

Contract choice and cost efficiency: the French urban public transport case

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Conference on the Regulation of Infrastructures, June 2015

Objective

The main objective of the paper is to study the impact of different regulatory contracts on the cost efficiency of public transit systems

- A positive analysis approach is taken to study the determinants of regulatory contract choices that in turn impact the operating costs of urban public transport operators in France
- The endogeneity of regulatory contract choices is a central feature of the analysis

The industry

- Organizational background
 - ▶ The local public authority is responsible for organizing urban public transport
 - ▶ It can provide the service itself or delegate this task to a private or public-private transport operator (90%)
 - ▶ In the case of delegation a public-private partnership is established and regulated through an agreement
- Regulatory contracts
 - ▶ The agreement specifies the characteristics of the service to be provided, the resources put at the disposal of the operator and the conditions of subsidizing the service
 - ▶ The two main contract types observed in the industry are fixed-price and cost-plus contracts

Principal-Agent framework

- The Principal asks the Agent to produce a given level of output in exchange for a reimbursement and this relationship is regulated by a contract
- Asymmetric information may give rise to two phenomena:
 - ▶ Operators have better experience and information on the costs of providing the service than local authorities (adverse selection)
 - ▶ The non-observability of effort undertaken by the operator on the delegated operation of the transport service (moral hazard)
- Regulatory contracts could affect the cost-reducing effort undertaken by the operator

Econometric approach

Endogenous treatment-effects model

- Translog cost function

$$\ln C_{it} = \ln C(Y_{it}, w_{it}, Z_{it}, DT_{it}; \beta) + (\alpha_i + \xi FP_{it}) + \varepsilon_{it}$$

- FP_{it} is a binary endogenous variable that stems from an unobservable latent variable

$$FP_{it}^* = \gamma_0 + \gamma_{priv} Priv + \gamma_K Keolis_{it} + \gamma_T Transdev_{it} + \gamma_v Veolia_{it} + \gamma_N \ln N_{it} + \gamma_t t_{it} + \eta_{it}$$

- The value of FP_{it} is taken accordingly to the rule:

$$FP_{it} = \begin{cases} 1 & \text{if } FP_{it}^* > 0 \\ 0, & \text{otherwise} \end{cases}$$

Data and variables

Original database of a 16-year panel of 103 bus networks in France for the years 1995-2010 created from an annual survey conducted by CERTU, GART and UTP

- Cost function [details](#)
 - ▶ Operating costs (C)
 - ▶ Quantity of output (Y)
 - ▶ Input prices (w_L, w_m)
 - ▶ Commercial speed (CS)
 - ▶ Network size (N)
- Contract choice [details](#)
 - ▶ Contract type (FP)
 - ▶ Affiliation to the three major groups (*Keolis, Veolia, Transdev*)
 - ▶ Legal entity of the operator (*Priv*)
 - ▶ Network size (N)

Main results

Parameter estimates of the cost function

Variables	Exogenous contract type			Endogenous contract type		
	Estimates		St. Error	Estimates		St. Error
First order terms						
$\ln(Y)$	0.269	***	0.025	0.230	***	0.020
$\ln(N)$	0.106	***	0.013	0.095	***	0.012
$\ln(CS)$	-0.112	**	0.060	-0.187	***	0.052
$\ln(w_L)$	0.903	***	0.017	0.872	***	0.016
FP	-0.044	***	0.014	-0.236	***	0.013
Second order terms						
<i>Second order terms</i>	yes			yes		
<i>Time dummies</i>	yes			yes		
<i>Network dummies</i>	yes			yes		
Sample size	1349			1349		

Note: ***: Significant at 1%, **: Significant at 5%, *: Significant at 10%.

Operating costs and labor price were normalized to material costs to account for homogeneity of degree one.

As all variables were normalized to their sample mean, the first-order terms can be interpreted as cost elasticities.

Main results

Marginal effects of the contract choice function

Variables	Endogenous contract type		
	Marginal effects		St. Error
<i>Priv</i>	0.113	***	0.034
<i>Keolis</i>	0.102	***	0.024
<i>Veolia</i>	0.035		0.026
<i>Transdev</i>	0.272	***	0.014
<i>N</i>	-0.054	***	0.015
<i>t</i>	0.023	***	0.002

Note: ***: Significant at 1%, **: Significant at 5%, *: Significant at 10%.

Summary

- The results show a significant and important impact of regulatory choices on the operating costs of transport operators
 - ▶ Given similar network characteristics, networks operated under fixed-price contracts appear to exert approximately 20% lower costs
- Ignoring the endogeneity of contract choice could lead to undervaluing the importance of regulatory incentives for the urban transport network