Public Transport - Contract Variation Guidance

Integrated Procurement Resource

NZ Transport Agency Waka Kotahi

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Introduction

Purpose

This document provides nationally consistent requirements and guidelines for Public Transport Authorities (PTAs) when developing public transport operating contracts and approaches to pricing variations during the contract term.

Audience

The intended audience includes people new to the subject of variations as well as experienced practitioners. Accordingly, this document covers both first principles, along with more detailed guidance and requirements.

Relevant legislation

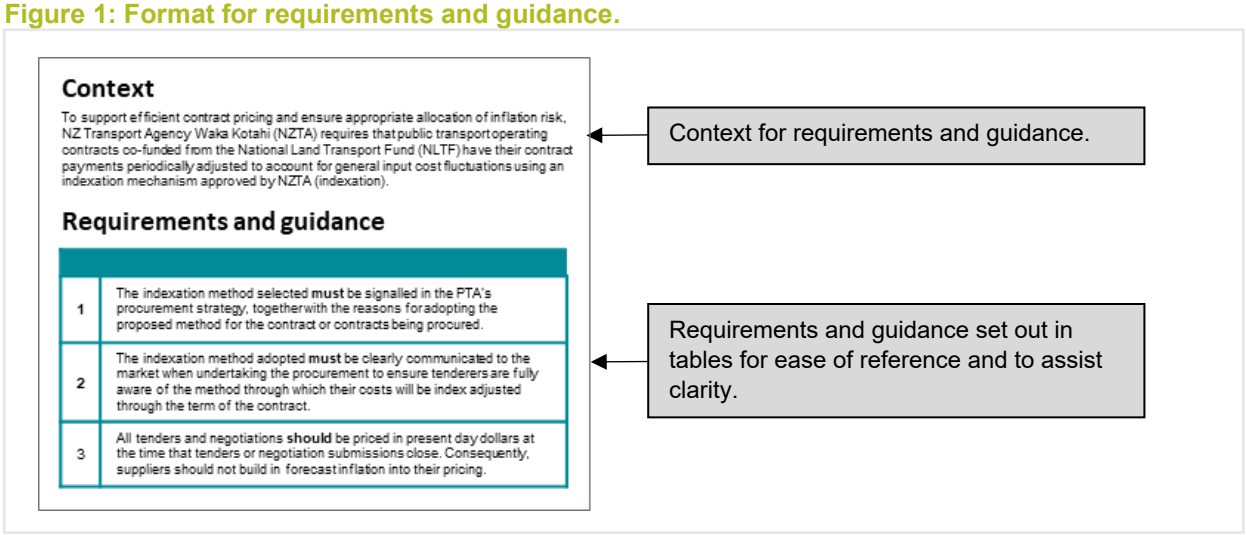
Under the Land Transport Management Act 2003 (LTMA):

- Activities funded from the NLTF must be procured in accordance with procedures approved by NZTA[1]. Aligning with nationally consistent minimum requirements and guidance for variation to bus operating contracts forms part of obtaining procurement procedure approval for public transport operating contracts.
- Planning, procuring, and operating public transport services must be carried out in an open and transparent manner, including with respect to operating costs[2]. Approaches to contract variations must therefore contribute to openness and transparency.

Using this document

For ease of reference and to assist clarity, this document tabulates requirements and guidance as illustrated in Figure 1 where relevant.

Figure 1: Format for requirements and guidance.



The following terms are utilised to distinguish between requirements and guidance:

[1] Section 25 of the Land Transport Management Act.
[2] Section 116 of the Land Transport Management Act.

- "**Must**" denotes requirements. This term refers to content that PTAs must adhere to. These requirements can stem from either a statutory provision within the LTMA or statutory powers granted to NZTA under the LTMA, such as defining conditions of receiving funding from the NLTF or approving procurement procedures.
- "**Should**" and "**May**" denotes guidance. The term "should" indicates strong recommendations or best practices, while "may" suggests optional guidelines.

NZTA may update requirements and guidance from time to time.

Related documents

Variations, indexation, and pricing workbooks are closely linked components of public transport operating contracts:

- **Pricing workbooks** define the cost structure of a contract, including how prices are broken down into transparent cost components and indexation categories. [Insert reference to Price Book guidance]
- **Indexation** adjusts contract prices over time to reflect changes in input costs such labour and energy (e.g. electricity and diesel). The elemental indexation methods require some information from the pricing workbook to be maintained over the life of the contract. [Insert reference to Price Book guidance]
- **Variations** methods rely on pricing workbook to provide a trusted and transparent basis for pricing contract changes over time. Variations also need to clearly link back to relevant indexation categories.

It is important to develop these components in a coordinated way when developing contracts and preparing for a competitive tender process. It is therefore important to read this document alongside the other guidance referenced above.

Contract variation methods

Overview

Purpose of variations

- The purpose of variations is to enable PTAs and PTOs to implement service delivery changes successfully over the life of the contract.

Risk allocation

The recommended contract variation regime has been designed based on the following assumptions with respect to contract risk allocation:

- The PTA sets the service and timetable requirements and is therefore best placed to manage risks associated with unknown future changes to planned service volumes.
- The Public Transport Operator (PTO) is best placed to manage the efficient deployment of resources on the network (e.g. to minimise out-of-service running based on tendered assumptions).
- The PTA should take some risk, with appropriate contractual mechanisms, where this reduces the need for PTOs to include significant risk price premiums. For example:
    - While cost inflation risk is managed by the PTOs, this is mitigated through contract price indexation (PTAs and NZTA Waka Kotahi)
    - Where out-of-service risk for service variations may result in material impacts on dead running, this may be mitigated by specified tolerances and effective, transparent monitoring & reporting.

