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**Transit Service Contracting:  
Experiences and Issues**

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## INTRODUCTION

The recent fiscal problems of public transit in many large metropolitan areas have stimulated interest in alternative service delivery systems for public transportation. One strategy, that of contracting with private providers for public transportation services, has received particular attention. Private sector contracting is viewed as attractive due to its cost and subsidy savings potential--savings of 25 to 50 percent of public agency transit operator costs have been cited.(1,2,3) The reality, however, is that relatively little transit service contracting currently takes place and that substantial political, organizational, and legal obstacles confront plans to increase the use of this strategy. In addition, little detailed information is available on the extent of service contracting, its economic benefits, and the institutional factors which affect its feasibility.

The purpose of this paper is to contribute to remedying this information deficiency by providing a review of selected experiences and issues of transit service contracting. The paper focuses on five major topics. (1) How widespread is transit service contracting, who practices it, and what services are involved? (2) Why do public agencies engage in private sector contracting, and what are typical situations in which they do so? (3) What is the magnitude of the estimated cost and subsidy savings which have been realized from contracting? (4) What are the major obstacles to service contracting and when are they able to be overcome? (5) What issues involving service contracting require additional research?

These topics are explored with primary reference to service contracting experiences in California. In California, large numbers of local governments contract with the private sector to provide a variety of public transportation

services. In addition, local governments and transit agencies in Arizona, Michigan, Minnesota, New York, and Virginia have engaged in service contracting with interesting results. Their experiences are also included in this analysis. While the data is by no means exhaustive, it is probable that the experiences included in this paper are representative of the types of service contracting which occur, the economic benefits of contracting, and the problems this strategy encounters.

## THE SCOPE OF TRANSIT SERVICE CONTRACTING

### Service Contracting in California

Contracting for public transportation services is a nationwide phenomena, but it has been particularly prevalent in California. Because relatively complete information is available on service contracting in California, that state's experiences are used to indicate the relative magnitude of contracting, the types of services which are contracted, and the local government entities which are most likely to utilize this strategy.

As of mid-1984, it was possible to identify 204 individual public transportation services or systems in California which used a private transportation operator as service provider. The large majority of these private providers are for-profit transportation providers, although a small portion (less than 10 percent) are not-for-profit organizations which in most cases initially provided social service transportation. Table 1 presents a breakdown of these 204 systems by type of service, total expenditures for that service category, and average expenditure per contracted service.

To place the numbers in Table 1 in perspective, California contains approximately 375 public transportation systems, counting separate systems

TABLE I  
Expenditures for Contracted Public Transit Services

<u>Type of Service</u>	<u>Number of Systems</u>	<u>Total Expenditures</u>	<u>Average Contract Expenditure</u>
Fixed Route Transit	46	\$17,178,000	\$373,400
Demand Responsive Transit, General Public	79	18,117,000	238,700
Demand Responsive Transit, Elderly and/or Handicapped	79	14,481,000	183,300
All Systems	204	49,768,000	244,000

individually. (That is, a transit agency which provides both fixed route transit and demand responsive transit would be credited with two systems.) During 1982-83, approximately \$1.3 billion was spent on public transportation operations in the state. Therefore, while \$50 million is now being spent on privately contracted transit services, this represents less than 4 percent of all operating expenditures for transit in California. Because the contracted services are small scale in nature, they represent only a small fraction of the transit service delivery system, even though they comprise over one-half of all public transportation services in the state. Virtually every large scale transit service is operated directly by a public organization.

It is unlikely that the magnitude of California's use of transit contracting can be extrapolated to the national level. A direct extrapolation would indicate nationwide expenditures of more than \$500 million on privately contracted services, but the actual, albeit unknown amount, is probably considerably less. The reason is that local governments in California are almost certainly more prone to engage in transit service contracting than their counterparts in most other states. This is the result of both California's tradition of private sector

contracting for a variety of local services and the cost-effectiveness incentives built into the state's transit subsidy program.(4,5) Nonetheless, the evidence from California implies that transit service contracting is not a rarity, but a relatively common occurrence for small transit systems and supplemental demand responsive transit (DRT) services. This service delivery mechanism probably accounts for at least \$100-200 million in nationwide expenditures on public transportation.

