HIGHLANDS AND ISLANDS DEVELOPMENT BOARD

HIDB RESPONSE TO SCOTTISH OFFICE CONSULTATIVE PAPER "SEA TRANSPORT TO THE SCOTTISH ISLANDS"

INTRODUCTION

In 1974 the Board, in response to a request from the Secretary of State for Scotland, prepared and later published "Roads to the Isles" in which it proposed a formula by which ferry charges in the Highlands and Islands could be linked to a Road Equivalent Tariff (RET). Since then the proposal has received increasing support from local authorities, parliamentary committees and, most recently, from a report prepared for the European Parliament on the problems of marginal areas in Europe.

From its early years the Board had proposed that transport costs for people and goods to and from the islands should be brought more into line with transport costs on the mainland. The cost of transport rises steeply when a sea journey is involved, mainly because of the costs of changing modes of transport and the higher energy costs and additional labour involved in sea transport. With the introduction of modern car ferries and a move towards roll-on/roll-off operation, it became possible to propose that ferry fares should be based on a comparison with road transport. "Roads to the Isles" was concerned primarily to argue the case for that innovative, indeed revolutionary concept. In doing so it put forward a formula to demonstrate that the idea could be given a definite and practical expression. The paper did make it clear, however, that there were a number of other ways of formulating a Road Equivalent Tariff.

It should be borne in mind that the Board's 1974 proposals were put forward in very different conditions to those of today. At that time the Government had not accepted the principle that ferry services in general should be subsidised, the exceptions being specific routes operated by David MacBrayne and the Orkney Islands Shipping Company. A decision was taken in 1975, however, to subsidise the Caledonian MacBrayne services and with the introduction on 1 September 1979 of subsidies on the P&O Ferries' routes to Orkney and Shetland, the principle has now been applied to all parts of the Highlands and Islands, though not to all operators. One of the Board's objectives in ferry policy has, therefore, been achieved.

RET AND THE CONSULTATIVE PAPER

The Board welcomes the commitment to "the survival and prosperity of our island communities" in the Consultative Paper and the fact that the question of implementing RET has been considered more fully than by previous Governments. It is nevertheless disappointing that the Paper has not gone further to express a more positive view on the proposal or in examining how the concept could be incorporated into a system of fares.

The Board considers it is important to discuss the implementation of RET more fully than the Paper does in two respects: (i) it should be related to methods of reducing the resource costs of providing the ferry system; and (ii) it should look in detail at ways in which variations in the RET formula could provide a more practical basis for a new fare structure.

(i) Much of the research by the Board since 1974 on ferries has focussed on how, by restructuring of the system, costs could be reduced. The Board has circulated for staff comment a report on suggested changes to Scottish Office, local authorities and ferry operators, and in the next few weeks will publish its proposals in the light of the observations received. That document broadly concludes that the resource costs of the Scottish ferry system can, over a period of time, be significantly reduced in real terms.

(ii) This response is concerned with the questions put forward in the Scottish Office Consultative Paper on how RET can be implemented and on the proposal for a route licensing system.

THE IMPLEMENTATION OF RET

The Board concludes from the Consultative Paper that there are no insuperable obstacles to the application of a form of RET to the fare structure of ferries in the Highlands and Islands.

The main question is how the tariff should be calculated to achieve the aims of transport policy for ferry services. In the Board's view, part of the difficulty encountered in the argument of the Paper results from a lack of clarity in stating the objectives of such a policy. Since the choice of options in implementing RET will depend upon these, it is regrettable that the policy objectives were not clearly presented. The consequence of this omission is that the focus of attention shifts to the issue of which one set of island communities will benefit most as compared to others. The Board believes that a clear policy for transport to island communities based on RET will benefit all islands, although there are questions of distribution and fairness to be considered.

The Board's main objective on island transport is the removal of two major barriers to development on islands. The first is the high cost of transporting people and goods, and the second is the difficulties of access which developers perceive to exist in an island operation. The proposals which the Board has put forward on ferries have been directed at improving the 'road equivalence' of the ferry system as an important means of reducing these barriers. That is not to say that the Board advocates the complete removal of a charge, since the aim of road equivalence is to minimise the added burden imposed by a sea crossing, rather than the penalty of distance as such.

The Consultative Paper points out that an RET fare structure would be easily understood and the Board believes that it would in addition be widely accepted as an equitable basis for determining ferry charges. At present with the 'block' subsidy to STG routes it is not explicit where the existing subsidy or additions to it are being applied. While it may be possible to envisage an explicit allocation of the subsidy between islands, it would be a most intricate exercise, involving a wide range of social and economic judgements. Road Equivalent Tariff 'solves' that problem by applying the same principle to all services.