Pricing principles

In addition, the following pricing principles have been adopted for the purposes of designing the contract variation regime:

- The contract price adjustment should reflect the underlying changes in cost items attributed to the contract variation.
- The administration of contract price adjustments should be simplified to reduce contract management burden on both the PTA and PTO where cost relationships are reasonably predictable.
- Where cost relationships are less predictable there should be mechanisms for managing cost uncertainty to reduce the need for the PTO to include price risk premiums.

Variation methods

This document defines three variation approaches:

- **Pre-priced options:** Where variation options are known at the time of tendering and can be competitively priced by PTOs, with the right for a PTA to proceed or set aside the option during the contract term.
- **Rate card method:** For routine variations over the term of a contract with pre-agreed pricing elements, risk apportionment, and procedures.
- **Net financial impact method:** For unforeseen or unique circumstances handled on a case-by-case basis, with specific procedures for open book negotiation and approval to ensure fairness and transparency.

Further guidance and requirements for each method are provided in the balance of this document.

Pre-priced method

Overview

Pre-priced options are a method for pricing known but unapproved variations at the time of tender. They allow the PTA to secure competitive pricing in advance for changes that may be implemented during the contract term. By way of overview:

- The variation option (or options) is included in the tender documents with a clear scope and pricing template.
- Tenderers provide a price or pricing formula for the option.
- The PTA retains the right to proceed or set aside the option during the contract term.
- If approved, the option is implemented at the pre-agreed price.

Benefits

- Locks in competitive pricing early.
- Reduces future negotiation and admin effort.
- Provides cost certainty for both parties.

Risks

While pre-priced options can offer pricing certainty and reduce administrative effort, they can also introduce risk for PTOs—particularly when scope, timing, or scale are unclear. These risks may lead to conservative pricing or risk premiums being built into bids.

To encourage efficient and competitive pricing, it is important PTAs consider potential risks from a PTOs perspective and mitigate avoidable risk. The table below outlines some potential risks and possible mitigations. However actual risk depends on context, which varies by location and contract.

Risk	Description	Potential mitigation
Scope uncertainty	Vague or unclear scope may lead to conservative pricing / risk premiums.	Include clearly define scope, assumptions, and timing in tender documents.
Timing risk	Delayed activation may cause cost increases or availability issues.	Indicate likely activation timeframes. Include a clearly defined validity period beyond which the PTA forfeits the right to proceed without a pricing review and potential adjustment.
Volume or scale risk	Uncertain scale may lead to risk premiums in pricing.	Include clear assumptions and associated ranges / tolerances in tender documents.
Competitive disadvantage	Uncertainty around how the variation option will be evaluated and its effect on winning the tender.	Provide clarity on evaluation criteria and process.

Rate card method

Overview

The standard approach for pricing routine service level variations in public transport operating contracts is the "rate card approach". This method allows contracting parties to quickly price routine variations, such as timetable amendments, using predefined variation rates as outlined in Table 1 below:

Table 1 Service variation rates

Variation rate	Purpose
Per hour rate ($/Hr)	To account for bus driver labour costs.

Per kilometre rate ($/KM)	To account for vehicle operating costs that are a function of how much a bus is utilised.
Per vehicle rate ($/Bus) for operating costs	To account for vehicle operating costs that exist irrespective of how much a vehicle is used.
Per vehicle rate ($/Bus) for capital / asset costs	To account for vehicle capital costs related to ownership of the vehicle assets.

The price of a contract variation is determined by summing the relevant rate card elements. For example, if a timetable variation results in an increase or decrease to:

- Total driver hours per year, and
- Total kilometres per year, and
- The total number of buses within a contracted fleet

Then the variation price would be calculated as follows:

***Variation to AGP** = (annualised change in driver hours × per hour rate) + (annualised change KMs × Per KM Rate) + (change in number of buses × [Per Vehicle Rate operating costs + Per Vehicle Rate capital / asset costs])*

Requirement and guidance	
1	**Rate card method as standard** All public transport operating contracts **must** include a rate method for pricing contract variations.
2	**Determining variation rates** Variation rates **must** be sourced during the tender. This approach supports competitive tension and gives PTAs greater confidence that future variations, calculated using rate cards, offer value for money. Where rates are negotiated later, this **should** be clearly justified and treated as an exception, requiring additional effort to ensure value is maintained.

The following sub sections provide context and guidance for designing rate card approach.

Cost elements

Table 2 sets out the intended relationship between variation rates and typical cost items related to each.

Table 2 Cost elements

Variation rate	Cost category	Cost items
Per hour rate ($/Hr)	Bus driver labour	Bus driver remuneration & on-costs
Per kilometre rate ($/KM)	Maintenance	Mechanic remuneration & on-costs
		Cleaner remuneration & on-costs
		Parts, materials and consumables
		Outsourced maintenance and cleaning
	Energy consumption	Energy consumption by bus motive power (e.g. electricity, diesel, hydrogen)
	Road User Charges (RUC)	By NZTA RUC class

Per vehicle rates ($/Bus)	Incremental vehicle fixed costs / overheads	Costs that remain constant irrespective of vehicle use, such as vehicle insurance, registration and licencing.
	Capital / asset costs	Cost of providing buses such as financing, amortisation, lease charges, and other related costs.

Benefits and risk

Being clear about benefits, limitations and key risks is an important element of establishing a rate card method.

