

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

# 11<sup>TH</sup> CONFERENCE ON COMPETITION AND OWNERSHIP IN LAND TRANSPORT

## CONNECTING COMPETITION AND INTEGRATION. A CONCEPT OF NEW ORGANIZATIONAL FRAMEWORK FOR POLISH LOCAL BUS TRANSPORT

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At present Polish local bus transport (outside cities) requires radical changes. Up till now solutions based on market deregulation, lack of active transport authorities and a number of operators competing ‘on the road’ have stopped being effective – the decisive factors are rising costs, ever increasing market requirements and related declining incomes.

It gives rise to the challenge of joining the existing potential of competing operators to a greater engagement of local authorities which will be forced to finance public service – expanding the transport offer, improvement of quality and subsequently also integration of fares, information and timetables. Another difficulty is that local governments do not possess competences enabling them to create public transport authorities and implement a ‘London’ model, which also succeeds in a number of Polish towns (Wolański, 2008).

This paper is dedicated to an attempt to find the optimum solution to the existing problem. It is based on a project carried out at the turn of 2007 and 2008 at the request of Polish Chamber of Road Transport and Forwarding (PIGTSiS), which unites many local bus carriers, mainly deriving from the split of a former state-owned enterprise PKS. The expertise was obtained from a team consisting of: Prof. Olgierd Wyszomirski (head), Krzysztof Grzelec, Ph.D., Hubert Kołodziejcki Ph.D., Marcin Gromadzki, Mariusz Józefowicz and Michał Wolański.

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

Due to the needs of foreign readers, the paper includes a detailed description of organisation and financing of local bus transport in Poland. On the other hand case studies concerning such countries as: Sweden, Germany, Denmark, the Netherlands, Great Britain and the Czech Republic, which provide important inspirations for the postulates included in this work, have been omitted. Finally, the current state of work on the Public Transport Act, which might significantly facilitate meeting the described challenge by local governments, has been presented.

## **THE CURRENT SYSTEM OF ORGANISING AND FINANCING LOCAL BUS TRANSPORT IN POLAND**

The Polish local bus transport market is in principle a deregulated market, based on the ‘on the road’ competition. Transport services may be offered by any operator meeting technical requirements resulting from detailed regulations related to bus transport and from formal and legal requirements related to the access to this profession. Some possibilities of regulation are only the effect of the need for an operator to have a licence issued by local authorities (gminas – communities, powiats – counties / districts or voivodships – regions) to run passenger transportation according to a specific timetable.

The licence can be refused only in specific situations, according to the existing Road Transport Act. The most controversial of which is defined by a clause that the refusal may be the result of “a threat to the already existing lines”. Accepting that a traffic line is defined as “a transport link on a specified way between stops (...) where regular passenger transport takes place”, it is difficult to practically imagine a situation which might pose such a threat (Rudnicki, 2007). Besides, this provision arouses fears of a corruption nature (Jastrzębski, Gleń, 2004).

Practice shows that existing regulations, although liberal, in numerous cases remain fictional, which is testified by: (Dyr, Osuch, 2005, Maksymiuk, 2006)

- obtaining licences for servicing a line and not undertaking any transportation, which results in “blocking” possibilities of other carriers obtaining a licence;
- providing services on regular lines without the required permit – as an occasional transport, for which the permit is not required;
- lack of or not obeying agreed on and accepted time-tables;
- rendering transport services without needed licences.

The carrier has the right to determine prices for transport services on his own. Therefore – as it has been already mentioned – the carriers are competing with each other ‘on the road’, determining their routes, time-tables as well as fares by themselves.

The Road Transport Act includes a possibility to conclude an agreement concerning paying the operator “a refund for the cost of a reduced fare”. Such an agreement is concluded between the local authority granting discounts and rights to travel free of charge (usually a voivodship local government settling statutory relieves) and a carrier offering services. However, this regulation means that the entity granting the reduction cannot choose another operator to whom a refund for the cost of a reduced tariff is paid than the one who has an appropriate agreement. There is no place for any other procedure for public procurement than

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

a contract under the free order procedure (without a tender) and the local government is forced to accept potentially arduous financial conditions, e.g. by a full (not a partial, considering price elasticity) refund of the granted reduction and no influence on full fares level (Jastrzębski, Gleń, 2004).

