



MTM franchise renewal negotiations: new conditions required to protect the public interest

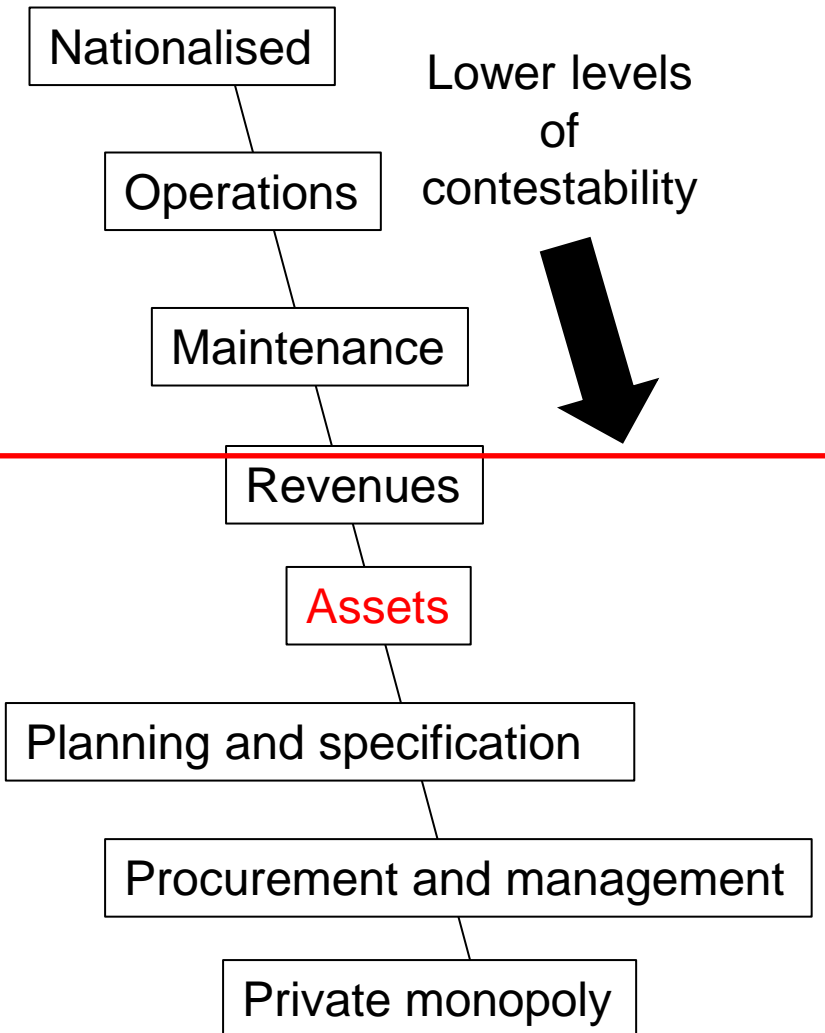
Dr John Stone

26 September 2016

“(It is time) for everyone to start paying more attention to the terms and conditions of privatisations” John Daley, CEO Grattan Institute, Guardian 27 July 2016



Melbourne's rail 'privatisation' – theoretically a competitive market



- By keeping the assets in public ownership (and leasing them to operators) the market in Melbourne is *in theory* contestable.
- Melbourne's rail 'privatisation' is "an outsourced operations and maintenance franchise"

Metro Trains Melbourne (MTM) has three contracts with Public Transport Victoria (PTV)

- Joint venture:
 - Mass Transit Railway Corporation
 - John Holland Limited
 - UGL Rail
- Three contracts with the PTV
 - Eight-year contracts from 2009 with a 7-year negotiated rollover option

Franchise Agreement	Infrastructure Lease	Projects Agreement
Lump Sum Fixed Price	Lump Sum Fixed Price	Cost Plus
\$500m	\$270m	\$400m
Operate railway and maintain rolling stock	Maintenance & renewals on railway infrastructure	Enhancements of the railway as determined by PTV & State
Margin approx \$10-15m NPAT	Margin approx \$10m NPAT	Margin approx \$15-20m NPAT

*NPAT = net profit after tax

Source: Email from MTM to author , 9 August 2016

The rollover negotiations are underway

- MTM must annually meet five performance benchmarks:
 - Reliability and customer service (publicly reported)
 - Three others agreed annually between PTV and MTM (but not reported)
- In December 2015, we believe that MTM was told that it had met the performance benchmarks necessary for rollover.
- The formal rollover negotiations must begin by 30 September 2016

Operating performance meets contracts, but ...

