

Date: 07 October 2019

Subject: Bus Reform : Audit & Consultation

Report of: Eamonn Boylan, Chief Executive Officer, GMCA & TfGM

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## PURPOSE OF REPORT

This report sets out and explains the recommendation to the GMCA to approve proceeding to the next stage in the consideration of a proposed franchising scheme, following on from the work undertaken in connection with bus reform. The proposed recommendations and associated next steps in accordance with the Transport Act 2000 (as amended by Bus Services Act 2017) ("the Act") are also set out in this report.

## RECOMMENDATIONS:

Members are requested to:

- i. Note the contents of this report;
- ii. Note the contents of the report from the independent auditor dated 26<sup>th</sup> September which was prepared in accordance with section 123D of the Act;
- iii. Note that the independent auditor's report is an opinion on the assessment of a proposed franchising scheme previously reviewed by Members in June 2019;
- iv. Approve the publication of the independent auditor's report and the assessment supplied to the independent auditor;
- v. Note that minor typographical amendments will be attached to the assessment;
- vi. Approve the amended Proposed Franchising Scheme as set out in Appendix 1.2;
- vii. Approve the preferred funding scenario for the proposed franchising scheme;
- viii. Note mitigating responses to a downside risk scenario as set out in Section 6;

- ix. Agree to proceed with the proposed franchising scheme by undertaking a consultation in accordance with section 123E of the Act, which would commence on 14 October 2019 and end on 8 January 2020, and to agree the funding for the consultation as set out in paragraph 6.16 of this report;
- x. Approve the publication of a notice of the proposed scheme in accordance with section 123E(2)(d) of the Act;
- xi. Instruct TfGM to carry out all tasks necessary to carry out that consultation on its behalf; and
- xii. Note that a further report will be made to the GMCA on the outcome of the consultation.

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#### **Appendices**

1. Draft Proposed Franchising Scheme
  - i June 2019
  - ii as amended September 2019
2. Report of Independent Auditor
3. Observations of Independent Auditor
4. Response to observations of Independent Auditor
5. Draft Equality Impact Assessment on the proposed scheme
6. Notice of Proposed Franchising Scheme

#### **BACKGROUND PAPERS:**

- Report of the GMCA titled Bus Services Act 2017, dated 30 June 2017
- Report of the GMCA titled Bus Reform Objectives Update, dated 25 May 2018
- Report of the GMCA titled Bus Reform, dated 27 July 2018
- Report of the GMCA titled Transport Revenue Budget 2019/20, dated 15 February 2019
- Part A Report of the GMCA titled Bus Reform Update, dated 28 June 2019

## 1 INTRODUCTION

- 1.1 On the 30 June 2017, the GMCA decided to use the new powers set out in the Act to prepare an assessment of a proposed franchising scheme.
- 1.2 On 28 June 2019 and upon completion of the assessment, the GMCA decided to proceed to the next stage in the development of the proposed scheme by agreeing to instruct an independent auditor to prepare a report in accordance with section 123D of the Act.
- 1.3 Following the completion of this process and upon receipt of the auditor's report, this report sets out the outcome of the auditor's report and recommends proceeding with the proposed scheme by undertaking a consultation in accordance with section 123E of the Act.

## 2. BACKGROUND

- 2.1 Members will recall the work undertaken by TfGM to prepare an assessment of a proposed franchising scheme and how the GMCA's Vision for Bus, as set out in the Greater Manchester Transport Strategy 2040, has been considered and applied in the assessment.
- 2.2 The draft franchising scheme is attached at **Appendix 1**. Appendix 1.1 attaches the Scheme provided to the Auditor in June following the CA decision; Appendix 1.2 is an updated version identifying various minor amendments which will be included in the consultation documents. In brief the proposed franchising scheme would apply throughout the entirety of Greater Manchester ("GM") and identifies those local services the GMCA would provide under local service contracts, which private operators would then bid to operate on the GMCA's behalf. The proposed scheme also excludes some services from being franchised. Such excluded services could operate in GM and any services not franchised or excluded would require a service permit to run in GM. For the purposes of efficiently and effectively transitioning from the existing market to the proposed scheme, the proposal is that GM would be split into three areas and the proposed scheme makes provision for services to operate between those areas whilst franchising is rolled-out across GM.
- 2.3 The Act and *The Bus Services Act 2017: Franchising Scheme Guidance* ("the Guidance") set out several procedural steps that must be undertaken by the GMCA before a decision can be made to introduce a franchising scheme. This includes, but is not limited to, having an independent audit organisation prepare a report on the assessment and undertaking a consultation on the proposed franchising scheme.

