



Major impediments to private participation in urban transportation in Belarus

Summary

Private provision of urban transportation services plays an important role in satisfying customer demand for this kind of socially important service. Yet there are large number of artificially created impediments to further development of public participation, which are discussed in detail in the paper. Among all, this paper is based on the results of the survey of private providers, working in urban transportation, carried on by the German Economic Team in Belarus in September 2005. The paper provides some recommendations on how to foster private participation, including ensuring fair competition with public providers, abolishing superfluous technical requirements and restrictions, and eliminating abuse of the right to control and corruption.

Contents

Summary	1
1. Introduction	2
2. Description of the situation in the sphere of local passenger transportation	2
3. Why should we care about private participation?	3
4. Major impediments to private participation	4
5. Conclusions and policy recommendations	7

1. Introduction

Issues of private provision of public services are discussed worldwide. For developing economies like Belarus, where public funds are short and infrastructure inherited from the Soviet Union has already deteriorated, this issue becomes even more important. The case of private transit providers in Belarus is an outstanding one, as they showed remarkably rapid growth, reaching at least 10% share of the market. Yet the growth of private participation slowed down couple of years ago, due to changing legislative and institutional environment in this sector. Hence, this paper is dedicated to the analyses of factors that prevent development of private providers of passenger transportation services.

In September 2005 the German Economic Team in Belarus conducted a survey (through questionnaire) of private carriers who work in the sphere of local passenger transportation using route cabs and buses. The objective of survey was to determine the most serious problems that prevent the development of local passenger transportation services in the Republic of Belarus.¹ To a large extent, this paper is based on the results of the survey.

This paper describes current situation in public transportation (part 2), provides some arguments for private participation in this sector (part 3) and analyses major impediments to private participation (part 4). Final remarks and policy recommendations can be found in part 5.

2. Description of the situation in the sphere of local passenger transportation

Private firms began entering the urban passenger transportation market in mass by 1999–2000. Private firms and individual entrepreneurs developed quickly due to the absence of administrative impediments, especially in the towns where public companies failed to satisfy the demand for transportation services. Up to 2003 private providers were regulated very slightly, mostly by the local administrations. They gave both licenses and permissions to operate routes while special national legislation was absent. System of regulation was quite obscure providing local administrations with many legal mechanisms to bound development of private participation in public transportation. Since November 2002 Ministry of Transport and Communications started to issue licenses through specially established regional transport inspections. During the period from 2000 to 2005 private providers developed in all regions across the country, occupying along with urban suburban routes – heavily subsidized and supposed to be not profitable.

Private urban transportation became one of the most profitable businesses in the country since many entrepreneurs drew their investments from elsewhere and entered transportation market. Without any government subsidies and credits they managed to make large investments into the sector. Within just two-three years of operation (in 2002) number of private-owned vehicles reached the amount of 8000 or just as many as public companies operate. Beginning from 2002, private firms are providing services for about 20% of the total number of routes.² Establishing new routes by private providers became common practice as well.

All together, there are about 3400 licenses for in-country passenger transportation in Belarus. Only less than a thousand are companies, the rest is individual entrepreneurs. Private owners primarily operate minibuses with the number of seats ranging from 7 to 20. They operate closer to capacity limit than public companies. In this regard, the offi-

¹ The sample included 75 representatives of this business selected in different regions of Belarus and the city of Minsk. The structure of sampling by principle of organizational and legal form of ownership repeated the existing structure of the market: 90% of respondents were individual entrepreneurs, 10% represented legal entities of various types (private unitary enterprises and other).

² In 2003 overall number of routes amounted to 5204 and private providers operated 1141 (21%) of them.

cial figures on the private sector share in the total amount of passenger transportation services (measured as number of passenger carried) that equals only 10%-11% (in 2004-2005, 2001-2003 – about 13%) would seem to be underestimated.

The institutional framework for private passenger transportation companies is very obscure. On one hand, since 2002 the licenses are issued by Ministry of Transport instead of local authorities. On the other hand private transportation companies still have to acquire a permission to work on a specific route from the local authorities. At the local level route tendering procedures are not transparent. The rules of route sharing out among various contractors are not clearly stated and public control is lacking. This leads to ad hoc decisions by local authorities. The role of the local authorities in regulating local transportation market is not defined in national law. In towns where local authorities made the procedure of getting the permission to work on a route complicated and expensive, local passenger transportation markets are not competitive. In such towns private companies are underdeveloped and the service is more expensive than in towns where authorities were more market-oriented.