ISSUES IN A SYSTEM OF RET

The Board is concerned that the Consultative Paper has exaggerated the difficulties of introducing RET by the implicit assumption that the 1974 formula illustrated in "Roads to the Isles" is the only one which might be applied. The Board considers that once the principle of a Road Equivalent Tariff has been accepted, it is possible to arrive at a fare structure which meets the doubts expressed in the Paper about RET while retaining the concept's essential advantages.

The Consultative Paper does incorporate one of the changes to the 1974 formula which the Board has developed and suggested recently, namely passenger charges based not on the fiction of a one-metre passenger, but on British Rail fares. It is nevertheless felt that the assumption of a 1979 charging coefficient of 5p per mile is rather high, because it does not take into account the wide extent to which British Rail offers a range of reduced fares.

Further variation to the 1974 formula could be made in the toll element which might be either eliminated, or varied by type of vehicle, as on major toll-bridge crossings.

Perhaps the area of greatest variation, however, lies in which elements of total operating costs should be included in setting the charging coefficient for vehicles under RET. It was pointed out in "Roads to the Isles" (page 17) that whereas total operating costs of road vehicles were used as the basis for the calculations outlined, strictly speaking only running costs should be charged. Standing costs, such as insurance and interest charges, do not cease when vehicles are on a ferry, and hence the inclusion of these elements in a Road Equivalent Tariff would amount to double-charging.

Analysis of the Commercial Motor Tables of Operating Costs and guide to rates 1979 reveals that running costs comprise 49.7% of total operating costs for commercial vehicles and 25.2% of total operating costs for cars. RET fare structures have, therefore, been prepared for cars and commercial vehicles based on running costs only, and these are shown in Tables 1 and 2 respectively of the Appendix. The Board favours this application of the formula and while recognising that its full implementation will create certain problems in the provision of public expenditure, it appears to be the level of RET which most fully reflects road equivalent costs for cars and commercial vehicles.

Dealing with the alternative options mentioned in paras 15 and 16 of the Consultative Paper, the Board is not clear how RET as a <u>guide</u> to subsidy would be different from the current system. If the Government is proposing to allocate an annual subsidy to each route, based on a comparison between estimated revenue under RET and the cost of providing the service, the Board would wish further details before commenting. It would certainly be a step forward to have information on costs and revenue by individual route.

The Board does not favour the suggestion of RET applied to freight traffic only. In preparing "Roads to the Isles", the Board's major purpose in 1974 was to seek assistance for freight carriage and the costs of commercial trade, but with the growth of roll-on/roll-off car traffic and tourism, cars are now more important to island economies. The objective of helping island commerce (para 6) would thus not necessarily be achieved by a freight-only RET as most businesses also depend upon personal travel and many types of goods are carried in light vans, estate cars and private cars.

The Board recognises that full implementation of a running-costs RET would take longer than one based on total operating costs. Until full implementation is achieved, the Board would suggest that fares on all routes should be the same fixed percentage above the RET level. Until the real level of future subsidy is known, it is difficult to foresee where conflict would occur with the existing fare strucutre. The most likely area would be that of the discounts offered by multi-journey tickets on certain routes, but the Board would wish to know more about the numbers and users of these fares. Until fares were reduced to the RET level, it might be preferable to lower the cost of return tickets purchased on islands.

OTHER ISSUES

The Consultative Paper makes the point that more distant isles will benefit less from the introduction of RET (although the fact is that longer routes will benefit less). If fares were entirely abolished on ferries it would still be true that these islands would gain proportionately less than others. The Board would reiterate that the main goal of implementing an RET fare structure, together with a higher real level of subsidy, is to benefit all island communities. The vast majority of island populations will gain substantially from the introduction of RET, and islands such as the Uists and Barra which are served by long routes from Oban will benefit from reduced fares on the shorter-distance connections with Skye and the rest of the Western Isles.

The Board does not agree that the introduction of a regulated fare system would reduce the incentive for ferry operators to act efficiently. Assuming that inflation was within reasonable control, it should with experience be possible for the Government and operators to determine in advance each year both the expected level of revenue and the anticipated operating costs of individual services; the difference between these figures would be the required level of subsidy. This would appear to be an arrangement and a financial discipline similar in many respects to that which currently obtains. The operators would not be expected to absorb unforeseen increases in costs, such as those resulting from changes in world oil prices, but they would be expected to keep within the indicative cost levels agreed with the Government.