- 2.4 Further information on these steps, including the outcome of the auditor's report and the proposed approach to undertaking the recommended consultation, is set out below.

### **3. THE ASSESSMENT**

- 3.1 On 28 June 2019 a completed version of the assessment was shared with members in a Part B Report so that a decision to proceed to audit could be taken. At that time, the GMCA also delegated authority to TfGM to carry out final minor amendments to the assessment and a small number of such typographical amendments have been made and were also passed to the auditor. This ensured that the version of the assessment that was shared with the auditor was as accurate and up to date as possible; and was without any minor errors or omissions.

### **4. THE AUDIT**

- 4.1 The Act and Guidance prescribe which matters an authority must consider when selecting a person to act as its auditor in accordance with the Act. In summary, these include:
- the auditor must be a person or body with a recognised professional accountancy qualification offered by a qualifying body;
  - the auditor needs to be a qualified accountant with no conflicts of interest that would lead to difficulties in acting as the authority's auditor;
  - the auditor should act with independence and ensure that the authority is in the best position to take a well-formed decision in the interests of passengers; and
  - the auditor must not have been engaged by the authority to assist with any aspect of the preparation of the assessment or proposed franchising scheme. This is to ensure that the preparation of the assessment and the audit are kept separate.
- 4.2 On 27 July 2018 the GMCA instructed TfGM to secure the conditional availability and preliminary briefing of a suitably qualified independent audit organisation so that after having prepared the assessment, the auditor may then be instructed to prepare the report described above. This led to a competitive procurement process being undertaken by TfGM to secure the conditional availability of an auditor who satisfied the criteria set out in paragraph 4.1 above.
- 4.3 Section 123D of the Act requires an authority to obtain a report from an independent audit organisation on its assessment. On 1 July 2019, TfGM instructed an independent auditor to prepare a report.
- 4.4 The auditor's report must state whether, in the auditor's opinion:

- the information relied on in considering whether the GMCA would be able to afford to make and operate the scheme, and in considering whether the proposed scheme would represent value for money, is of sufficient quality;
  - the analysis of that information in the assessment is of sufficient quality; and
  - the GMCA had due regard to the guidance issued under section 123B of the Act in preparing the assessment.
- 4.5 When forming its opinion on the first two matters listed above, the Guidance makes it clear that the auditor should consider the quality and timeliness of any information received from bus operators and the following criteria:
- whether the information comes from recognised sources;
  - whether the information used is comprehensive or selectively supports the arguments in favour, or against, any 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.
- 4.6 As such, the auditor is not required to report on or pass judgment on the decision taken or the outcomes of the assessment. Whilst the Act does refer to this report as an “audit”, the Guidance instead refers to it as an “assurance report” reflecting the difference between this report and what is commonly understood to be included in a traditional financial audit.
- 4.7 Initially the assessment (and all its supporting data) were provided to the auditor. Following this, various meetings and briefings took place between TfGM, the GMCA and the auditor to discuss and provide an overview of each of the cases of the assessment (as well as the appropriate supporting papers, technical notes and models). The auditor then reviewed the assessment and its supporting papers. During this review, the auditor asked several clarification questions, which TfGM and GMCA responded to as appropriate on a case by case basis. These responses primarily consisted of further explanations being given. In some instances, further information (such as technical notes, meeting papers and minutes) were provided to the auditor.
- 4.8 In order to prepare a report in compliance with the requirements of both the Act and the Guidance, the auditor’s work was structured around various areas and topics, which included the following:
- Process review: this included consideration of the process followed by TfGM in developing the assessment and consideration of how the objectives, the ‘case for change’, the proposed franchising scheme and the other options were developed.

- Assessment review: this included a review of each of the cases of the assessment (i.e. the Strategic, Economic, Commercial, Financial and Management Cases).
  - Information review: this included reviewing the information used and/or considered by TfGM in preparing the assessment, including that from bus operators, and whether those sources of information complied with the requirements of the Guidance, as summarised above at paragraph 4.5.
  - Model review: this included reviewing the models used in the assessment to determine the quality of the analysis underpinning those models.
- 4.9 The auditor's report was completed and sent to TfGM on 26th September 2019. A copy of the auditor's report is attached to this report at **Appendix 2**.
- 4.10 In considering the contents of the audit report, members will note that the auditor has provided an informative summary of the work performed, as well as their opinion that:
- the information relied on by TfGM in considering whether the GMCA would be able to afford to make and operate the scheme, and in considering whether the proposed scheme would represent value for money, was of sufficient quality;
  - the analysis of that information in the assessment was of sufficient quality; and
  - the GMCA had due regard to the guidance issued under section 123B of the Act in preparing the assessment.
- 4.11 In addition to the auditors unqualified opinion they have provided TfGM with a number of observations. These are set out in **Appendix 3** and are addressed by way an Audit Observation Response in **Appendix 4** attached.