Benefits

The rate card method has the following key benefits:

- **Certainty and efficiency:** Predefined rates provide clear and predictable costs for routine variations for both PTAs and PTOs and simplifies the process of pricing variations, saving time and administrative effort.
- **Incentive and risk allocation:** Design choices can help to align risk with the party best able to manage it. For example, different design approaches variation rates help incentivise:
    - Efficient network and timetable design by PTAs.
    - Efficient resource deployment (e.g. minimising dead running) by PTOs.
- **Transparency:** The use of predefined rates enables transparency in how variation costs are calculated, fostering trust between contracting parties.

Risks

The rate card method has the following limitations and key risks:

- **Context:** While the rate card method can cover a range of variation scenarios, it is not the most effective method for every scenario, especially those with unique or unforeseen circumstances.
- **Cumulative change:** Variations can accumulate into substantive operational changes, potentially leading to misalignment between adjusted contract prices and actual service delivery cost. This could lead to higher prices for PTAs than might otherwise be warranted, or eroded margin or even lead to a loss-making situation for PTOs, depending on the nature of the variations over time.

PTOs will price in risk based on their interpretation of tender requirements, contract terms, and operating context. To help enable PTOs price contracts efficiently, it is important PTAs avoid unnecessary risk and clearly apportion the balance.

The following sections provide guidance on different variants for each rate card element and how they can be used to apportion and manage risk differently. By way of summary, the following elements each have sub-options:

- Treatment of profit / margin
- Treatment of in-service and out-of-service time and distance
- Treatment of cumulative change

When developing a rate card approach for a given contract, a PTA will need to select the approach for each element that best suits the context of that contract, with the overarching aim of obtaining the best value for money.

Treatment of profit / margin

When designing a rate card methodology, PTAs must consider early on how they intend to treat profit or margin within variation rates. Margin is a critical component that supports supplier participation, encourages competition, and underpins the financial sustainability of service delivery over the contract term.

The approach to margin should be clearly defined and consistently applied across the rate card framework. Importantly, the chosen approach may influence other design decisions—such as how rates are structured, evaluated, and applied in variation calculations.

There are two primary approaches:

A. **Integrated margin**: Under this approach, the PTA will design the rate card approach with the expectation PTOs will incorporate their desired margin directly into the variation rates submitted at tender. This simplifies the rate structure and application but may reduce transparency and limit the ability to reuse rates for other purposes (e.g. Net Financial Impact (NFI) method).

Variation rate	Metric
Per hour rate	$ / Hr inclusive of margin
Per kilometre rate	$ / KM inclusive of margin
Per vehicle rate (operating)	$ / per bus inclusive of margin
Per vehicle rate (capital / asset)	$ / per bus inclusive of margin

B. **Separable margin**: In this approach, the PTA will design the rate card approach with the expectation PTOs will submit variation rates exclusive of margin and will separately bid a margin rate (expressed as a percentage). The margin is then applied to the total variation value calculation. This method enhances transparency and allows for clearer differentiation between operational costs and margin.

Variation rate	Metric
Per hour rate	$ / Hr exclusive of margin
Per kilometre rate	$ / KM exclusive of margin
Per vehicle rates	$ / per bus exclusive of margin
Margin	% applied to total variation value

PTOs will price rates based on their cost structures, assessment of risk and competitive tension. Note margin may be different between variation rates and the base price, and PTAs should consider whether to align the approach to margin between all elements or not.

While pricing decisions ultimately rest with the PTO, PTAs must clearly communicate the intended pricing basis in tender documentation. This includes specifying whether rates should be inclusive or exclusive of margin, and how margin will be treated in variation calculations.

Clear guidance ensures consistency across bids, improves comparability, and supports fair and transparent evaluation. Both integrated and separable margin approaches are valid, and the choice should align with the contract's objectives and context.

Requirement and guidance	
2	**Standard approach** Question for sector consultation, should there be standard approach? PTAs **may** use alternative approaches where more effective for the specific context of a contract, having regard to transparency, intended risk and incentive allocation and obtaining good value for money.
3	**Tender bid requirements** PTAs **must** explicitly state the intended treatment of margin with respect to variation rates in the tender documentation, tender price submission template, and contract terms.

Treatment of in-service and out-of-service components

When designing the rate card method for a specific contract, PTAs must consider how to treat in-service and out-of-service time and distance. The choice of method directly affects how risk is apportioned between the PTA and the PTO.

There are three primary approaches:

A. **In-service only:** In this approach, variations are priced solely on the change in-service hours and KMs – i.e. the time and distance when a bus is available to the public. This approach places the risk of out-of-service operations (e.g. dead running) on the PTO, which will factor an allowance for dead-running into its rates. It incentivises efficient scheduling and depot placement, as PTOs are not compensated for additional out-of-service time or distance beyond the allowance they have made. This is suitable where future timetable or network changes are unlikely to result in excessive or atypical dead-running. This approach requires PTOs to tender variation rates on the basis of in-service km and hours ($/in-service km and hour) only.
B. **Capped:** Variations are priced based on in-service metrics up to a defined threshold of out-of-service operations, beyond which the PTO is compensated for out-of-service time and distance that exceed the threshold. This approach shares risk between the PTA and PTO. It provides a baseline incentive for PTOs to optimise out of service elements while limiting pricing risk for atypical scenarios. This approach places some out-of-service pricing risk with PTAs. Suitable where both parties influence operational efficiency. This approach requires PTOs to tender out-of-service variation rates ($/non-service km and hour) in addition to in-service variation rates ($/in-service km and hour).
C. **Total change:** Variations are priced on the total change in hours and KM, including both in-service and out-of-service components. This approach places out-of-service pricing risk with PTAs. Appropriate where PTAs have significant influence over operational design. This approach requires PTOs to tender variation rates on the basis of total km and total hours ($/total km and hour).

