

Mayoral Combined Authority Board

18 October 2022

Tram Operating Model

Is the paper exempt from the press and public?	No
Reason why exempt:	Not applicable
Purpose of this report:	Policy Decision
Is this a Key Decision?	No
Has it been included on the Forward Plan?	No

Director Approving Submission of the Report:
Pat Beijer, Director of Public Transport Development

Report Author(s):
Chris Coleman, Light Rail Programme Director
chris.coleman@southyorkshire-ca.gov.uk

Executive Summary

The Tram Concession with South Yorkshire Supertram Limited (SYSL) expires on the 21st March 2024. A decision is required by the South Yorkshire Mayoral Combined Authority (SYMCA) on the future tram Operating Model. This paper sets out a recommended option for approval that will be implemented for a timely and seamless transition in March 2024.

What does this mean for businesses, people and places in South Yorkshire?

The tram system is very important for South Yorkshire as it supports economic growth and social inclusion as well as benefits to the environment. Ensuring that the tram system continues to run safely and reliably is important to residents and businesses in South Yorkshire and is a key priority for the MCA.

Recommendations

That Board members:

1. Authorise the MCA to establish an arm's length wholly owned subsidiary company (NewCo) to operate the Supertram system (with effect from 22nd March 2024).
2. Agree to receive further reports regarding the financial sustainability as soon as modelling work is concluded.

Consideration by any other Board, Committee, Assurance or Advisory Panel

N/A

1. Background

- 1.1 The light rail network infrastructure in South Yorkshire (“Supertram”) is publicly owned by South Yorkshire Passenger Transport Executive (SYPTTE). In 1997 SYPTTE awarded a 27-year concession to a wholly owned subsidiary South Yorkshire Supertram Limited (SYSL). As part of restructuring due to borrowing issues, the Government at the time required SYPTTE to dispose of the operating element of the system to a private entity. In 2000 it sold the operating company SYSL to Stagecoach Group. In 2018, the system was extended via Tram Train to Rotherham. The concession contract covers responsibility for the operation, day to day maintenance and revenue risk of the full system and expires on 21st March 2024. At expiration of this contract, SYSL no longer have the right to operate Supertram and operational, managerial and financial responsibility for the system reverts to SYPTTE/MCA.
- 1.2 A key milestone for the successful and seamless transition to a new operator in March 2024, is a decision on the future Operating Model. The net operating costs (including revenue risk) for running the tram system transfers to the MCA at this point.

2. Current Position

- 2.1. Although the tram had previously generated a profit, in the year prior to Covid-19, the tram system was operating at a loss, which is largely attributed to a mix of long-term patronage decline reinforced by the closure of parts of the system for renewal works.
- 2.2 General suppression in demand for public transport during Covid-19 including changes to travel habits has exacerbated a further decline in passenger numbers, and an increase in operating costs as a result of inflation, is leading to an increase in financial losses.
- 2.3 Passenger demand is showing signs of recovery but remains uncertain as the rate of recovery post-Covid needs to settle and demand may be plateauing.
- 2.4 The tram infrastructure and vehicles are assets that are owned by the MCA but are nearing the end of their economic life and the renewal programme would see disruption to operations. The MCA has secured c. £100m of capital from DfT to commence this programme of works but requires significantly more funding in the medium term to enable the renewal of all life-expired assets. The MCA is in the process of submitting a business case to DfT for further funding.

3. Challenges

- 3.1 A new operator is required to be in place from March 2024 (17 months).
- 3.2 Mobilisation for a new operating model of this scale and complexity represents a significant workload and requires time and additional specialist resources to

achieve a seamless transition. This includes the development of a new fares retailing strategy and supporting platform, including a website and retail systems ready for operation in March 2024 and migrating the Shared Services (retailing, Information Technology (IT) business support functions: HR, finance, procurement) from Stagecoach to NewCo.

4. Financials

- 4.1 Since March 2020, due to the impact of Covid-19, which led to a shortfall in fare-paying passengers, the current operator has been receiving ongoing financial support from the public sector; this will end in the current year.
- 4.2 Based on the current and predicted financial performance of the current operator (Stagecoach) through to March 2024 and the forecasted operating costs and passenger numbers, the tram system will require ongoing financial support from March 2024 for the foreseeable future.
- 4.3 The MCA is currently reviewing options to reduce future operating costs and improve the longer-term financial affordability of the tram system. These will be presented to board members as soon as practicable for decision.

