authority) for the provision of transport information, management of customer information and complaints, safety and security, marketing, ticketing and revenue protection.
Facilities Management	Refers to responsibility for the management and maintenance of customer-facing facilities such as stations, stops and interchanges. Services typically include responsibility for cleaning, graffiti removal, presentation and light maintenance of the facilities. Facilities maintenance might also include repair and renewal, or this might be dealt with separately as a shared function or be retained by the transport authority.
Fleet Management	Refers to responsibility for the management and maintenance of the fleet of vehicles used to provide passenger services. As with Facilities Management, this typically includes cleaning, graffiti removal and presentation, and may include scheduled maintenance, reactive maintenance and major overhauls. Alternatively, maintenance and major overhauls may be contracted for separately by the transport authority in conjunction with fleet procurement. Fleet Management may also include responsibility for the management and maintenance of depots and stabling facilities.
Infrastructure Management	Refers to responsibility for the management and maintenance of the network infrastructure required to provide passenger services. In a rail context, this includes track and traction power systems and signalling systems. Stations and stops could also be characterised as infrastructure, as could depots and stabling facilities. However, it is useful to distinguish them from network infrastructure (as outlined above) as they are generally treated differently in practice in service model design. On this basis, Infrastructure Management in the sense used here is usually not relevant to bus and ferry service contracts, as there is generally no network infrastructure equivalent to the rail network.
Revenue Protection	Refers to responsibility for enforcing fare rules. As noted above, revenue protection is aligned with responsibility for passenger services, but it is useful to consider it separately. Most jurisdictions require enforcement powers to be exercised by persons holding an authorisation or accreditation to do so, and the question is whether this function is carried out by the operator or the transport authority. Where the transport authority is responsible for enforcement, the operator may still have obligations to support and cooperate in the transport authority's revenue protection activities as part of the passenger services function.

A variety of factors will influence the approach to service model design. These include the perceived implications of the service model for customer experience, the governance and institutional framework, the regulatory environment, policy and political preferences concerning the scope of delegation of transport authority functions, and the implications of the service model for the market's response to the opportunity where a competitive procurement process is involved.

Table 6 provides a high level summary of the service model across each of the contracts reviewed. This indicates a relatively high degree of service integration, especially in Australian jurisdictions. The provision of passenger services represents the defining characteristic of public transport service contracting, and so is reflected in all contracts. Most Australian contracts include Facilities Management, Fleet Management and, where relevant to the transport mode, Infrastructure Management (although there are many differences in the detailed scope of those services). Australian jurisdictions also generally include responsibility for revenue protection. This contracts with the position in New Zealand, where service contracts tend more often to be limited to passenger services. Some of the reasons why this might be the case are touched on below.

Customer experience

The potential influence of the service model on customer experience is a key consideration in service model design. As a general proposition, it is thought that better customer-experience outcomes are likely to be achieved where a single operator has responsibility and accountability for each aspect of the service with the potential to impact the customer. This is both because of the operator's ability to ensure consistency in the style and standard of service delivery, as well as to control the multiple inputs that make up the passenger's end-to-end journey. This tends to favour a service model where the operator is responsible for more (rather than less) of the service model components described above.

There are, however, several constraints on a fully integrated service model in particular settings, and there are some considerations that may tend to argue against greater integration.

Governance and institutional framework

The governance and institutional framework is a significant determinant of the service model and can impose practical and legal constraints on the scope of services contracted to the operator. In jurisdictions where rail infrastructure is owned and operated by a separate entity to the transport authority and provided to one or more operators under an access regime, integration is not practically or legally possible without significant sectoral reform. This is further complicated where different levels of government have responsibility for rail infrastructure and passenger services, as in New Zealand where KiwiRail, a national government agency, owns and operates rail network infrastructure while local government organisations are responsible for providing passenger services.

Regulatory environment

A third factor is the impact of the regulatory environment. Consideration needs to be given to the regulation of government procurement in general, as well as transport-specific regulation which may mandate factors such as contract term, elements of contract design, and tendering requirements and constraints. The Land Transport Management Amendment Act 2008 (LTAM) in New Zealand and the Bus Services Act 1995 (formerly the Public Transport Competition Act) in Victoria are examples.

The need and process for obtaining the accreditations required for particular services must also be reviewed, as this may affect the practicality and timing of the service procurement. The requirements for safety accreditation are particularly important in this context. In the context of revenue protection services, there will typically be a requirement for enforcement functions to be performed by persons who hold an authorisation or accreditation to exercise coercive powers, such as to require names and addresses of offenders and to issue infringement notices. Consideration needs to be given to whether it is possible for the operator's employees to obtain and hold the required authorisation or accreditation.

Policy preferences

The last point highlights the potential relevance of broader policy preferences, and policy constraints, that might influence service-model design in particular jurisdictions. There may be political or institutional predispositions which suggest that certain services are most appropriately carried out by the transport authority rather than the operator. Revenue protection is an example, but this may also be the case in relation to asset management, customer information and customer complaints management. In addition to policy preferences, these positions may also be influenced by the industrial relations environment and the attitudes of unions, workers and government to the transfer of employees from public to private-sector employers, and the mechanisms for, and implications of, doing so. More broadly, the use of PPPs as a project procurement model, which tends to lead to a high degree of service integration, can be viewed as reflecting the outcome of the relevant government's policy preferences.

Market engagement

Finally, in a context where transport services are being tendered through a competitive procurement process, the impact of the service model on the market response to the franchise opportunity is a further important consideration. The service model will determine the size of the opportunity as well as the scope that the new operator has to apply its expertise and capacity for innovation to implement efficiencies and service improvements, and to capture the value of doing so, over the term of the contract. The time and resources required to submit a competitive proposal in a tender process mean a service model which is overly constrained - eg limited to the provision of passenger services alone – may be less likely to attract a competitive field of potential operators, especially those who do not already have a presence in the relevant market.

Table 6: Service model

Contract	Passenger Services	Facilities Management	Fleet Management	Infrastructure Management	Revenue Protection
Sydney Metro Northwest	\checkmark	√	\checkmark	\checkmark	×
Sydney Light Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark
Newcastle Integrated Services	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark
Paramatta Light Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark
Sydney Bus Services	\checkmark	\checkmark	\checkmark	NA	\checkmark
Sydney Ferry System	\checkmark	\checkmark	\checkmark	NA	\checkmark
Melbourne Rail Franchise	\checkmark	\checkmark	\checkmark	\checkmark	✓
Melbourne Tram Franchise	\checkmark	\checkmark	✓	\checkmark	\checkmark
Melbourne Bus Franchise	\checkmark	\checkmark	✓	NA	\checkmark
Metropolitan Bus Services	\checkmark	✓	\checkmark	NA	\checkmark
Gold Coast Light Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark
Capital Metro Light Rail	\checkmark	\checkmark	✓	\checkmark	\checkmark
Auckland Bus Services	\checkmark	×	\checkmark	NA	\checkmark
Auckland Metro Rail	\checkmark	×	×	×	×
Wellington Metro Rail	\checkmark	×	\checkmark	×	\checkmark
Wellington Bus Services	\checkmark	×	\checkmark	NA	×



5.3 REVENUE MODEL

The revenue model refers to the treatment of farebox revenue derived from the provision of passenger services, as well as the treatment of revenue that can be generated from commercial opportunities associated with the use of transport assets, such as advertising on vehicles and at stations and stops.

Table 7 provides a high level summary of the revenue model across each of the contracts reviewed.

Farebox revenue

The principal design issue concerns the treatment of farebox revenue, where a distinction can be drawn between the use of gross cost contracts and net cost contracts. Under a gross cost contract, the transport authority retains all farebox revenue and pays the operator the agreed cost of providing the services for which the operator is responsible. Under a net cost contract, the operator is entitled to retain farebox revenue derived from the provision of passenger services (or some part of it) and is paid the additional subsidy required to make up the difference between the farebox and the agreed cost of providing services.

In both cases the agreed cost of providing the services is determined through the service contract procurement process. The difference is that under the gross cost model the operator is not required to make any forecasts about patronage or revenue in formulating its financial offer, whereas under the net cost model these will be key elements that contribute to the financial aspects of the operator's offer. The operator must take a view on patronage and revenue over the term of the contract, and then bid the difference between assumed revenue and the cost of providing services.

Prevalence of the gross cost model

As appears from Table 7, the gross cost model is by far the most commonly used in Australian and New Zealand service contracts. This most likely reflects judgments about the most appropriate allocation of revenue risk.

By its nature, the net cost model confers revenue risk on the operator, whereas under the gross cost model revenue risk sits with the transport authority. The assumption of revenue risk by the operator can be expected to result in higher cost contracts because of the likelihood that operators will require a premium to assume the risk. The prevalence of gross cost contracts in large part reflects a judgment that this risk premium may not represent a value for money outcome because the factors driving patronage and revenue are largely outside the control of the operator. Service quality and reliability are certainly factors that will influence patronage, and these are matters in respect of which the operator has substantial control. The allocation of revenue risk to the operator has the benefit of incentivising operator performance in these and other areas that impact customer experience. However, macro-economic factors such as economic growth, urbanisation and population growth are likely to be far more significant, and these are clearly outside the control of the operator. Similarly, network investment will have a role to play in service quality and reliability, and this is typically the responsibility of the transport authority rather than the operator.

Moderating the differences between gross cost and net cost models

There are two important ways in which the gross cost and net cost models have been modified to take account of these considerations, and which tend to diminish the distinctions between them.