Implementation of this refund is erroneously interpreted as an instrument regulating the market of local bus transport. In fact, firstly, local authorities have no possibilities to refuse repaying the refund if the operator met all the statutory requirements, among others independently from actual realisation of the transport offer (punctuality, number of departures cancelled etc.). Secondly, a refund of reductions is not the same as a subsidy to unprofitable line or rides. Getting a refund does not result in, which some local governments believe, each launched ride being profitable, therefore financing local bus transport in this way and form is not enough.

Lack of a dominant entity in this sphere of organisation – a number of local authorities instead of one public transport authority in voivodship or at least powiat – allows local operators to easily meet all requirements to run a line, which include making the market situation analysis required by the law, designing time-table and tariff information and making it available to passengers and concluding an appropriate agreement regarding the use of bus-stops.

Capital requirements are not a barrier to market access, either. The planned transport offer may require just one bus to execute it. The costs related to having a fleet reserve may be limited through outsourcing replacement transport (in case the basic vehicle is unavailable) or they may be totally disregarded, for although not executed rides do have negative effects directly for the operator in the form of reduced income and a worse image of the transport company, they do not bring about any other economic restrictions, e.g. contractual or administrative fines. The cost that also has to be incurred is purchasing fiscal equipment allowing the operator to apply to the market regulator for repayment of concessions in relation to the get the refund of reduced-fare and free tickets.

The biggest competition barrier on the local market of bus transport is the access to bus stations (and to a lesser extent to bus stops) in towns where particular lines have their termini or intermediate stops at hubs. Those terminals allow interchanges not only within the framework of local bus but also within local and national railway routes, as well as urban public transport. The bus stations are usually owned by former PKS companies, rarely by urban local authorities. A fight for passengers against other carriers caused that PKS companies did not, and do not, want to enable other operators to use bus stations. Having access to bus stations is a serious competitive advantage and at the same time a barrier for development of competitive and integration processes on the market of local bus transport. Towns, not being responsible for local public transport functioning, do not appreciate the importance of convenient location and equal access of local bus operators to bus stations.

Operators acting in conditions of deregulation of local road transport market, in their activities primarily take into consideration the need to satisfy passengers' expectations and the wish to maximise profits. Economic effectiveness of each line, and even of each ride, is calculated separately. While valuing the level of fares, only market criteria are taken into account. The

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

operator calculates the price for his service on his own, based on the one hand on costs and on the other on profitability of a given line. Profitability of a line is determined by ticket prices, intensity of competition, passengers' financial possibilities and passenger structure which conditions the level of financial compensation from public authority in relation to using statutory reductions. Political, social or macroeconomic criteria have a limited influence on individual carriers' shaping the level of tariffs.

The issues of quality management look similar, which often causes running exploited, high-floor buses, without providing the necessary passenger information.

The principles of functioning of deregulated local road transport allow achieving sufficient standards of service, primarily on high-demand lines. Whereas in relations to areas with small density of population and in unattractive for commercial operators parts of the day or week (e.g. late evening or holidays), the inhabitants may be deprived of the possibility to use public transport. As already mentioned, this phenomenon is intensified together with the currently observed increase of drivers' wages and growing availability of cars which results in decreasing passenger flows.

An essential problem of functioning of this market form is a limited possibility of creating a transport offer which is attractive for passengers. A relatively large number of small competing operators cause disintegration and significant diversity of the assortment of offered services. The basic negative effects of a deregulated local transport market regarding individual fragmentary local markets us a leak of:

- integrated one-trip and seasonal tickets honoured by individual operators on specified routes or groups of routes;
- network tickets within different local buses or integrated with urban and railway transport;
- an integrated information system concerning local public transport functioning (timetables, tariffs);
- coordination of timetables at terminals, allowing easy interchanges.