State owned transportation companies perform as independent legal entities. Their number is 117. These companies are obliged to provide free service or charge lower prices to privileged customers. The law on the state budget ensures subsidization 25% of revenues of local transportation companies (50% in case of Minsk). In practice, however, the "cost plus" approach is used to calculate amount of subsidy for a given enterprise. This subsidy only covers production costs (the difference between costs and revenues) and generally is too small to allow for the enterprise' development. In 2005, revenues of urban public transport covered only 56% of the total costs; for suburban public transport only 61.5%³. The number of privileged consumers is extremely large. For example, in the city of Minsk whose population is 1.8 m people, approximately 800.000 people are privileged passengers, 200.000 of whom are transported free of charge.

3. Why should we care about private participation?

There are a number of arguments that show private provision in many cases can provide a better alternative than public provision for both policymakers and customers.

Ineffective management at public firms – high costs – high tariffs. The management of public companies is often inefficient. There is a complete lack of incentives to decrease employment and lower costs. Public firms rarely think of meeting customers' demand – new routes are not established, traffic of buses is not synchronized with other modes of public transport.

Lack of funds for investments at public firms/local budgets – undersupply of the service. All public firms operate at a loss. Government subsidization is based on "cost plus" approach leading to underinvestment into the transport sector. Public finances are also quite poor especially at the local level to put large sums in vehicles. At the same time, private providers just in two-three year period managed to draw sufficient investments to buy as many vehicles as public providers own. This brought a serious relief to public providers and local budgets.

Poor ecological standard of vehicles in public firms. Lack of investments at public companies leads to deterioration of vehicles. Over 60% of vehicles are older than 10 years⁴. Buses made in the former Soviet block have shorter period of exploitation, consume more fuel and make higher emissions into atmosphere of cities than western-made analogs. Private providers mostly operate vehicles made in Western coun-

³ Data for December-September. In 2004 the ratio was 55.4% for urban public transport and 62.3% for suburban transport. Calculations are based on data from the Ministry of Statistics.

⁴ 01.01.2005, The state program of development auto passenger transportation in 2005-2010.

tries that not so harmful for the environment and also more reliable and comfortable for passengers.

Private participation eliminates overloading of public buses and thus decreases the costs of public transportation companies. Before rapid development of private providers of transportation services public providers were not able to satisfy demand for these services. Circulation of public buses was not intense, long breaks in circulation were normal (for example 2-hour break during lunch time). Buses began circulation later and stopped earlier than private buses. Buses went around overloaded leading not only to discomfort of the passengers (some of them just preferred to walk) but also to the fast degradation of vehicles. This considerably increased the costs of public providers and correspondingly, amount of subsidies to be given to them.

Obviously, in modern Belarus more private participation in transportation market is required to improve the services provided to customers. What matters also is the system of regulation of transportation market that should ensure fair competition between public and private providers.⁵

4. Major impediments to private participation

In the above-mentioned survey, when respondents were asked “What, in your view, are the main problems in the sphere of auto transportation business?” and each of the suggested problems was to be ranged from 1 to 5 points (5 – the most serious problem; 1 – is not a problem at all), the following answers were received (Table 1):

Table 1. Impediments to private participation in the sphere of auto transportation (business survey results)

Problem	Average score*
1. Difficulties with importing vehicles from Western countries	4.9
2. Requirements for equipping of vehicles, including installation of cash registers (KSA)	4.4
3. Obtaining the permission to work on the route on the basis of contest	3.8
4. Interrelationship with the operator	3.3
5. Caps on tariffs for the transportation of passengers	3.0
6. Difficulties with obtaining a license	2.6
7. Excises taxation	2.5

* Average score on a scale from 5 (is the most serious problem) to 1 (is not a problem at all).

Below the most crucial impediments to private participation are described in detail.

Difficulties with importing vehicles from the Western countries. Import duties on vehicles used in commercial passenger transportation were increased to prohibitively high level in 2004.⁶ Private cars can be imported at lower import tariff, the cars from Russian Federation are imported at zero tariff. Increase of duties forced all providers to switch to Russian-made vans, which are less reliable, safe, ecologically-sound and comfortable. This also increases the costs of the service and hence tariffs charged.