First, many gross cost contracts incorporate a patronage incentive mechanism where the operator receives additional revenue if growth in patronage exceeds a benchmark level specified in the contract. The aim is to incentivise the operator to improve operational performance and customer service, but the operator's financial exposure is calibrated in a way that recognises the limited control the operator has on aggregate patronage. This is shown in Table 7, which identifies those gross cost contracts incorporating patronage incentives.

Second, net cost contracts may incorporate risk-sharing mechanisms that ameliorate the operator's exposure to revenue risk. Again, this recognises the limited ability the operator has to manage the risk, as well as the prospect of financial instability that can arise where the operator's revenue assumptions prove to be materially incorrect. The Melbourne Rail Franchise and Melbourne Tram Franchise contracts both incorporate risk-sharing mechanisms that limit the operators' exposure to revenue risk over the term of the contract, despite the contracts



being net cost contracts. This is achieved through two mechanisms:

- The first is a 'cap and collar' mechanism under which the transport authority shares 50% of the downside risk where actual revenue falls short of forecast revenue beyond a specified lower bound. The authority also shares 50% of the upside risk where actual revenue exceeds forecast revenue by more than a specified upper bound.
- The second is a 'revenue reset' mechanism under which the franchise payments are adjusted every two years to take account of differences between forecast and realised revenue. Where actual revenue is below the forecast level, the subsidy payments are adjusted up by a corresponding amount, and where actual revenue is more than forecast, the subsidy is adjusted down. The adjustment only operates prospectively, so that the operator effectively takes the risk of a divergence between forecast revenues and actual revenues in the period between resets.

The Auckland Bus Services contract incorporates a risk sharing mechanism based on a 'Base Revenue', which is equal to the actual revenue from the first contract year. The Base Revenue is adjusted:

- annually for movements in indices for the weighted average of costs for public transport, as published by the New Zealand Transport Agency; and
- at the end of each third contract year to equal the actual revenue from the third contract year.

For a non-Commercial Unit (which uses a gross cost model), the transport authority pays the operator a proportion of any increase in annual revenue from the Base Revenue and the operator pays the transport authority a proportion of any decrease in annual revenue from the Base Revenue. For a Commercial Unit (which uses a net cost model), the operator pays the transport authority a proportion of any increase in revenue from the Base Revenue, but the transport authority is not required to make any payments for a decrease in revenue from the Base Revenue. The share proportions may differ between service contracts for different operators.

Treatment of commercial opportunities

The second aspect of the revenue model concerns the treatment of revenue that can be earned from commercial opportunities associated with the transport network. These can arise in several ways. The most obvious is the opportunity to use transport assets and infrastructure, such as rolling stock, buses, stations and stops, for advertising. There may also be opportunities to grant leases or licences for the provision of retail services on transport property, such as retail concessions at stations, and opportunities to generate revenue from the customer interface and access to customer data. In a PPP context, where new transport infrastructure is being procured in addition to O&M services, there are potentially significant alternative revenue streams arising from value-capture mechanisms such as over-station development. These are not within the scope of this report.

As with farebox revenue, the contract design issue is whether revenue derived from commercial opportunities of this kind is retained by the transport authority or is made available to the operator. In the latter case, the value of the anticipated revenue over the term of the contract will be considered in formulating the operator's offer as part of the procurement process, and would be expected to result in a corresponding reduction in the contract price for providing services.

As Table 7 shows, the transfer of revenue from commercial opportunities to operators is more common than the transfer of farebox revenue. This is especially so in relation to advertising. It is likely this reflects the greater certainty with which operators are able to value commercial revenue opportunities and the greater degree of control they have over the realisation of that value through, for example, their approach to, and negotiation of, advertising arrangements. Industry knowledge and innovation creates the opportunities than the transport authority, and for this to be reflected in their financial offers when tendering for the right to provide services.

There are, however, competing considerations. From the public's perspective the transport infrastructure to which these commercial opportunities attach is generally identified with the transport authority rather than the operator, meaning the transport authority has a strong



interest in ensuring that commercial activities and the way in which they are undertaken are consistent with its desired image and community expectations. In some cases, this concern may be strong enough to warrant the retention of these opportunities. In those cases where they are delegated to the operator, the service contract will generally include controls on the way the rights are exercised, especially in relation to advertising rights.

Finally, consideration needs to be given to the treatment of commercial revenue opportunities that

might not be foreseen at the time of contracting. This becomes more important as the value of data and the opportunities arising from controlling the interface with customers becomes more apparent. In principle, it seems appropriate that commercial opportunities of any kind arising from the provision of passenger services should reside with the transport authority, so that the sole revenue streams available to the operator from providing services to passengers are those prescribed in the service contract. This position is reflected in several of the service contracts covered in the review.

Table 7: Revenue model

Contract	Farebox revenue	Patronage incentive	Commercial opportunities
Sydney Metro Northwest	Gross cost	No	Operator may only pursue advertising, retail licences and other commercial opportunities with TfNSW's approval.
Sydney Light Rail	Gross cost	No	Operator can engage in advertising on the interior and exterior of LRVs and engage in other commercial opportunities with TfNSW's approval. The agreement specifies a process for seeking approval, which includes revenue sharing according to a specified percentage or other percentage proposed by the operator.
Newcastle Integrated Services	Gross cost	Yes	Operator entitled to advertise on vehicles and TfNSW on other assets. Operator can pursue other commercial opportunities with TfNSW approval.
Paramatta Light Rail	Gross cost	No	Operator may only pursue advertising and other commercial opportunities with TfNSW's approval.
Sydney Bus Services	Gross cost	Yes	Operator entitled to advertise on vehicles and undertake private charter work. Operator can pursue other commercial opportunities with TfNSW approval.
Sydney Ferry System	Gross cost ¹⁵	No	Operator entitled to advertise on the interior of ferries and TfNSW on the exterior of ferries and all other assets. Operator can pursue other commercial opportunities with TfNSW approval and based on agreed revenue sharing arrangements.
Melbourne Rail Franchise	Net cost	No	Operator is entitled to advertise in stations and on Franchise Assets. Operator is entitled to grant sub-leases and licences for retail purposes or other commercial activities within the station precincts.

¹⁵ The operator retains farebox revenue it collects and TfNSW remits to the operator revenue collected via the ticketing system that is referable to fares. However, the Payment Schedule provides for a fixed monthly payment and the actual monthly farebox revenue is deducted from this payment. The net effect is that this operates as a gross cost contract.

Contract	Farebox revenue	Patronage incentive	Commercial opportunities
Melbourne Tram Franchise	Net cost	No	Operator is entitled to advertise on Franchise Assets, except for W Class trams and City Circle trams.
			Operator is entitled to grant sub-leases and licences for retail purposes or other commercial activities within the light rail stop precincts.
Melbourne Bus Franchise	Gross cost ¹⁶	Yes	Operator is entitled to apply advertising material on any assets other than Smart Buses.
Metropolitan Bus Services	Gross cost	Yes	Operator is entitled to advertise on buses and at depots with TfV's prior consent. TfV is entitled to a specified percentage of advertising revenue (redacted).
Gold Coast Light Rail	Gross cost	No	Operator is not entitled to undertake any commercial opportunities except with TransLink's consent. Under these arrangements the operator is entitled to grant sub-leases and licences for retail purposes or other commercial activities within the light rail stop precincts subject to TransLink consent. The state reserves the right to undertake advertising on the system.
Capital Metro Light Rail	Gross cost	No	Operator can earn revenue from commercial opportunities with the Territory's consent. The Territory is entitled to 50% of the revenue from approved commercial opportunities unless another percentage is agreed in relation to a particular opportunity.
Auckland Metro Rail	Gross cost	No ¹⁷	Not dealt with expressly. On that basis, commercial opportunities remain with Auckland Transport.
Auckland Bus Services	Net cost for a Commercial Unit ¹⁸ Gross cost if not a Commercial Unit	No	Operator is not entitled to enter into any advertising contracts. Transport authority manages advertising on the interior and exterior of buses. The operator is entitled to 20% of the net revenue from advertising.
Wellington Metro Rail	Gross cost	Yes	Operator may only undertake additional revenue generating services or facilities to the extent contemplated in an approved business plan or otherwise approved by GWRC. GWRC is entitled to receive 50% of the profit from such approved activities. GWRC controls all advertising space on vehicles.
Wellington Bus Services	Gross cost	Yes	Operator may only undertake additional revenue generating services or facilities to the extent contemplated in an approved business plan or otherwise approved by GWRC. GWRC is entitled to receive 50% of the profit from such approved activities. GWRC controls all advertising space on vehicles.

¹⁶ The Melbourne Bus Franchise also provides for payment of a 'shadow fare' which is essentially a patronage incentive mechanism, paid at a rate for each passenger above the benchmark patronage amount for the period.

¹⁷ The Financial Schedule (Schedule 9) states that the operator will be rewarded for growth of annual fare revenue but will bear the risk of underachievement. However, it is not clear from the published version how this principle is reflected in the payment provision.

¹⁸ See section 5.1 above for a description of a Commercial Unit.