#### Types of Privately Contracted Services

As Table 1 indicates, all types of public transportation services are contracted to private operators. DRT services are the most likely to be contracted, but 46 fixed route transit services in California also use a private operator as service provider. Almost all of these are entire fixed route systems: in a few cases, commuter express service is the only contracted service. Outside of California, there are several important examples of fixed route services being provided by private contractors. In Westchester County, N.Y. the entire transit system, consisting of 321 buses operating on dozens of routes, is operated by private carriers. In both Phoenix and the Tidewater, VA (Norfolk-Virginia Beach SMSA) region, the regional transit agency contracts with a private transportation firm to operate small vehicles (vans or mini-buses) on low density transit routes. In the Houston area, most of the regional transit agency's park and ride express services are operated by private bus companies in a large contract service which uses 113 buses. The Dallas transit agency has just initiated a similar contract service involving more than 60 buses.

Transit service contracting is most frequently practiced with DRT. In fact, public agency operation of DRT is rare in California. Of the 85 general public

DRT systems in the state, only 6 are operated by public agencies. This is a nationwide trend. Even transit agencies which initially operated DRT themselves, such as in Rochester, NY and Portland, OR, eventually turned the service over to the private sector due to excessive operating costs. Some transit agencies have even substituted DRT for unproductive fixed route services. For example, Phoenix Transit replaced its entire Sunday fixed route service with a privately contracted DRT system, and Tidewater Transit has terminated several bus routes and replaced them with DRT services.

#### Who Contracts?

In California, transit service contracting is most frequently practiced by general purpose local governments, i.e. cities and counties. Table 2 reveals that nearly two-thirds of all contracting entities are cities, and another one-fifth are counties. While a relatively small number of regional transit agencies engage in service contracting, they represent over 40 percent of all regional transit agencies in the state. Transit agencies typically contract only for DRT services: only two urban or suburban transit agencies contract for any fixed route service, and in both cases this is express bus service into San Francisco which has historically been privately provided.

California's experiences thus tend to support the widespread perception that transit agencies only rarely contract for fixed route service, although they are much more likely to contract for specialized DRT services. The few transit agencies which do contract for any type of fixed route service--e.g., Houston's Metropolitan Transit Authority (MTA), Tidewater Regional Transit (TRT), Golden Gate Transit (GGT), Phoenix Transit--have received considerable national attention precisely because they are so unusual. It is much more common for

TABLE 2  
Types of Contracting Entities

<u>Contracting Entity</u>	<u>Number of Entities Which Contract</u>
Municipality	104
County	35
Transit Agency	16
Others (e.g., joint power authority)	6
Total	161

cities and counties to engage in service contracting for fixed route transit. Of course, such local governments are also more likely to contract for all types of public transportation services.

#### MOTIVATIONS FOR TRANSIT SERVICE CONTRACTING

Local governments contract for public transportation services for two interrelated reasons. First, service contracting saves money. Second, it forestalls the need to create or expand a public bureaucracy to deliver a local service.(4.5) Not only does this usually also save money, but in addition it gives the local government more flexibility in adjusting the service output level. Public officials recognize that cutbacks in public agency operated services tend to be difficult to achieve due in part to the political influence of public employees.

These benefits of contracting represent necessary but not sufficient conditions for its utilization. Local governments are most likely to contract either when they cannot afford a transit service otherwise or when the monetary savings which result from contracting can be used for other government purposes or to keep taxes low. These conditions do not exist for many transit operations, particularly large regional transit agencies. A major reason that transit service



contracting is so prevalent in California is that the state's transit subsidy program is structured in such a way that most local governments have a strong incentive to consider the monetary implications of service delivery mechanisms.

In California, funds for public transportation subsidies are generated by a sales tax on gasoline, most of the proceeds of which are distributed back to the state's cities and counties in proportion to their contribution to gasoline sales. Except in the state's 10 most populous (and most urbanized) counties, these Local Transportation Funds (LTF) can be used for either transit or highways, provided that no unmet transit needs exist. That is, once a basic level of transit service is provided, a city or county can use the remaining LTF for streets and highways. Since funds for street and highway repairs are in continual demand, local governments have a strong incentive to maximize the portion of the LTF which can be used for that purpose. Local governments have determined that the most effective way of minimizing transit expenditures while still providing an adequate level of service is to maximize the amount of service contracting. In the 48 counties where the LTF can be used flexibly, private sector contracting by cities and the county for transit services is the norm, not the exception.

