

Our Reference: L98/176

Ms Helen Owens
Presiding Commissioner
Progress in Rail Reform
Productivity Commission
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MELBOURNE VIC 8003

Dear Ms Owens

Thank you for the opportunity to comment on the Productivity Commission's draft report on Progress in Rail Reform.

The draft report provides a useful analysis of the rail industry and the progress to date on rail reform. In recent years the rail industry has been described in terms of "major reform", "renaissance" and "the rebirth of rail". However as the draft report points out, reforms in some areas are slow and several problems identified in the Industry Commission's 1991 report remain unresolved. The Commonwealth is mainly involved in the reform processes that relate to interstate rail services. Here, rail reform received major impetus following the 1997 National Rail Summit and the Intergovernmental Agreement for establishment of the Australian Rail Track Corporation. However, in our opinion and despite the lack of tangible outcomes on key issues to date, the momentum for reform in this sector of the industry may be waning. It will be necessary to maintain the momentum that was developed through the Rail Summit for a lengthy period to realise the improvements envisaged at that time.

Our main concern with the Commission's draft report is that the conclusions and recommendations are not as strong as the supporting text and analysis suggests is warranted. The chapter on competitive neutrality and diesel fuel excise is a case in point here, however it is acknowledged that sections of this chapter will need major revision following the recent outcome of discussions between the Government and the Democrats on diesel fuel excise.

We also think that the vertical separation model remains the best approach for urban systems where competition must be encouraged if urban transport is to fulfil its potential role in our cities in the future. Similarly, the recommendations on further commercialising the rail industry do not convey sufficiently how important it is for governments to take decisive measures to achieving this.

For your consideration, I have attached some more detailed comments which I hope will be of assistance to you in finalising the report.

Yours sincerely

Chris O'Grady
A/g Assistant Secretary
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Comments on Productivity Commission's Draft Report on *Progress in Rail Reform*

Specific comments by the Department of Transport and Regional Services on a chapter by chapter basis are as follows:

Chapter 2 Railways in Australia

While it is understood that Chapter 2 has been drafted on the basis of the most recent available data (1994-95 and 1996-96), the reforms that have been effected in the last 3 years are significant and need to be reflected and/or acknowledged. If later data is not available before the report is finalised, it is suggested that some commentary be provided on whether there have been any significant changes since the last available data.

A key concern to some State governments (and one which seems to influence their commitment to the interstate rail network) is the relative size of the interstate rail freight task compared to the intrastate rail task. The specific point of concern usually expressed in this context is that the size of the intrastate task dominates the rail task to the extent that the interstate task is an insignificant component. There is a concern that reinforcement of this (in many cases) false perception means that States may be reluctant to implement reforms that would benefit interstate rail due to their impact on intrastate rail, with no apparent benefit to that sector.

While the interstate rail freight task in 1994-95 was only 15 per cent of the total rail freight task:

1. Interstate non-bulk rail freight represents approximately 66 per cent of the total non-bulk freight task (on the basis of the draft report's Chapter 2 data);
2. The major coal and many of the major bulk grain movements have only limited impact on the interstate freight line;
3. This level of activity has been achieved in an environment which it can be argued has not been conducive to a high performing rail industry. The statistics are based on 1994-95, when there was little private sector involvement in the industry and the One Nation gauge standardisation had not been completed; and
4. Interstate non-bulk freight, as demonstrated by your Figure 2.5, is a rapidly growing market, and unlike commodity traffic a market where rail has the potential to increase its market share and profitability considerably.

Increased emphasis on the significance of the interstate rail freight task should be made in the report, even though it may represent only a relatively small proportion of the total rail task. Perhaps it would be worth looking at the comparison of dollar values of interstate non-bulk freight with the value of bulk intrastate products which dominate the rail task. In view of the reforms that have occurred in interstate rail and the proposed changes to diesel fuel excise arrangements, some assessment of the likely future for interstate rail would also be relevant in Chapter 2.

Chapter 3 Rail Reform in Australia

We understand that the SRA was separated into four agencies on 1 July 1996 (rather than 1997, page 35).

Chapter 5 Structural Reform

Urban passenger transport (pages 98,99)

We do not agree with the Commission's conclusion that *vertically integrated urban rail networks* is the preferred structure. Regardless of whether urban operations are commercial at the moment, such a structure would preclude the possibility of competition in the future. Urban rail operations are a major component of the rail industry which under private ownership may well prove to be commercial operations. The Sydney metropolitan network in particular would not benefit from such a structure in the long term. Our concern is that decisions to privatise operations as a vertically integrated entity at a particular point in time are often difficult to reverse at a later time when an alternative structure might be more appropriate.

Interstate network (page 103)

As the Commission would be aware, the situation described in this section is precisely the problem that the Australian Rail Track Corporation was established to address. However, the primary concern of States and State track owners is that the costs to the intrastate rail sector of vertical separation and horizontal integration of the interstate network under a single network manager, may outweigh the benefits they would realise from improved access arrangements to the interstate rail market.