5.4 PERFORMANCE REGIMES

Performance regimes are commonly included in public transport service contracts to incentivise the performance outcomes the transport authority is seeking, give operators a greater stake in the system and help to ensure alignment in the objectives of the transport authority and the relevant operator. The introduction of a performance regime has been identified as key to the success of passenger rail franchising in Victoria, with performancebased payments and penalties recognised as a key factor in improving service standards.¹⁹ That said, there is no one regime that suits all systems and the regime needs to be carefully structured and calibrated for the relevant system to encourage the desired behaviour and avoid perverse outcomes or manipulation by operators. For example, incentivising on-time performance has been reported to lead to station/stop skipping by operators if services are running late, or slow operation speed and stop dwelling if services are running early, in order to achieve punctuality targets.

Targets and thresholds also need to be set at the right levels in order to create a genuine incentive, preferably based on robust historical data.

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Prevalence and nature of performance regimes

Performance regimes are a standard feature of all PPP contracts, not just those relating to public transport infrastructure. In a PPP contract, performance is measured against specific key performance indicators (KPIs) and deductions are made from payments due to the operator (called 'abatements') if the relevant facility is not available or fails to perform at the levels specified in the KPIs. Failure to meet KPIs most often results in deductions from the contract fee, but some contracts, such as the Sydney Metro Northwest contract, also include financial incentives for high performance.

Performance regimes are also included in all the non-PPP contracts reviewed; however, there is significant variance in the approaches adopted, including as to whether the performance regime:

- triggers financial consequences, triggers the default/ termination regime in the contract, or both; and
- triggers penalty (or abatement) payments, triggers incentive payments, or both.

Table 8 below provides a summary of the use of performance regimes in the public transport service contracts reviewed as well as the nature of the incentive and penalty mechanism employed.

Failure to meet KPIs triggers Failure to meet KPIs triggers Sydney Metro Northwest Sydney Light Rail 1 1 x Newcastle Integrated Services Paramatta Light Rail Redacted Redacted Redacted Sydney Bus Services ✓20 Sydney Ferry System × × Melbourne Rail Franchise **Melbourne Tram Franchise** Melbourne Bus Franchise **Metropolitan Bus Services** Gold Coast Light Rail 21 Capital Metro Light Rail × Auckland Metro Rail **Auckland Bus Services** Redacted Redacted Redacted Wellington Metro Rail Wellington Bus Services

Table 8: Incentive and penalty payments

(Reform Series Report 2017).

²⁰ Note that this reflects the position in the Region 6 Bus Service Contract. It does not apply across all Sydney Bus Service Contracts.

²¹ The incentive component is limited to fare evasion. GoldLinQ receives a bonus for lower than target surveyed fare evasion rate. based on an agreed formula.

In all contracts reviewed, incentives and penalties are capped to manage the risk assumed by both the transport authority and the operator. The regimes also allow for adjustments in circumstances reasonably beyond the operator's control such as weather events, special events, public emergencies and road congestion.

The Melbourne Bus Services and Wellington Metro Rail contracts also reward strong performance, with contract extension tied to meeting KPIs, while the former Melbourne Rail Franchise and Melbourne Tram Franchise contracts gave an exclusive right to negotiate a subsequent contract.

Typical KPIs

KPIs in the reviewed service contracts typically fall into three categories:

 operational performance, including the reliability and punctuality of services;

- asset management, including the presentation, availability and condition of assets; and
- customer experience on the network, including passenger information and general measures of customer satisfaction.

The service contracts also include a range of 'other' KPIs, which largely reflect the specific issues and priorities of the transport authority for the relevant system.

Table 9 below provides a high level overview of the KPIs used in each of the contracts reviewed. There is a degree of overlap between the Asset Management and Customer Experience categories, particularly with respect to the cleanliness and presentation of vehicles, stations and other customer facing assets.

Contract	Operational Performance	Asset Management	Customer Experience	Other
Sydney Metro Northwest	 Train and platform availability Timeliness 	 Cleanliness, condition and graffiti Environment (temperature and lighting) Lift and elevator access 	 Customer information Gate management Customer satisfaction Complaints management 	Energy Consumption Incentive
Sydney Light Rail	AvailabilityTimeliness	 Cleanliness, condition and graffiti Asset Availability 	 Customer satisfaction Customer information Complaints management 	• Revenue management
Newcastle Integrated Services	 Punctuality rates Incomplete trips Cancelled trips Reliability Availability of accessible bus services 	 Safety Contract vehicle maintenance Asset presentation 	 Customer satisfaction Customer complaints Customer response times for On Demand Services Passenger information 	 Revenue protection Incident management Data maintenance Implementation of projects CCTV and Duress Alarms Patronage incentive
Parramatta Light Rail	• Redacted	• Redacted	• Redacted	• Redacted

Table 9: Performance regimes

Contract	Operational Performance	Asset Management	Customer Experience	Other
Sydney Metropolitan Bus Services	 Punctuality Reliability Accessibility Incomplete trips Cancelled trips 	 Presentation and condition of assets Vehicle maintenance 	 Customer satisfaction Customer complaints Passenger information Customer response times for On Demand services 	 Patronage incentive Revenue Data maintenance Project delivery CCTV and duress alarms Reporting Provision of information
Sydney Ferry System	PunctualityReliability	 Availability Asset presentation Asset condition Contract ferry maintenance 	 Customer satisfaction Customer complaints Passenger information Data maintenance 	 Revenue collection rate Reporting CCTV and duress alarms Provision of information Project delivery
Melbourne Train Franchise	 Punctuality Reliability of On Demand service Incomplete trips Cancelled trips Accessibility 	 Fleet availability Distance between failure Faults and unplanned out of service Maintenance Graffiti Scratching Cleanliness and condition 	 Customer satisfaction Passenger information 	 Priorities incentive new priorities determined annually
Melbourne Tram Franchise	• Punctuality • Reliability	 Fleet availability Distance between failure Faults and unplanned out of service Maintenance Graffiti Scratching Cleanliness and condition 	 Customer satisfaction Passenger information 	 Priorities incentive new priorities determined annually
Melbourne Bus Franchise	 Reliability Punctuality	• None	• Customer satisfaction	Patronage incentive
Metropolitan Bus Services	 Reliability Punctuality	 Vehicle specification Presentation 	 Volume of complaints Complaint resolution 	• Patronage incentive

Contract	Operational Performance	Asset Management	Customer Experience	Other
Gold Coast Light Rail	 Tram availability Tram punctuality 	 Upkeep of assets Asset maintenance condition and cleanliness Critical systems availability Graffiti and vandalism Lift and elevator access 	 Disruption notification and passenger communications Passenger satisfaction Complaint management 	 Fare evasion Monthly reporting Environmental impact CCTV and emergency help management Ride quality and system noise management.
Capital Metro Light Rail	AvailabilityPunctuality	 Asset condition and cleanliness Systems availability 	 Customer service and communications Customer comfort 	• Revenue protection
Auckland Metropolitan Rail	• Reliability • Punctuality	• None	 General customer satisfaction Complaints 	• None
Auckland Bus Services	• Punctuality • Reliability	 Fleet conformity to specification Vehicle quality standards 	 Customer satisfaction Customer complaints Complaint resolution 	 Non reporting of accidents Revenue protection Reporting Operator safety rating
Wellington Rail Service	• Redacted	• Redacted	• Redacted	• Redacted
Wellington Bus Services	• Reliability • Punctuality	• Vehicle age	 Customer complaints Customer resolution Customer satisfaction 	 Reporting Patronage incentive Revenue protection Non reporting of notifiable events



Case study 1: Victorian rail franchising KPIs

The Victorian rail franchising contracts include one of the more comprehensive performance regimes of the reviewed service contracts. These contracts incorporate three categories of KPIs:

- Enhanced Operational Performance (EOPR)

 focusing on reliability and punctuality of services;
- Passenger Experience (PX) focusing on the quality of passenger experience on the network, particularly relating to rolling stock and station/ stop presentation and passenger information; and
- Rolling stock focused on rolling stock availability, especially during the morning and evening peak.

EOPR and PX have financial consequences where KPIs are not met as well as the possibility of triggering the default regime. By contrast, the rolling stock related KPIs solely trigger the default regime. There are no KPIs or penalty/incentive payments specifically directed at the management or condition of rail network infrastructure.

Case study 2: Newcastle Integrated Services KPIs

The Newcastle Integrated Services contract is another example of a comprehensive KPI regime. KPIs are divided into a number of categories. Some categories are broad, such as the service reliability and contract vehicle maintenance categories, while others are narrower, such as the CCTV and Duress Alarm category. KPIs are divided into three classes: Class 1, Class 2 and Class 4.

Failure to meet Class 1 KPIs results in a financial penalty becoming payable by the operator. Failure to meet Class 2 KPIs will not usually result in a penalty, but the transport authority can elevate Class 2 KPIs to Class 1 status, with applicable penalties, by giving 30 days' notice to the operator. Up to two Class 2 KPIs can be elevated in this manner at any given time. Class 4 KPIs relate to customer satisfaction. Failure to meet Class 4 KPIs may result in a financial penalty, and also requires an incident report be prepared by the operator.

Class 1 and Class 4 KPIs can also trigger the default regime if repeatedly not met.

5.5 SERVICE CHANGE REGIMES

The service change regime refers to arrangements under the contract providing for changes to be made to the passenger services the operator is contracted to provide, as distinct from general contract variations. A service change regime is an important feature of public transport service contracts given that the transport authority (rather than the operator) will generally have the responsibility and accountability for what services are provided, and will be the party required to make necessary trade-offs between service levels and available funding. This means the authority needs the ability, and an effective mechanism, to increase and reduce the level of services, as well as to change timetables to better satisfy community needs and preferences.