The propensity of California local governments to contract for transit services in order to use public funds most efficiently exemplifies the incentive for cost-effectiveness created by non-dedicated transit subsidies. When the funds used to subsidize transit can be used for other local government purposes and are not dedicated exclusively to transit assistance, service contracting becomes a much more appealing strategy. Tidewater Transit and Phoenix Transit, two of the most active contracting agencies among regional transit operators, both use non-dedicated local subsidies, as do many municipalities and counties around the country which contract for transit service.

Powerful incentives for transit contracting are also created by a relative paucity of funds for transit, even when these funds are dedicated solely to transit assistance. Local governments in Michigan and Minnesota have made extensive use of transit contracting, and in both states the major source of non-federal subsidies is state funds which are subject to annual or bi-annual appropriation and are quite limited in magnitude. Cities in these two states cannot afford to pay a high price for transit service, for to do so would mean no transit service at all. Similarly, Los Angeles County is rapidly becoming a stronghold of transit service contracting as the result of a local transit subsidy program (funded by a 1/2 cent sales tax increment) which returns substantial sums to the cities in the county, but not enough money to afford expensive transit agency service. For example, a city of 50,000 population receives over \$400,000 annually for community transit services from this subsidy program. This is enough to purchase a large amount of contracted service but represents only a meager amount of public operator service. Consequently, most communities which did not already have a municipal transit operator have contracted with a private provider for transit or paratransit services. There are now more than 25 privately contracted public transportation services in operation within the county.

One other motivation for employing service contracting is to implement transit services more rapidly than would be possible otherwise. The Houston MTA turned to private bus companies for its commuter express bus program when it became apparent that the transit agency lacked the buses and trained personnel to quickly respond to rapidly increasing demands for peak period service. Cities and counties in California often cite the lag time required to develop a public sector operated service as an important reason to engage in

service contracting. This factor is usually less significant, however, than expected cost savings from contracting and avoiding creating (or expanding) a public bureaucracy for transit service delivery.

Prototypical Service Contracting Situations: Regional Transit Authorities

Regional transit authorities have almost invariably contracted for supplemental services--DRT, commuter express services, and low density fixed route services--when they have contracted at all. Table 3 gives several examples of regional transit agency service contracting, including some of the best known cases.

TABLE 3

Examples of Regional Transit Authority Service Contracting

<u>Agency</u>	<u>Type(s) of Services Contracted</u>	<u>Magnitude of Service Contracting</u>
Tidewater Regional Transit	general public DRT, fixed route with 3 vehicles	13 vehicles in 8 DRT modules; 2 fixed routes
Golden Gate Transit	commuter express (subscription)	27 buses on 15 routes
Houston Metropolitan Transit Authority	commuter express	113 buses on 13 routes
Orange County (CA) Transit District	general public DRT	130 vehicles in 5 regional DRT modules
Omnitrans (San Bernardino, CA)	general public and specialized DRT	35 vehicles in 11 municipal DRT modules and 20 vehicles in 2 regional specialized DRT services
Phoenix Transit	general public DRT, fixed route	3 DRT services with 20 vehicles, 1 fixed route with 2 vehicles

These transit authorities have engaged in service contracting for one of three reasons. Tidewater Transit, Phoenix Transit, Omnitrans, and Golden Gate Transit face strong subsidy minimization pressures due to their use of non-dedicated local subsidies. Orange County Transit has provided DRT service since its inception, and has always contracted for such service because of a recognition that to do otherwise would lead to unacceptable costs. If OCTD wished to provide this service at all, and it was subject to strong community pressures for DRT, then contracting was a necessity. Houston MTA contracted for its commuter bus service because this was the only feasible method of implementing the service in timely fashion, and the agency was under great political pressure to expand its peak period services.

In general, these transit agencies have established relatively clear cut demarcation lines between services which are subject to contracting and those which are not. None contract with the private sector for all day transit service using standard size transit buses. Tidewater Transit, however, has contracted with one of its constituent local governments to provide fixed route service in that city using TRT buses. TRT is also unusual in that it has converted unproductive bus lines to privately provided fixed route van service--none of the other agencies have replaced their own fixed route service in this fashion.

