Mayoral Combined Authority Board

Tuesday, 12 March 2024

South Yorkshire Bus Reform

Is the paper exempt from the press and public?	Partly – Appendices A and B are exempt
Reason why exempt:	The information contained in Appendix A [the franchising assessment] and Appendix B [draft franchising scheme] are exempt under paragraph 3 of Part 1 to Schedule 12A of the Local Government Act 1972 as it contains information relating to the financial or business affairs of any particular person including the MCA. It is considered that the public interest in maintaining the [confidential nature of] content of the appendices outweighs the public interest in disclosing the information, as publication could prejudice current and future decision making
Purpose of this report:	Policy Decision
Is this a Key Decision?	Yes
Has it been included on the Forward Plan of Key Decisions?	Yes

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Executive summary

On election in May 2022 the Mayor made a strategic priority of fixing South Yorkshire's buses so that public transport is the efficient and effective public service it used to be.

On 4 March 2022, the Mayor and Leaders at the MCA Board approved the recommendation to issue a Notice of Intention to prepare an assessment of a proposed bus franchising scheme (Franchising Scheme) in accordance with the Transport Act 2000 (as amended by the Bus Services Act 2017).

The Department for Transport (the "DfT") guidelines stipulate that the MCA is required to undertake a franchising assessment ("Franchising Assessment"), an Independent Audit and Public Consultation before a decision can be made on the preferred regulatory model for buses in South Yorkshire. South Yorkshire's Bus Reform programme is currently at the end of the Franchising Assessment phase.

This paper sets out the outcomes of South Yorkshire's Franchising Assessment and seeks a decision on whether to progress the proposed franchising scheme to Independent Audit.

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

Bus services provide essential journeys allowing people to access employment, education, healthcare, leisure and social activities. Bus services are fundamental in supporting South Yorkshire Mayoral Combined Authority's ambitions to drive economic growth and to improve the prosperity, health and environment for the people of South Yorkshire.

However, the bus market in South Yorkshire has been experiencing a cycle of decline, an issue that has been further exacerbated by the impacts of the Covid-19 pandemic and rising levels of cost inflation. The effects of this are a growing reliance on public funding to sustain bus service levels.

The Franchising Assessment considers a range of possible operating models for bus services in South Yorkshire against the underlying bus market challenges and considers implications for the people of South Yorkshire.

Recommendations

That the MCA Board:

1. Note the outcome of the assessment of the proposed franchising scheme.

2. Subject to recommendation 3 below, approve the progression of the proposed franchising scheme to Independent Audit, in accordance with s.123D of the Transport Act 2000.

3. Delegate authority to the Head of Paid Services, in consultation with the Section 73 Officer and Monitoring Officer, to approve final amendments to the Franchising Assessment and the proposed Franchising Scheme prior to progression to Independent Audit, provided that such final amendments do not materially impact the outcome of the Franchising Assessment. The Franchising Assessment and the proposed franchising scheme are set out at Appendices A and B to this report.

4. Approve the entering into contract with an Independent Auditor to undertake the statutorily required audit under s.123D of the Transport Act 2000.

5. Receive a further report following the completion of the Independent Audit

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

Mayoral Combined Authority Board	04 March 2022
Transport and the Environment Board	27 October 2022
Audit and Standards Committee	20 September 2023
Overview and Scrutiny Committee	21 September 2023
Audit and Standards Committee	13 December 2023

1. Background

1.1 The bus market in South Yorkshire has been experiencing a continuous cycle of decline whilst growing its reliance on public funding to sustain bus service levels:

- Over the past decade, bus mileage declined by 42%.
- In 2012/13, 13% of the bus network mileage was supported by public funding. By 2022/23 this had grown to 20%.

For 2023/24, the forecast is that the proportion of publicly supported buses will increase further to 24%, which is being enabled by the MCA investing one-off reserves to maintain and stabilise service levels.

Sustained underinvestment in customer service standards is resulting in passenger dissatisfaction. Bus services have become less frequent, less reliable and operated by an ageing fleet of buses. South Yorkshire's buses on average are 11.5 years old (the national average is 8 years) against a life expectancy of 15 years. Investment to renew the ageing bus fleet is required urgently from an economic perspective, but also to achieve net zero aims for South Yorkshire, to reduce pollution and improve the health of residents.

The imminent need to invest in overdue bus renewal will further increase the cost of the bus network and put additional pressure on the financial sustainability of the commercial bus network and the support required from public sources to sustain service levels.

Under the current commercial system, the growing need for public funding is not controlled by the public sector.

Through a Franchising Scheme, the MCA would have strategic control of the bus network in South Yorkshire, and the flexibility to make changes within a more sustainable investment model and reinvesting revenue upside in growing the bus network. In turn this could help improve punctuality, reliability, consistency of standards and accessibility, and hence could contribute to improving patronage. Franchising could also have a greater impact on addressing the existing challenges around fare and ticketing complexity, as fares policy would solely reside with the MCA in this model. A Franchising Scheme would also provide the MCA with stronger contractual levers to ensure performance standards (e.g. reliability and punctuality) are maintained.