There are two principal elements that need to be addressed. The first relates to the process for making service changes and the second concerns the financial implications of the service change.

Process for making service changes

The contracts reviewed typically allow both the operator and the transport authority to propose service changes. Where service changes are proposed by the operator, it is within the transport authority's discretion as to whether to implement the proposed change. There are no contracts where the operator can mandate a service change, nor where a service change proposal can be referred to independent review. This reflects the transport authority's ultimate accountability for the cost and suitability of services.

Where the transport authority requires a service change, there is generally a process (specified in greater or lesser degrees of detail) for the operator to prepare an implementation plan and to specify its assessment of the cost implications of the change. Provisions which require the operator to participate in service change reviews and to support service planning by the transport authority are also common.

Financial implications of a service change

In contrast to the change process, there is a significant degree of variability in the way the financial implications of service changes are addressed.

In some contracts, the matter is governed by a standard contract variations framework under which the variation proposal is priced by the operator and the transport authority then determines whether to proceed with the change or not. The authority may proceed on the basis of the operator's proposed pricing or elect to proceed without agreeing the pricing and have the pricing determined through an independent dispute resolution process.

The contracts provide varying degrees of prescription as to the basis on which price adjustments are to be determined, often including relatively detailed methodologies for determining the 'net financial impact' of the change. Net financial impact is usually defined broadly by reference to the incremental costs the operator will incur as a result of the change, net of any cost savings, and taking account of any changes in revenue.

Other contracts seek to provide for a greater degree of certainty, or 'pre-pricing' of service changes. These contracts specify a fixed price per additional service kilometre or service hour to cover operating costs and possibly a separate payment in respect of incremental maintenance costs. The fixed charge may only apply to service changes up to a certain specified threshold. Changes beyond the threshold are priced based on a 'net financial impact' assessment. The expectation is that the threshold is set at a level where it is anticipated that a step change in costs is likely to be incurred because of the magnitude of the service level change.

The Melbourne Tram Franchise contract provides an illustration of this kind of service change regime.

Case study 3: Melbourne tram franchise service changes

The Melbourne tram franchise contract distinguishes between 'standard' service changes, to which preagreed rates for rolling stock and other costs apply, and 'fundamental changes', where the net financial impact adjustment process applies.

A fundamental change is defined as a timetable change which involves either:

- an extension of a passenger service or the introduction of a new passenger service, in either case along a new piece of track which has at least one new stop; or
- an expansion or reduction in the standard hours of operation of the tram network which the operator can demonstrate will result in a material increase in the costs to the operator and that those costs will not be adequately addressed by applying the standard service adjustment rates.

The Sydney Bus Service contract provides a useful example of a regime that includes a requirement for the operator to participate in service-change reviews and to support service planning by the transport authority.

Case study 4: Sydney bus service changes

Under the Sydney Bus Services contract the operator is required to:

- undertake regular reviews of the contract service levels and timetables;
- work collaboratively with TfNSW to develop the services, having regard to the contract objectives and the requirements of the contract, and to consider and develop incentive strategies to:
 - utilise capacity;
 - optimally manage dead running;
 - improve the safety of the services; and
 - improve the security of the transport network; and
- proactively engage with key stakeholders in accordance with the Operator Stakeholder Engagement Plan.

The operator is required to submit an annual report to TfNSW recommending any changes to the contract service levels and timetables it considers will facilitate these outcomes. It is within TfNSW's discretion as to whether it accepts any of the operator's recommendations.



5.6 **RISK ALLOCATION**

Risk allocation in public sector procurement contracts is a very broad topic. As an illustration of the range of potential risks, Table 10 provides a list of the risks identified in the National PPP Guidelines as needing to be addressed in PPP concession contracts.

Table 10: Risk categories – National PPP Guidelines

- Asset ownership risk
- Design, construction and commissioning risk
- Financial risk
- Force majeure risk
- Hard and soft facility and maintenance operations risk
- Industrial relations risk
- Interest rate risk
- Legislative and government policy risk
- Market risk
- Network and interface risk
- Site risk
- Sponsor risk
- Tax risk

The general guidance provided by the National PPP Guidelines in relation to the allocation of risk is that optimal risk allocation seeks to assign project risks to the party in the best position to control them and therefore minimise both project costs and risks. The party with greatest control of a particular risk has the best opportunity to reduce the likelihood of the risk eventuating and to control the consequences if it does.²²

The risks in Table 10 above are focussed on contracts dealing with the procurement of new infrastructure, not all of which will be relevant in a public transport service contract. Moreover, the allocation of this broad range of risks is a matter of considerable detail and is very much influenced by the particular circumstances of the project and services being provided. There is limited value in seeking to review the approach to risk allocation generally across the suite of contracts reviewed for the purposes of this report. However, it is useful to focus on two particular risk issues which are central to public transport service contracting and where common themes can be identified: the treatment of revenue risk, and operating cost risk.

Revenue risk

The approach to the treatment of revenue risk has already been canvassed in the discussion of the revenue model in section 5.3 above. As outlined there, revenue risk can be borne by either the transport authority or the operator in one of two ways:

- Entitlement to farebox relates to the entitlement to receive and retain farebox revenue. Where the operator is entitled to farebox revenue and is paid under a net cost contract, revenue risk is transferred to the operator. Conversely, under a gross cost contract, where the transport authority is entitled to farebox revenue and pays the operator the agreed service fee, revenue risk is retained by the authority.
- Patronage incentives relates to the performance and incentive regime. Where the regime includes an incentive payment referable to patronage or revenue growth as against a specified benchmark, this transfers a degree of revenue risk to the operator, albeit usually quite limited.

Table 7 in section 5.3 provides a summary of the allocation of revenue risk under the contracts reviewed, according to this framework. The review demonstrates that revenue risk is almost universally retained by the transport authorities, with the only exception being the Melbourne Train and Tram Franchise contracts, and Commercial Units under the Auckland Bus Services contract.²³ However, there are many contracts which include patronage incentive mechanisms. As discussed in section 5.3, this most likely reflects an assessment by transport authorities that they, rather than operators, are best able to manage revenue risk. Neither transport authorities nor operators have control over the macroeconomic factors, such as economic and population growth, that are the major drivers of changes in patronage. However, transport authorities are in a better position to respond to these risks, including through fares policy and modifications to service levels and funding allocations.

Section 5.3 (Revenue Model) also outlines some of the mechanisms for sharing revenue risk where relevant.

Operating cost risk

The transfer of operating cost risk to the operator means that a contract specifies a fixed service charge payable to the operator for provision of services under the contract,

²² Australian Government Department of Infrastructure and Regional Development, National Public Private Partnership Guidelines (Guidelines, December 2008).

²³ As noted in Table 7, while the Sydney Ferry System contract provides for the operator to retain farebox revenue, the payment mechanism effectively transfers revenue risk under the contract to TfNSW.

and the operator takes the risk that the actual cost of doing so will be greater than anticipated at the time the service charge was agreed and specified in the contract. This contrasts with management style contracts which operate on a 'cost-plus' basis, where the operator is entitled to be paid the actual cost of providing the services plus an agreed margin.

In contrast to revenue risk, operating cost risk is almost universally borne by the operator rather than the transport authority. Although, as discussed further below, the extent to which operating cost risk is transferred is a matter of degree – only the Auckland Metro Rail contract substantially allocates cost risk to the transport authority.

The transfer of operating cost risk to the operator reflects an assessment that the operator is likely to be best placed to predict and manage the level of operating costs over the term of the contract. In most cases a large portion of operating costs will be those associated with the workforce, and this is best managed by the operator as employer. In contracts requiring new investment in infrastructure or rolling stock, or their management and maintenance, the operator is also best able to manage these costs through its procurement strategy and ongoing management of sub-contractors.

Nevertheless, where particular categories of costs are outside the control of the operator or are prone to volatility, there will be a case for these cost risks to be retained by the authority. Transfer to the operator may come at an inefficient risk premium, and where neither party is able to control the risk, it may be best managed by the authority through fares policy and service level adjustments.

As indicated in Tables 9 and 10 above, the two most common cost risks retained by transport authorities are those associated with changes in law and the cost of energy or fuel.

Change in law risk

Change in law risk refers to the risk of changes in the legal and regulatory environment in which the services are provided, leading to material changes in the costs of operation. Although the scope of such changes in law is open-ended, the most common areas of concern are changes to safety, environmental or accessibility laws that impose additional or more onerous obligations on operators, and which are clearly outside their control. On an economy-wide basis, the costs of changes in law of this kind are ultimately passed through to consumers in the form of higher prices. However, operators are not able to manage the risk in this way because they typically do not control fares policy. It follows that, in principle, change in law risk should be borne by the transport authority, and this position is reflected in the suite of contracts reviewed.

There are, however, several features of the change in law regimes which modify this simple proposition and provide for a degree of risk sharing.

The first issue relates to the definition of 'change in law'. Typical exclusions from the definition include changes in law which were announced but not yet enacted at the time the contract was signed, changes in law which an experienced and competent operator should reasonably have anticipated, and changes in tax laws. The latter are excluded on the basis that the after-tax return of the operator is a general business risk rather than a project risk and should be borne by the operator.

Second, in most cases the change in law provisions are reciprocal, in the sense that if a change in law results in a reduction in the operator's operating costs, the transport authority is entitled to the benefit of the cost savings through a reduction in the service charge.