- *‘.....‘in the 18 months to September 2015 MTM received \$16.7 million in incentive bonuses....achieved in part by..... running hundreds of incomplete services.....’*

<http://www.theage.com.au/victoria/metro-pulls-up-short-to-meet-performance-targets-20150324-1m6mel.html>

- *‘.....Metro ran just 85 per cent of trains on time in the morning peak and 89 per cent of afternoon peak services were punctual..... By contrast, it ran 95 per cent of trains on time on Saturdays and Sundays when patronage is lower and services are less frequent..... helping the company to avoid paying out customer compensation to monthly and yearly myki pass holders.’*

<http://www.theage.com.au/victoria/punctual-offpeak-trains-help-metro-meet-its-performance-targets-20150324-1m6p0w.htm>

Our understanding of the next steps

- PTV provides MTM with an Invitation to Negotiate (ITN) by 30 September 2016
- This:
 - Sets out the timetable, process and evaluation criteria for the second phase contracts.
 - Offers scope for contract modifications in a new draft franchise agreement.
 - Negotiations are open book: full financial transparency of cost allocation; risk and profit margin must be clear and linked

MTM claims efficiency success?

Subsidy per revenue train kilometre



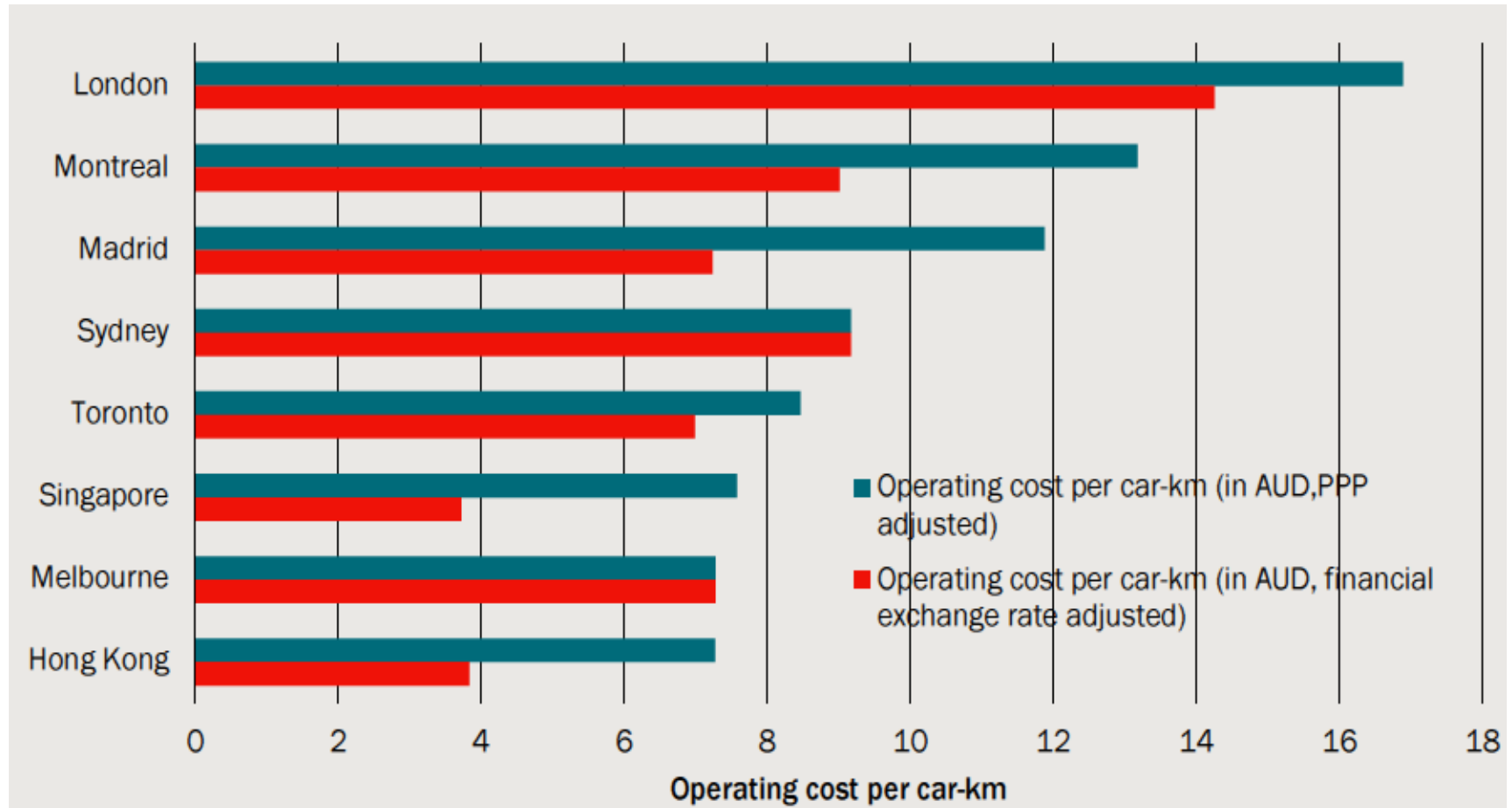
Melbourne	Sydney	Brisbane
\$1.88	\$5.00+	\$9.00+