The deregulated form of local road transport market does not exclude operators' cooperation on different levels covering, for example, joint line servicing, a common tariff, a common information system and a joint sale of tickets in order to achieve defined effects, similar to an integrated transport system. Such cooperation is sometimes forced by high intensity of competition on certain transport routes, while on the other hand it radically reduces effectiveness of economic activity pursued by operators. It integrates existing offer and raises its attractiveness from the passengers' point of view, as well as increases stability of operators' activities on the market, by creating certain barriers to market access and limiting the scope and intensity of competition. It should be mentioned that integrating tariffs by operators may be treated as price collusion by Office of Competition and Consumer Protection.

Cooperation between operators would be facilitated if there were institutionalised forms of local bus transport management. Under present market as well as formal and legal circumstances there are no solutions enabling creating an integrated offer. However, one

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

should pay attention to an important positive role of competition processes existing on this market, particularly in the price-cost aspect, and to the fact that separate regional markets undergo gradual evolution, thus ensuring additional benefits to passengers in local bus transportation.

As for the supply side of the market, in the 90ies of last century processes of division and ownership transformation of the state-owned PKS were started. These processes aimed at increasing economic and financial effectiveness of local bus transport, improving operators' financial position, increasing the quality of provided services, and thus competitiveness of this kind of transport.

Privatisation of PKS branches, dominant on the local bus transport market and as a rule covering 1 or 2 poviats, was implemented through selling the companies, contributing capital of smaller firms to the already existing companies, liquidation or employee leasing. The most important private investors are an international corporation Veolia Transport Polska (formerly Connex Polska), which owns 13 PKS companies, and two urban transport operators. Orbis Transport (Accor), which presently owns two PKS companies, is the second significant strategic investor. Also capital groups participating in privatisation of 2 or 3 companies are formed. However, it should be stressed that many PKS companies still operate as state-owned enterprises or the State Treasury companies.

The results of the research show that the managers of non-privatised PKS companies unwillingly undertake activities aiming at privatisation. Majority of management in these companies declare for privatisation with the participation of employees and local self-government (Dyr, Osuch, 2005). This is the official standpoint of the Car Transport Employers' Union of Poland, which recognizes employee leasing as proven and best solution to privatisation of companies and therefore prepared a suitable project within the framework of the Act on Commercialisation and Privatisation (Osuch, 2007).

Companies based on former branches of PKS continue to remain main operators realising passenger carriage in local bus transport. Their position results from the transport potential they own (more than 17,000 buses).

Small private operators in local bus transport function within the framework of their own transport offer, which is subject to coordination with local operators dominant on the given fragmentary market. According to the estimates of the Polish Chamber of Commerce of Road Transport and Forwarding in 2005 in Poland some 1.5- 2 thousand private entities functioned within services offered by local bus transport (Szczerbaciuk, 2005). Some of them exploit 1 or 2 buses; nevertheless others are quality leaders on local markets, providing services of a higher standard than PKS. However, this may be the result of their servicing solely the most profitable lines.

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

## **AUTHORS' PROPOSAL OF CHANGES**

As already mentioned at the beginning, on the basis of the diagnosis of the current state and analyses of both foreign and national experiences in the field of competitive tendering, an organisational model for Polish local bus transport, based on the policy of open market with regulated competition, was prepared.

Due to the need to guarantee a suitable standard of services, their basic scope – covered by public service obligation – should be provided by operators contracted to carry out transport tasks specified by public authorities through Regional Transport Authorities (RTAs), organising within the scope of one entity as many kinds of transport in the region as possible and being responsible for their integration, promotion and unified information.

The RTAs should adopt one of the following organisational and legal forms:

- a voivodship local government department or a budget unit;
- a voivodship, powiat and gmina local government company or only a voivodship and powiat local government company;
- a voivodship, powiat and gmina local government municipal union or only a union of voivodship and powiat local government, on condition that there will be legal possibilities of establishing such unions.

Operators would be contracted under public procurement procedure (a tender). A possibility to employ an operator under a direct award, in accordance with The European Parliament and the Council of Europe Regulation (EC) No. 1370/2007 of 23<sup>rd</sup> October 2007, would be limited in compliance with the regulations included there.

