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TTF AUSTRALIA
Tourism & Transport Forum

10 November 2006

Mr Gary Banks
Presiding Commissioner
Road and Rail Freight Infrastructure Inquiry
Productivity Commission
Locked Bag 2
Collins Street East
MELBOURNE VIC 8003

Dear Mr Banks

Submission to the Productivity Commission's Draft Report into Road and Rail Freight Infrastructure Pricing

TTF Australia (TTF) appreciates the opportunity to make a submission to the Productivity Commission's (PC) Draft Report into Road and Rail Freight Infrastructure Pricing.

By way of background, TTF is a national, member-funded CEO forum, advocating the public policy interests of the 200 most prestigious corporations and institutions in the Australian transport, property, tourism and infrastructure sectors.

Tourism is an important driver of regional development. 38 per cent of tourism jobs for example are located outside Australia's capital cities, and tourism employment intensity is higher in regional Australia (6.5%) compared to metropolitan areas (5.3%).[1]

The Australian Government recognises the importance of tourism for regional Australia. In July 2005 the Minister for Tourism, the Hon Fran Bailey MP stated that:

> "The tourism industry is a vital cog in the economic wheel of regional Australia, which generates over $30 billion for regional Australia. Increasing access to regional areas will continue to grow yield and dispersal throughout regional Australia.
>
> …Regional tourism's contribution to Australia's $73 billion tourism industry will continue to increase by opening the gateway to regional communities." [2]

[1] TTF Australia (2004) National Tourism Employment Atlas.
[2] http://minister.industry.gov.au/index.cfm?event=object.showContent&objectID=6055656B-65BF-4956-B89D6AA75B7A3A5C

Great Southern Rail's (GSR) submission to the PC highlights the important contribution their Long Distance Passenger Rail (LDPR) services make to Australian tourism, particularly regional tourism and facilitating the Australian Government's objective of promoting regional dispersal.

GSR accesses rail infrastructure in New South Wales, Victoria, South and Western Australia as well as the Northern Territory and it remains the only national LDPR service in the country. GSR's services provide both scheduled and on demand stops at over 44 remote, rural and regional centres across Australia. In 2005 GSR carried approximately 52K passengers on The Overland, 74K on The Ghan and 79K on the Indian Pacific.

The Ghan alone resulted in over 38K tourist visits to Alice Springs in 2005 which generated an estimated $50.8M in expenditure, creating 190 jobs for the region.[3]

GSR's contribution to regional Australia is estimated at $1B.[4]

The PC has sought comments about the "potential impacts of pricing reform options on rural and remote communities".[5]

While I acknowledge GSR's use of rail infrastructure accounts for a small portion of total usage compared to freight, any pricing reform options will have an impact on its LDPR services.

TTF therefore recommends that the PC take into consideration any potential impacts of pricing reform options on GSR given its important contribution to tourism in rural, regional and remote Australia.

TTF Australia is alarmed by GSR's submission that the magnitude of its access fees, particularly the fixed flag-fall component, threatens the long-run viability of its LDPR services.[6]

The absence of rail infrastructure operators differentiating between freight and passenger services in their pricing structures is a significant impediment to GSR delivering an adequate return on investment.

TTF Australia therefore supports draft recommendation 11.3, and specifically the need to incorporate in all rail access regimes, the pricing principles embodied in Part IIIA of the Trade Practices Act 1974.

The PC in making draft recommendation 11.3 indicated that 'freight's usage of rail is widely viewed as more price sensitive than passenger use'.[7]

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[3] Great Southern Railway (2006) Submission to the Productivity Commission Road and Rail Freight Infrastructure Pricing pg.8.
[4] Ibid. pg 9.
[5] Productivity Commission (2006) Road and Rail Freight Infrastructure Pricing – Discussion Draft pg.1.1.
[6] Op.cit. GSR (2006) pg.10.
[7] Op.cit. PC (2006) pg.5.11.

LDPR however is price sensitive. This is reflected in the evidence presented by GSR in relation to price volume movements for Gold and Red Kangaroo pensioners travelling north of Alice Springs, and on the basis that the intensity of inter-modal competition has escalated with the introduction of low-cost air carriers (including Virgin Blue in 2001 and Jetstar in 2004).