Requirements for equipping of vehicles, including installation of cash registers (KSA). According to the numerous legislation acts and instructions a vehicle should be equipped with some equipment which is not clearly necessary. Failure to do so results in revoking the license of a provider.

One example is compulsory use of cash registers. According to the presidential Decree No.4 individual entrepreneurs (in public transportation also) can operate without cash registers because they are subject to flat tax. Yet the Ministry of Transport, using a Resolution of the Council of Ministers⁷, started in 2004 to require installation of cash

⁵ See “Regulation of public auto transport: the main issues”, <http://www.research.by/pdf/pp2005e07.pdf>.

⁶ See “Belarus Infrastructure Monitoring 2005”, <http://www.research.by/pdf/BIM2005e.pdf>.

⁷ No.1388 from 20.10.2003.

registers in private buses. Entrepreneurs who refused to buy one had their licenses revoked. Moreover, tickets are not used for fiscal purposes – individual entrepreneurs simply continue paying flat tax regardless of how many tickets they sell. Mintrans backs up its position saying that passengers should use tickets in the courts as an evidence of being in a bus during an accident. From the legal point of view a ticket can hardly be evidence in the court especially compared to classic evidences like testimony, medical expertise etc. The price of recommended cash register was around USD 450 after the regulation was adopted and later dropped to USD 150. The number of vehicles to be equipped with cash registers is about 8000, so the regulation provided approved firms with overall sales of USD 1.2-3.6 m. From the legal point of view, the installation of cash registers became absolutely compulsory only after October 1st, 2005, when the appropriate resolution came into power. Yet necessity of their use remains questionable.

Recently, in many cities operators forced private providers to launch check-in system for their vehicles. The system is used by state providers to control employed drivers – they should check in at the main (usually 1 or 2) points of the route. It's absolutely unclear why private providers should be integrated into this system, especially not on the voluntary basis and at their own costs.

Interrelationship with the operator/Obtaining the permission to work on the route on the basis of contest. This problem is quite complex and can be also described through the terms of "monopolization" and "discrimination". This can be generally divided into the following issues:

- Monopolization by state transportation companies. In some cities state transportation companies were granted (with no legal basis for that) by local councils the power to regulate the use of road network by private providers. Thus these enterprises perform functions of service provider and regulatory body simultaneously. This is basically prohibited by national legislation – the law "On auto transport and transportation"⁸. The problem exists due to the lack of regulation: national law does not define clearly the role of local authorities.

- Intervention of state transportation firms into the niche of private providers. Private providers generally operate so-called express routes and use minibuses with the number of seats 9-12 (up to 20). A driver charges the fee directly in cash.⁹ In some cities local authorities started to engage in minibus transportation market themselves after private business discovered this niche and proved operation in it profitable. In 2004 a state-owned company bought number of mini-buses in Gomel and took the most profitable routes leaving private providers with the rest. In Minsk, state service provider Minsktrans bought 200 20-seat minibuses formerly operated by a private company. In 2003 this company had been sued and it was essentially forced to sell its buses.¹⁰

- Unequal treatment as compared with state transportation companies. Requirements of all kinds are less strict for state transportation companies than for private firms and entrepreneurs in the business. This concerns mostly technical characteristics of vehicles used (age etc.) and amount of various fees to be paid. While public providers may use 20 year old buses (15 years plus 5 years after reconstruction) private providers are said to be prohibited to operate vehicles older than 10 years after 01.01.2007. Other parameters such the minimal distance between seats or two exits requirement are often ignored in public-owned minibuses. Moreover, there are cases when some private firms were allowed to operate technically unsound vehicles while others were

⁸ Articles 36, 50.

⁹ In some cities private providers also operate regular buses with the number of seats 40 and more. In these buses fee is charged not by the driver but by the special person. As a rule, these buses are also imported used from Western-European countries.

¹⁰ The banking account of the firm was frozen so as it couldn't submit leasing payments to the owner of buses – Daimler Chrysler. After some time passed, Daimler Chrysler had to withdraw the leasing agreement and sell it to the public company – Minsktrans.

refused permissions. Grodno provides an example where private transportation firms were asked by local officials to make contributions to the local budget in order to get permissions for working on specific routes. Some contributions amounted to as much as 10.000 USD. There are some evidences that the use of cash registers is not controlled as in the case of private firms.

