
I The purchaser-provider framework

This appendix describes the purchaser-provider approach to the provision of subsidised transport services. Issues associated with the provision of such services are discussed in chapter 11.

I.1 The framework

The purchaser-provider framework separates the responsibility for deciding which goods and services are provided to the community from the responsibility for delivering the services.¹ The framework can improve accountability, transparency and efficiency (box I.1).

Box I.1 Purchaser-provider framework

The purchaser-provider framework aims to clarify a government's role as purchaser. When applied effectively, the framework yields the following benefits:

- improved accountability — by providing a clear delineation of responsibilities and through the use of performance monitoring;
- transparency — with the introduction of formal contracts between the government and its providers, potentially the community can have access to improved information on the cost and quality requirements of the services purchased;
- resource allocation — purchasers have greater freedom and incentives to determine those goods and services that most effectively and efficiently promote the government's stated objectives; and
- efficiency — the provider is given greater freedom and incentives to seek new ways of delivering a service, resulting in more output for a given level of resources, or reduced unit costs for a given output.

¹ Variations of the purchaser-provider framework include *output-based management* and *managing for outcomes*. A general discussion of output-based management can be found in Abrams, Cribbitt and Gunasekera (1998).

Who should be the purchaser?

An appropriate government purchaser is one which has no conflict of interest in determining the most cost effective way to achieve stated objectives. As argued by the Independent Pricing and Regulatory Tribunal:

The best value for the CSO [community service obligation] dollar is most likely to be established by negotiation between the transport agency and a CSO purchasing agency which has no interest other than to achieve the best value for money for the CSO dollar — a purchaser-provider model. (IPART 1996, p. 21)

Appropriate purchasers are likely to be those agencies with the greatest knowledge of the needs of end users. For example, concessions for school children could be administered by an education department. This does not preclude the purchasing agency seeking assistance from other organisations (such as a department of transport) in the planning, specification and purchase of required services.

Purchasers should not be the provider of any potential goods and services, own assets used in production or be responsible for any debt liability (including deficit funding) of providers.

The performance of the purchaser should be assessed in regard to the appropriateness of the goods and services purchased (whether they are the most cost effective means of promoting the government's stated objectives).

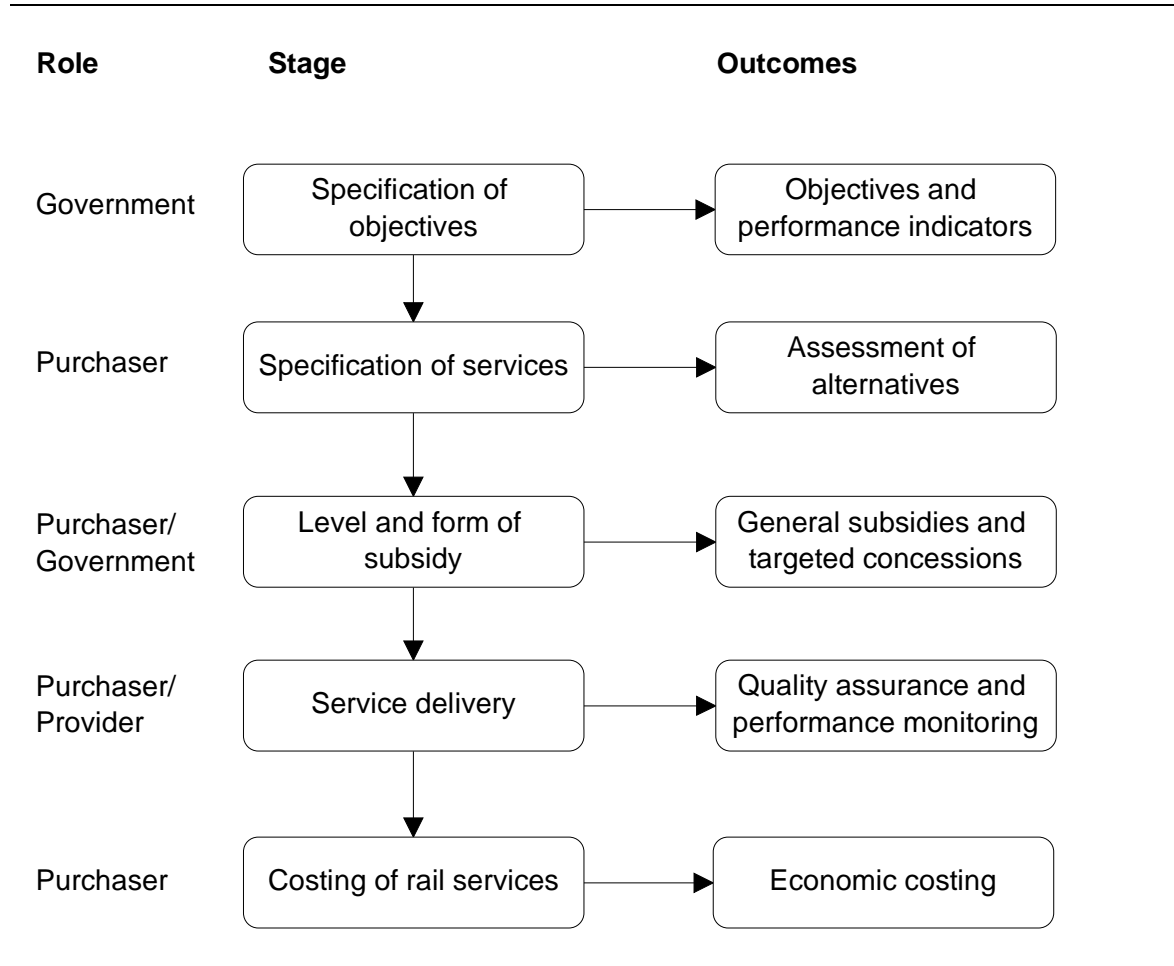
I.2 Stages of the purchaser-provider framework