1.2 **Structure of the Franchising Assessment**

The statutory steps an Authority must follow to undertake an assessment of a Franchising Scheme are set out in the Act and related DfT guidance. These comprise:

- the development of a Case for Change (approved by the Transport and the Environment Board on 27 October 2022);
- setting objectives;
- options generation;
- an assessment of the options;
- selection of a preferred option.

The Franchising Assessment must be subjected to an Independent Audit and Public Consultation before a final Mayoral Decision can be made on whether to proceed with the implementation of a Franchising Scheme.

South Yorkshire's Franchising Assessment has followed the principles of a five case Outline Business Case (in accordance with Section 123B of the Act). The five cases that make up the Franchising Assessment are:

- Strategic
- Economic
- Commercial
- Management
- Financial

1.3 **Objectives**

In the early stages of the Franchising Assessment process, and in accordance with the Act, outline objectives were set. These objectives were mainly derived from South Yorkshire's 2019 Transport Strategy and were refined further during the assessment as the Strategic Case developed. The extent to which the MCA can achieve these objectives under each of the options tested through the Franchising Assessment, has been a critical factor in determining the preferred option. If these objectives can be achieved, it will support the MCA in addressing some of the fundamental issues experienced in the bus network; stabilising and improving the bus service, creating a more stable financial environment and better aligning public transport solutions to support local placemaking, net zero and economic policy aims.

The final objectives used in the Franchising Assessment are provided in the table below;

Theme	Objective
Affordability	The delivery model must be affordable to the MCA
Value for Money	The delivery model must achieve value for money to the MCA
Passenger Demand	The delivery model should drive increases in passenger demand
Coverage and Connectivity	The delivery model should increase in coverage and connectivity across the region
Punctuality and Reliability	The delivery model should increase in punctuality and reliability of bus services
Market Conditions	The delivery model should increase the presence of operators in the bus network
Environmental Sustainability	The delivery model should drive an environmentally sustainable bus network

Societal Responsiveness	The delivery model should drive improved responsiveness to societal needs through connectivity
Supporting Most Vulnerable	The delivery model will support a network that supports society's most vulnerable
Equity in Customer Experience	The delivery model will drive equity in experience for customers
Deliverability	The delivery model must be deliverable

Each of the options within the assessment have been tested against these objectives, with affordability and deliverability being pass / fail criteria.

1.4 **Options consideration: Background**

The two distinct operating models (Enhanced Partnership and Franchising) exercise powers introduced under the Bus Services Act 2017 and there are several variations within these models. The variations that have been considered within the Franchising Assessment have been informed by engagement with internal and external stakeholders.

Engagement with external stakeholders:

- South Yorkshire Bus Operators through the existing delivery of the Enhanced Partnership
- Request of relevant information from bus operators required to develop the Franchising Assessment
- South Yorkshire Bus Operators with regards Enhanced Partnership Plus
- Market engagement with bus operators
- Neighbouring Transport Authorities

The existing Enhanced Partnership arrangements continue to focus on delivering improvements and progress against the delivery of South Yorkshire's Bus Services Improvement Plan (BSIP) and the Enhanced Partnership Scheme is recorded and monitored on an ongoing basis through the Enhanced Partnership Board. This has informed the assumptions used within the Franchising Assessment.

An Enhanced Partnership Plus would deliver improvements compared to the existing Enhanced Partnership, with additional investment in buses, customer service, passenger research, customer resource support and profit sharing. The assumptions made in this option have been informed by the engagement with South Yorkshire bus operators.

Bus Franchising would mean that most bus services in South Yorkshire would be contracted by the MCA through franchise agreements, with full control over the specification of those services, the fare box, depots, and fleet. The responsibility for the revenue and cost of the operations would transfer to the MCA, with franchise operators being paid a margin by the MCA on the service provided. Routes not included within the Franchising Scheme (included as Appendix B to this report), would be operated under a service permit or be exempt, as is required by the Bus Services Act 2017 Franchising Scheme Guidance.

Franchise packages would be offered to the market to bid for in stages and in different contract sizes (number of routes/services) to facilitate competition.

The reference case and two options assessed within the Franchising Assessment have been modelled based on the bus network effective from 29 October 2023 and using operator data submitted.

1.5 **Options consideration: South Yorkshire's Franchising Assessment**

South Yorkshire's Franchising Assessment has evaluated six options using the Green and Aqua Book principles. These options are considering Enhanced Partnership ("EP"), Enhanced Partnership Plus ("EP Plus") and four variations of bus franchising with sensitivities around bus fleet, including zero emission, and bus depot ownership.

<u>Enhanced Partnership (Do-Nothing option)</u>

An EP is already in place between the MCA and operators running Local Qualifying Bus Services (the "Operators"). This existing regulatory model will form the Do-Nothing option (or Reference Case) for the Franchising Assessment.

The Operators own and manage their own depots and fleet, with the exception of Doncaster depot, which is owned by the MCA and leased to the operator. Transition to Zero Emission Buses ("ZEBs") would be delivered at the operators' discretion.