Graph 1 illustrates air and rail usage by domestic overnight visitors over the last six years.[8] From 2000 to 2005 the use of air transport increased 21 per cent while rail use fell by 27 per cent. This change in air and rail usage is also reflected in the year on year growth shown in Table 1.

Graph 1 Air and Rail Transport use by Domestic Overnight Visitors 2000 - 2005[9]

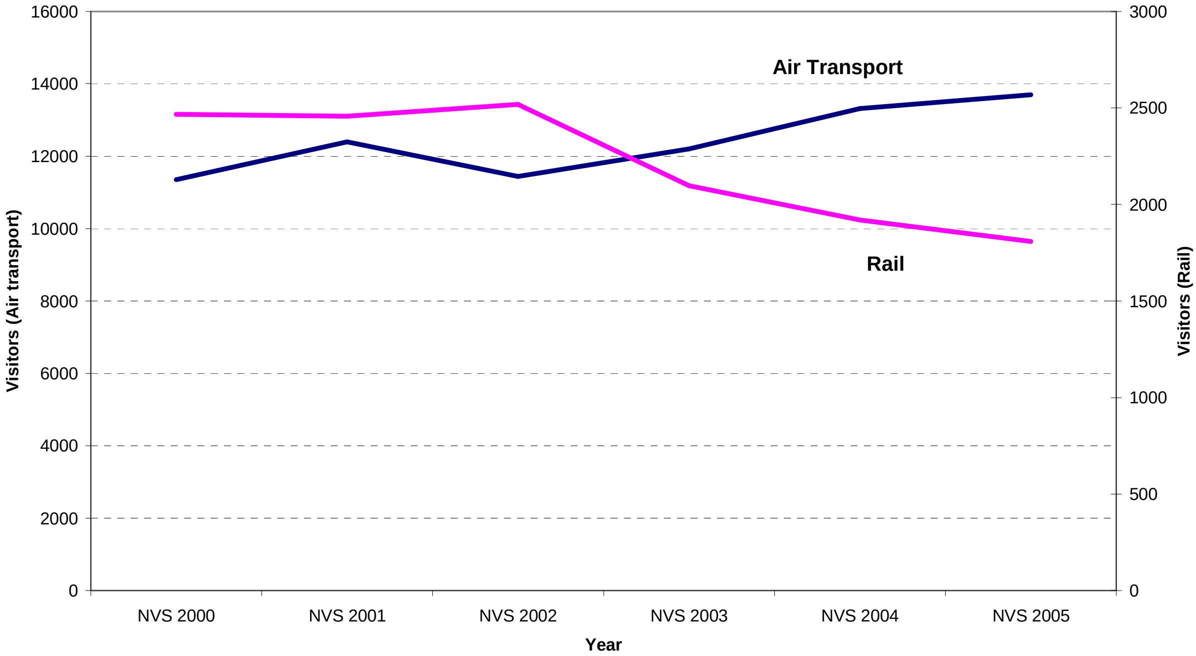

Table 1 Year on Year Growth for Rail and Air Transport 2000 - 2005[10]

	2001	2002	2003	2004	2005
Air transport	9%	-8%	7%	9%	3%
Railway	-0.45%	3%	-17%	-8%	-6%

[8] Data is based on the main transport used by a domestic overnight visitor.
[9] Data source derived from Tourism Research Australia, National Visitor Survey (NVS) – CD Mota.
[10] Data source derived from Tourism Research Australia, National Visitor Survey (NVS) – CD Mota.

I note the Australian Competition and Consumer Commission's (ACCC) view that 'it is extremely difficult to estimate demand elasticities with accuracy'.[11] Albeit, TTF Australia recommends the PC review its observation on price sensitivity comparisons between freight and passenger, and take into account LDPR.

In the Australian Rail Track Corporation (ARTC) Access Undertaking Decision (May 2002), the ACCC accepted that, under certain conditions, price discrimination would facilitate both the efficient allocation of common costs[12], and train operator market entry[13]. The ACCC also stated that the capacity to price discriminate is in fact provided for in the ARTC's current Undertaking.[14]

Appropriately, the PC noted that despite the absence of any 'explicit regulatory prohibitions' that 'it appears rail infrastructure operators perceive that regulators may not find such pricing acceptable'.[15]

Access providers to date have rejected all approaches from GSR to negotiate a pricing structure that recognises LDPR separately.