In the context of subsidised rail services, the Commission has identified five stages in the implementation of the purchaser-provider framework:

- the specification of policy objectives;
- the specification of rail services required to promote the stated objectives;
- the determination of the level and form of subsidy;
- the delivery of specified services; and
- the costing of rail services.

The five stages of the framework are presented in figure I.1, including the party responsible for implementing each stage (government, purchasing agency or provider) and expected outcomes. The five stages are elaborated upon below.

Figure I.1 The purchaser-provider framework



Specification of policy objectives

The first step in the purchaser-provider framework involves the government clearly specifying its objectives to the purchasing agency. Table I.1, reproduced from the Australian Urban and Regional Development Review (AURDR 1995) provides a list of suggested transport-related policy objectives.

To give substance to policy objectives, performance indicators (preferably quantitative) need to be developed. As argued by Australian Urban and Regional Development Review:

... setting objectives and developing policies and programs is an inadequate response without a method of monitoring their various (and perhaps unintended) outcomes. (AURDR 1995, p. 24)

Making stated objectives and performance indicators available for public scrutiny can strengthen the accountability of both the government and purchasing agency.

Table I.1 Transport policy objectives

<i>Policy area</i>	<i>Specific objectives</i>
Environmental and urban amenity quality	Increase air quality and reduce emissions Reduce traffic noise and impact Improve safety and reduce accidents, injuries and deaths Reduce transport energy and consumption Reduce CO2 emissions Improve visual, aesthetic and other aspects of urban amenity Reduce air pollution costs associated with congestion
Accessibility	Improve accessibility to work (people with cars) Improve accessibility to work (people without cars) Improve accessibility to other activities (people with cars) Improve accessibility to other activities (people without cars)
Economic efficiency	Reduce costs for urban freight and commercial traffic, including costs of congestion Reduce travelling times and costs for work trips Reduce travelling times for non-work trips Reduce capital and other subsidies for providing transport except where these form part of a wider pricing policy Increase opportunities for economic integration

Source: AURDR 1995.

Specification of services

Once the government has specified its objectives, it is then the role of the purchasing agency to assess and choose the most cost effective and efficient services to achieve these objectives. It is here that the purchasing agency makes the *allocative* decision on the level, quality and choice of transport services to be subsidised.