Under the EP, the MCA does not have strategic control of the network and therefore lacks the ability to make changes beyond tendered services. The operators specify the network design and set their own fares and operate services to the performance standards specified by the MCA. Performance standards cannot be legally sanctioned by the operator as this power lies with the Traffic Commissioner.

The Franchising Assessment demonstrates that the continuation of an EP, without intervention (i.e. Do-Nothing), would result in a continuation of the systemic decline of South Yorkshire's bus network.

<u>Enhanced Partnership Plus</u>

The EP Plus option builds on the existing EP with additional investment and interventions around network, fares and ticketing, fleet, and branding which are assumed to be comparable to investments that would be made through the Franchising Scheme assessed.

The EP Plus option assumes a slightly larger bus network than EP (Do-Nothing) through an increased investment in tendered services. The same network has been assumed to be deliverable under the EP Plus as the Franchising Scheme, and the same outcomes assumed to be achieved. The MCA could influence the network design through the tendered services, however, this would still be operator controlled and any network changes would require buy-in from Operators.

A portion of renewal and upgrade of fleet costs to move towards a faster rollout of ZEBs is assumed to be covered by the operators securing third party grant funding with the remaining costs covered directly by the Operators. It is also assumed that an integrated ticketing service could be provided through negotiation with operators.

Franchising Scheme

Under all four Franchising Options (A to D), the MCA will have strategic control of almost all of the South Yorkshire bus network and will therefore be able to design and specify the network, routes and service provision. The MCA will be able to more easily specify, monitor and enforce performance standards on each route, and can set consistent fare structures and prices across South Yorkshire. It would also own and operate overarching ITS infrastructure, including ticketing systems, real time travel information, contract and procurement/performance management systems. The MCA would specify requirements for Operators to integrate and ensure interoperability of buses and support better integration with other transport solutions such as light rail, active travel and rail. Fleet would be operated and maintained to the MCA standards with the MCA also having control over depots under Franchising Options B and D.

	Franchising Option A	Franchising Option B	Franchising Option C	Franchising Option D
Depots	Operator Owned	MCA Owned	Operator Owned	MCA Owned
Vehicles	Operator Owned	MCA Owned	MCA Owned	Operator Owned

Franchising Option A – Operator Owned Depots and Fleet

Under Franchising Option A, the MCA would gain control of the full network and service design, but operators would continue to retain ownership of their depots and fleet. New operators to the market would need to provide their own depot facilities and fleet. The only depot directly owned by the MCA is in Doncaster.

The MCA would work with the operators to consider enhancements to the depots and fleets, such as the transition to zero emission technologies, and set standards for fleet. The operators would then be responsible for financing, procuring and delivering these enhancements.

Franchising Option B – MCA Owned Depots and Fleet

Under Franchising Option B, the MCA would gain control of the full network and service design. Depots and fleet would be acquired by the MCA and be made available to bidders for the relevant franchise lots, to be used for franchise contracts under the contract terms.

The MCA would acquire the legacy fleet from incumbent operators. The MCA would be responsible for financing, funding, procuring and delivering enhancements to the depots and fleet, with the operators being responsible for routine maintenance of the fleet and depots.

This option means that the MCA will be able to offer bidders for franchise contracts full access to depot and fleet assets needed to operate the franchise lots put out to market to bid on. This opens up access to new entrants to South Yorkshire's bus market and encourage financially competitive bids.

Franchising Option C – Operator Owned Depots and MCA Owned Fleet

Under the Franchising Option C, the MCA would gain control of full network and service design, but operators would continue to retain ownership of their depots, other than the existing MCA owned depot at Doncaster. New operators would need to provide their own depot facilities. The fleet would be acquired by the MCA and be made available to operators bidding for franchise contracts.

The MCA would acquire the legacy fleet from incumbent operators. The MCA would be responsible for financing, funding, procuring and delivering enhancements to the fleet, but would need to work with the operators to consider enhancements to the depots.

This option means that the MCA will make available to bidders for franchise contracts the fleet needed to operate franchise lots put out to the market, but bidders would have to secure their own depot facilities to operate and maintain the fleet needed to support the service requirements specified by the MCA. This could significantly inhibit the ability for new operators to enter the South Yorkshire market and put competitive bids forward for franchise lots put out to market, owing to the significant upfront capital investment required and lead times for acquiring depot facilities. This option could drive financial inefficiencies into South Yorkshire's bus market.

Franchising Option D – MCA Owned Depots and Operator Owned Fleet

Under the Franchising Option D, the MCA would gain control of the full network and service design, but operators would continue to retain ownership of their fleet. Depots would be acquired by the MCA and be made available to operators bidding for franchise contracts (including the existing MCA owned depot at Doncaster).

The MCA would be responsible for financing, funding, procuring and delivering enhancements to the depots, and specifying the standards of the fleet which they would not own.

This option means that the MCA will be able to offer bidders full access to depot facilities needed to operate the franchise lots put out to market to bid on. This opens up access to new entrants to South Yorkshire's bus market and encourage financially competitive bids. However, those bidders would have to acquire their own bus fleet to support their bids, which carries a high upfront capital investment that might not be available to all bidders and could drive financial inefficiency or limit the MCA's ability to achieve other policy objectives around service standards for fleet and net zero.