MTM offers the government value for money with a comparatively low subsidy of \$1.88 per revenue kilometre

Source: Metro Key Statistics,
20 January 2016.

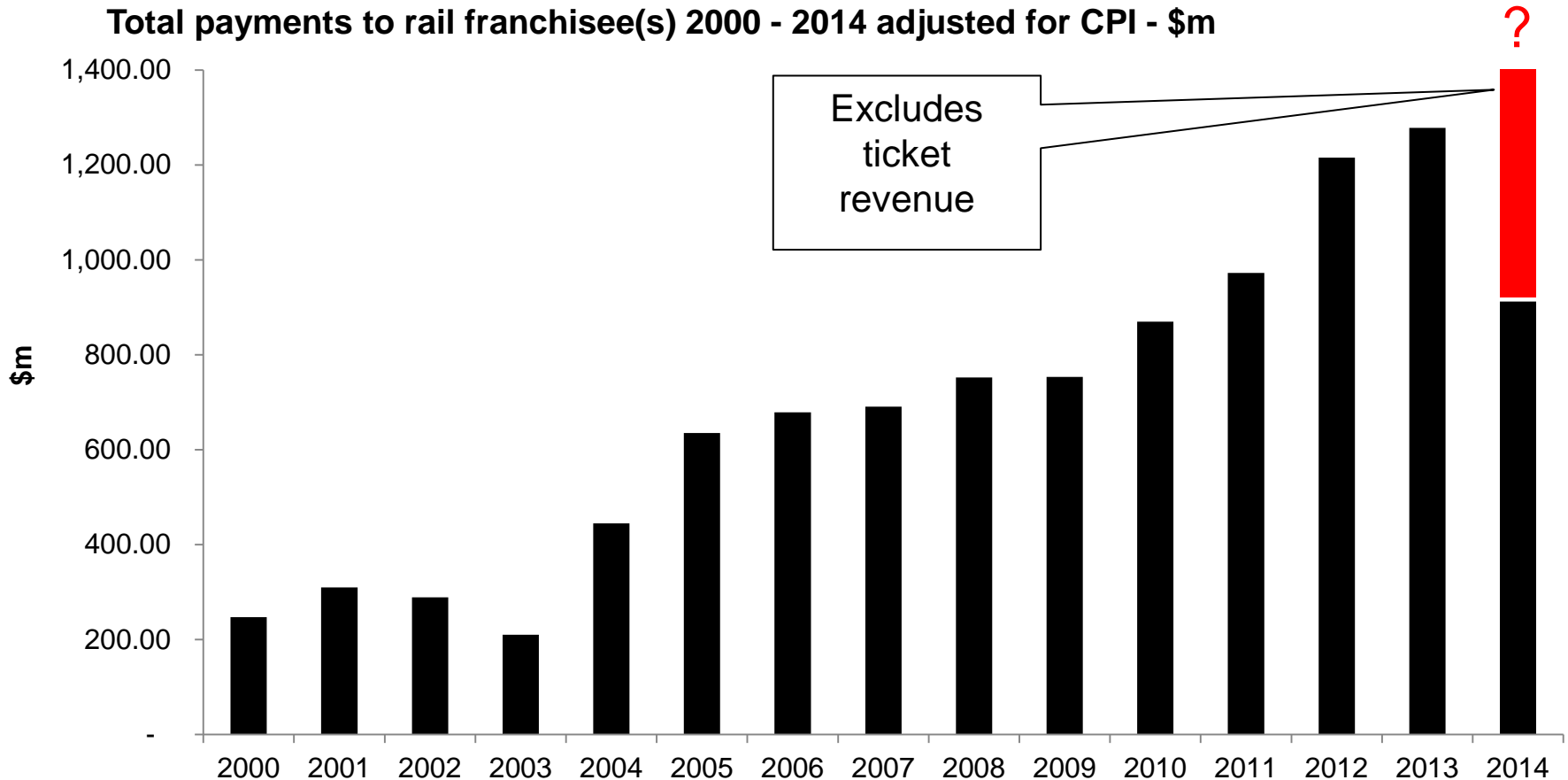
Subsidy almost three times greater in Sydney?
Just because of franchising?