Within the framework of a tender the subject of evaluation are fares not exceeding maximum ticket prices set by the RTA that specify the required parameters concerning quantity and quality of delivered services (bus type, age, equipment etc.). In case no subsequent bidder submits an offer within the range of maximum prices, the authority invites further bids in which the expected budget subsidy to the provided services, with maximum prices set by the RTA, is valued. It means that entering the bid for the first time, the operator calculates the price level which is necessary from his point of view. In case the bid remains unsettled, the operator enters a further bid stating the expected budget subsidy, with maximum prices set by the authority, and taking into account price elasticity.

The RTA would only decide about routes and the number of connections on each route considering different times of day, week and year and standard of the fleet, for the suggested model of net contracts should be tied to the possibility of operators' independent operational shaping of the carriage offer. In Poland this would be a new solution, different from those used in urban transport systems and as a rule based on gross contracts. The most important reason for this diversity is the fact that in local transport planning competences are currently owned by operators and the local government must develop them yet.

Also independent carriers who would on their own shape their offer and are granted licences to put this offer into practice should have a possibility to render services. The scope of

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

activities of such operators, gaining income only directly from passengers, would depend on quantitative and qualitative level of the RTA's and the operators' he employs joint offer. Considering specificity, determined by the area and distance of a journey, of providing transport services in a region one may assume that for independent operators there would always be a specific market niche ensuring profitability of operation.

In the situation of well-planned and integrated (by tariffs and time-tables) local transport assisted by public means, operators' functioning outside the basic lines sub-system is connected with risk, for without getting refunds on applied discounts, rights to free passage or budget payments, they will not be competitive. However, we should allow for the possibility of their performing services as a complement to the basic offer. In regions where there is no suitable transport policy, there is a risk of autonomously functioning operators taking over a significant market share. Yet this will have a favourable effect on the size of the transport offer, though in effect may lead to an increase of the deregulation level. Nevertheless, this is a better solution than the RTA, who may not be enough passenger-oriented, artificially closing market niches.

Foreign as well as Polish experiences in urban transport point to the purposefulness of a regulation leading in to giving up the 'on the road' competition and substituting it by high quality demands. In such a case regulations should impose on operators' demands concerning environment requirements, adjusting the fleet to the needs of disabled persons, outlining the tariffs and also securing appropriate supply of services in specified times of the day, peak and off-peak. The condition of efficiency of the discussed solutions is, on the one hand, introducing and enforcing stipulated penalties and on the other hand including in the contracts a limited operators' influence on the size of demand due to introducing some regulations (e.g. integrated fares).

Operators who gained access to the market should be controlled as regards their activities on the market, in accordance with the contract or licence. Effective control is an indispensable condition of proper functioning of individual markets. One of essential causes of improper functioning of local bus transport market is lack of suitable control over operators' activities according to licences. Some operators altogether do not execute carriages on this market or execute them regardless of time-tables. Financial and administrative penalties should be imposed for not respecting provisions of contracts and licences.

In the suggested solution of the issue of access to the local bus transport market there will be a possibility of providing services by operators of different sizes, including small ones using fewer than 10 busses. This will allow the companies run subsidised high quality lines, instead competing with them for price sensitive customers. In relation to spatially separated defined market segments, it will be possible to organise tenders with the view of choosing one operator in order to ensure his direct interaction with the client, which will allow providing a high quality service.

Securing access to infrastructure is a condition of proper transport service on separate fragmentary markets. Primarily access to stops, termini and hubs in local bus transport needs to be solved. An appropriate solution would be for the RTA to have bus stations and bus stops

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

at his disposal. Bus stations should be owned by gminas on the area of which they are located. Gminas would pass on stations and stops on their area to the disposal of RTA. The access to the station, if it remains the property of one of the operators, should be provided for all other companies on non-discriminative principles.

At the same time one should aim towards privatisation of bus transport companies acting as State Treasury companies and state-owned companies, after their prior commercialisation through:

- capital privatisation;
- setting up employee companies (employees buyout, usually combined with management buyout);
- buying out companies by external entities;
- bringing companies as a contribution in kind to another entity functioning as a company.