## 5. SUMMARY OF THE FINANCIAL CASE AND AFFORDABILITY

- 5.1 The financial case for the assessment includes detail on how the GMCA could afford to make and operate the proposed scheme. The assessment sets out a range of credible funding sources which, in aggregate, exceed the modelled net costs to implement the proposed scheme over the proposed transition period.
- 5.2 Based on the information contained in the assessment, members agreed in June 2019 that the proposed scheme (including, in particular, the transition costs required for the proposed franchising scheme) was affordable on the basis of the range of credible funding sources and would represent value for money.
- 5.3 Since the assessment was completed the Government has indicated that it will support Greater Manchester to '*deliver a London style bus system in the area*' which could include revenue funding. If Government funding does become available this could offset any local contribution including council tax/precept requirement.

- 5.4 It is proposed that a preferred funding scenario, reflecting the application of a set of specific funding sources from within the range of credible sources identified in the assessment, and as set out below in paragraph 5.6 will be outlined for consultation purposes. This will allow consultees to consider the same and provide their feedback as part of their consultation response.
- 5.5 As set out in the financial case of the assessment, the forecast net costs over the transition period up to 2024/25 are approximately £134.5 million (which includes approximately £12.5 million of forecast cost escalation in current budgets over the period relating primarily to concessions and supported services).
- 5.6 The preferred funding scenario to fund the transitional costs of the proposed franchising scheme is:
- i) £78.0 million, in total, of Mayoral 'earn back' funds provided by central government as part of Greater Manchester's Devolution Agreement. It should be noted that in terms of this funding including 'earn-back' for this purpose would mean that it would not be available for other (as yet unidentified) projects. However, the funding was originally provided for projects that are now complete or substantially complete;
  - ii) £11.0 million, in total, raised by the existing precept as part of the Mayor's 2019/20 budget for bus reform purposes (equating to £2.2 million per annum applied each year from 2020/21);
  - iii) £17.8 million, in total, of contributions by Local Authorities as a proposed one-off increase in the statutory contribution in 2020/21;
  - iv) £5 million, in total, of existing and forecast business rates pooling receipts held by the GMCA; and
  - v) £22.7 million, in total, of Mayoral precept required from future years' budgets.
- 5.7 An indicative profile for these funds is shown in Table 1 below which reflects progressive requirements of a precept per Band D property up to approximately £18.20 in total, phased over a four-year period commencing in 2021/22. GMCA would need to consider whether this was additional funding or to be met from savings elsewhere in the budget. Whilst the precept is expressed per Band D property, approximately 82% of properties in Greater Manchester are below Band D and would pay less than the sums set out above.
- 5.8 A summary of the forecast profile of cash outflows and the profiled funding sources is shown in Table 1 below.

**Table 1**

<u>Uses</u>	FY 19/20 £ms	FY 20/21 £ms	FY 21/22 £ms	FY 22/23 £ms	FY 23/24 £ms	FY 24/25 £ms	TOTAL £ms
Revenue cashflow	(2.9)	(15.0)	(21.3)	(25.0)	(18.2)	(9.9)	(92.3)
Capital cashflow	(0.7)	(8.0)	(14.8)	(7.7)	(10.8)	(0.2)	(42.2)
<b>Total cashflow spend</b>	<b>(3.6)</b>	<b>(23.0)</b>	<b>(36.1)</b>	<b>(32.7)</b>	<b>(29.0)</b>	<b>(10.1)</b>	<b>(134.5)</b>
<b><u>Funding Requirement</u></b>	<b>(3.6)</b>	<b>(23.0)</b>	<b>(21.3)</b>	<b>(28.0)</b>	<b>(33.5)</b>	<b>(25.1)</b>	<b>(134.5)</b>
<b><u>Funding</u></b>							
Local Authority contribution - statutory charge	-	17.8	-	-	-	-	17.8
Business rates pooling receipts	2.5	2.5	-	-	-	-	5.0
Existing 2019/20 precept for bus reform	-	2.2	2.2	2.2	2.2	2.2	11.0
Future years' precept	-	-	2.6	2.6	6.3	11.2	22.7
Earn back	1.1	0.5	16.5	23.2	25.0	11.7	78.0
<b>Total sources</b>	<b>3.6</b>	<b>23.0</b>	<b>21.3</b>	<b>28.0</b>	<b>33.5</b>	<b>25.1</b>	<b>134.5</b>