Chapter 8 Safety regulation and operating standards

Section 8.1 – 'Safety regulation and accreditation'

An update on recent decisions relating to rail safety by the Australian Transport Council is given under our comments on section 8.3 "Advancing regulatory reform".

Section 8.2 – 'Operating standards and procedures'

The operational uniformity work being undertaken by the Industry Reference Group (IRG) is a joint government and industry initiative which has received positive support from rail sector participants. It is the first time that governments and industry have worked together and jointly allocated financial and human resources to address operational uniformity issues. The Commission should highlight this positive aspect of the operational uniformity work.

The Department endorses the adoption of best practice regulation for activities which may have a significant impact on business. We also believe that if best practice regulation is adopted, then the requirement of a Regulatory Impact Statement (RIS) should not prove to be an onerous task for regulators to comply with and that wherever it is **appropriate** then they should be sought.

We believe that Chapter 8 of the Commission's report needs to clearly separate discussion of existing safety regulation and operational uniformity issues. The codes of practice described towards the end of Section 8.1 (page 175) have not, as indicated in the draft report, been specifically developed as a safety management tool through which to demonstrate compliance with the relevant parts of Australian Standard (AS) 4292.

The main driver behind the development of the codes is the need to facilitate more efficient interstate train operations. Accordingly, the codes aim to remove or minimise jurisdiction specific operational requirements which hinder efficient train operations. Safety is a key element of train operations and the codes will address jurisdictional differences in safe operating practices which impact on efficiency. We therefore suggest that the codes of practice (as a key element of the operational uniformity work) should be discussed in Section 8.2 'Operating standards and procedures'.

At the recent Australian Transport Council (ATC) meeting in Adelaide (April 30 1999) Ministers endorsed the development of an Intergovernmental Agreement (IGA) to provide for interim arrangements to facilitate implementation of the IRG's operational uniformity work. Ministers agreed that the IGA (to be completed by the November 1999 ATC meeting) should contain the following elements:

- Government commitment to a nationally consistent implementation mechanism to ensure timely adoption of uniform operational requirements;
- Establishment of a non-statutory unit attached to the Commonwealth Department of Transport and Regional Services to facilitate and coordinate implementation arrangements; and
- Establishment of Commonwealth custodianship arrangements to provide for ownership of intellectual property and an entity for legal liability issues.

Ministers agreed that the proposed IGA should be finalised for endorsement at the November 1999 ATC meeting."

Implementation is a critical issue for the operational uniformity work and a subsection on this topic could be included in Section 8.2 'Operating standards and procedures' or Section 8.3 'Advancing regulatory reform'. The Commission may wish to note that the ATC decision only provides for interim implementation arrangements for the uniformity work, pending the development of a more permanent mechanism. The interim arrangements were developed to allow for implementation in early 2000, recognising that a more permanent mechanism (such as legislation) would take up to 18 months to finalise. A permanent implementation mechanism is

important to ensure that the uniformity work is sustained into the future and we would support the inclusion of a recommendation to this effect.

Section 8.3 – Advancing regulatory reform

We agree with the Commission's comments in relation to the need for a nationally consistent regulatory approach to rail safety and operational uniformity. To that end, the Commission should be aware of the following recent ATC decisions (30 April 1999).

Rail Safety:

Ministers announced 2 initiatives in relation to rail safety:

- (1) Ministers noted that while the major objectives of the Intergovernmental Agreement (IGA) on Rail Safety, which came into effect in July 1996, have been achieved, interstate rail operators remain critical of the operation of its mutual recognition provisions and the variation in accreditation regimes between states. Accordingly, Ministers agreed that, consistent with the review provisions in the original IGA, and given the continuing need to refine rail safety arrangements, an independent review be undertaken of rail safety in general and, in particular, rail safety on the interstate network. The review is to be completed for consideration at the November 1999 ATC meeting.
- (2) Ministers endorsed adoption of the report on *Independent Investigation and Open reporting of Rail Occurrences* and requested that further development of the Australian Standard AS 4292.7 "Railway Occurrence Investigation" be consistent with its content. A copy of the report is enclosed with this submission.

Operational Uniformity:

Again, we refer to the Ministers' endorsement at the April 1999 ATC meeting, of the development of an Intergovernmental Agreement(IGA) on Operational Uniformity as an interim arrangement to facilitate implementation of uniform operational requirements and rail standards (refer our comments under section 8.2).

In relation to the Commission's request for comment on the different institutional and legislative arrangements outlined on page 187 of the draft report, the independent review on rail safety will address this issue. However your arguments on page 184 regarding existing NRTC and rail approaches suggest that a single national body would remove the potential for jurisdictional interpretations.

In relation to the proposed land transport commission (page 187), the Commission should be aware of the following recent ATC decision:

“Ministers agreed that a National Transport Secretariat be established to directly advise ATC on major issues of National Importance” [ATC Communique 30 April 1999]

The exact role and function of this new Secretariat is still to be determined. A subcommittee has been established to prepare a paper on issues which is to be circulated to ATC members.