Finally, while many contracts provide full compensation for the cost impacts of a change in law it is also common for change in law regimes to include a degree of risk sharing under which the operator bears the cost risk associated with changes in law up to a specified monetary threshold. This avoids the need to enter into complicated and contentious negotiations over the cost implications (and consequential financial adjustments) arising from changes that fall below the threshold. It also incentivises the operator to manage the risk, to the extent there are opportunities to do so, through modifications to its operating practices. In many cases these provisions distinguish between 'project specific' changes in law, where full compensation is provided, and 'general' changes in law where the risk sharing financial thresholds apply. Table 11 provides a number of examples of contracts which provide for this kind of risk sharing.



Contract	Risk sharing thresholds							
Sydney Light Rail	TfNSW is responsible for 10 environmental law and char	00% of the NFI of project-spe nges in rail safety law.	cific changes in law, changes in disability law, changes in					
	For general changes in law, the operator is compensated for the NFI, subject to the following thresholds (which apply to the aggregate of all changes)							
	Net Financial Impact (who per event	ether positive or negative)	Percentage of Net Financial Impact compensated or reimbursed					
	Capital expenditure component of NFI	Less than \$250,000	0%					
		More than \$250,000	0% of the Net Financial Impact up to \$250,000 and 100% of the Net Financial Impact above \$250,000					
	Operating cost and revenue component of NFI	Less than \$50,000 per month	0%					
		More than \$50,000 per month	0% of the Net Financial Impact up to \$50,000 -and 100% of the Net Financial Impact above \$50,000					
Melbourne Rail Franchise	TfV is responsible for 100% of the NFI of project-specific changes in law							
	Net Financial Impact (who	ether positive or negative)	Percentage of Net Financial Impact compensated or					
	per event		reimbursed					
	in law occurring after the agree	eement date	0.6					
	More than \$1.5m but less tha year in respect of all changes agreement date	n or equal to \$3m in any financial in law occurring after the	50% of Net Financial Impact above \$1.5m					
	More than \$3m in any financ in law occurring after the agre	ial year in respect of all changes eement date	\$750,000 plus 100% of Net Financial Impact greater than \$3m					
Melbourne Bus	TfV is responsible for 100% of the NFI of project specific changes in law.							
Franchise	For general changes in law,	the operator is compensated f	or the NFI, subject to the following thresholds:					
	Net Financial Impact (who per event	ether positive or negative)	Percentage of Net Financial Impact compensated or reimbursed					
	Up to \$500,000		0%					
	More than \$500,000 up	to \$1m	50% of Net Financial Impact above \$500,000					
	More than \$1m		50% of Net Financial Impact above \$500,000 up to \$1m, plus 100% of Net Financial Impact above \$1m					
Gold Coast Light Rail	Operator is entitled to com which occur at any time aft commencement of the ope	changes in law and changes in environmental law and for general changes in law which occur after the of the agreement.						
	There are separate monetary thresholds for project-specific changes in law and for general changes in I general changes in law there are separate thresholds for capital expenditure and for operating costs that cumulative basis. The regime is structured in a similar way to the Sydney Light Rail contract. However, thresholds are redacted.							

Table 11: Change in law risk sharing - illustrative provisions

Energy and fuel cost risk

The second common exception to the transfer of operating cost risk to the operator concerns energy and fuel cost risk. Aside from employee costs, this represents one of the most significant cost components associated with the provision of public transport services – traction power in the case of rail and light rail services, and diesel fuel in the case of buses and ferries.

The contract review demonstrates that energy and fuel cost risk is commonly, though not universally, retained by the transport authority rather than being transferred to the operator.

The rationale for allocating fuel cost risk to the transport authority presumably reflects an assessment that energy and fuel costs can be volatile and are influenced by a range or economic and regulatory factors that make such costs difficult to predict or control by operators. This has been particularly relevant over the past decade in relation to traction power costs, where there has been significant uncertainty concerning the potential cost implications of climate policy responses such as emissions trading schemes and carbon taxes. In addition, while there are sometimes mechanisms to manage these price risks through fixed-price contracts and hedging instruments, these are often not available with a tenor that matches the term of the service contract. Moreover, the strategy for managing such costs, including the extent to which they should be fixed through long-term contracts or hedging, is often more appropriately approached through a whole-of-government risk management strategy. There may also be the opportunity for the

transport authority to leverage whole-of-government risk management contracts and hedging instruments. All these factors tend to suggest the risk should be retained by the transport authority and the costs treated as a pass-through for operators.

In those contracts where energy or fuel cost risk is retained by the transport authority, there are several different approaches evident in how this is achieved. One particular issue is whether a distinction is drawn between price risk and consumption risk. While price risk is subject to the considerations outlined above, this is less so in relation to consumption risk. The operating practices of the operator may have a material impact on consumption, and a straight cost pass-through removes any incentive for the operator to achieve energy or fuel cost efficiencies. At the same time, however, the primary determinant of consumption is the number of service kilometres required to be run under the contract, which is controlled by the transport authority. If consumption risk is to be allocated to the operator, it may be difficult to separate out the extent to which consumption volumes vary because of service changes, as opposed to factors within the operator's control. Where these are considered too difficult to disentangle, the alternative approach is to allocate energy or fuel cost risk entirely to the transport authority but to include obligations on the operator to satisfy specified fuel efficiency objectives, practices or outcomes in the contract.

Table 12 summarises the energy and fuel cost provisions in a number of contracts which illustrate these alternative approaches.

Contract	Risk allocation / sharing mechanism
Sydney Metro Northwest	TfNSW procures electricity for the provision of services and makes this available to the operator, so TfNSW retains fuel price risk. The contract seeks to manage usage risk (in this case network demand charges rather than consumption) by requiring the operator to comply with a Demand Strategy. The service payment is subject to an energy deduction where the demand strategy is not complied with (being the difference between the maximum demand component of the network charges payable by tfnsw and the changes that would have been payable if the demand strategy had been complied with. There is also an energy consumption incentive payment which is payable where actual energy consumption is less than a specified baseline.
Sydney Ferry System	The operator procures and pays for fuel. The monthly service fee payable by TfNSW to the operator includes a fuel adjustment component which is designed to allocate price risk to TfNSW and volume risk to the operator. There is a bid fuel volume which is subject to adjustment for changes in service hours (but not otherwise). There is also a bid fuel price which is subject to adjustment based on actual fuel prices in the preceding month.

Table 12: Energy and fuel cost risk -illustrative provisions

Risk allocation / sharing mechanism
The operator procures and pays for electricity. The franchise payment payable by TfV to the operator includes the actual cost of electricity incurred by the operator in the relevant payment period. This operates as a pass-through of electricity costs, such that both price and volume risk are borne by TfV.
The contract enables TfV to manage price risk by giving TfV control over the tender process for retail energy contracts entered into by the operator. In relation to volume risk, the contract imposes an energy efficiency obligation on the operator.
The operator procures and pays for fuel. The service payment includes a payment for fuel for each contract month. The fuel payment is a specified sum set at contract commencement and is escalated by a fuel index multiplier, which escalates the original price based on a market price index. Hence, fuel price risk is borne by TfV; consumption risk is borne by the operator.
The operator procures and pays for electricity. The service payment includes a separate energy payment. This is the product of the retail energy price and a specified volume, plus connection charges. The effect is that DTMR retains price risk and the volume risk for exceeding an agreed base consumption is borne by the operator. DTMR is entitled to control the tender process for retail energy contracts entered into by the operator.

Additional operating cost issues

Apart from change in law and fuel costs, there are a range of other operating cost risks which are sometimes allocated to, or shared by, the transport authority. The main examples are cost risks arising from pre-existing contamination and latent defects in rolling stock or infrastructure. The treatment of these risks tends to be developed and negotiated with reference to the specific characteristics of the service environment, as well as the scope of the services provided. In particular, the treatment of these risks will vary significantly depending on whether the context is a PPP contract for the construction and operation of a new network, or a service contract for the operation of an existing network.

Finally, it should be noted that the discussion of operating cost risk here is premised on the contract providing for a defined scope and level of services. Many contracts will also contain provisions dealing with cost adjustments for changes in service levels (as discussed in section 5.5 (Service change regime) above), as well as for the provision of certain services on a cost-plus basis or based on pre-agreed unit rates. The primary example of this is the inclusion of regimes governing special events, where additional services are required to serve the event, but this may vary from year to year and cannot readily be accommodated in a fixed annual service fee. Another common example is the provision of support for the transport authority to undertake new investment on the network, where the operator's assistance may be required for such things as input to planning and design and the

management of safety case variations. These services are typically provided on a cost-plus basis.

5.7 NETWORK INTEGRATION

Public transport service contracts generally relate to the provision of services by a single transport mode in a city or region, and are often only one of a number of contracts making up the service suite within a mode. As the overview of governance and institutional arrangements in Chapter 3 illustrates, service contracts form part of a wider multi-modal public transport system which is planned and managed by the transport authority. This means that an important design feature of service contracts is the manner in which they integrate with, and contribute to, the planning and management of the broader network.

The contracts reviewed for this report typically include express obligations on operators to support the broader network in key areas such as ticketing, system integration and planning, and other network-wide functions and activities such as marketing and passenger information. However, the review found considerable variation in the approaches taken between jurisdictions.

Ticketing

Most Australian public transport networks, as well as Auckland in New Zealand, have in place a centralised multi-modal ticketing system based on smartcard technology.²⁴ These systems are provided by a third party provider that operates and maintains the ticketing system under contract to the transport authority.