Table 3 method comparison

Considerations	Method variants		
	A: In-service only	B: Capped	B: Total change
Pricing premiums	Higher: PTO risk may lead to higher variation rates at tender to compensate for uncertainty.	Lower: Moderates risk exposure for both parties, potentially leading to efficient pricing of variation rates.	Lowest: PTO risk may result in more competitive variation rates, but overall costs may be higher if inefficiencies are not managed.
Transparency	Lower: Simple but may obscure total cost drivers.	Higher: Clear rules for when out-of-service costs apply, full visibility of cost components.	Higher: Full visibility of cost components.
PTO risk exposure	Higher: Bears all risk for out-of-service operations.	Shared: PTO bears some risk, PTA covers atypical scenarios.	Lower: PTA bears full risk of operational design.
PTA risk exposure	Lower: Avoids paying for inefficiencies best manged by a PTO.	Shared: PTA accepts some exposure to out of service elements from effects of network design.	Higher: PTA pays for all operational impacts, with less incentive for PTO efficiency.
Incentives for efficiency	Strong: Incentivises efficient depot placement and scheduling.	Balanced: Encourages efficiency within capped limits.	Lower: Limited incentive for PTO to optimise operations.

Admin burden	Lower: Simple to calculate and apply.	Higher: Requires monitoring of thresholds and service mix, and PTA to have scheduling capability for monitoring / testing.	Higher: Requires detailed tracking of all service components, and PTA to have scheduling capability for monitoring / testing.
Relational delivery	May create tension if out-of-service impacts are driven by PTA decisions but not compensated, potentially straining trust and collaboration.	Supports a balanced approach, recognising both parties influence operational efficiency.	May create tension if PTA perceives out of service elements are not being managed efficiently by PTO.

Requirement and guidance	
1	**Standard approach** Question for sector consultation, should there be standard approach? PTAs **may** use alternative approaches where more effective for the specific context of a contract, having regard to transparency, intended risk / incentive allocation and obtaining good value for money.
2	**Setting thresholds for the capped method** PTAs **should** consider applying the capped method and setting appropriate thresholds. This should include: • Supplier market engagement conducted prior to tendering, to understand typical out-of-service ratios and industry experience. • PTA's assessment of potential service delivery change scenarios. • PTA's own due diligence, considering the specific nature, scale, and operational context of the unit contract(s) being procured. Where a PTA adopts the capped method, the threshold **must** be clearly stated in both the tender and contract documents, to ensure suppliers can price variation rates accurately. This approach helps ensure that thresholds are practical, transparent, and align with the PTA's intended allocation of risks and incentives, while also allowing suppliers to price variations rates accurately. Where a PTA does not adopt the capped method, it **must** ensure this is clearly stated in both the tender and contract documents. Variations under the capped method are priced based on in-service time and distance, up to a defined out of service running threshold as a proportion of in-service running. Once this threshold is exceeded, the PTO is compensated for out-of-service impacts greater than the threshold.

Treatment of cumulative and step changes

The rate card method assumes that fixed overhead operating costs remain relatively stable within the expected bounds of service changes over the contract term.

However, this assumption may no longer hold when cumulative service variations, whether increases or decreases, reach a scale that causes a material step change in the PTO's fixed cost base. These impacts may include step changes in depot capacity, supervisory staff, or fleet utilisation, which are not adequately captured by rate card method. This can lead to excessive risk premiums or future pricing disputes.

To manage this risk and provide greater certainty to both parties, the following approach is recommended:

Requirement and guidance	
1	**Threshold-based trigger for Net Financial Impact (NFI) process** Contracts **should** include a clearly defined cumulative service variation threshold, beyond which either party **may** formally trigger a Net Financial Impact (NFI) process. The threshold **should** be determined through market engagement and analysis of the expected variability in the network over the contract term. This needs be consistent with a PTA's planning documents (e.g. RPTP) and planned growth / service delivery changes. The threshold **must** be clearly stated in the contract and expressed as a percentage of the original contracted service hours or KMs at tender time.
	Obligation to engage in good faith If the threshold is reached, the NFI process **may** be triggered by either party. Both parties are then obligated via appropriate contract terms to engage in the process in good faith. This may include: • Open-book sharing of relevant cost data. • Joint assessment of whether cumulative changes have materially affected the cost structure. • Negotiation of a fair and reasonable adjustment to pricing and/or contract terms. While the right to trigger the process should be certain, the outcome of the process cannot be predetermined. This ensures flexibility while maintaining fairness and transparency. If the parties are unable to reach agreement through the NFI process, either party may refer the matter to the contract's dispute resolution mechanism. This ensures that unresolved issues do not remain indefinitely open and provides a structured path to resolution.

The following sections provide specific guidance for design of each of the three rate card elements.

Rate card design - per hour rate

Bus driver labour is a core cost in delivering public transport services. The per-hour rate card is used to calculate the labour component of contract variations.

Base costs and on-costs

Two key components should be considered when determining a per-hour variation rate:

- **Base Labour:** This is intended to reflect the weighted average of wage rates paid to drivers across the PTO's workforce. Being a weighted average, a per hour variation rate will not directly match the wage of any individual driver. May differ from wage-related figures presented in the pricing workbook associated with the Annual Gross Price (AGP) submitted at tender.
- **On-Costs:** These are additional indirect costs incurred by the PTO on top of base labour. On-costs are often expressed as a percentage of the base labour rate and may include allowances, leave entitlements, payroll tax, superannuation, and administrative overheads.