Independent review suggests differences are nothing like those claimed by MTM



Operating cost comparisons per carriage-km 2015 (Source: IPART, 2015. Efficiency of NSW public transport services)

Franchisee payments have been consistently rising above inflation



CPI adjusted payments to train franchise operators 2000-2014 (Source Public Transport Victoria, 2016); **2014 figure excludes farebox revenue**

What is 2014-2015 revenue? Where is it reported?

TABLE 5: METROPOLITAN TRAIN PAYMENTS (\$'000s)

Payment type	Oct – Dec 2013	Jan – Mar 2014	Apr – Jun 2014	Jul – Sep 2014	Oct – Dec 2014
Base contract	47,126	47,326	46,204	44,284	45,770
Incentive and penalty	3,117	2,503	2,777	2,701	3,420
Customer experience performance regime	0	0	0	0	200
Ticketing revenue guarantee payment	86,767	0	0	0	0
Revenue reset adjustment payment		23,369	23,629	23,007	23,007
Maintenance and projects ¹	65,921	55,100	64,217	57,651	54,071
Rolling stock ²	25,880	21,782	21,423	25,315	27,422
Operations and systems ³	20,918	9,756	18,608	18,440	14,823
Total	249,730	159,837	176,857	171,398	168,711

1. Maintenance and projects combines maintenance and capital projects payments.
2. Rolling stock payments include rolling stock adjustments and exams.
3. Operations and systems include payments for business system upgrades, driver establishment, electricity and employee entitlements.

https://static.ptv.vic.gov.au/siteassets/PTV/PTV%20docs/Track%20Record/PTV_Track-Record-61_Oct-to-Dec-2014_FINAL.pdf



TABLE 8: METROPOLITAN TRAIN PAYMENTS (\$'000s)

Payment type	Jul – Sep 2014	Oct – Dec 2014	Jan – Mar 2015	Apr – Jun 2015	Jul – Sep 2015
Base contract	44,284	45,770	57,500	63,799	50,989
Incentive or penalty	3,147	3,268	1,969	2,462	3,162
Customer Experience Performance Regime	0	200	0	0	0
Revenue Reset Adjustment Payment	23,007	23,007	24,685	24,593	19,492
Maintenance and projects ¹	57,651	54,071	58,637	80,059	102,425
Rolling stock ²	25,315	27,422	25,589	23,899	27,852
Operations and systems ³	18,440	14,823	8,614	15,543	18,775
TOTAL	171,844	168,561	177,401	210,355	222,695