The Board accepts that the biggest stumbling block to the introduction of RET is the cost of implementation. On the basis of the 1974 formula contained in "Roads to the Isles", the introduction of RET would add around £4.5 million to the existing level of subsidy on Scottish ferry services; the full implementation of RET based on running costs would add perhaps £5 million on top of that, making a total required subsidy for 1980 of about £15 million. The attainment of that level of subsidy would clearly be a long-term objective but the Board believes it to be a legitimate one. Successive Governments have tended alternately to control the level of subsidy and then to allow it to increase, usually during periods of rising fuel costs. It would be much more desirable for Governments to link each year's subsidy to that implied by the full implementation of RET with progressively smaller gaps between actual charges and the desired RET fare structure.

When the cost of implementing RET is considered, it should be noted that the cost of building a road network to the islands of equivalent length to the present ferry system would be extremely high. The Board has calculated (see "International Ferry Comparisons", HIDB Transport Research Paper 2) that a subsidy based on the amortised cost of this theoretical road construction to the Western and Argyll islands would cost at 1977 prices between £10.5 million and £18 million annually, depending on the standard of road. This, of course, takes no account of access to Orkney and Shetland.

One of the fears expressed by the Consultative Paper is that of traffic generation as a result of low fares causing increased demand on a number of routes, particularly at summer peaks. It should be noted that these peaks (mainly over summer weekends) are comparatively short-lived, and Adams and McCallum in a report to Caledonian MacBrayne, for example, have concluded that "peak traffic to the Western Isles is handled, on the whole, adequately by the present vessels, routes and frequencies". The Board supports the view that the ferry system in the Highlands and Islands should not be designed to cater specifically for the type of peak demand encountered, and that such rationing devices as advance booking and embarkation tickets should be employed. It should be borne in mind, however, that at most times on most routes there is substantial spare capacity which would not be taken up, even if a considerable volume of new demand was generated by the introduction of a Road Equivalent Tariff.

ROUTE LICENSING SYSTEM

The Board has previously suggested a route licensing system on similar lines to that outlined in the Consultative Paper (paras 21 to 23). The main justification is that, partly because of seasonality, the volumes of traffic on the majority of Scottish ferry routes are so low that normal competition between operators on individual routes would be uneconomic since the total traffic would be divided. Equally it is unfair that there should at present be competition on heavily-trafficked routes between private companies which can choose where they wish to operate and a nationalised company which has to provide services on many loss-making routes.

A system of regulated competition would, therefore, seem to offer the best solution in providing incentives not only to lower costs but also (and this may be even more important) to maintain a high standard of service to the consumer. Much criticism is levelled at existing operators on the assumption that alternative companies could do better and improve upon their performance. The problems of implementation mentioned in para 22 are twofold: (a) control and (b) the likelihood of effective tendering for routes.

(a) The Government would initially become more involved in administering and regulating such a system than under the present arrangements, but in this respect two important points should be borne in mind. Firstly, there are very strong social obligations incumbent on ferry operators to the islands which cannot be fully recognised by setting financial targets; and secondly, there is a need for the establishment of a framework within which both the nationalised sector and the private sector (which the Government envisages playing a larger part) can operate on equal terms. The level of Government involvement in the long-term need not be on a different scale, however, from the negotiations between local authorities and public transport operators in their areas which relate the level of subsidy to the standard of service. Under the current system, consumers and local authorities tend to hold the Government responsible for many aspects of the performance of the ferry system, yet in fact the Government's influence may be limited, except in the long-term.

It might be appropriate that the machinery set up to administer a system of route licensing should also supervise the implementation and regulation of the RET fare structure.

(b) The Board believes that a route-licensing mechanism would operate best if terminals were standardised throughout the Highlands and Islands, and were owned by local authorities or by the Government. If this were the case, the level of capital investment required in ships would not be a major obstacle to the generation of alternative tenders. While there is an efficient second-hand market for ships, the Board considers that the introduction of a limited range of standardised vessels on most routes (as proposed in the forthcoming paper on the long-term restructuring of the ferry system) would best facilitate the availability of ships.

APPENDIX

Tables 1 and 2 show RET fare structures for cars and commercial vehicles respectively based on both total operating costs and running costs.

The sources of the data on costs are the Commercial Motor Tables of Operating Costs and guide to rates 1979, and since these are compiled in April, the comparison is with the Standard and Discount fares operating at that time in 1979.

The RET rates illustrated are not directly comparable with those in the Scottish Office Consultative Paper, principally for two reasons.

(i) On a number of routes, the Paper appears to assume a longer route distance than that employed by the Board. The distances measured by the Board were those given by the most direct sea routes between the existing terminals (ie avoiding headlands, islands, etc).