1.6 **Franchising Assessment conclusions**

The Franchising Assessment has effectively been completed and this report recommends that any final, non-material changes, may be made by delegated authority to the MCA's Head of Paid Service, in consultation with the Section 73 Officer and Monitoring Officer.

South Yorkshire's Franchising Assessment concludes that the strategic benefits of the option of Bus Franchising exceed the benefits of the reference case of Enhanced Partnerships and the alternative option of EP Plus.

Overall, from the Franchising Assessment, the four Franchising options better meet the MCA's objectives when compared to EP Plus. Within these options, Franchising Option B (where MCA owns both the depots and fleet) is the preferred and most affordable option. It also provides the MCA with greater control and more certainty in delivering its objectives. This compares to the EP Plus option which does not provide the same level of control to the MCA and wholly relies upon reaching agreement with Operators.

Franchising Option B is affordable, demonstrates VFM, is deliverable and better meets the MCA's objectives when compared to the other options assessed.

A sustained, enhanced and financially sustainable bus network is a key enabler to achieve the MCA's policy aims and ambitions to drive economic growth and to improve the prosperity, health and the environment. The Franchising Assessment demonstrates that without intervention through additional public support, the bus service in South Yorkshire will be set on an inevitable course of further decline. Each of the six options assessed would require significant public intervention to head off this spiral of decline and inhibit the MCA's ability to achieve its policy aims.

However, such intervention under a Franchised model is more affordable, more financially sustainable and delivers better value for money when compared to the existing Enhanced Partnership and the option of an EP Plus. In return, a franchise model offers the MCA greater control over the network's ability to support its policy objectives (including economic growth, prosperity, health, place-making and net zero aims) through public control over service specification, fare box, the pace and type of bus fleet renewal and customer service. This is traded off against the additional risks imported by the MCA taking responsibility for running costs, fare box income, the transition to implement franchising and the ownership of depots and fleet.

Franchising requires significant capital investment to procure depots and renew the bus fleet. It will require funding to support the transition period. It also requires ongoing revenue support which will be achieved by raising income through the transport levy, the element of which funds bus activity, would need to be inflation linked (RPI +1% from 2030 onwards). These financing methods are making the franchising option affordable and able to generate a surplus that can be used to support a further cycle of fleet investment needs.

To reverse the decline and to achieve a stand-still in bus services under an Enhanced Partnership or EP Plus option, additional financial support from public funding is required alongside private sector investment, but this would be less affordable overall. This is as a result the public sector's access to capital grants to invest in the sustainability of the network and lower loan borrowing cost.

The EP Plus model is not offered by all South Yorkshire's operators, which makes it less effective owing to the consequential lack of consistency in operating models within South Yorkshire. Also, commercial operators would have to find ways to finance the costs required for the additional investment which could lead to reduced financial sustainability and further service reductions.

Although Franchising Option B and the EP Plus option deliver VFM, and are deliverable, Franchising is affordable over the appraisal period and there is greater certainty with delivery of required outcomes when compared to EP Plus. EP Plus is not affordable over the appraisal period and there are risks to the delivery of outcomes as these are contingent upon reaching agreement with operators.

The outcome of the Franchising Assessment is that Franchising is the preferred option for the MCA to progress through to Independent Audit. The audit results would be reported to the MCA to consider progression to Public Consultation.

Considering the potential opportunities arising from the EP Plus proposals and the lead time to implement the first package of franchised services, it is proposed to continue engaging with local bus operators to improve services through the Enhanced Partnership (Plus) arrangements.

1.7 **Next steps – independent audit**

Following completion of the Franchising Assessment, the MCA must obtain a report from an independent auditor in order to proceed with the Franchising Scheme in accordance with section 123D of the Act and paragraphs 1.77 – 1.87 of the DfT Guidance.

The auditor's report must state whether, in the opinion of the auditor:

- the information relied on by the authority or authorities in considering the matters referred to in section 123B(3)(d) or (e) of the Act is of sufficient quality;
- the analysis of that information in the assessment is of sufficient quality; and
- the authority or authorities had due regard to guidance issued under section 123B of the Act in preparing the assessment.

When forming their opinion as to whether the information relied upon, and the analysis of the information by the authority, is of sufficient quality, auditors should take into account the quality and timeliness of any information received from bus operators and the following criteria:

- whether the information used comes from recognised sources;
- whether the information used is comprehensive or selectively supports the arguments in favour, or against, any particular option;
- whether the information used is relevant and up to date;
- whether the assumptions recorded as part of the assessment are supported by recognised sources; and
- the mathematical and modelling accuracy of the analytical methods used to calculate the impacts of the options.

Should the auditor consider that one or more of these criteria have not been satisfied, then they should advise the franchising authority or authorities accordingly.