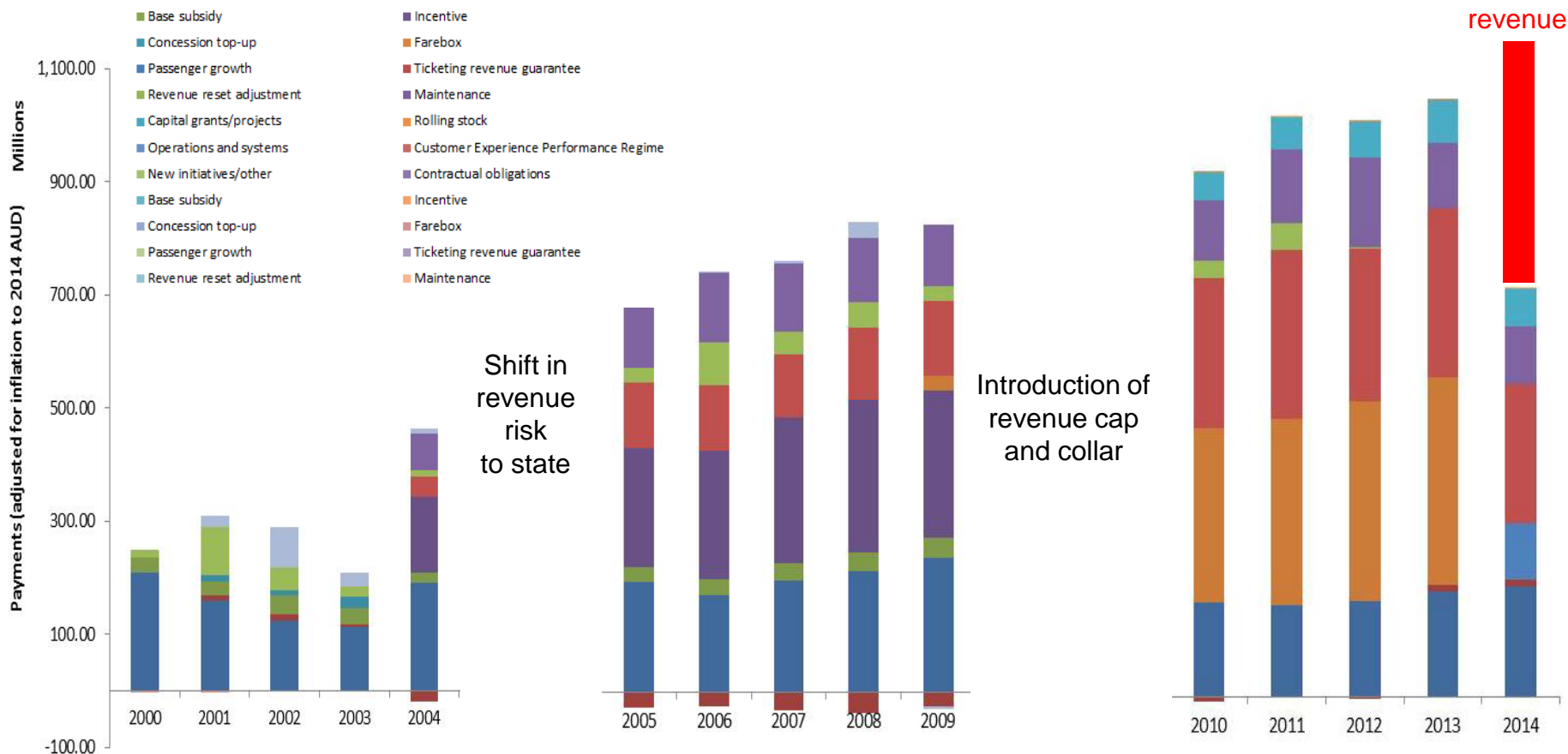
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https://static.ptv.vic.gov.au/siteassets/PTV/PTV%20docs/Track%20Record/PTV_Track-Record__64_July-to-September-2015_FINAL.pdf

- Until Dec 2013 – ticket revenue ‘guaranteed’ while Myki was settled in.
- Actual payments from Myki to MTM now not public reported.
- PTV Annual Report shows total Myki payments, but there is no breakdown of payments to individual operators.