Explicitly allowing for multi-part pricing and pricing based on demand elasticities in all rail access regimes will therefore remove any concern rail infrastructure operators purport to have about the regulators views of acceptable pricing structures.

The PC has also sought views concerning draft recommendation 11.5, in relation to the costs and benefits of vertical reintegration, as well as comments about the potential effects of removing access regulation.

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[11] Australian Competition and Consumer Commission (2006) Submission to the Productivity Commission Draft Report into Road and Rail Freight Infrastructure Pricing pg.3.

[12] "Indeed, in circumstances where ARTC is constrained by market forces to pricing below the levels necessary to recover the full economic cost of providing services, the Commission has concerns regarding the sustainability of the Network infrastructure. If ARTC is not able to generate sufficient cash flow to replace assets as becomes necessary, the longer-term viability of the industry is compromised. The Commission notes that in these circumstances, a degree of price discrimination, even between different users operating the same type of service, may be a desirable practice. Such an approach may facilitate the efficient allocation of common costs." ACCC (2002) Decision Australian Rail Track Corporation Access Undertaking, pg.123.

[13] "Freebairn argues that a two-part tariff may actually have detrimental effects in the downstream market. That is, it may result in a relatively inefficient train operator market because of the way it affects operators' market entry and exit decisions. Since the flag fall charge is fixed per entrant, the minimum efficient scale for operators is higher than it would be if only a variable charge applied. Operators will have incentives to run fewer, heavier trains than may be desirable. The resulting market will therefore be characterised by fewer, larger operators than may be socially optimal. For these reasons, it may be desirable to allow an access provider to discriminate the level of fixed charges between different users of the infrastructure in order to facilitate entry." Ibid. pg.130.

[14] "In ARTC's case, this is enabled through clause 4.5(c) of the Undertaking, which expressly provides for negotiation over price structure." Op.cit. ACCC (2002) pg.130.

[15] Op.cit. PC (2006) pg.5.12.

The Report on National Competition Policy (The Hilmer Report, 1993) noted that a fundamental condition for establishing an access regime to essential facilities included the situation:

> "Where the owner of the 'essential facility' is vertically-integrated with potentially competitive activities in upstream or downstream markets – as is commonly the case with traditional public monopolies such as telecommunications, electricity and rail the potential to charge monopoly prices may be combined with an incentive to inhibit competitors' access to the facility".

TTF also notes the ACCC's view that 'the task for access regulation is typically more challenging in the case of vertical integration'.[16]

The ACCC also noted that 'access providers can have an incentive to abuse the freedom to price discriminate'.[17]

TTF is concerned that vertical reintegration, particularly in combination with a capacity to price discriminate, would exacerbate the potential for rail infrastructure operators to misuse their market power.

Ultimately this could result in the rail infrastructure operator setting terms and conditions that deny access to LDPR.

It follows that, in relation to draft recommendation 11.5, any detailed independent examination of vertical reintegration should incorporate the impact on LDPR.

TTF Australia also recommends that appropriate access regulations and oversight mechanisms remain available in order to ensure LDPR is protected from any misuse of market power in the future.

In summary, TTF Australia:

- recommends the PC take into consideration any potential impacts of pricing reform options on GSR given its important contribution to tourism in rural, regional and remote Australia;

- supports draft recommendation 11.3, specifically the need to incorporate in all rail access regimes, the pricing principles embodied in Part IIIA of the Trade Practices Act 1974;

- recommends the PC review its observation on price sensitivity comparisons between freight and passenger, and take into account LDPR;

[16] Op.cit. ACCC (2006) pg.5.
[17] Op.cit. ACCC (2006) pg.3.

- in relation to draft recommendation 11.5, any detailed independent examination of vertical reintegration should incorporate the impact on LDPR; and that

- appropriate access regulations and oversight mechanisms remain available in order to ensure LDPR is protected from any misuse of market power in the future.

Should you wish to discuss this submission, please contact Dr Mark Dimech, National Manager TTF Australia on (02) 9240 2015 or via at email at mdimech@ttf.org.au.

Yours sincerely

CHRISTOPHER BROWN
Managing Director & CEO