Cost structures can vary significantly between PTOs due to differences in workforce strategies, regional labour markets, and employment agreements. When designing a rate card, PTAs should anticipate different base and on-cost rates because:

- Some PTOs may offer flat wage rates, while others provide higher pay for unsociable hours (e.g. early mornings, late nights, public holidays).
- External factors such as regional wage pressures, collective bargaining outcomes, and legislative changes can influence wage structures.

To support transparency and collaborative contract management, especially in response to unforeseen changes (e.g. legislative changes affecting leave entitlements), PTAs should request information about assumptions used to calculate the variation rate as part of the tender process. This promotes a shared

understanding of cost drivers and basis for understanding potential change of the term life of a contract. On-costs may include some of the following:

- Annual Leave
- Statutory holidays
- Sick Leave
- Bereavement Leave
- Domestic violence leave
- Kiwi Saver
- ACC
- Training
- Out-of-service hours (dead running)
- Penal rates
- Allowances

Rate card structure

PTAs may request a single rate for each bus type that applies to all scenarios, or it may seek differentiated rates where this is warranted. For example, differentiated rates may be used to distinguish between peak and off-peak, or to distinguish between different bus types (e.g. Medium Vehicle vs Large Vehicle, Electric vs Diesel).

Depending on context, differentiated rate structures can help reduce pricing risk for PTOs and potentially enable more competitive pricing for PTAs. However, increased differentiation also adds complexity, making it more administratively intensive to calculate and manage contract variations. If a PTA includes the ability to submit differentiated rates in a tender, PTOs should only be required to submit rates relevant to their cost structure. Leaving irrelevant categories blank helps align the rate card with actual cost structures and avoids unnecessary complexity.

Each method has it merits and drawbacks. The following table provides a high-level comparison.

Table 4 method comparison

Considerations	A: Single rate method	B: Differentiated rates method
Pricing premiums	Higher: PTOs may include a buffer to cover variability risk (e.g. risk of service mix skewing toward higher cost scenarios overtime).	Lower: Rates are more tailored to actual cost conditions, reducing need for risk premiums.
Cost accuracy	Lower: Blended rate may not reflect true cost of specific variations.	Higher: Better alignment with actual cost drivers
Transparency	Lower: Cost drivers are blended and less visible.	Higher: Fosters shared understanding of cost component and drivers.
PTO risk exposure	Higher: Bears risk of service mix skewing toward high-cost periods.	Lower: Compensated based on actual service timing.
PTA risk exposure	Lower: Pays a fixed rate regardless of context.	Moderate: Cost varies with service mix (e.g. more public holidays) but PTA can mitigate through for timetable design.
Incentives for efficiency	Weaker: Simplicity may obscure cost drivers and reduce incentive to optimise scheduling.	Stronger: Clearer cost signals support efficient planning and delivery.
Admin burden	Lower: Simple to apply and manage.	Higher: Requires more detailed oversight and management by both parties.

Relational delivery	May erode over time if PTO feels undercompensated or PTA feels overcharged.	May encourages greater trust and ongoing dialogue.

Requirement and guidance	
1	**Method selection** PTAs **should** select a method based on the specific context of a contract, having regard to desired transparency, capability and capacity, intended risk / incentive allocation and obtaining good value for money.

Rate card design – per kilometre (KM) rate

The per kilometre (per km) rate accounts for vehicle operating costs that vary with the distance a bus travels. This rate is essential for capturing the marginal cost of service delivery involving changes to distance travelled.

Rate card structure

The structure of per KM rate is influenced by several factors, including:

- **Vehicle Size:** Larger vehicles typically incur higher fuel, maintenance, and tyre costs.
- **Motive Power:** Different propulsion types (e.g. diesel, electric, hydrogen) have distinct cost profiles, including energy consumption, maintenance regimes, and infrastructure requirements.
- **Indexation categories:** Different components that make up a per KM rate sheet back to different indexation categories necessitating an elemental approach to structuring the rate card.

Cost type	NZTA cost component index
Maintenance	Other (PPI road transport, excl. fuel, road and water transport)
Diesel	Commercial diesel (bulk)
Electricity	Electricity (commercial consumers)
RUC	RUC (representative bus rates)

To ensure fair and accurate pricing, per km rates should be differentiated based on key characteristics for vehicles included within the contracted fleet. The following table provides an illustrative example

Component	Vehicle type 1	Vehicle type 2	Vehicle type 3	Definition
Maintenance	$	$	$	e.g. per in-service km
Diesel	$	$	$	e.g. per in-service km
Electricity	$	$	$	e.g. per in-service km
RUC	$	$	$	e.g. per in-service km
Total rate	$	$	$	e.g. per in-service km

Notes

- Each vehicle type needs to be defined in tender and contract documents, including the rate card table. For example, “Vehicle type 1” may be a large diesel bus, in which case the electricity row would remain blank.

Rate card design – per vehicle rates

Where a service variation results in a change to the contracted fleet size, the PTA may apply a per vehicle rate to adjust the Annual Gross Payment (AGP) when adding or removing vehicles from the contracted fleet.

The per vehicle rate is organised into two key components:

- **Incremental vehicle fixed costs / overheads** such as insurance, registration, and licensing.
- **Capital / asset costs** including financing, depreciation, or lease charges and other capital-related expenses.