- 5.9 Any differences between the cashflow spend profile and the funding requirement would be balanced through prudential borrowing for capital spending and the phasing of associated Minimum Revenue Provision.
- 5.10 The preferred funding scenario reflects sources that can be locally prioritised, however the Assessment also recognises that opportunities will be sought to secure additional Government funding for bus services on an ongoing basis.
- 5.11 The mix of Local Authority contributions and precept in the preferred funding scenario balances providing one off funding during transition and an ongoing level of precept after the transition period.
- 5.12 After the transition period the Assessment notes there is a mixture of forecast annual deficits and surpluses in the central scenario and the proposed precept required during transition for this purpose would provide an ongoing source of revenue funding to manage any annual deficits and provide a level of base funding for forecast future escalation in bus services budgets. As such it is proposed that the £17.8m additional contribution to transport by Local Authorities gives a proportionate and acceptable balance of contributions.
- 5.13 Members are requested to approve the preferred funding scenario for the purposes of consulting on the proposed franchising scheme.

## **6. SUMMARY OF DOWNSIDE RISKS AND MITIGATING ACTIONS**

- 6.1 The assessment sets out the risks to GMCA of the proposed franchising scheme in particular that it takes on the risk that income, particularly farebox revenue, is sufficient to pay for franchised services (Strategic Case Section 8.4; Commercial Case



Section 24; Financial Case Section 42.1 and 42.4.7). The financial forecasts include a quantified allowance for specific risks that accompany the Franchising Scheme (Section 42.4), and there are sensitivities presented in the Economic and Financial cases showing how the forecast outcomes would be different if key assumptions and trends varied – for instance ‘exogenous’ assumptions in Greater Manchester population forecasts or car ownership forecasts and franchising ‘scheme specific’ assumptions such as the assumed profit margin required by franchised operators (Sections 15.5 and 42.7).

- 6.2 Variations in some of the long-term trends tested in the Financial Case sensitivities could have significant effects on the bus network over the period to 2051 and, as noted, some of these factors are ‘exogenous’ whereby the GMCA would have limited influence or control of these trends.
- 6.3 TfGM explains the mitigations available to the GMCA in the assessment’s conclusion at sections 64.1.5 – 64.1.7, in the event that a ‘downside’ scenario materialised.
- 6.4 The mitigating responses would be both operational – through reducing the size of the network and / or increasing fares – and financial by allocating more funding to support services. Therefore a ‘downside’ scenario would necessitate prioritisation decisions to be made by GMCA and/ or the Mayor, in line with its public accountability and control of key policy decisions under the proposed franchising scheme, around the level of services, fares and funding in order to achieve a balanced budget. Whilst the financial pressures on the bus market would be likely to be similar in different market scenarios, if the Franchising Scheme were not implemented, these risks and decisions would to a large extent remain with current operators.

## **7. CONSULTATION ON PROPOSED SCHEME**

- 7.1 Should the GMCA wish to proceed with the proposed franchising scheme then it would be required to undertake a consultation in accordance with section 123E of the Act,
- 7.2 Section 123E(2) of the Act states that if undertaking a consultation, the GMCA should:
  - publish a consultation document relating to the proposed scheme;
  - publish the assessment of the proposed scheme dated June 2019;
  - publish the auditor’s report on that assessment; and
  - give notice of the proposed scheme in such manner as the GMCA considers appropriate for bringing it to the attention of the persons in the area to which it relates.
- 7.3 In addition to the above GMCA will publish the auditor’s observations and its responses.