Railways are only one transport mode that can be subsidised to promote non-commercial objectives. In addition, there may be alternatives to subsidising transport, such as parking restrictions, road pricing and car emission standards. As noted by the National Capital Planning Authority:

Evidence from overseas suggests that there are four components of a balanced urban transport strategy: appropriate investment in public transport ‘hardware’, investment in complementary ‘software’ such as passenger information systems and training; the application of appropriate transport policies such as restrictions on parking, use of toll roads and traffic demand measures; and the use of complementary land use policies such as urban consolidation and the focussing of development on centres with good public transport links. (NCPA 1993, p. 2)

Techniques such as cost-benefit analysis, when applied in a consistent and rigorous manner, are tools that purchasers can use to determine the most appropriate goods

and services to provide to the community. Public consultation and disclosure of any such analysis can strengthen the purchaser's accountability to the government and wider community.

Level and form of subsidy

Once the purchaser has specified those transport services to be subsidised, it is then necessary to decide the contribution users make to the cost of provision (within budget constraints determined by government).

Subsidies for public transport are commonly provided as general subsidies for all users with additional concessions for targeted groups. Subsidies for freight are usually directed to the transport of specific commodities as well as payments for the maintenance of unprofitable branch lines.

Rail subsidies directly affect the price paid by users. To estimate the appropriate level of subsidy, the purchaser should determine first the level of output (such as passenger numbers or freight levels) required from the railway. The role of the subsidy is then to 'bridge the gap' between what users are willing to pay at the level of output chosen by the purchaser and the cost of providing the service.

The level of the subsidy required to induce sufficient passengers or freight to use rail depends on the price elasticity of demand and this needs to be taken into account by the purchaser.

The Independent Pricing and Regulatory Tribunal commissioned the University of Sydney's Institute of Transport Studies to conduct a survey within the Sydney region to estimate the sensitivity of travel choice to fare changes (IPART 1996). The study indicated that demand for urban passenger rail services is quite inelastic with respect to price (table I.2). For example, a 1 per cent increase (decrease) in the price of a weekly train ticket would lead to a reduction (increase) in the purchase of this ticket of 0.25 per cent.

Table I.2 Price elasticities for CityRail in New South Wales

<i>Ticket type</i>	<i>Elasticity</i>
	per cent
Train single	-0.08
Train off-peak	-0.12
Train weekly	-0.25
Train travel pass	-0.53

Source: IPART 1996.

Service delivery

Purchasers should seek to obtain specified services at least cost to taxpayers. For railways, this objective can be promoted primarily through ‘competition for the market’ (chapters 6 and 11).

Once a suitable provider has been selected, it is up to the provider to meet its obligations under the contract. The purchasing agency is responsible for ensuring that an adequate quality assurance system is in place to enable the contractor to meet these obligations. Discussion on quality assurance and performance monitoring can be found in the Industry Commission’s (IC 1996) report, *Competitive Tendering and Contracting by Public Sector Agencies*, and is not repeated in this appendix.

Costing of rail services

An accurate costing of subsidised rail services involves an *economic costing* of each service, based on the *opportunity cost* of all of the resources used in delivery. This provides a basis for making valid comparisons between the cost of providing different transport services (such as buses, taxis, trams and trains) within and across jurisdictions.

Economic costing covers all variable operating costs, such as labour and fuel, plus a rental charge based on an appropriate rate of return on the assets used. The difference between the economic cost of the service and the payments made by users accurately represents the subsidy by the community in providing non-commercial transport services.

Government funded assets

In the case of railways, the government often provides the funding to purchase the assets used in production (through either government equity or borrowings). For example, the NSW Government provided \$350 million in capital grants to the State Rail Authority of New South Wales in 1997-98 (chapter 11). In most instances, as is the case in New South Wales, governments choose not to recoup a return on the capital invested. However, the opportunity cost of the assets still exists; the government (and ultimately taxpayers) incur this cost.

It is therefore important that the opportunity cost of assets funded by the government is added to negotiated subsidy payments to providers when presenting information on the cost of providing non-commercial transport services.