PTO risk perspective

From a PTO's perspective, the financial risk associated with changes to fleet size is influenced by several factors—most notably the timing of the variation, and the uncertainty surrounding future technology and asset prices:

- **Late-term variations** (e.g. in the final years of the contract) are particularly risky, where there is uncertainty about the ability to redeploy or recover value from the asset beyond the contract term. This is known as extended asset risk – the risk the PTO is left with stranded or underutilised vehicles after the contract ends. This risk can be addressed through end of term transfer arrangements.
- **Technology and price:** Rapid technological change (e.g. advancements in electric or hydrogen propulsion) and asset prices change (e.g. battery costs, vehicle supply chain volatility) make it difficult for PTOs to accurately price a per vehicle variation rate that remains valid over the full contract term.

These risks are particularly relevant when the PTA requires the PTO to commit to fixed capital rates at the outset of the contract. How risk should be apportioned and how PTOs are likely to view risk is a key consideration for PTAs when designing their rate card approach for the per vehicle element.

Overview of vehicle rate methods for capital / asset costs component

There are two primary approaches for setting these:

- **Fixed Price Method:** The PTO submits a fixed annualised rate per vehicle type at the time of tender. This rate is used to price both fleet expansions and reductions throughout the contract term. It offers simplicity and predictability but may expose PTOs and PTAs to pricing risk if asset costs or technology change significantly over time. Refer discussion below for further detail.
- **Prescribed Capital Recovery Method:** Under this method, the PTA sets a clear formula for calculating the capital charge per vehicle, giving both parties certainty about how vehicle value will be determined during variations and at contract end. While the formula is fixed at tender time, some inputs (e.g. the vehicle's capital cost) can be confirmed later during the term of the contract. This provides pricing transparency and flexibility to reflect market conditions at the time of variation. This can work alongside the vehicle being transferred to the PTA or its nominee at the end of the contract. Because the PTA takes on the long-term asset risk, it gives the PTO more certainty and potentially enables more efficient pricing. Refer discussion below for further detail. It can also be used for non-transferring assets.

Each method has merits and drawbacks. The following table provides a high-level comparison.

Table 5 method comparison

Consideration	A: Fixed price	B: Prescribed capital recovery
Pricing premiums	Higher: PTOs may include a buffer to cover future cost uncertainty and late-term risk.	Lower: Pricing is tailored to actual cost inputs at the time of variation.
Cost accuracy	Lower: Fixed rates may become misaligned with actual market conditions over time.	Higher: Reflects real-time asset costs and recovery assumptions.

Transparency	Moderate: Based on submitted assumptions but not always visible to PTA.	Higher: Clear breakdown of cost drivers and recovery parameters.
PTO risk exposure	Higher: Bears risk of cost escalation or stranded assets, especially for late-term changes.	Lower: Recovery is structured around actual variation timing and PTA-defined parameters.
PTA risk exposure	Lower: Pays a fixed rate regardless of market changes and is not exposed to extended asset risk.	Higher: PTA takes on extended asset risk where the assets transfer at the end of term, and takes on future capital cost (price) risk for assets.
Incentives for efficiency	Weaker: Less responsive to changes in technology or procurement opportunities.	Stronger: Encourages timely, cost-effective procurement aligned with actual needs.
Admin burden	Lower: Simple to apply and manage using pre-agreed rates.	Higher: Requires more detailed oversight and variation-specific calculations.
Relational delivery	May erode if rates become outdated or misaligned with actual costs.	Supports trust – Enables collaborative, transparent pricing and asset planning.
Indexation	"Other" index category may not provide a good match for cost fluctuation risks associated with fixed rates for new vehicle purchases or re-purposing old / existing vehicles.	If new vehicle capital costs are determined at the time of purchase, indexation is not required.

Fixed price method

Under this method, the PTO is required to tender a **per vehicle rate**—an annualised capital charge for each vehicle type included in the contracted fleet. These rates are used to price both:

- **Fleet expansions** – where additional vehicles of the same type are introduced.
- **Fleet reductions** – where vehicles are removed from service.

The rate may be:

- **Bundled** – A single rate covering the vehicle, battery, and charger.

Table 6 illustrative overview of fixed price bundled rates

Component	Bus type 1	Bus type 2	Bus type 3	Definition
Incremental vehicle fixed costs / overheads	$	$	$	e.g. per vehicle per annum
Capital or lease charge	$	$	$	e.g. per vehicle per annum
Total rate	$	$	$	e.g. per vehicle per annum

Notes

- Each vehicle type needs to be defined in tender and contract documents, including the rate card table. For example, the variation "Vehicle type 1" may be for a large newly built electric bus and Type 2 may be for medium sized existing diesel bus.
- The actual mix of vehicle types will depend on tender requirements and PTO bid responses.

- **Disaggregated** – Separate rates for each asset component, depending on the level of transparency required by the PTA.

Table 7 illustrative overview of fixed price bundled rates

Component	Bus type 1	Battery type 1	Charger type 1	Definition
Incremental vehicle fixed costs / overheads	$	$	$	e.g. per asset per annum
Capital or lease charge	$	$	$	e.g. per asset per annum
Total rate	$	$	$	e.g. per asset per annum

Notes

- Different type of electric bus may require different types of batteries or chargers.
- The actual mix of asset types will depend on tender requirements and PTO bid responses.

To support tender evaluation, the PTA may request PTOs to provide the inputs and assumptions underpinning their submitted rates, such as capital value, recovery period and cost of capital.

Prescribed capital recovery method

In this approach, the PTA specifies the formula used to calculate the capital recovery rate for each asset class (e.g. vehicle, battery, charger). Some parameters are set by the PTA, while others are submitted by the PTO as part of their tender.