- 7.4 The purpose of the consultation is to allow consultees to provide their views on whether the proposed franchising scheme should be made, with or without modification.
- 7.5 On 27 July 2018 the GMCA also instructed TfGM, ahead of completion of the audit, to take all appropriate steps to prepare the materials necessary to allow the GMCA to undertake the consultation process under section 123E of the Act, so that as soon as reasonably possible after obtaining the auditor's report, the GMCA may (amongst other matters) determine whether to proceed to consultation. These materials, in particular, the required consultation document and notice, have been prepared and will be published by the GMCA in undertaking the consultation.
- 7.6 The Act sets out the requirements of the consultation document. To summarise this includes, but is not limited to:
- a description of the area to which the proposed scheme relates;
  - a description of the local services that are proposed to be provided under local service contracts (i.e. franchised) and a description of the local services which are proposed to be excluded from the scheme;
  - the date on which the scheme is proposed to be made and the date or dates by which it is proposed that local service contracts (i.e. franchise contracts) may first be entered into;
  - the date by which responses to the consultation must be received; and
  - a summary of the assessment.
- 7.7 This means that a description of the proposed scheme will be included as part of the consultation document and will guide consultees through the contents of the proposed scheme. This will be accompanied by a copy of the proposed scheme itself.
- 7.8 A summary of the assessment will also be published which gives consultees an overview of each section of the assessment, including each of the five cases and the conclusion.
- 7.9 A draft equality impact assessment on the proposed scheme will also be published as part of the consultation and is attached to this report at **Appendix 5**. Subject to the responses received, the EIA will continue to be reviewed throughout the development of the proposed scheme and may therefore be updated post consultation as may be appropriate.
- 7.10 In addition to the above, section 123E(3) states what must be included when giving notice of the proposed scheme for consultation purposes. This includes having to:
- describe the proposed scheme; and

- state where copies of the proposed scheme and other consultation materials may be inspected.
- 7.11 A copy of the notice of the proposed scheme is attached to this report at **Appendix 6** and members are asked to agree to publish this notice for consultation purposes. If approved, this notice will be published on the GMCA's website and in the Manchester Evening News on the day of the consultation launch.
- 7.12 In terms of persons who must be consulted, section 123E(4) of the Act lists various categories of persons (who together are known as "statutory consultees"). These are:
- all bus operators running local services in Greater Manchester;
  - all other persons holding a PSV operator's licence or community bus permit who would be affected by the proposed scheme;
  - such persons who appear to represent employees of bus operators running local services in Greater Manchester;
  - such organisations appearing to represent bus passengers;
  - any other relevant local authority whose area would be affected by the proposed scheme;
  - a traffic commissioner;
  - The Chief Constable of Greater Manchester Police;
  - The Passengers' Council (which changed its name in 2014 to Transport Focus); and
  - The Competition and Markets Authority.
- 7.13 In addition to the above statutory consultees, the Guidance states an authority should *"consult widely on their proposals"* so as to *"ensure that local passengers, businesses and transport providers are able to comment on the proposals..."*. The Guidance also states that an authority *"should aim to make their consultation materials as accessible as possible to all interested parties and ensure that local passengers in particular are aware of, and able to input to, proposals relating to their local bus services"*.
- 7.14 It is therefore proposed to consult both passengers and non-passengers, to ensure that the general public will have the opportunity to review and comment on the proposals.
- 7.15 Subject to the recommendations sought in this report, the proposal is that the consultation will commence on 14<sup>th</sup> October 2019 and end on 8<sup>th</sup> January 2020 . This is to allow respondents a proportionate and adequate amount of time to consider the materials and respond to the consultation.

7.16 Should the GMCA decide to undertake a consultation then the total costs are estimated to be £660,000. These cost projections include all costs to deliver a consultation that fulfils the requirements of the Act and Guidance, including:

- £150,000 for response management/analysis by third party supplier;
- £130,000 for consultation best practice support and expertise;
- £100,000 for deliberative research to support the open survey responses;
- £100,000 for design, production and print of materials, including core consultation documentation and assets to support the awareness-raising activity; and
- £180,000 for communications and engagement activity to ensure full reach and awareness across the public, businesses, and other interested parties in GM and beyond. This is in addition to activity on existing GM free channels.

## **8. NEXT STEPS**

8.1 The Act sets out the further legislative steps that must be undertaken by an authority once a consultation has been undertaken. Section 123G of the Act provides that the GMCA must publish a report setting out:

- its response to the consultation; and
- its decision on whether or not to make the proposed franchising scheme.

8.2 The Act confirms that any decision on whether or not to make the proposed franchising scheme is exercisable only by the Mayor.

## **9. RECOMMENDATIONS**

9.1 Members are recommended to endorse the recommendations set out in this report.

**Eamonn Boylan**

**Chief Executive, TfGM and GMCA**