The auditor should not report or pass judgement on the decisions taken by the authority or authorities or the outcomes of the assessment – their role is purely to consider the process that has been followed, the accuracy and robustness of the information that has been used in the analysis, and that the mechanics of the process have been carried out correctly.

1.8 **Next Steps – public consultation**

Following the preparation of the Franchising Assessment, and the report prepared by the auditor, the MCA should then consult widely on their proposals. This should ensure that local passengers, businesses and transport providers are able to comment on the proposals before the MCA takes the decision as to whether to implement the franchising scheme. It is important to note that in accordance with s123G(4) of the Act the decision whether to make a Franchising Scheme is a decision to be taken by the Mayor on behalf of the MCA.

The Act requires an authority or authorities to publish, as part of the consultation process, the following documents:

- A consultation document relating to the proposed scheme;
- the assessment of the proposed scheme; and
- the report prepared by the auditor.

The consultation is proposed to last twelve weeks and will include statutory consultees as well as broader public engagement.

2. Key Issues

2.1 The Franchising Assessment is clear in that without public sector intervention, South Yorkshire's bus network will continue to decline. Further decline will act as a constraint on the MCA's ability to drive economic growth and to improve the prosperity, health and the environment.

In all options considered through the Franchising Assessment, in order to sustain the bus network and to achieve the MCA's objectives, the MCA has to intervene through capital and revenue funding with Franchise Option B being the most affordable, best value for money and deliverable model to achieve the objectives.

2.2 The Franchising Assessment also concludes that such intervention to prevent further and continuous decline of the bus network will be required irrespective of the three headline operating models evaluated in the Franchising Assessment; Enhanced Partnership, EP Plus or Franchising.

The Franchising Assessment demonstrates that bus franchising delivers the best value for money and affordability, when compared to the Enhanced Partnership and EP Plus options. To sustain the 2023/24 bus network, each of these operating models would require additional public sector investment. However, such investment would deliver better value for money and be more affordable to the MCA under a franchised model.

2.3 Key considerations for the MCA Board are: 1. Whether it wants to invest in sustaining the current bus network and if so, 2. Whether it wants to make this investment through a franchised model (full control) or through the model of Enhanced Partnership or EP Plus (without direct control).

2.4 Franchising significantly impacts the financial profile of the MCA with higher volumes of costs and revenues going through the MCA's accounts, with revenue investment required to sustain the current network. The MCA also has to earmark capital investment to acquire the bus fleet and depots and funding to support the transition phase.

3. Options Considered and Recommended Proposal

3.1 Option 1

Progress the Franchising Assessment to Independent Audit

Progressing the Franchising Assessment to Independent Audit will provide assurance to the MCA that the outcomes of the assessment are informed by robust information, that the preferred option is affordable to the MCA and that the implications are comprehensively considered.

If the Franchising Assessment is successfully audited, this enables the MCA to consider if it wishes to progress the Franchising Scheme to Public Consultation and potentially implementation.

3.2 Option 1 Risks and Mitigations

Progressing the Franchising Assessment to Independent Audit serves to give the MCA the assurance that the assessment undertaken is robust, considering quality and compliance with legislation. The auditor's report may identify issues or changes that are required to the assessment, which could change the findings of the assessment. If any changes needed require significant rework, then this would attract additional costs.

This risk is partly mitigated by Grant Thornton, alongside ARUP, undertaking the Franchising Assessment for South Yorkshire. Grant Thornton were the Independent Auditors for GMCA and WYCA's Franchising Assessment and have a full appreciation of the audit requirements.

In addition, the assessment has been subjected to Quality Assurance by Grant Thornton and undergone robust internal review by senior finance officers from the MCA.

The Enhanced Partnership arrangement will remain in place in the interim and Enhanced Partnership Plus arrangement could be pursued in parallel.

3.3 Option 2

Not to progress the Franchising Assessment to Independent Audit

This will mean that the Franchising Assessment will not be considered further by the MCA at this point in time, which means that the Enhanced Partnership as is will be continued with or without Enhanced Partnership Plus options.

3.4 Option 2 Risks and Mitigations

If it is decided not to progress the Franchising Assessment progression to Independent Audit stage, the current Enhanced Partnership will continue, and the risk of managed decline of the bus network would continue. In mitigating this risk the Enhanced Partnership Plus options could be pursued.

3.5 **Recommended Option**

Option 1

4. Consultation on Proposal

4.1 A comprehensive stakeholder engagement programme has been undertaken to keep key stakeholders engaged and informed in the process.

Stakeholders can be described in three categories:
1. Elected Officials and Public Sector Officers
2. Industry
3. User Group

Elected official and public sector officer engagement has been ongoing from the summer of 2023, they include briefings with:

- Mayor of South Yorkshire
- Leaders of constituent authorities
- Transport Officers of constituent authorities
- Directors of Finance of constituent authorities
- Executive Directors of constituent authorities
- Chief Executive Officers of constituent authorities
- Neighbouring authorities – East Riding of Yorkshire, Lincolnshire County Council, Derbyshire County Council, West Yorkshire Combined Authority, North Yorkshire Council, Nottinghamshire County Council
- South Yorkshire Mayoral Combined Authority Executive Leadership Team

Industry engagement consists of:

- Regular operator forum for all operators who run services in South Yorkshire
- Department for Transport officers
- National and international transport operators who do not currently run services in South Yorkshire
- Trade Unions
- UK Infrastructure Bank

User Group Engagement consists of:

- Regular meetings with Better Buses for South Yorkshire

5. Timetable and Accountability for Implementing this Decision

5.1 Should the decision be made to conduct an Independent Audit. It is expected to have contracted an auditor in April 2024. It is expected, based on comparable MCA audits that the audit will take approximately eight weeks. The Executive Director of Transport will be responsible for implementing the decision.