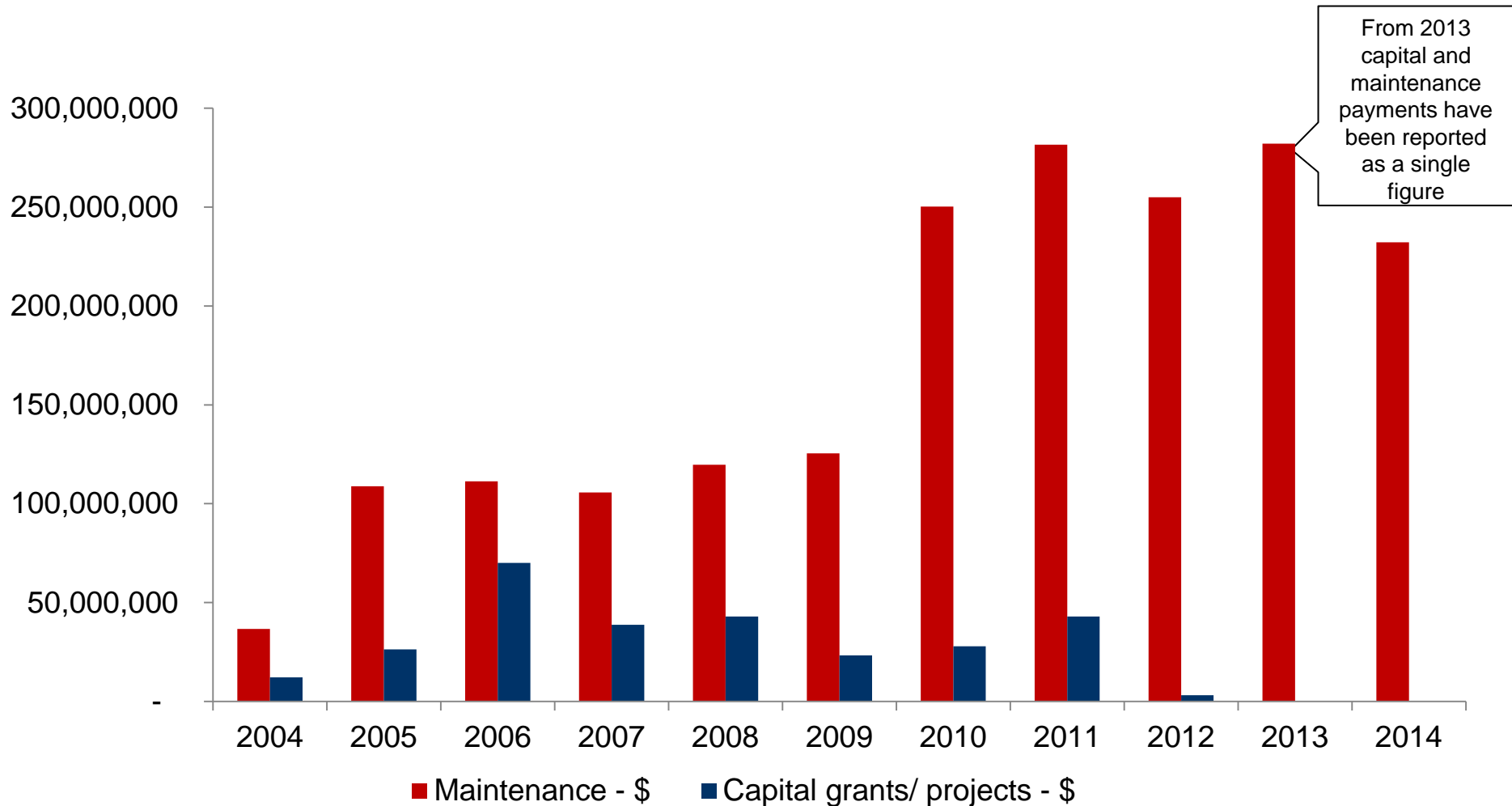
How can anyone draw any conclusions when the categories keep changing?

Payments to train franchise operators 2000 - 2014



CPI adjusted payments to train franchise operators 2000-2014 (Source Public Transport Victoria, 2016); **2014 figure excludes farebox revenue**

Capital and maintenance spending now reported as one figure



The three MTM contracts: are 'projects' cross subsidising the others?