- Also, state firms are the first in the line to get permission to operate a route. Public companies do not fall under requirement to participate in route sharing-out procedure. Only private providers have to compete for the right (permission) to operate certain route. Local administrations, especially in large cities limit number of buses on the routes and many entrepreneurs are simply rejected the permission. Needless to say, such protection of the market from new entrants decreases the quality of the service provided (longer time of waiting at a bus stop) and increases price charged.

Caps on tariffs for the transportation of passengers. In 2004, the Ministry of Economy initiated adoption of regulations at oblasts' councils which set the maximum tariffs for private passenger transportation (except for Vitebsk oblast). Legal basis for that was found in the presidential Edict "On some measures of stabilizing prices (tariffs) in Belarus".¹¹ The Edict should only concern publicly owned firms but not private providers of transportation services. The same year in Gomel city private providers were asked by the city council to provide one free seat for veterans and handicapped persons¹². Practice of limiting tariffs and imposing privileges have already resulted in losses for private companies and undersupply of the service.

Unreasonably high number of inspections and arbitrary behavior on the part of controlling bodies. Permanently growing number of inspections by various controlling bodies is one of the main factors that prevent development of local passenger transport. About $\frac{3}{4}$ of the respondents of the above-mentioned survey stated that the number of inspections increased during the last year. On average per year carriers have been subject to inspection:

- by operator of transportation services – 8-9 times,
- by transport inspection – 7 times,
- by road police – 6 times,
- by taxation authorities – 3 times,
- by environmental protection services – 2 times.

In certain cases the number of inspections that 1 carrier was subject to by road police and operator's inspectors has been reaching 100. The frequency and number of inspections that the small business is subjected to (up to 3 employees, and, accordingly, up to 3 transportation facilities) causes concern.

The license can be revoked – and sometimes was – very easily for even minor offences. For a fault of one employed driver, operation of an entire firm can be stopped, leaving other employees and the owner without income, and customers without service.

Also, the results of the survey proved the fears about development of corruption in the process of issuing licenses and permissions for routes. More than 50% of respondents faced corruption directly, and only 47% did not or have hidden such facts. It is important to notice that all interviewed legal entities have faced this problem.

¹¹ No.285 from 19.05.1999.

¹² Private firms generally are not obliged to provide privileges. In many cases the prices charged by private firms resemble the prices of their public competitors (price discrimination).

5. Conclusions and policy recommendations

The factors that prevent the development of private providers of passenger transportation services in Belarus are of a legislative and institutional nature. There are a number of artificially created impediments that do not allow further development of this socially important kind of services. A policy directed towards improving the situation should, in our view, concentrate primarily on the following recommendations:

Abolish limitations on the maximum “age” of a vehicle and minimum number of passenger seats. These limitations paralyze the private passenger transportation market, especially in small and medium size towns, where route cabs account for about 30% of the total volume of transportation.

Enforce fair competition between private and state-owned carriers. The market is monopolized by state-owned carriers; on top of this many of them have been empowered with transportation operator’s rights. Without an independent operator taking decision based solely on economic grounds, efficient development of local passenger transportation is not possible.

Reduce the number of inspections and bring to an end arbitrary behavior on the part of controlling bodies. Unclear regulations and regulations that obviously cannot practically be complied with cripple the development of this kind of services. Entrepreneurs are deterred from investing into this particular sphere of activity and may transfer the already invested resources into other spheres. This results in the deterioration of the social position of the population in the sphere of making use of passenger transportation services. As well, it increases pressures to increase the subsidies provided to the state-owned carriers.

Eliminate corruption in the process of issuing permits for routes. The absence of independent operators in the sphere of transportation results in abuses of power on the part of officials who are responsible for distributing permits for routes between carriers. All possible measures must be taken, first of all of an economic nature (creation of independent transportation operators, establishing an appropriate legislative environment that provides opportunities to appeal the decisions of the tender committees in court) to put an end to such practices.

Lower prohibitively high import duties on vehicles used in commercial passenger transportation. Increase of duties force all providers to switch to Russian-made vans, which are less reliable, less safe, less ecologically-sound and less comfortable. This also increases the costs of the service and hence the tariffs that must be charged (or the subsidies that must be provided). Providers should have the right to freely choose what kind of vehicles to buy.

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