6. Financial and Procurement Implications and Advice

6.1 Summary

The assessment shows that the existing bus network being operated within South Yorkshire is not financially sustainable without intervention or an increase in fare-paying patronage that is not currently forecast.

This aligns to the MCA's Medium-Term Financial Strategy ("MTFS"), where modelling shows that the funding available to support bus services will reduce significantly following the assumed end of Government funding by financial year 2025/26.

The MTFS assumes that no new revenue funding is available to backfill the loss of this grant funding, and therefore the cost base will need to be reduced through the withdrawal of tendered services.

It is against this backdrop that the franchise assessment has been undertaken: to test whether there are more financially efficient means of delivering bus services.

A move to a franchise model would represent a fundamental change to the way in which bus services could be delivered in South Yorkshire.

The proposal would significantly change in the way in which the MCA could use its funding to support provision of bus services and materially alter the financial exposure the MCA would be subject to.

Currently, the MCA has limited means of intervening in the bus network. The MCA can choose to fund individual at-risk services through its tendered services budget but is limited in its ability to act strategically.

Modelling shows that in recent years despite significant publicly funded intervention - through tendered services - mileage and service provision has continued to decline, posing ongoing value-for-money considerations.

The assessment suggests that a franchised network could be more suited to the MCA's funding environment and strategic aims. The proposal would allow for the use of available MCA capital funding to invest into bus services, particularly through fleet renewal. Using capital funding to invest into capital assets in this manner is more efficient than allowing for the costs of capital investment to fall onto the revenue account as currently happens.

A move to a franchise model would materially change the way in which the MCA is exposed to the financial performance of the bus network. Currently, when services become unviable the MCA is presented with an option to either fund those services or see them withdrawn by operators. Interventions are largely transactional, with limited scope to manage the totality of bus service provision.

Under a franchise model the MCA would more directly own the financial performance, having to sustain losses until decisions could be made to withdraw or retain services, but equally retaining any surpluses generated and being free to reinvest those surpluses at its discretion. The MCA would also be free to proactively design a network to meet available funding rather than dealing with individual services reactively.

Accordingly, whilst moving to a franchise model would increase direct exposure to the financial performance of the network it may also afford more tools and options to manage that exposure than are currently available.

The assessment concludes that the franchise option would be affordable over a thirty-year appraisal period. The assessment is modelled with consistently prudent assumptions around patronage, costs, and funding available to invest into the network. These assumptions are stress-tested for varying scenarios.

As with any long-term financial model, it is likely that assumptions will change over time. The modelling detailed in this assessment represents a forecast at a point in time using the best available information. As with the rest of its business, the MCA will need to continue to iterate its financial forecasting and adjust its planning.

Sensitivities & Assumptions

The financial case is predicated on a number of fundamental assumptions, the robustness of which will be tested by the independent auditor. These assumptions have been agreed with the Executive Director Resources & Investment and the Assistant Director Strategic Finance, after being subjected to a series of core sensitivity tests and considering best practice.

Where a choice has existed, the MCA has opted to err on the side of caution to ensure prudency throughout the modelling.

Further details of these tests can be found in the financial case. Of note are the following assumptions:

- No Government funding is made available to the MCA beyond the CRSTS2 capital funding announced. This funding is partly modelled to support capital activity but is assumed to end without successor funding in 2032. Any additional funding would support the financial model.
- No efficiencies associated with the ability to redesign the bus network are assumed. An optimised model that could reduce costs and generate additional farebox income would support the financial model.
- No efficiencies associated with a move to electric vehicles are assumed. Any operating efficiencies realised would support the financial model.
- Patronage is assumed to decline in line with DfT models. This represents a key prudent assumption and should patronage decline be arrested or improved the financial model will also improve.
- Changes to patronage and fare pricing would have a direct impact on ticket revenues – a 10% change in ticket revenues would cause a variance of c.£10m per annum;
- Price inflation is modelled at OBR forecasts in the near term with an assumed 3% per annum in the long term. Should inflation increase by 1% additionally per annum throughout the 30-year appraisal period the additional costs would

be significant at c. £440m albeit offset by assumed farebox inflation that is also modelled as tracking inflation;

- The assumed pace at which depots can be acquired will largely be dictated by the outcome of commercial negotiations with operators, and clearly there is a high degree of uncertainty in relation to the cost estimates, although the financial model builds in the maximum appropriate percentage of optimism bias;
- The costs and financing of fleet acquisition is a material sensitivity. All capital expenditure post 2035 (the majority of which relates to fleet) will be financed through prudential borrowing at an interest rate of 5% per annum. If the cost of replacement vehicles exceeds the estimates in the model by 10%, the annual surplus would deteriorate by £2-3m from the 2040s onwards;
- Cash balances are assumed to attract a coupon of 2% in the model. Any financial surpluses that arise are assumed to grow at this rate and are used to fund the years where deficits may arise. A variance of 1% in the interest rate would change the cumulative position by c.£55m.
- The transport levy increases in line with the MTFS up to the end of the decade, and then increases at 1% above the rate of inflation thereafter.