5. Preferred Operating Model

- 5.1 All possible options and permutations have been explored which satisfy the constraints within legal, procurement, financial and timescale dimensions.
- 5.2 In conclusion and for the following reasons, the preferred operating model is to establish an arm's length wholly owned subsidiary company (NewCo) (with appropriate private sector support to mobilise and manage operations):
 - i) It provides a clear and straightforward contractual route to provide the required flexibility for funding considering revenue and cost risk will lie with the MCA;
 - ii) It retains the potential to utilise private sector resource/capability where it can add most value;
 - iii) It mitigates risk of tram operations impacting on core MCA resources and functions by either buying in the management capacity/capability from the private sector or recruiting to an appropriate management structure, bolstering the TUPE'd resource in areas where more management capability is required;
 - iv) It is the operating model that best mitigates renewals risk by providing the maximum flexibility in terms of delivering capital renewals work and delivering such works in a manner that best meets competing impacts (revenue cost v capital cost v longer term impacts);
 - v) It retains a split in functions between MCA as commissioner and operator with the NewCo being a separate legal entity responsible to the MCA under contractual arrangements but physically separate;
 - vi) It provides clear governance and focus to drive actions to improve financial sustainability;

- vii) It minimises the number of contractual interfaces and is a joined-up structure, making clear where responsibility lies;
- viii) It represents better value for money overall than transferring operations in their entirety to the private sector while uncertainties over post-covid patronage and renewal works are ongoing;
- ix) It provides the maximum flexibility to manage costs and future sustainability by:
 - a) optimising allocation of financial risk where it can best be managed;
 - b) decisions on financial sustainability can realistically only be taken by public sector client side (e.g. frequency, hours of operations, staffing);
- x) It does not prejudice a future tendering of the tram operations or private investment once operations stabilise and become more financially predictable and sustainable;
- xi) It has been assessed as the more deliverable operating model structure in the timescales available.

5.3 Any perceived downsides in not being able to transfer risk to private sector and/or export difficult decisions to a contractor are likely to be illusory given the difficulty of transferring revenue risk at the present time contractually and the reality that decisions will ultimately come back to the public sector.

6 Recommendation

6.1 The recommendation for approval is for SYMCA to establish an arm's length wholly owned subsidiary company, with private sector resource/support to mobilise and manage operations.

7. Consultation on Proposal

7.1 Constituent members of the Mayoral Combined Authority were briefed on 27th September 2022 on the proposed Operating Model.

8. Timetable and Accountability for Implementing this Decision

8.1 A Programme is being prepared that sets out the key milestones to complete the process, including a mobilisation period by 21st March 2024.

9. Financial and Procurement Implications and Advice

9.1 This report notes the preferred operating model for the tram network following the end of the current concession in 2024. The report notes that at the end of the concession it is likely that the tram will be operating in deficit requiring public subsidy. Over the last few decades the MCA has been shielded from this risk.

9.2 Whilst the model proposed will still leave the MCA exposed to the financial performance of the network, the model will allow for that risk to be held at arms-

length. This will allow the MCA to consider how best to support the subsidiary to manage its financial affairs and mitigate the inherent risk.

- 9.3 The proposed model also notes the potential to source some key services from the market. Access to skills, expertise, and capacity will be critical in ensuring operational risks can be appropriately managed, ensuring that wherever possible they don't become financial pressures.

10. Legal Implications and Advice

- 10.1 The tramway is owned by SYPTE (SYMCA). The existing concession with South Yorkshire Supertram Limited (wholly owned subsidiary of Stagecoach Group) ends on 21st March 2024. Under the South Yorkshire Light Rail Transit Acts SYMCA have the option to operate the system via a wholly owned subsidiary of SYMCA. To ensure the transition to operation by a new entity is successful external legal support has been retained to support the in-house function.

11. Human Resources Implications and Advice

- 11.1 On the date of transfer of operations, the Transfer of Undertakings Protection of Employees Regulations will apply with the effect that employees of SYSL can opt to transfer into the new operating entity on their existing terms and conditions. An HR lead will be appointed to ensure a smooth transfer.

12. Equality and Diversity Implications and Advice

- 12.1 None

13. Climate Change Implications and Advice

- 13.1 None

14. Information and Communication Technology Implications and Advice

- 14.1 An independent IT expert has completed an assessment of the implications of the proposal. This work has identified several systems relating to Shared Services that will need to be procured prior to March 2024 and allowed a programme of activity to be developed that will deliver a seamless transfer in March 2024.

15. Communications and Marketing Implications and Advice

- 15.1 None

List of Appendices Included

None

Background Papers

None