In fact, only TRT and Phoenix Transit have directly substituted any type of privately provided service for their own agency operated services. Omnitrans, despite operating one of the largest paratransit contracting programs in the country, is very resistant to proposals to convert agency operated fixed route services into privately operated fixed route or paratransit services. This is in spite of the fact that the agency's farebox recovery ratio on some of its fixed routes is less than 10 percent, and the average subsidy per passenger is in excess of \$4 on these routes. Golden Gate Transit is similarly uninterested in contracting out services it now provides. It plans to operate all additional commuter express service itself, even

though the agency's unit cost for such service is more than 35 percent higher than that of the private bus companies it uses for its contracted subscription bus program. The major reasons agencies have established fences around contract services are potential labor problems, perceived service quality problems with contracting out "regular" transit services, and the antagonism of some transit managers to relinquishing operation of "mainline" transit service.

Prototypical Service Contracting Situations: Municipalities and Counties

Table 4 gives several examples of city and county transit service contracting. As is apparent, these local governments are likely to contract for entire transit

TABLE 4

Examples of County and Municipal Service Contracting

<u>Agency</u>	<u>Type(s) of Services Provided</u>	<u>Magnitude of Service Contracting</u>
Westchester County (NY)	entire fixed route system	321 buses
Los Angeles County	fixed route, commuter express, and specialized DRT	30 fixed route vehicles, 6 DRT vehicles
Yolo County (CA)	entire fixed route system	12 vehicles
San Diego County	fixed route and specialized DRT	19 fixed route vehicles, 5 DRT vehicles
El Cajon, CA	DRT (entire local transit system)	22 vehicles
Carson, CA	fixed route and specialized DRT	4 vehicles, subsidized taxi service
Hayward, CA	specialized DRT	subsidized taxi service
Tucson, AZ	specialized DRT	12 DRT vehicles

systems, not just supplemental services, although there is a considerable amount of contracting for specialized DRT services by cities and counties. These cities and counties typically use non-dedicated local sources of subsidy, and thus have compelling fiscal reasons to practice service contracting. In addition, the California counties which contract have no desire to operate public transit themselves, and the only question was whether they would contract with a private or public operator. Competitive bidding resolved this question in favor of the private sector, as the relevant public operators invariably submitted a much more expensive bid than the competing private providers.

El Cajon and Hayward are typical of literally dozens of California cities which contract for either general public DRT or specialized service for the elderly and/or handicapped. Because they are located in large metropolitan counties these two cities cannot use state transit subsidies for non-transit purposes, but in neither case are the available funds so abundant that the city can afford expensive transit services. El Cajon, for example, would have to pay the regional transit agency more than 2 1/2 times as much per vehicle mile as it is charged by the taxi company which actually provides the community's DRT service.

Los Angeles and Westchester Counties are among the largest general purpose governments in the country to contract for transit service. Fiscal factors and a reluctance to become directly involved in transit service provision were the motivating factors in both cases. The Westchester County transit system is probably the largest contract operation in the U.S., and one of the most interesting as well. Several private companies are involved in the system, each operating multiple routes and responsible for vehicle maintenance as well as vehicle operations. The contractors receive a fixed fee per mile for their services, provided that they meet certain performance standards (e.g.,

maintaining schedules). If performance is subpar, the contractor's compensation is reduced. Los Angeles County contracts for much less service than Westchester County, as its transit responsibilities are confined to unincorporated or unurbanized areas, but it has made no less of a commitment to this strategy. It contracts for all day-fixed route service, commuter express service, and specialized DRT, at costs far below comparable public agency operated services. Both of these counties have contracted for transit service from the outset, and thus never confronted labor or management obstacles to this method of service delivery.

#### ECONOMIC BENEFITS OF SERVICE CONTRACTING

The economic benefits of transit service contracting are the primary reason for its appeal. Private sector contracting usually saves money compared to public agency operation of a transit service; however, the magnitude of the savings are subject to considerable uncertainty. Several comparisons of public agency and private operator service costs are presented here, but these comparisons must be treated cautiously.

Only in the case where a private operator replaces or is a substitute for public agency operation of an entire public transportation service can any precision be attached to cost savings. For example, if public and private operators bid \$40 per vehicle hour and \$20 per vehicle hour respectively to operate a city's entire fixed route transit system, then it is possible to conclude with high confidence that the municipality saved 50 percent by contracting.