Franchise Agreement	Infrastructure Lease	Projects Agreement
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*NPAT = net profit after tax

Source: Email from the franchisee to author , August 9th 2016

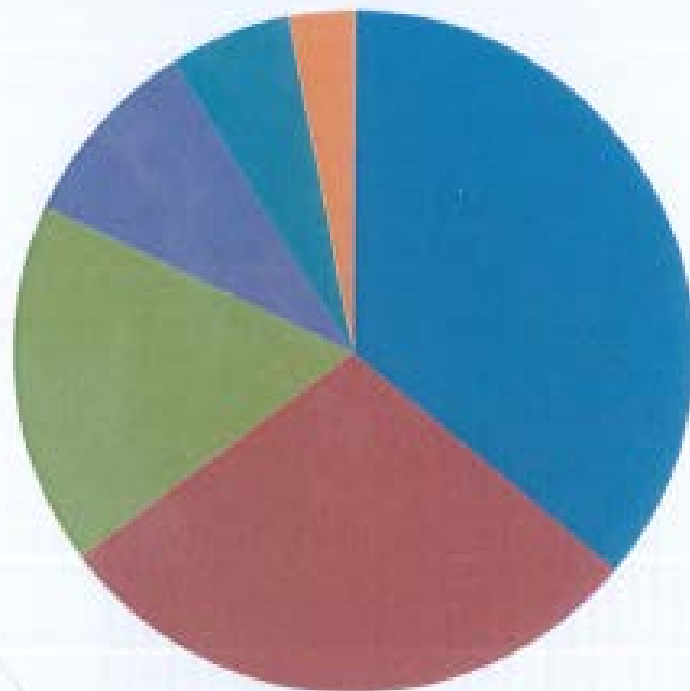
- Which renewals are done under the infrastructure lease and which under the projects agreement?
- Who drives decisions about 'enhancements'?
- Cross subsidisation?
- Were these tendered as separate contracts or as a bundle?
- Contracts let as fixed or variable margins?

Projects and business development as a source of profit?

MTM Profit Breakdown



MTM Projected Profits After Tax 15/16



- Projects
- Business Development
- OPR
- Maintenance Efficiencies
- Metro Academy
- Other

What is business development and why is it listed as a source of profit?

Total \$39.6M (representing 3.1% of revenue)

\$9bn in projects over 11 years



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Metro Trains Melbourne, VIC

PROJECT NAME:
Metro Trains Melbourne

LOCATION:
Melbourne, VIC

CLIENT:
Department of Transport (Victoria)

PARTNER(S):
MTR Corporation, UGL Rail

VALUE:
\$9 billion (over 11 years)

START:
December 2009

END:
December 2017

ENGINEERING DISCIPLINES

RAIL CONSTRUCTION, O&M

The Metro Trains Melbourne (MTM) rail network spans 15 lines and 218 stations covering 869km of track, with an average weekday patronage of approximately 800,000 trips.

MTM is an outstanding team of rail and construction businesses including John Holland, Hong Kong's MTR Corporation and UGL Rail, and is responsible for operating, maintaining and developing all assets associated with the network including train operations, rolling stock, train control, infrastructure, depots, stations, structures and facilities.

Our project scope includes operations and maintenance of the network including signalling, rail construction, relationship management, management of railway assets, management of above rail operations including train control, management of property assets, systems, documentation and standards, transition management and interface management with key stakeholders including Public Transport Victoria and the Department of Transport, Planning and Local Infrastructure. Metro's YTD punctuality performance at December 2014

Who is driving the capital works and major maintenance?

- Does the government have a strategic vision for asset renewal and maintenance?
 - What are the indicators of progress?
 - Does PTV have strong tendering and procurement skills?
- How much are MTM steering maintenance and renewal programs?
- Is MTM taking control of capital assets?

Unsolicited proposals for major capital works

Victorians hit for \$1 million a day for rail upgrade

Adam Carey, Royce Millar



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Victorians will have to pay up to \$5.2 billion, or almost \$1 million a day, for the Naphthine government's Pakenham/Cranbourne rail upgrade, the first long-term major privatisation of a key part of Melbourne's rail network.

Leaked cabinet documents reveal the government has fast-tracked the multibillion-dollar project – Australia's biggest-ever rail public-private partnership – to ensure contracts are signed ahead of the November state election.