These tests therefore demonstrate that the financial model is sensitive to marginal changes in the core assumptions. Prudent assumptions mean that should Government funding become available or patronage levels be improved more funding would be available for investment. Conversely, should upside potential not accrue and adverse effects take hold, the model can tip into deficit relatively quickly.

Risks

As noted in the main body of the report, the additional risks associated with franchising option B include the MCA taking responsibility for fare box income, the transition to implement franchising and the ownership of depots and fleet. Indirectly, the MCA will also be exposed to running costs such as driver salaries and fuel prices because operators will price in risk on pay and price inflation when bidding for contracts.

The key risks include:

- The MCA's ability to use CRSTS2 for the purposes of bus franchising – at this stage, it is uncertain whether this is permissible because DfT has not yet published the terms and conditions of CRSTS2;
- The MCA's ability to acquire depots and fleet – external factors, such as commercial negotiations with the current depot owners, and the bus manufacturing sector's capacity to produce and deliver new zero emission vehicles in the proposed timescales, would have an impact on the cost and deliverability of the transitional phase of the franchising programme;
- Access to key skills and capability is a risk to the MCA, as it will be competing with other MCAs for a limited talent pool of staff and/or external consultants with the relevant expertise and experience;
- The MCA's assumptions around transport levy increases could be subject to review in the future, given the scale of long-term funding uncertainty and cost pressures facing the constituent member authorities;
- Farebox income is at risk of reducing beyond the assumptions set out in the model due to factors like economic downturn, demographic changes or shifts in transportation trends.
- Challenges to offsetting price increases through assumed farebox increases.

Mitigations

The financial case carefully considers an appropriate set of mitigations for the principal risks identified, including but not limited to:

- The creation of a £10m revenue reserve from a refresh of the MCA's reserves strategy, undertaken as part of the 2024/25 budget-setting process;
- The ability to optimise the network to create efficiencies, or in extremis reduce it to lower the cost base;
- The ability to acquire cheaper vehicles than zero emission buses if required, as a result of CRSTS2 restrictions or supply chain pressures;
- The likelihood of BSIP+ funding being extended to 2028/29, which would assist in stabilising the commercial network in the transitional phase immediately prior to franchising going live;
- The probability of capital funding being extended beyond the CRSTS2 funding period, and also ongoing Government support via ZEBRA;
- Upside potential in relation to prudent assumptions around fleet efficiencies (e.g. diesel fuel vs electric); and,
- The ultimate option to consider increases on the transport levy, or subject to legislation a mayoral precept.

Transition costs

In the financial model it is assumed that any implementation phase will be compressed to three years, in order to make effective use of capital grant and to access operating surpluses as early as possible. This would result in transition costs of c.£25m.

Should the MCA/Mayor determine to progress with franchising then the proposed funding strategy for these transition costs would be as follows:

- £5m from CRSTS1 capital grant to cover the cost of implementing ticketing systems;
- £4m from windfall treasury management income retained from 2023/24;
- £8m from the Protection of Priority Services Reserve;
- £2m from the MCA's allocation of gainshare revenue in 2024/25, and;
- £6m from treasury management income surplus forecast in 2024/25 – underwritten from the MCA's allocation of gainshare revenue.

6.2 Procurement – All procurements will be undertaken in accordance with the requirements of the Utilities Contract Regulations (UCR) 2016 and the Procurement Act 2023.

7. Legal Implications and Advice

7.1 In accordance with the requirements of the Transport Act 2000 and the Department for Transport's Franchising Scheme Guidance (2017), the next stages of a franchising process would, subject to determining to proceed, include (as further detailed below):

- Complete the assessment;

- MCA approval to proceed to Audit/appoint Auditors
- Commissioning a report to be prepared by an independent auditor
- MCA approval to proceed to Consultation following consideration of the Auditor’s report
- Statutory consultation
- Preparing and publishing a report setting out the MCA's response to the statutory consultation together with a recommendation as to whether to proceed with the proposed franchising scheme
- If the decision is to proceed with the franchising scheme (which is a Mayoral decision under S123G(4) of the Act), making and publishing the scheme, and
- Transition to and implementation of the franchising scheme.

Following preparation of the assessment, the MCA must obtain a report from an independent auditor on its assessment. The independent auditor’s report must state whether (in its opinion):

a) The information relied on by the MCA in producing the economic (value for money) and financial (affordability) cases of the assessment is of sufficient quality;
b) The analysis of that information is of sufficient quality; and
c) The MCA has had due regard to guidance issued by the Secretary of State under section 123B of the Act in preparing the assessment.