In many situations, however, only a portion of a transit system will be contracted to a private operator. In such cases cost savings are less clear cut. This is because the cost to the public agency of operating the relevant service can only be estimated through the use of a cost allocation model, and cost

allocation methods do not necessarily produce reliable estimates of avoidable or incremental costs. Consequently, in those cases where cost models are used to determine public agency costs, there may be an overestimation of cost savings which result from contracting. On the other hand, private operators are often required to supply the vehicles for a contracted service, and the absence of capital expenses in public agency service costs will lead to an underestimate of cost savings in these cases.

#### All-Day Fixed Route Services

Table 5 presents six different cost comparisons of comparable public and privately operated fixed route services. These services all operate the entire

TABLE 5  
Difference between Public Agency and Private Contractor  
for Fixed Route Transit Services

<u>Type of System</u>	<u>Cost Difference</u>	<u>Basis of Cost Comparison</u>
18 California small municipal systems	-22%	direct comparison
Phoenix Transit bus route	-62%*	agency unit costs vs. private service costs
Yolo County transit system	-37%*	competitive bids
Tidewater Transit bus route	-48%	agency unit costs vs. private service costs
2 NYC suburban transit systems	-32%	direct comparison
San Diego County transit system	-34%*	competitive bids

\* Cost savings understated because private contractor responsible for vehicle provision.

Source: Data obtained from government agencies responsible for transit planning and provision, from private operators and from references 1, 3 and 10.



day--none are peak period only operations. As is apparent, substantial cost savings are indicated for private sector contracting, ranging from 22 to 54 percent of public agency unit costs. As might be expected, cost savings are greatest for regional transit agencies and lowest for municipalities. Small municipal bus operators typically have lower unit costs than regional transit agencies due to lower wage rates, lower peak to base ratios, and the ability to share overhead expenses with other municipal services. Even compared to such municipally operated fixed route services in California, however, similar privately contracted services are more than 20 percent less expensive.

#### Commuter Express Bus Service

Proponents of transit service contracting often cite commuter bus service as a particularly promising application of this strategy. As a supplemental service, commuter express operations are believed to avoid some of the labor constraints that confront contracting of all-day transit services, particularly for expansion of commuter service. In addition, the cost saving potential of contracting for peak period only services is believed to be great, as these are a transit agency's most expensive services due to severe labor inefficiencies. Table 6 presents cost comparisons for the relatively few commuter bus services which have been contracted to private operators, as well as cost savings estimates derived from studies of public vs. private provision.

The studies and direct comparisons reveal that large cost savings are indeed possible with contracting, provided that enough service is involved to enable the public agency to reduce overhead expenses when contracting out existing services or to forego additional overhead expenses in cases of service expansion. If only one or two bus runs are contracted by a public transit operator, the savings will probably be minor or non-existent.

TABLE 6

**Estimated Cost Savings for Commuter Bus Services  
Operated by Private Contractors**

<u>Public Agency Sponsor or Potential Sponsor</u>	<u>Cost Difference</u>	<u>Basis of Cost comparison</u>
Golden Gate Transit*	-25%	private operator actual costs and cost models for public agency
Los Angeles County*	-38%	private operator actual costs and cost models for public agency
Houston*	-35%	private operator actual costs and cost models for public agency
Cleveland*	-58%	private operator actual costs and cost models for public agency
SCR TD*	-51%	analytical cost models
Boston (MBTA)	-50%	analytical cost models

\*Private operator supplies vehicles, thus cost savings are understated.

Source: Data obtained from government agencies responsible for transit planning and provision, from private operators and from references 1, 2, 7, 8 and 9.

The magnitude of cost savings also depends on whether the contractor must supply the vehicles or not. This is a common requirement for commuter services, but can add substantially to the private operator's costs due to the high costs of suitable buses and the difficulty of achieving other utilization of the vehicles. It has been estimated that the capital costs of the vehicles added as much as 30 percent to the service costs of private operators in Houston, where new or recent buses were required to be used by the contractors.(2)