In relation to the **Draft Recommendation 8.4** on page 188, we advise that the Commonwealth is already taking a leadership role in this area. As such, the recommendation does not really appear to add much to the debate. If the Commission would like a more substantial process/mechanism to progress regulatory and operational uniformity then it should consider modifying its recommendation accordingly.

Chapter 9 Competitive neutrality

Section 9.2 Competitive neutrality across rail and road transport

Investment in road and rail systems (page 195-207)

The following points are made in relation to the discussion on rail versus road investment (page 195):

- If looking to justify the disparity between the level of road investment and the level of rail investment by governments, one only needs to look at the difference in size of the respective networks;
- The rail network was largely developed before the advent of heavy vehicles on roads. Consequently the rail network represents a mature network with the focus of works on maintenance and realignments, while the road network has until recently been under development to meet current demands placed on the network; and
- The Commission’s analysis does not take into account off-budget investment by organisations such as the Australian National Railways Commission (AN), the Australian Rail Track Corporation (ARTC) and the NSW Rail Access Corporation (RAC). While the RAC is probably the largest rail track investor, AN historically invested substantial amounts into the network that it managed and the ARTC is also expected to undertake investment on the network it manages, on a commercial basis.

We disagree with the observation that governments *have almost ignored [investment] in the railways* (page 195). Such an observation would not take into account the large operational subsidies provided by governments for rail operations over many years, in addition to the substantial investments made by government owned rail entities.

We also disagree with the observation (page 197) that *nearly 70 percent of the interstate standard gauge network is under temporary speed restriction*. Analysis

conducted by Booz Allen & Hamilton for the Department in 1998, identified that approximately 26 per cent of the interstate standard gauge network (excluding Kalgoorlie to Perth) was subject to speed restriction.

The discussion on National Highway investment (page 198) implies that Commonwealth road investment has been high relative to rail infrastructure investment. A critical point omitted from that observation is that the Commonwealth is responsible for construction and maintenance of the National Highway System however it had previously only had any responsibility for track in South Australia (through to Kalgoorlie) through its ownership of Australian National.

As a general comment on this section of the report, there has been considerable criticism of the relative disparity between the level of Commonwealth road and rail funding and the lack of a consistent set of criteria in assessing projects across the two modes. The critical difference between road and rail project assessment is the social criteria and time savings benefits that are evident in assessing roads projects which do not occur to the same extent in rail projects. This difference occurs as a result of the road transport industry sharing the asset with private motorists whereas railways do not have to contend with a similar element of private use.

Another consideration is that, by virtue of the nature of its infrastructure, the railways compete in the less time sensitive segment of the transport market, therefore the value of time savings would not be as high in the assessment of rail projects. Consequently, this means that under consistent assessment criteria a comparable road project will have a higher BCR than an alternative rail improvement project. Unless the assessment of rail projects is able to demonstrate similar social and time value benefits accruing from the investment, under consistent assessment criteria road improvement projects will almost always be favoured as a result of the superior BCRs that are generated.

Under BCR analysis, rail investment would normally be favoured where the assessment is able to take into account additional externality criteria such as the social benefits resulting from the removal of substantial volumes of heavy vehicle traffic from the roads. Such an approach could only be undertaken on the basis of the fundamental presumption that the rail alternative would provide a suitable substitute to road transport.

To some extent, the inability of rail investment projects to compete effectively for Government funding against alternative road investment projects on the basis of their comparable BCRs, is now able to be addressed through the recent establishment of commercially based track owner arrangements in most jurisdictions. The profit motive of track owner organisations means that as an alternative to Government funded investment, the rail industry is now able to determine its own investment priorities based on commercial decision making processes rather than awaiting the allocation of scarce Government funds.

The claim by the Campbelltown and Districts Commuters Association (page 197) regarding the investment requirements on the Adelaide Hills to save 2 hours transit time warrants verification. The ARTC would be best placed to verify this, however it

is our understanding that investment of \$90m would only achieve a very basic realignment within the existing corridor and would save up to 30 minutes while a more extensive realignment costing in excess of \$250m would still only cut 1 hour from the current transit time.

Diesel fuel excise (page 207)

Based on the current arrangement in place regarding diesel fuel excise, it was our opinion that this section needed to be much stronger. There are good arguments that fuel excise rates should clearly differentiate between components of general revenue (payable irrespective of mode), components for external costs related to fuel use (may vary by mode but reflecting real costs) and components of infrastructure usage charge (taking account of alternative access charges applying to each mode).

In light of recent passage of the adjusted GST through the Senate, the above point of view is likely to no longer be a relevant issue.

Chapter 11 The way ahead

As the concluding chapter to the report, this chapter would benefit from a more positive tone being taken in the text. There are a number of times where the word *may* is used (eg pages 243, 244, 247) where the word *would* would send a much stronger message.

The Commission should also take a stronger position in regard to the desirability of privatisation. The conclusion (page 243) should be that privatisation is desirable wherever the industry is operating in a commercial way.