(ii) In contrast to its treatment of car rates, the Paper does not adopt a standard vehicle length for all routes in presenting the table of commercial vehicle rates. An average length of vehicle appears to have been calculated separately for each route through dividing the revenue from commercial vehicles by the number carried. This average charge seems then to have been compared with the published rate per metre to arrive at an average vehicle length. The Board believes that this method is confusing, leads to underestimation of the actual average length of vehicle and inhibits comparison among routes. In preparing Table 2 , the Board has therefore shown present and RET rates for a 9-metre commercial vehicle on all routes.

The Board would hope that in future the calculation of RET fare structures and their comparison with existing charges could be based on common assumptions.

TABLE 1

4-METRE CAR RATES (1979 PRICES)

	Standard fare £	Discount fare (multi-journey) £	RET (total costs) £	RET (running costs) £
1 Gourock - Dunoon	2.00	1.58	1.83	0.46
2 Wemyss Bay - Rothesay	2.90	2.12	2.50	0.63
3 Largs - Cumbrae	2.40	1.45	1.00	0.25
4 Lochranza - Claonaig	6.55	-	2.00	0.50
5 Rhubodach - Colintraive	1.65	1.24	0.75	0.19
6 Ardrossan - Brodick	7.60	5.79	4.17	1.05
7 Kennacraig - Port Ellen	10.15	6.47	9.51	2.39
8 Kennacraig - Gigha	7.25	6.17	4.34	1.09
9 Oban - Craignure	8.85	4.07	3.34	0.84
10 Oban - Coll/Tiree	15.35	9.35	14.85	3.74
11 Oban - Lochboisdale	17.65	10.08	24.69	6.22
12 Barra - Lochboisdale	10.20	6.01	7.17	1.81
13 Oban - Colonsay	12.00	7.13	10.51	2.65
14 Oban - Lismore	7.90	4.08	2.50	0.63
15 Fishnish - Lochaline	2.90	1.65	1.17	0.29
16 Raasay - Sconser	2.95	1.68	1.17	0.29
17 Mallaig - Armadale	5.00	3.29	2.00	0.50
18 Uig - Tarbert/Lochmaddy	12.25	6.74	8.17	2.06
19 Scalpay - Kyles Scalpay	1.85	1.10	0.75	0.19
20 Kyle - Kyleakin	1.20	0.77	0.80	0.20
21 Ullapool - Stornoway	15.80	9.46	14.68	3.70
22 Scrabster - Stromness	15.00	-	8.34	2.10
23 Aberdeen - Lerwick	39.50	-	56.88	14.32
24 Aberdeen - Stromness	-	-	-	-

NOTES:

1 The Standard and Discount fares shown are those which applied from March 1979 (for STG routes) and January 1979 (for P&O routes).

2 RET fares are computed on the basis of HIDB route distances, and include a toll element equivalent to 4 km.

TABLE 2

9-METRE COMMERCIAL VEHICLE RATES (1979 PRICES)

		Standard rate £	RET (total costs) £	RET (running costs) £
1	Gourock - Dunoon	12.15	4.35	2.16
2	Wemyss Bay - Rothesay	16.55	5.93	2.94
3	Largs - Cumbrae	16.74	2.37	1.18
4	Lochranza - Claonaig	26.05	4.74	2.36
5	Rhubodach - Colintraive	6.19	1.78	0.88
6	Ardrossan - Brodick	36.16	9.88	4.91
7	Kennacraig - Port Ellen	48.60	22.52	11.19
8	Kennacraig - Gigha	27.90	10.27	5.10
9	Oban - Craignure	39.60	7.90	3.93
10	Oban - Coll/Tiree	74.70	35.16	17.47
11	Oban - Lochboisdale	91.80	58.47	29.05
12	Barra - Lochboisdale	49.50	16.99	8.44
13	Oban - Colonsay	79.20	24.89	12.37
14	Oban - Lismore	31.50	5.93	2.94
15	Fishnish - Lochaline	28.80	2.77	1.37
16	Raasay - Sconser	29.70	2.77	1.37
17	Mallaig - Armadale	24.30	4.74	2.36
18	Uig - Tarbert/Lochmaddy	57.60	19.36	9.62
19	Scalpay - Kyles Scalpay	33.30	1.78	0.88
20	Kyle - Kyleakin	7.56	1.90	0.94
21	Ullapool - Stornoway	73.80	34.77	17.27
22	Scrabster - Stromness	138.65	19.76	9.82
23	Aberdeen - Lerwick	335.70	134.73	66.94
24	Aberdeen - Stromness	265.95	99.57	49.47

NOTES:

1 The Standard rates shown are those which applied from March 1979 (for STG routes) and April 1979 (for P&O routes).

2 RET rates are computed on the basis of HIDB route distances, and include a toll element equivalent to 4 km.