Table 7 presents a more detailed comparison of the cost and subsidy requirements for commuter express bus service provided by Golden Gate Transit and by the private operators who furnish its contracted subscription service. At

the time of this comparison 27 buses were used in the subscription bus program, operating on routes of 20 to 60 miles in length. GGT's service costs were calculated by applying the transit agency's cost model to a route which was the same length as the average route in the subscription program. Other aspects of the two services were also similar. Because the 27 buses then involved in the subscription service represented about 11 percent of GGT's peak bus fleet, it is likely that the overhead expenses implied by the cost model would come into play if the transit agency were to take over the privately provided services or contract out a similar amount of commuter service. The indicated 25 percent cost savings and 50 percent subsidy savings are probably conservative, as the private operators must supply their own vehicles. Depreciation charges would add at least 5 to 10 percent to the private operators' total service costs (the buses are not new, having an average age of 10 years), whereas the transit agency purchases its buses with public subsidies and thus does not include depreciation in its operating expenses. Despite the conservative estimate of

TABLE 7

## Comparative Cost of Operation of GGT Subscription Bus Service

<u>Provider</u>	<u>Cost</u>	<u>Subsidy</u>
Private Bus Company	\$1,589,510	\$575,480
Golden Gate Transit	2,123,260	1,167,790
Difference	533,750	592,310
	+33.6%	+102.9%

Source: Golden Gate Transit Annual Report and data supplied by transit agency.

cost savings, this comparison indicates that GGT saves approximately 5 percent of its annual subsidy requirements by contracting for its subscription services rather than operating these services itself.

### Demand Responsive Transit

DRT is the transit service most commonly contracted to the private sector. Because service contracting is so pervasive for DRT, it is difficult to identify publicly operated DRT systems for cost comparison purposes. The scattered evidence which is available, however, indicates that large savings are also possible for this transit service when it is privately contracted.

Table 8 reveals that cost savings of approximately 50 percent are the norm for regional transit agencies, and such savings may even be conservative as the agencies included are relatively low cost by national standards. On the other

TABLE 8

#### Cost Savings for General Public DRT Services Operated by Private Contractors

<u>Public Agency for Comparison Purposes</u>	<u>Cost Difference</u>
Phoenix Transit	-54%*
Rochester-Genesee Transit Authority	-45%**
Orange County Transit District	-49%*
Omnitrans	-55%*
Tidewater Transit	-49%*
4 California municipal systems (compared to 21 taxi company operated systems)	-12%**

\* DRT service costs vs. bus service costs for comparable service areas.

\*\* Comparable DRT services.

Source: Obtained from agencies responsible for transit planning and provision, from private operators, and from References 3, 10, and 11.

hand, several of the comparisons involve the replacement of fixed route bus services by small vehicle (van or mini-bus) DRT operations, and the added dispatching costs of the latter may be more than offset by the higher vehicle maintenance and fuel expenses for large transit buses. Nonetheless, the cost savings will always be large.

Large subsidy savings are also possible by substituting DRT for unproductive fixed route services. Phoenix Transit estimates that it has saved \$700,000 annually by substituting DRT for its Sunday fixed route services.(1) This represents nearly 5 percent of total agency subsidy. Tidewater Transit has reduced subsidy per passenger by as much as 64 percent in particular conversions of fixed route transit to privately contracted DRT. (3)

Although much lower cost savings are indicated for municipally operated DRT services in California, this is due to that fact that the few cities which operate their own DRT systems engage in the same cost reduction practices as private providers. They pay low driver wages, they use part time labor, and they share overhead with other municipal services. These are not unionized transit operations, and thus all wage rates are more reflective of private sector conditions. In contrast, the small municipally operated fixed route bus services cited in Table 5 are about twice as expensive as privately operated DRT. It thus appears that it is possible for public agencies to save upwards of 50 percent by contracting for DRT service. Even the most cost conscious public operators cannot match the service costs of private providers.

#### INSTITUTIONAL OBSTACLES TO SERVICE CONTRACTING

There exist several potentially significant obstacles to transit service contracting. First, transit managers tend to view service contracting

unfavorably. Second, transit labor unions are almost invariably strenuously opposed to contracting. Third, when subsidy sources are dedicated exclusively to transit, as is often the case for large transit agencies, transit policy makers usually lack the incentive to support contracting. Fourth, the service quality of private operators may be below public agency standards, creating dissatisfaction on the part of both the sponsor and transit riders. Fifth, finding a suitable private provider may be problematic, and maintaining a potentially competitive situation for contract renewals may also be difficult. Finally, although the monetary savings from contracting are impressive in percentage terms, they may not represent large enough dollar amounts (because such a small amount of service is contracted) to induce a transit agency to overcome other reservations about this strategy.