Jurisdiction	Transport Modes	Ticketing System	Ticketing System Operator
Auckland	Trains, Bus, Ferry	AT Hop Card	Thales Group
Canberra	Light Rail, Bus	MyWay	Parkeon/ Downer EDI
New South Wales	Train, Light Rail, Bus, Ferry, Metro ²⁵	Opal	Cubic
Queensland	Train, Light Rail, Bus, Ferry	Go Card	Cubic
Victoria	Train, Tram, Bus	Myki	NTT Data

Table 13: Ticketing systems

As a consequence, operators are required to facilitate the use of a centralised ticketing system and are either expressly prohibited from issuing their own tickets or only permitted to issue their own tickets with consent. Obligations are also typically included to support the provision, operation and maintenance of the ticketing system by the relevant ticketing operator or otherwise by or on behalf of the transport authority.

As discussed in Chapter 3, responsibility for revenue protection can either be the responsibility of the transport authority or the operator, or may be a shared responsibility.

System integration and planning

Many of the contracts reviewed include provisions designed to support system integration and planning by the transport authority, although this is not an area where the contracts exhibit a high degree of consistency in approach. The most common provisions include obligations for the operator to:

- provide input on timetable coordination;
- provide service information to the transport authority;
- support the development and implementation of transport planning; and
- cooperate, coordinate and share information with other operators.

Network-wide functions and activities

Most contracts reviewed also include provisions which support the transport authority's responsibility for network-wide functions and activities such as marketing and passenger communications.

In relation to marketing, the Queensland, New South Wales and Victorian contracts all include restrictions on the operators' ability to undertake marketing or advertising without approval, or otherwise than in accordance with an agreed marketing plan. Similarly, branding and livery are also restricted in those contracts. This issue is not dealt with expressly in the Capital Metro Light Rail, Auckland Metro Rail and Wellington contracts.

Passenger communications is another area that is often both centralised and heavily regulated. In the contracts reviewed, relevant requirements on operators in relation to passenger communications vary depending on the nature of the system and transport authority priorities, and are often reinforced by way of the performance regime (see section 5.4 of this report). Obligations typically include:

- displaying or otherwise making available service information including planned and unplanned disruptions;
- facilitating the provision of feedback by passengers; and
- providing wayfinding signage.

Added to this, the channels and means by which operators communicate with passengers are typically heavily regulated, with a centralised information service established as the primary passenger interface in all jurisdictions except Canberra, Auckland and Wellington. For example, the New South Wales contracts all require the promotion of a central government transport information service as the primary customer interface in relation to service information, trip planning and customer feedback, and require operators not to compete with or duplicate those services or customer

²⁴ Metlink in Wellington uses both cash and an automatic fare collection system across the bus network using the Snapper card. Metlink ferry and rail use legacy paper tickets and cash. There is currently a national project underway called 'Project NEXT' which is seeking to procure a national, account-based, open-loop ticketing solution across New Zealand. Both Auckland and Wellington are participating jurisdictions.

²⁵ For bus services, this only applies to metropolitan and outer metropolitan areas. Rural and regional are not operating under the Opal footprint. Also, private operators such as Manly Fast Ferries don't operate within the public transport fare structure.

information channels. Similarly, Victorian contracts establish TfV as 'the comprehensive source for Transport Information' and the public face of the public transport system in Victoria in communications with the public. Some contracts (such as Sydney Metropolitan Bus Services) also expressly restrict the establishment or operation of social media channels without the transport authority's approval, and Victorian contracts establish a media protocol with which operators must comply.

5.8 PROJECTS REGIMES

Public transport passenger numbers in Australia and New Zealand have grown significantly over recent years, driven principally by a rapidly increasing and urbanising population. This has led to an unprecedented number of projects taking place to upgrade and extend existing public transport networks, including infrastructure and rolling stock. Sydney Metro, Melbourne Metro Tunnel and City Rail Link in Auckland are examples of transformative projects of this kind.

The need to facilitate network development, as well as to manage the disruption to existing services that major projects inevitably cause, has led a number of Australian jurisdictions to include detailed regimes governing project planning and development in their service contracts. Regimes of this kind have not been incorporated in New Zealand service contracts to date.

The nature and scope of these regimes varies across the contracts reviewed, but three distinct approaches are evident:

Augmentation/modification regimes

Most of the contracts reviewed rely on the transport authority enacting the general augmentations or modifications regimes within those contracts to the extent the transport authority or the relevant operator wishes to pursue a project on, or affecting, the network. These mechanisms generally have a wider scope and deal with projects, as well as more general changes to operation or maintenance requirements, or changes to relevant works or assets. In addition to the augmentation/ modification clause, most of these contracts also include an acknowledgement that the transport authority can undertake works proximate to the network with notice, and that the operator is required to assist and cooperate with the transport authority to allow those works to occur.

Where specific future project(s) are contemplated at the time the contracts were entered into, the transport authority has typically elected to include provisions directly dealing with those projects. For example, the Sydney Metro Northwest contract includes provisions in relation to a major extension of the North West Rail link involving a second harbour crossing, and the Sydney Ferry System contract includes provisions dealing specifically with the redevelopment of Circular Quay. These clauses adopt a similar process to the standard augmentations/ modifications regime in the contract. However, the fact that it is a known project that is being considered for an augmentation allows for additional tailoring and details to be included in the contract, whilst also maintaining a general augmentations/modifications regime for other future projects.

Projects regime

The service contracts relating to Victorian trains, trams and buses, as well as the Sydney Ferry System contract (which includes an augmentations/modifications regime as well as a separate, albeit similar, major projects regime) include clauses that prescribe in detail the operator's role in supporting (and potentially delivering) projects on or affecting the network. These projects regimes cover some or all of:

- an acknowledgement that the transport authority may undertake projects which affect or otherwise impact the network;
- a requirement to cooperate with the transport authority and its contractors in relation to the implementation of projects;
- a process for the development and delivery of projects involving or affecting the relevant operator and prescribing the operator's role;
- relief from contractual obligations, such as performance requirements, due to the impact of projects; and
- payment for involvement in projects, over and above agreed subsidy payments, to incentivise cooperation and reimburse the operator for costs incurred.

Of the contracts reviewed, the Melbourne Rail Franchise and Melbourne Tram Franchise contracts adopt the most comprehensive approach, with a detailed set of provisions covering governance arrangements and project planning and delivery. While the transport authority has ultimate decision making authority, the regime seeks to establish a cooperative planning and delivery framework. These contracts also include specific arrangements for known projects such as the Melbourne Metro Tunnel and the procurement of High Capacity Metro Trains.

As would be expected, a distinct projects regime covers similar concepts to an augmentations/modifications regime. The differences between the two regimes tend to lie in the manner in which the operator is involved in the process. At its heart, a projects regime aims to create a collaborative approach across the project lifecycle that leverages the experience and capability of the operator, while an augmentations/modifications regime tends to be more directive in its approach. This reflects the fact that augmentation/modification regimes are focussed on the operator undertaking the project works on behalf of the authority, while projects regimes are focussed on facilitating the transport authority's ability to implement the project under a range of alternative procurement models.

Variations regime

Absent an augmentation/modifications regime or a specific projects regime, the transport authority would need to rely on the general contract variations mechanism to manage network development. This is the position which applies under the Auckland and Wellington contracts reviewed. Whilst not providing a tailor-made mechanism for managing the impact of new projects on the existing network, the contract variation mechanism nevertheless provides a framework for the parties to negotiate and agree the terms on which the operator is to participate in project planning and delivery.

5.9 FINANCIAL SECURITY

Financial security arrangements are an important feature of public transport service contracts. Such arrangements are designed to address a number of risks faced by the transport authority, including the risk of non-performance of the operator's obligations under the contract and the risk of the operator becoming insolvent. Financial security arrangements also seek to ensure that the transport authority can step in to operate the relevant service if the operator defaults or otherwise becomes incapable of performing the contract.

The package of financial security arrangements varies across the contracts reviewed, with a 'belts-and-braces' approach preferred in some jurisdictions and a more selective approach adopted in others. Overall, the design of the security package should seek to achieve a balance between adequately protecting the transport authority's interests while not requiring unnecessary security from the operator which will ultimately be priced in to the service charge. The approach taken will also be influenced by consortium structure and whether the contract involves a PPP, with the operator being responsible for new capital investment using private finance.

The approach may also be coloured by practical experience in the jurisdiction in question. For example, the comprehensive approach taken in Victoria is likely influenced by the fact that three of the operators appointed under Victoria's first round of rail franchising became insolvent. This meant the transport authority was required to appoint receivers and managers to operate the services, with financial and operating risk thereby effectively reverting to the government.