An RTA should have a possibility of introducing an integrated ticket, in force on a narrow scale in a regulated local bus transport and on a wide scale in the whole local (urban transport included) and regional transport including railways. Of course, with this in force it is possible to keep the autonomy of urban local governments and their Public Transport Authorities in direct transport management. RTA's possibilities within this range will be determined by the scope of his operations. An RTA having the three kinds of transport – local bus, urban and railways – at his disposal will have the biggest possibilities. In a situation of a PTA introducing an integrated ticket, this entity will be the issuer of the ticket and will divide the means from its sale between him and the operators, according to the mechanism of financing transport activities. In this way an additional source of finance will be available also for some carriers running self-financing lines. The use of an integrated tariff does not have to exclude the operators from using their own tariffs.

Subject to the sole use of an integrated tariff, it is worth considering basing tender criteria, in case of a line not requiring a budget subsidy, on the quality of offered services as competition on the level of fares is no longer possible.

Motivating bonuses paid due to ensuring better quality services than the ordered ones or due to getting high grades in consumer satisfaction research carried out among clients using services of certain operators might be an addition to the presented system. As another source of financing operators in local bus transport one may also suggest concluding quality partnerships aiming at revitalising a line. Nevertheless, these solutions require introducing appropriate changes in the public procurement law.

The authors of the analysis draw attention to the fact that in order to introduce the postulated solutions, it is necessary to make changes in many existing Acts (including the Road Transport Act) as well as create a special Public Transport Act, the assumptions of which, at the moment of preparing this paper, were very vague.



Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

## **CONFORMITY OF THE PRESENTED POSTULATES WITH THE PUBLIC TRANSPORT ACT**

Currently the Public Transport Act has been in fact elaborated and has twice undergone inter-departmental agreements. However, it is very general in character, among others implementing the EC regulation no 1371/2007 and referring to all branches of public transport, with the exception of tourist and international transport.

The Act defines the notion and obligations of a local transport authority and assigns bus transport to the competences of gminas, poviats or voivodships – therefore statutory organisers' competence remains highly dispersed. Unfortunately, the Act does not provide for special preferences to create Regional Transport Authorities, although it does not exclude the possibility of their arising. However, still the cooperation between different levels of local governments may be difficult or even impossible (e.g. a legal possibility of establishing municipal relations between them has not been created yet) and in practice such relations are possible to be established only in conurbation areas, between urban local governments.

The Act keeps different possibilities of operators' procuring services to transport organisers – including a tender, an award of exclusive rights or a direct award in the light of EC regulation no 1371/2007. These agreements may include both single routes and whole networks. It also regulates some issues of access to bus stops and infrastructure, but the solution that access prices are stated directly in such an act is rather rare.

The Act also allows for a possibility of operators' providing self-financing transport not included under public service obligation. Nevertheless, the right to provide such transport is limited, among others by broadly understood not competing with operators performing transportation covered by public service obligation.

There are no regulations allowing forcing such an operator to join the integrated tariff or additional rules of making such an operator accept statutory discounts (or excluding him from the existing system of reduced fares).

Neither does the Act unify the widespread use of reductions whose scope is different in the case of urban transport, local buses and railway carriage, which considerably obstructs integration.

Therefore one can state that although implementing many of the solutions suggested in the chapter above is possible according to the Act, it neither promotes nor forces local governments to undertake integrating activities or increase effectiveness of the organised transport through tendering.

## **CONCLUSIONS**

The existing system of local transport organisation in Poland is inefficient and ineffective – within a few years it may lead to depriving some areas of any transport service. Voivodship

Connecting competition and integration.

A concept of new organizational framework for Polish local bus transport

local governments finance a wide range of statutory reductions, however without having a significant influence either on the quality of offered services or on their shape (fares, timetables etc.). Neither there exists any supervision over the implementation of the transport offer stated by the carriers.

The postulated system is to use the strength of almost 2000 operators active in Poland, allowing them both to apply for orders to render services under public service obligation in the system of net contracts tendered by an RTA and to perform self-financing transport services in the market niches they have found.

RTAs, integrating different modes of transport and issuing integrated tickets as a supplement to tariffs used by individual operators (all or only those providing public services), or best of all being exclusive in character, should supervise and contract the entire transport system.

Currently prepared statutory solutions bring us closer to this model but although they lead to covering a part of transport by public service obligation, we will still have to wait for general and mass integration. Own initiative of some local governments, which will still have to face up to many difficulties, is the hope in this instance.

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