Whether these obstacles in fact become manifest depends to a large extent on the type of public agency which is responsible for public transportation provision. When this is a city or county, the actual impediments to service contracting are usually relatively minor, unless the local government has operated a transit service itself for some time. As California's experiences indicate, general purpose local governments tend to view transit service contracting favorably, and frequently engage in this practice. Moreover, when a transit operator is subject to direct policy and fiscal control by cities and/or a county, particularly those which do not dedicate financial support to transit, it too may embrace service contracting. Westchester County and the City of Phoenix are directly responsible for their transit operations, and city governments in the Tidewater and San Bernardino regions directly determine the amount of transit service they receive and the amount of local funds which will be allocated to the transit agency. In all four cases service contracting is used far more than the national norm.

In contrast, many of the potential obstacles to service contracting become manifest when a relatively autonomous transit agency is the local entity with the greatest influence over transit decisions. The most important of these obstacles are rooted in the monopoly organization of public transportation in most large American urban areas. Monopoly organization, particularly when combined with dedicated transit subsidies, insulates transit managers from economic or political pressures to stress cost-effectiveness when making service delivery decisions. Even without such insulation, many transit managers would prefer to provide all services with agency personnel in order to maximize the size of the organization (usually a determinant of political influence) and to ensure maximal control over service quality. This combination of institutional arrangements and management attitudes blunts incentives for service contracting, and can represent an insurmountable obstacle.

The monopoly framework for public transit has also created serious labor constraints to service contracting. Section 13(c) of the Urban Mass Transportation Act, originally designed to protect transit workers from being displaced by capital investments, has been transformed into a powerful labor bargaining chip for preserving a monopoly on all jobs associated with transit service provision. The model 13(c) agreement tacitly endorses transit labor's claim on all transit jobs, and many local labor contracts explicitly verify this claim. Labor contracts can thus represent an absolute legal barrier to contracting, unless they can be changed through collective bargaining. Although 13(c) itself is not an absolute barrier to contracting, and tough-minded transit managers have been able to contract in spite of labor resistance, it is a rare transit agency which can engage in service contracting without a major struggle with its labor force. Unless strong management and policy support exists for

contracting, the prospect of a serious battle with labor may be enough to sink this strategy before it can be given a hearing.

Because of the 13(c) situation, service contracting is virtually out of the question if transit workers will be displaced as a result. This tends to limit transit agency applications to relatively small increments of service. Even some of the bolder uses of contracting, such as the activities of Tidewater Transit and Phoenix Transit, have not been of a magnitude to require the agencies to lay off workers. The few truly large contracting activities undertaken by transit agencies, notably OCTD's DRT program (130 vehicles) and the Houston MTA's express bus program (113 vehicles), do not represent replacements of agency services, but are new services instead. As they do not affect existing transit workers, such new services are by far the easiest to contract to the private sector. However, relatively few transit agencies have the fiscal resources for major service expansions.

Although the major obstacles to service contracting are most applicable to regional transit agencies, two other potential obstacles can affect any contracting entity. The first is the issue of the quality of the service provided by a private operator. Private providers may fall short of public agency expectations about service reliability due to their greater concern about keeping service production costs low. For example, the Southeast Michigan Transit Authority (SEMTA) has sharply reduced its use of contract services (it originally contracted for commuter express service and several DRT services) because of persistent service quality problems with private operators. Many of these problems were attributable to inadequate vehicle maintenance, which led to unreliable service. SEMTA staff believes that some contractors were simply not capable of providing the necessary quality of service, as they had never before operated in such a demanding service environment. Tidewater Transit has also



experienced service quality problems with its DRT contractors, and has tightened its contract requirements and administrative oversight in an attempt to prevent recurrences. (6) On the other hand, other major sponsors of contract services have not experienced serious service quality problems, nor have the vast majority of cities and counties in California. Nonetheless, the fact that negative experiences do occur gives credence to the belief of many transit managers that service quality can be a problem in contracting.

The second potential problem is that of maintaining a suitably competitive environment to keep private contracting costs low. Private transportation providers with the necessary capabilities to operate a public transit service are often not abundant, particularly in small urban areas. Even in metropolitan areas it is not uncommon for a public agency to have only one or two providers to choose from. For example, Tidewater Transit was able to interest only one local transportation company in bidding on its contract services, and several of the largest DRT systems in California have never had real competition for the service contract.