Financial security mechanisms

The financial and security mechanisms in the reviewed contracts include one or more of the following:

- SPV requirements The operator is required to be a special purpose vehicle in the sense that its activities are restricted to providing services under the service contract. This limits the risk of the operator's financial viability being impacted by other business operations and supports the transport authority's ability to 'step in' under the service contract if required.
- Minimum capital The operator is required to maintain a specified minimum level of equity. This aims to ensure the operator has sufficient working capital to manage short term cash flow issues arising from unanticipated cost or revenue variances.
- Security over assets The operator is required to grant security to the transport authority over all of its assets. This security allows the transport authority to appoint a receiver in the event of the insolvency of the operator or operator default.
- Security over shares The shareholders of the operator are required to grant security to the transport authority over their shares in the operator and their rights under any shareholder loans. This allows the transport authority to deal with the operator through a share rather than an asset transaction in the event of insolvency.
- Parent company guarantees The operator's parent company is required to guarantee the operator's obligations to the transport authority. The parent company guarantee is typically subject to an agreed cap on the parent company's liability.
- **Performance bonds** The operator is required to procure the issue of a performance bond by an acceptable financial institution. This provides the transport authority with immediate recourse up to the value of the bond to secure the operator's financial obligations to the transport authority.
- Set-off rights The transport authority is permitted to set off any amount owing to the transport authority against any payment due by the transport authority to the operator. These provisions also

typically require the operator to make all payments to the transport authority without set-off, deduction or withholding unless overwise agreed.

The rights above are almost always supported by broad step-in rights, which allow the transport authority (or its nominee) to step-in and operate the relevant network in various circumstances. In the contracts reviewed, stepin is typically triggered in the event of default by the operator, or insolvency of the operator. Some contracts also include step-in rights for threatened default by the operator, emergencies and where there is an imminent risk of harm or damage to persons, property or the public interest.

PPP versus non-PPP contracts

There is a notable difference between PPP contracts and non-PPP contracts resulting from the involvement of third party finance. Generally, for a PPP, the transport authority does not require a performance bond from the operator or require the provision of a parent company guarantee, and instead relies on the performance bonds and guarantees that the operator obtains from its subcontractors to satisfy its financiers. Handover bonds are, however, common as an alternative to payment reduction/withholding for end-of-term asset condition risk.

Table 14 below provides an overview of the package of financial and security arrangements in each reviewed contract.

Contract	SPV requirement	Minimum Capital	Security over Assets	Security over Shares	Parent Company Guarantee	Performance Bond	Set-off Right	Step-in Right
Sydney Metro Northwest	\checkmark	\checkmark	√ (General Security Deed)	X	X	√ (Handback Security Bond, Extension Security Bond)	\checkmark	\checkmark
Sydney Light Rail	\checkmark	X	\checkmark	X	X	√ (Handback Security Bond, Extension Security Bond)	\checkmark	\checkmark
Newcastle Integrated Services	\checkmark	X	X	X	\checkmark	√ (General Performance Bond, Handback Security Bond)	\checkmark	\checkmark
Paramatta Light Rail	Redacted	Redacted	Redacted	Redacted	Redacted	Redacted	\checkmark	\checkmark
Sydney Bus Services	\checkmark	×	X ²⁶	X	\checkmark	√ (General Performance Bond, Handback Security Bond)	\checkmark	\checkmark

Table 14: Financial security arrangements

²⁶ However, separate financier tripartite agreements provide TfNSW with certain rights in respect of operator assets including buses.

Contract	SPV requirement	Minimum Capital	Security over Assets	Security over Shares	Parent Company Guarantee	Performance Bond	Set-off Right	Step-in Right
Sydney Ferry System	\checkmark	×	√ (Fleet Security Deed, General Security Deed)	√ (Specific Security Deed)	\checkmark	\checkmark	\checkmark	\checkmark
Melbourne Rail Franchise	\checkmark	\checkmark	√ (General Security Deed)	√ (Shareholder Security Deed)	\checkmark	√ (General Performance Bond)	\checkmark	\checkmark
Melbourne Tram Franchise	\checkmark	\checkmark	√ (General Security Deed)	√ (Shareholder Security Deed)	\checkmark	√ (General Performance Bond)	\checkmark	\checkmark
Melbourne Bus Franchise	\checkmark	X	√ (General Security Deed)	√ (Specific Security Deed)	\checkmark	√ (General Performance Bond)	\checkmark	\checkmark
Melbourne Bus Services	X	X	Redacted	Redacted	\checkmark	√ (Terms redacted)	\checkmark	\checkmark
Gold Coast Light Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	√ (Handback Security Bond)	\checkmark	\checkmark
Capital Metro Light Rail	√	X (However, there will be a default if shares are redeemed etc without consent)	\checkmark	×	X (Parent guarantees are provided by subcontractors, but in favour of the operating vehicle)	√ (Handback Security Bond)	\checkmark	~
Auckland Metro Rail	\checkmark	×	×	\checkmark	\checkmark	√ (General Performance Bond)	\checkmark	\checkmark
Auckland Bus Services	×	×	X	×	√ (Dependent on operator)	√ (General Performance Bond)	\checkmark	×
Wellington Metro Rail	×	×	×	×	\checkmark	√ (General Performance Bond, optional Handback Security Bond)	\checkmark	\checkmark

Contract	SPV requirement	Minimum Capital	Security over Assets	Security over Shares	Parent Company Guarantee	Performance Bond	Set-off Right	Step-in Right
Wellington Bus Services	X	X	X 27	X	\checkmark	√ (General Performance Bond, optional Handback Security Bond)	\checkmark	X 28

27 GWRC does not have a security over all operators assets. GWRC does however have security over GWRC Assets and Transferring Assets.

28 In discrete circumstances GWRC has step in rights regarding the operator's Key Subcontractors and Transferring Assets. However it does not have general step in rights in the sense used here.

5.10 END OF TERM ARRANGEMENTS

A robust contractual framework governing the expiry of the service contract is critical both to the successful transition out of the current operator and the successful commencement of the new service provision arrangements. This applies whether the transition is to the same operator engaged under a new service contract, to a new private sector operator appointed through a competitive tender process, or to the transport authority itself (or another government agency) where services are being returned to public sector operation. Regardless of the context, the end of term arrangements need to focus on ensuring that all necessary staff, assets and knowledge are transferred or otherwise made available to the successor in the most efficient manner and so as to ensure continuity of passenger services and otherwise minimise operational and reputational risk to the transport authority.

Operator obligations to support retender process

In circumstances where the transport authority intends to retender the service contract, the authority needs to be able to provide complete and accurate information to all tenderers. This needs to be addressed expressly in the end of term provisions in the contract, as it will generally not be in the interests of the incumbent operator to fully cooperate with a retender process.

All of the service contracts reviewed contain provisions requiring the operator to support any retender process the transport authority elects to undertake. The scope of these obligations varies markedly across the contracts reviewed, but often include obligations for the operator to:

- provide assistance, cooperation and access;
- · assist with providing and verifying information; and
- ensure that documentation is not restricted from being disclosed in any retender process.

Some contracts take the extra step of requiring the operator to warrant that the information provided is true and correct.

Operator obligations to cooperate with transition

All contracts reviewed also require the operator to cooperate with the transport authority during the end of term period. Again, the scope of these obligations varies markedly, but the following features are relatively common:

- Preparing a handover package Handover packages are typically required to be maintained throughout the contract term and are usually required to contain key information about the operations and business, including key contracts, permits and approvals, tender documents relating to contractors, asset registers, information systems, details of organisational structure and daily operations, and payroll records.
- Preparing a transition-out plan Similarly, transition-out plans are usually required to be maintained throughout the contract term covering issues such as the mechanics of transfer, employee/ subcontractor engagement and retention, and governance and control frameworks to apply during transition. These plans are then implemented during a designated period at the end of term.
- Transition period The transition period is a period of time during which both the incumbent and the new service provider deliver services to allow for progressive handover. This is a key aspect of transition support across several of the contracts reviewed. Some contracts impose relatively onerous transition period obligations, such as requiring the incumbent provider to train the personnel of the new service provider.

Operator obligations to transfer assets, contracts and information to the successor

Most of the contracts reviewed require the operator to transfer specified assets to the successor, although the level of detail varies markedly. Methods of transfer include one or more of transfer agreements, statutory allocation and share transfers of the operator business. The contracts also detail the basis on which the operator is entitled to be paid for the assets. Most contracts also contain broad obligations for the operator to transfer contracts to the transport authority or its nominee. The approach to transfer of information is less uniform across the contracts, but typically requires the operator to provide, at a minimum, the information specified in the handover package, and sometimes additional information at the reasonable request of the transport authority.

In addition to specific transfer obligations, many contracts include general obligations requiring the operator not to prejudice or frustrate a transfer, and to do everything the transport authority reasonably requires to secure continuity of services.

Operator obligations to make employees available to the successor

Depending on the structure of the concession, employees and obligations in respect of their accrued entitlements may or may not pass to the successor operator. Most contracts reviewed require the operator to make some or all employees available to the successor, and a smaller number include a commitment from the transport authority to procure that the successor operator makes employment offers to the incumbent operator's employees on no less favourable terms. Some contracts also restrict the operator's ability to vary the employment terms of employees during the period prior to expiry.

Condition of assets at the end of term

In addition to general contractual obligations relating to maintenance and the condition of assets during the term, most contracts reviewed also include specific obligations about the condition of assets at the end of term.

Operators' entitlement to additional payments in respect of its end of term obligations

Although a breach of any end of term-related obligation would constitute a breach of contract, a number of jurisdictions provide an additional incentive for operators to comply with the end of term arrangements. The Victorian contracts adopt a 'negative incentive' approach whereby the operator's end of term obligations are secured by the transport authority withholding payments from the operator in the last 24 months of the contract term. The withheld amounts are paid to the operator when the transport authority is satisfied that the end of term obligations have been complied with. Examples of 'positive incentives' for meeting end of term obligations are more limited. The Parramatta Light Rail contract provides that the operator will be paid for meeting its end of term training obligations to the new provider's personnel. Similarly, under the Auckland Metro Rail contract the operator is paid for performing certain end of term obligations.