This method provides greater control over capital recovery assumptions and may offer better value for money – particularly in a context of evolving technologies and declining asset costs.

Table 8 illustrative overview of PCR method components and potential parameters

Components	Discussion
Capital value / purchase price ($)	Value of asset at time of variation. E.g. purchase price for a new asset or depreciated book value for an existing asset. This may be: • Tendered by PTOs at the time of the tender pricing • Set for any new asset through an agreed process (e.g. obtaining three quotes) • Set by the PTA at the time of tender pricing (e.g. where the PTO is to take on transferring assets)
Residual value ($)	Value of asset at end of term. This may be used in a formula to determine the loss of value over the contract term, or it may be specified by a formula e.g. to agree the end-of-term price of a transferring asset.
Capital recovery period (months or years)	This may be the remaining useful life of the asset at time of variation, or it may be a shorter period for capital recovery – e.g. a new bus may have a useful life of 20 years, but the agreed mechanism may involve capital recovery over 15 years (with the last five years essentially “free” of capital cost). There may be situations where the PTA fixes / requires the period at time of tender (e.g. 20 years for a bus), or where an operator is asked to bid the recovery period (e.g. bidding a ten-year life for a higher quality battery vs an eight-year life for a lower quality battery). PTAs need to take care selecting how to set recovery periods, also taking into account whether assets are transferring or not. For example, if the recovery period for a new bus is set at 15 years, and the bus is not a transferring asset, the PTO would carry the post-contract-term residual value risk (including the potential final five years “free” of capital cost).
Capital / financing rate (%)	The rate of return a business or investor needs to earn on an investment to make it worthwhile based on risk and opportunity cost. This should be bid at time of tender, including a reference rate (e.g. bond rate) with an operator-bid margin.

Formula	Different formulae may be considered, such as an annuity formula (yielding a fixed, monthly amount) or straight-line depreciation plus cost of capital on declining book value. Where vehicles are transferring assets, the formula for periodic payments should align with the formulaic approach used to determine values at the point of transfer.

Combining asset transfer with the prescribed capital recovery method

The Prescribed Capital Recovery Method is particularly well-suited to situations where the PTA intends for vehicles to be transferring – i.e. assets that are transferred to the PTA or nominees (e.g. a successor operator) at the end of the contract.

To enable this, the PTA must define a clear and consistent capital recovery framework at the time of tender, usually in conjunction with the mechanism for establishing the end of term transfer price for a transferring asset. This provides pricing certainty for both parties and ensures that:

- The PTO can recover an appropriate return on capital over the remaining contract term without risk of being left with a stranded asset.
- The PTA gains assurance over future asset continuity of service at a known price.

This approach supports:

- Fair risk allocation between the PTA and PTO
- Transparent and consistent pricing for fleet changes
- Long-term value for money, especially in a rapidly evolving technology environment.

An example Prescribed Capital Recovery Method is provided in Appendix 3.

Requirement and guidance	
1	**Method selection** PTAs **should** select a method based on the specific context of a contract, having regard to desired transparency, capability and capacity, intended risk / incentive allocation and obtaining good value for money.

Net financial impact method

In addition to service variations, the contract will define other change events where the PTO is eligible for a contract variation and an adjustment to the base AGP. These events may be prescribed in both specific and general terms (e.g. compensable change in law) and include cases where the service variation regime provides for circumstances when the AGP adjustment is to be negotiated (e.g. certain types of service change and service changes above a cumulative threshold). The cost impacts of these events generally cannot be anticipated and estimated reliably at the point of tender pricing.

The Net Financial Impact (NFI) method is a principles-based approach used to price unforeseen, complex, or significant contract variations that cannot be reasonably priced using the standard rate card method. It is intended for use only when standard pricing tools are not suitable and a tailored, transparent cost assessment is required.

This method supports value-for-money outcomes by focusing on actual cost impacts and promoting transparency through open-book review. However, it can be administratively intensive and may lead to disputes especially if baseline transparency is lacking. Strong documentation and process governance are essential to ensure consistency and fairness.

The following provides context and guidance for designing an NFI approach.

	Requirement and guidance
1	**National consistency** All public transport operating contracts **must** include a NFI method for pricing atypical contract variations.
2	**Usage of the NFI Method** All public transport operating contracts **must** include a description and definition of when the NFI method would be used. PTAs **should** develop this after pre-tender engagement with the market to understand PTO perspectives for the particular tender. In general, the method should be used where cost impact cannot be appropriately captured using the rate card method.
3	**Application of Principles** Specified NFI mechanisms **should** be consistent with the following principles: • Incremental Costs Only: The PTO is compensated only for the fair and reasonable incremental cash costs or savings directly related to the variation. • No Double Recovery: Costs already covered elsewhere in the contract or unrelated to the variation are excluded. • Value for Money: The PTO must take reasonable steps to mitigate costs and ensure competitive procurement of third-party services. • Open Book: The PTO must submit a transparent NFI proposal, with cost breakdowns and assumptions, for PTA review. Supporting records must be available for inspection.