The concern is that lack of competition could cause private operators to sharply increase their rates to the public agency. But while this may eventually occur, it does not appear to have become a serious problem to date. Service costs of most "sole source" contractors are very reasonable by national standards and far below comparable public agency costs. Private operators view contract revenues as so desirable, because they are a secure revenue source, that in most non-competitive situations they do not attempt to exploit their advantageous position.(5) Occasionally, private operator rates do appear somewhat excessive (the Houston MTA initially paid all-day charter rates for its peak period only express services), but this does not appear to be a widespread problem. The public agency almost always holds the upper hand in contracting situations, as it

can provide the service itself or encourage non-local firms to bid when the current provider attempts to exploit a monopoly position. Of course, private operator rates may be lower when many firms compete for a service, but the cost differential between public and private operators is typically so large that public agencies will find it advantageous to contract in non-competitive situations as well.

#### AREAS REQUIRING ADDITIONAL RESEARCH

This paper represents a reconnaissance of the current status and future potential of transit service contracting. As such, it does not delve deeply into some of the issues which are likely to determine just how widely this strategy will be used in coming years. It is possible, however, to identify three areas where additional research is urgently needed to help clarify the institutional feasibility and economic benefits of service contracting.

First, research is needed into the entire question of the magnitude of the cost savings which result from service contracting. The cost comparisons assembled for this paper range from relatively sophisticated attempts to model public and private operating costs for the same service (7) to straightforward but possibly misleading applications of agency cost models to commuter express services (8,9) to comparisons based simply on unit costs for the same or similar services. (1,2,5) None of these approaches are without their deficiencies, although it is encouraging that they all yield estimates of cost savings which range from 20 to 50 percent. Improved approaches are necessary for more accurate estimation of the cost savings which would result from either the contracting out of existing public operator services or using private operators to provide additional transit services.

This need is most acute for supplemental services, particularly commuter express service, and for all types of substitution services. In these situations cost savings are difficult to estimate due to the problem of accounting for relevant public agency overhead costs and, for commuter services, due to complicated labor scheduling interactions with off-peak transit operations. The magnitude of the research problem should be emphasized, for cost models must be relatively straightforward to apply and not require substantial amounts of data, yet they must somehow adequately represent the cost implications of changing the inputs to the service production process as well as changes in the level of output itself. Moreover, these cost models must be capable of giving reasonably accurate estimates when applied at the route level of analysis, and for different magnitudes of service contracting.

Research on cost differences is also needed to account for the effect of requiring private operators to supply the vehicles for a contracted service. For commuter express service such effects can be profound--it is estimated that vehicle capital costs can represent as much as 30 percent or more of total private operator service costs in some situations. (2.7) Without being able to take the vehicle cost factor into account, estimates of public-private cost differentials, such as some of those cited in this paper, will understate the private operator cost advantage.

A second major area requiring additional research is the determination of how much of a deterrent to service contracting is actually posed by the current labor situation in public transportation. There can be little question that federal law, local labor contracts, and the desire of many transit agencies to have smooth labor relations all make contracting quite difficult. Much too little is known, however, about why a few transit agencies are able to contract for a

variety of services, whereas most of their cohorts do not contract at all. Are labor constraints as much perceived as actual, or are they truly as formidable as they appear? How important are the generally unfavorable views of transit management towards service contracting in giving influence to labor opposition to this strategy? Is the incentive structure for transit service decisions as important as labor constraints in forestalling serious consideration of contracting? The answers to these, and other related questions, have major implications for the institutional feasibility of service contracting by relatively large transit agencies.

Finally, research is needed on the question of how best to administer a service contracting program while maintaining consistency with an overall agency objective of minimizing service delivery costs. Some transit agencies, such as OCTD, have established a bureaucratic structure to administer their contract services. While this ensures high quality of service and provider honesty, it is also quite costly--OCTD's administrative costs for its DRT program are 24 percent of the cost of service provision. But informal contract management can lead to problems, as Tidewater Transit has learned. There seem to be sufficient transit agencies now engaged in service contracting that comparative analysis of their experiences would yield valuable insight into the question of how much, and what type, of contract management is necessary.

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