Table 15 below gives an overview of the end of term arrangements adopted in each of the contracts reviewed for the purposes of this report.



Table 15: End of term arrangements

Contract	Retender Support	Transition Support	Transfer of Assets, Information & Contracts	Employee Access & Transfer	End of Term Asset Condition Regime	End of Term Payment or Payment withholding ²⁹
Sydney Metro Northwest	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	×
Sydney Light Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	×
Newcastle Integrated Services	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	×
Paramatta Light Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	√ (payment)
Sydney Bus Services	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	×
Sydney Ferry System	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	×
Melbourne Rail Franchise	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	√ (withholding)
Melbourne Tram Franchise	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	√ (withholding)
Melbourne Bus Franchise	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark (withholding)
Melbourne Bus Services	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	√ (withholding)
Gold Coast Light Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark (withholding)
Capital Metro Light Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	×
Auckland Metro Rail	\checkmark	\checkmark	\checkmark	\checkmark	N/A ³⁰	\checkmark
Auckland Bus Services	\checkmark	\checkmark	X ³¹	×	X ³²	×
Wellington Metro Rail	\checkmark	\checkmark	\checkmark	\checkmark	\checkmark	×
Wellington Bus Services	\checkmark	\checkmark	\checkmark	×	\checkmark	×

²⁹ Not including asset maintenance top-up, or payment withholding that applies only to the end of term asset condition (as is the case for the Newcastle Integrated Services, Sydney Bus Services, and Wellington metro rail and bus contracts).

³⁰ The operator providers passenger services only. Third parties are responsible for maintenance of rail infrastructure, stations, rolling stock etc.

³¹ The Auckland Bus Services contract does not expressly provide for the transfer of assets and contracts to the new operator. However, the services contract component of the Auckland Bus Services contract requires the operator and transport authority to prepare an 'Exit Plan' with which the operator much comply. The contents of an Exit Plan are not publicly available but could include obligations in relation to transfer of assets, contracts and employees.

³² $\,$ Again, there are no specific obligations in the Auckland Bus Services contract in relation to the condition of assets at the end of the term of the contract, but an Exit Plan could contain such obligations.

6 TRENDS ANALYSIS AND CONCLUSION

The public transport landscape in Australia and New Zealand has evolved rapidly over the past two decades. This has been driven in part by policy trends concerning the governance and institutional settings for the sector and in part by external factors such as the population growth experienced in our capital cities and the corresponding need for major infrastructure investment programs, particularly transport infrastructure, to deliver transport services to meet this new demand.

Whereas Australia and New Zealand have traditionally operated their public transport systems through public sector provision and administrative regulation, governments have been progressively moving away from this model in favour of private sector service provision under a franchising model where the relationship between the transport authority and the operator is governed by contract. The practical effect of this arrangement is that the private operator delivers public transport services on a day-to-day basis, whilst government typically retains ownership of transport infrastructure and responsibility for oversight and strategic decision-making.

This report has demonstrated that whilst there is significant commonality amongst the topics and themes addressed in public transport service contracts, there is also significant variance in the way these topics and themes are addressed, as highlighted in our discussion of the key design variables. The trends outlined in this report are likely to see the continued evolution of public transport service contracts to address new issues arising across each of the key design variables and in response to the changing public transport landscape. Changing attitudes and preferences in relation to risk transfer, an increasing focus on contractual relief for unanticipated events (such as the current pandemic), and a continued focus on major project delivery and management of disruption are all issues of particular significance in the current environment. We expect the mix of commonality in topics and themes and diversity in approach will remain a characteristic of public transport service contracting, as transport authorities continue to develop new solutions to issues that are unique to their own jurisdictions, as well as adopting learnings from others.

There are a number of broader trends and developments that are also likely to impact public transport service contracts going forward:

Redefining public transport

First is the changing nature of public transport and the services it provides. As consumer preferences and expectations change, public transport systems and service contracts will need to adapt. Significant change is already occurring to what is perceived to be public transport, with 'on demand' services currently being trialled in over 40 cities globally, including in Australia and New Zealand. These services have the potential to enhance community transport options, as well as to promote greater utilisation of existing mass transit services by filling the gap for 'first and last mile' services. Among the challenges to which service contracts will need to respond are defining an appropriate service model and integrating on-demand services with traditional forms of public transport.

Pursuing innovation and new technology

Second is the growing emphasis on innovation and technological change. The ability for service contracts to take advantage of, retain scope for, and require service providers to pursue innovation and adopt technological advances is key. For example, the increased use of 'Mobility as a Service' (MaaS) platforms can not only provide for an enhanced customer experience and options for multi-modal trip planning, but also opportunities for data collection which can be used to further enhance public transport systems and services. Service contracts will need to define the respective roles of transport authorities and operators in pursuing innovation, and include flexibility for technological change to be implemented by operators in partnership with government.

Managing disruption to the network

Governments in Australia and New Zealand have been investing heavily in major new transport infrastructure, and it seems evident that this will continue to be the case. This has resulted in transport authorities having to focus more and more attention on managing the disruption to existing transport services that these new projects inevitably bring. It has also highlighted the important role which transport operators have in supporting the design, development and implementation of those projects. While service contracts have traditionally tended to focus on prescriptively defining and allocating the risks associated with network development, they will need in future to develop mechanisms that acknowledge and facilitate change, including through more collaborative governance mechanisms and mechanisms which provide the operator with a stake in successful project outcomes.

Responding to congestion

As our cities continue to struggle with congestion on the roads and overcrowding of public transport services during the morning and evening peaks, governments can be expected to look to innovative pricing solutions such as road pricing and the introduction of variable pricing for public transport trips. Efforts to reduce congestion and overcrowding may be addressed by incentivising transport users through a complementary pricing system with inbuilt flexibility around time and mode of travel. An Infrastructure Victoria report earlier this year considered a range of network pricing options across roads, public transport and parking, designed to encourage changes in consumer behaviour.³³ While these are primarily matters for governments and transport authorities to address through legislation and regulation, the implications for transport service contracts will need careful consideration, including with respect to fare and revenue provisions and change in law protections.

Promoting sustainability

Another trend which is likely to have an impact on public transport service contracts is the continued focus of governments and transport authorities on environmentally sustainable public transport systems. While public transport is already promoted as a sustainable transport option, efforts to foster a sustainable environment by encouraging increased use of public transport, as well as making transport infrastructure and services greener, will have flow-on effects for public transport service contracts. As various governments move towards targets of net-zero emissions, service contract design will need to support those initiatives. This is likely to include new commercial and contractual models to underpin the procurement of zero emissions bus fleets and the infrastructure needed to support them, provisions which mandate or incentivise the use of renewable energy, and obligations or incentives for operators to improve energy and fuel efficiency.

Leveraging and protecting data

The proliferation of data collection and utilisation is likely to have a profound impact on a number of industries, including public transport. Transport authorities are already acutely aware of the power of data to optimise transport systems and understand customer behaviour. Data is key to the development of effective transport solutions, but needs to be managed by both private sector operators and government entities within stringent privacy and data protection legislative frameworks. How data is collected, stored, shared and used is likely to remain a prominent issue moving forward, and will be reflected in obligations under public transport service contracts in addition to the legislative and regulatory settings.

Responding to COVID-19

Finally, the COVID-19 pandemic has had, and will continue to have, a significant impact on the public transport sector. Prior to the onset of the pandemic, public transport systems in Australia and New Zealand were under capacity pressure caused by patronage growth. This has suddenly and unexpectedly eased with the dramatic reduction in patronage due to COVID-19. The need for physical distancing and other measures to ensure the safety of drivers and passengers will continue to impact the capacity of public transport services in the short to medium term. The economic impacts of the pandemic on transport authorities and operators has already been significant, resulting from a dramatic decrease in patronage and increase in some operating costs, such as cleaning. In the United Kingdom, Transport for London has forecast a reduction in passenger income of up to £500m.³⁴ Public transport patronage in Australia has been estimated to have decreased by approximately 80%.³⁵ To date, we have largely seen bespoke arrangements being entered into by transport authorities and operators in respect of the pandemic, addressing the short-term revenue and cost impacts. It remains to be seen what the longer term implications will be, but it is likely operators will focus more carefully on contractual regimes governing similar unforeseen events, while transport authorities can be expected to focus on mechanisms that provide flexibility to deal with unforeseen events in line with government policy and priorities at the relevant time.

Each of these trends is having, and will continue to have, an impact on public transport service contracts and the sector more broadly.

Our aim with this report is to highlight the commonalities between existing public transport service contracts, as well as to identify some of the varied approaches taken to address issues arising from the rapidly changing public transport landscape. Governments and industry participants alike will need to be mindful of continuing developments in the sector as they consider how service contracts can be designed, negotiated and implemented in a way that achieves the multiple policy objectives of governments under a commercial and contractual model that remains attractive and sustainable for transport operators. The purpose of this report is to provide a resource that we hope will be useful for those involved in contract design and development to assist with that process.

³³ Infrastructure Victoria, Good Move: Fixing Transport Congestion (Report, March 2020).

³⁴ $\,$ International Association of Public Transport Australia / New Zealand, Public transport authorities and COVID-19: Impact and response to a pandemic (Report, March 2020).

^{35~} WSP, Public transport and COVID-19: How to transition from response to recovery (Report, 2020).

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