Critics, including academics and Labor, have slammed the private-sector proposed upgrade – dubbed "Project Flinders" in the documents – as a corporate hijacking of transport planning in Victoria.

In a surprise announcement in March, the government spruiked the project as costing \$2 billion to \$2.5 billion. The developer, a consortium led by Hong Kong-based rail operator Metro Trains Melbourne (MTM), says the scheme will deliver a 30 per cent boost to capacity along the congested Dandenong corridor, enabling 2 million extra passenger journeys a year.

But the cabinet-in-confidence documents reveal taxpayers will be left to pay up to \$360 million a year as "annual service payments" to the consortium until 2034 in "nominal" dollars – the actual amount spent, including inflation. The total payments in nominal terms will be as much as \$5.2 billion.



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John Holland has won a contract for

preparatory works for the AU\$10.9bn (£5.6bn) new metro in Melbourne, Australia.



The early works contract includes excavation of major shafts in the centre of the city as part of preparations for the tunnel and five new underground stations.

It will involve excavation of huge open shafts adjacent to Swanston Street to enable the underground construction of the two new city

stations.

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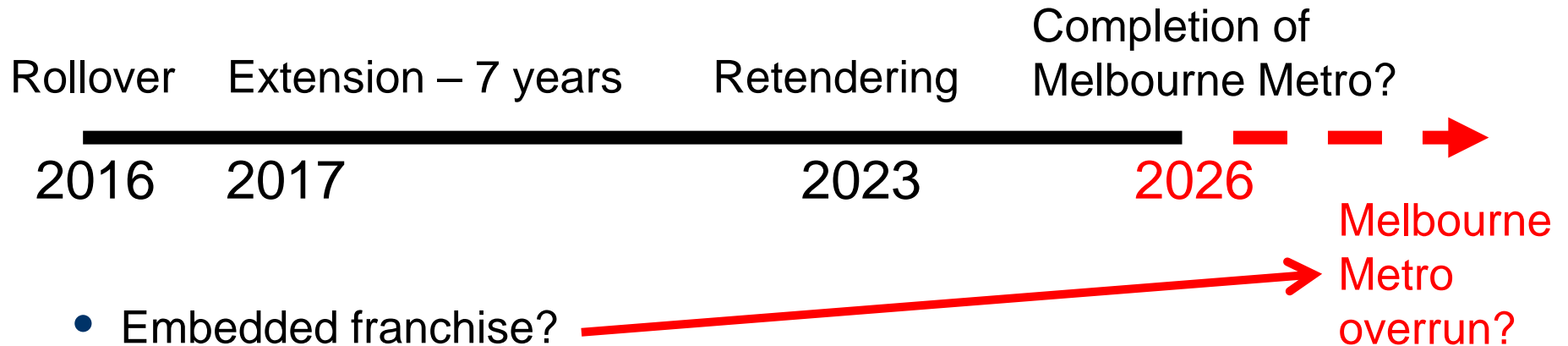
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Fall Arrest Systems

Aggregates

Future contestable market?



- Embedded franchise?
- Cross subsidisation from the 'projects' contract?
- Crucial skills leaking to the private sector or being downsized in the state?
- Who is likely to bid against MTM in 2023?
 - Will a private monopoly develop?
 - Where are the skills for public operation?

Five ways to protect the public interest


1. Strong and public negotiation of the rollover.
2. Separate and credible profit and loss accounts for each of the three agreements.
3. Complete and consistent reporting of expenditure.
4. Show that maintenance and renewal is linked to long-term strategic outcomes.
5. Strengthen public-sector skills.

ACCC's Rod Sims says privatisations 'severely damaging' economy

Australian Competition and Consumer Commission chairman says governments need 'uppercut' for putting profits first


Gareth Hutchens

 @grhutchens

 email

Wednesday 27 July 2016 16.05 AEST



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 Rod Sims says governments have repeatedly botched the sale of airports, electricity infrastructure and major ports. Photograph: Alan Porritt/AAP

The head of the competition regulator and a former advocate of privatisation has called for the privatisation of public monopolies to stop because the government is mishandling them.

“(It is time) for everyone to start paying more attention to the terms and conditions of privatisations” John Daley, CEO Grattan Institute, Guardian 27 July 2016