Following the preparation of the assessment, and the report prepared by the independent auditor, the MCA should, if it wishes to proceed with the proposed scheme, then consult widely on its proposals. This should ensure that local passengers, businesses, and transport providers are able to comment on the proposals before the MCA takes the decision as to whether to implement the franchising scheme.

The following documents must be published in support of this process:

- a consultation document relating to the proposed scheme;
- the assessment; and
- the report prepared by the independent auditor.

The MCA must consult on its proposals with key stakeholders which will include:

- Local bus operators
- Representatives of employees of such operators
- Organisations representing local passengers
- Local authorities who would be affected by the proposed scheme
- The Traffic Commissioner, Chief Officers of Police for areas to which the proposed scheme relates, Transport Focus (the Passengers' Council), and the Competition and Markets Authority
- Any other bodies or individuals it considers to be appropriate

Following the consultation process, the MCA must prepare and publish a report setting out its response to the consultation together with its decision as to whether or not to proceed with the proposed franchising scheme. The MCA should address issues raised by respondents to the consultation as part of their response, including setting out any changes to the franchising proposal that they intend to make as a result. Depending on the significance of any changes, the MCA may choose to consult again.

If the MCA decides to proceed with the franchising scheme, it must include within its response to the consultation, how it will facilitate the involvement of small and medium sized operators in the provision of services through their procurement processes.

At the same time as the MCA publishes its response to the consultation, it must also make and publish the franchising scheme. This is the process of finalising and establishing what the franchising scheme will look like in practice.

As the MCA is a Mayoral Combined Authority, it must be the Mayor that takes the decision as to whether or not to proceed with a franchising scheme.

The Assessment has been produced by Grant Thornton UK LLP together with Deloitte, Arup and Addleshaw Goddard LLP, in order to support compliance with all legal requirements surrounding the Act, subject to the risks noted in this Report.

The MCA is therefore confident that it has proceeded lawfully in its consideration of the issues around bus franchising and will continue to do so throughout the next stages of the process.

Members should be aware that, as with any decision taken by the MCA, there is a risk that the MCA may be required to defend itself from legal challenge through judicial review given the significance of the impact of bus franchising on the commercial operations of major bus operators within South Yorkshire and elsewhere.

8. Human Resources Implications and Advice

8.1 Should the MCA decide to progress the Franchising Assessment to the stage of Independent Audit, it is recommended that support is secured to provide programme director oversight of the process. Such support arrangements would need to be extended if the MCA Board approve progression to Public Consultation, when a programme director oversight role would need to be complemented with an temporary people engagement expert as an intelligent client to support the procurement of consultancy services to undertake the public consultation.

8.2 Should the MCA decide to progress franchising to implementation upon conclusion of the independent audit and public consultation stages, a Bus Reform team to support the transition would need to be mobilised to support the transition workload as set out in the Management Case.

9. Equality and Diversity Implications and Advice

9.1 In making the decisions contained in this report, Members are reminded of their legal duty under section 149 of the Equality Act 2010 to have due regard to the need to:

- i) Eliminate discrimination, harassment and victimisation;
- ii) Advance equality of opportunity between those who share a protected characteristic and persons who do not share it; and
- iii) foster good relations between those who share a protected characteristic and persons who do not share it.

In having due regard to the need advance the equality of opportunity between persons who share a protected characteristic and persons who do not, Members should have due regard to the need to:

a) remove or minimise disadvantages suffered by persons who share a relevant protected characteristic that are connected to that characteristic;
b) take steps to meet the needs of persons who share a relevant protected characteristic that are different from the needs of persons who do not share it;
c) encourage persons who share a relevant protected characteristic to participate in public life or in any activity in which participation by such persons is disproportionately low.

An Equality Impact Assessment has been undertaken and this shows that there are no negative/material adverse impacts on persons with a protected characteristic. Attached to this report at Appendix C is the Equality Impact Assessment. It is for Members to determine the weight to be given to the various factors that inform the decision, including the equality impacts and the legal duty under section 149.

10. Climate Change Implications and Advice

10.1 The aspiration is to transition to a zero-emission bus fleet as soon as practically and financially possible. The franchising assessment assumes that 30% of all new buses from the start of a potential franchising scheme would be zero-emission buses up to 2035. From 2035 100% of all new buses would be zero emission. This would support clean air targets and improve the air quality of the region.

11. Information and Communication Technology Implications and Advice

11.1 There are no direct implications for ICT arising from a decision made in respect of this particular report. There will be ICT implications that need to be considered at later stages in the Franchising process that are subject to further decision points by the MCA, specifically public consultation and transition to implementation of a Bus Franchising Scheme.

12. Communications and Marketing Implications and Advice

12.1 A communications plan has been developed to raise awareness of the Franchising Assessment.

List of Appendices Included:

A Franchising Assessment (exempt)

B Franchising Scheme (exempt)

C Equality Impact Assessment Bus Reform

Background Papers