4	**Basis of pricing**
	Specified NFI mechanisms **must** be aligned with the following for determining the net impact:
	• Calculations must be in real dollars at the date of determination.
	• Inclusions (inter-alia and as relevant):
	  • Operating and capital cashflows
	  • Redundancy costs (excluding accrued entitlements)
	  • Asset sale proceeds
	  • Insurance or compensation received
	  • Cost savings
	  • Impacts on end-of-term payments
	• Exclusions (inter-alia and as relevant):

	• Commercial revenue or profit impacts • GST and income tax • Costs funded or reimbursed separately by the PTA • Costs arising from the PTO's non-compliance • Financial performance regime penalties or incentives • Non-cash impacts A preset or bid margin is applied to net cost impacts.
5	**Payment and Adjustment** • A positive NFI is payable by the PTA to the PTO. • A negative NFI is payable by the PTO to the PTA. • Payments **may** be structured as lump sums, milestones, or annual adjustments. Annual NFI payments **must** be included in the AGP for future indexation. This may involve deflating the amounts to the base indexation date to then carry forward.
6	**Retrospective Review** Where cost impacts are uncertain, the PTA **may** require a post-implementation review of the NFI to ensure value for money.
7	**Minor Variations** For minor changes, the contract **may** allow a simplified quote process instead of the full NFI method.

Tender requirements

The PTA should address the following aspects in their tender documentation and evaluation in respect to the service variation rates.

Bid inputs

The service variation rates will require bid inputs from the PTO as part of their tender submission and will be captured in the tender price template returnable.

The tender documentation should include instructions for the PTO to ensure the bid inputs required are cost reflective and relate only to the cost categories and items set out in Table 2.

Appendix 1 contains a sample bid input table for the service variation rates (assuming the Cost Elemental indexation methods).

Single versus multi-year inputs

The PTA may specify bid inputs for a single year which remain constant in real terms for the term of the contract. This would be appropriate when the cost profile of the contract is expected to remain relatively constant.

If the cost structure is expected to change significantly over the contract term (e.g. due to introduction of new fleet or depots) the PTA may require bid inputs for each year of the contract term.

Price evaluation

Given the potential impact the service variation rates can have on the whole of life costs of a contract it is important that the bid rates are factored into the tender evaluation. This can be achieved through the following means. The evaluation method used should be made clear to the tenderers in tender documents.

- Adjust the tendered AGP for evaluation purposes using the service variation rates for an expected level of service growth during the contract term.
- Compare the bid inputs with corresponding average cost derived from the base AGP and clarify material differences with the tenderer.
- Subject the service variation rates to SME review.

Requirement and guidance	
1	**Different variation rates across years** PTAs **may** require separate variation rates for each year of the contract, where there are good reasons to do so.
2	**Price evaluation approach** PTAs **should** include variation rates in price evaluation. The approach taken **must** be communicated clearly through the tender documents.

Documenting contract variations

Effective management of contract variations requires strong processes, systems and documentation. Note NZTA may audit documentation from time to time.

	Requirement and guidance
1	**Document management** PTAs **must** have specified document management standards and processes, appropriate for large commercial contractual arrangements.
2	**Information management** PTAs **must** provide and maintain a single authoritative source of key pricing and network information, accessible by relevant PTOs. This is important for transparency, managing service changes, and avoiding disputes over key information.
3	**Range of information** As part of the information management above, parties **should** track both in-service and out of service elements (e.g. km and hours). This includes regular reporting, as well as specific variations.

Appendix 1 - Bid input tables

Service variation table (using Cost Elemental indexation method)

Service variation rate	Service unit	Bus type 1	Bus type 2	Bus type …
Hr*	In-service hours	Bid $x.xx		
Km*				
Maintenance*	In-service kms	Bid $x.xx	Bid $x.xx	Bid $x.xx
Diesel*	In-service kms	Bid $x.xx	Bid $x.xx	Bid $x.xx
Electricity*	In-service kms	Bid $x.xx	Bid $x.xx	Bid $x.xx
RUC*	In-service kms	Bid $x.xx	Bid $x.xx	Bid $x.xx
PVR (Operating)*	Peak vehicles	Bid $x,xxx	Bid $x,xxx	Bid $x,xxx
PVR (Capital cost only)	Peak vehicles	Bid $x,xxx	Bid $x,xxx	Bid $x,xxx
PVR (% Cost of Capital)	Peak vehicles	Bid x.x%		

* Inclusive of profit on operating costs

Net Financial Impact	Percentage (%)
Mark-up on operating costs	Bid x.x%

Appendix 2 – Variation template

Contract variation agreement

Contract ID: PTA-12345

Sequential variation ID: VAR-2023-001

Date variation takes effect: 04-06-2025

Parties

PTA:

PTO:

Variation overview

e.g. Increase in service hours and kilometres to accommodate increased passenger demand and improve service coverage in new areas.

Summary of change

Metric	Pre-Variation	Post-Variation	Change
Annual gross price (NZD)	500,000	550,000	50,000
In-Service Hours	18,000	20,000	2,000
Out-of-Service Hours	2,000	2,000	0
Total Hours	20,000	22,000	2,000
In-Service KM	270,000	300,000	30,000
Out-of-Service KM	30,000	30,000	0
Total KM	300,000	330,000	30,000
Fleet total number of buses	50	55	5

Agreement

e.g. The Parties agree to increase / decrease the contract price by XX effective from XX date and add / remove xyz buses from the contracted fleet.

All other terms and conditions of the contract remain unchanged.

Signatures

e.g. Name, signature, date

Appendices (initialled by signatories)

- Pricing calculations
- Updated pricing workbook
- New timetable (if relevant)
- Updated fleet list (if relevant)

Appendix 3 – PCR formula example

The following annuity formula provides an accepted methodology for establishing the end of term transfer price for a transferring asset.

The component P_n represents the monthly PVR (capital) rate that would apply as a variation payment from the point at which the asset is employed in delivering services to the end of term.

Transfer price for a transferring asset