
3 Rail reform in Australia

The Industry Commission's 1991 inquiry identified a number of problems which were impeding the performance of Australia's rail industry. These included monopoly pricing in coal freight, inappropriate government intervention and conflicting objectives, and a lack of competitive neutrality between transport modes.

Since 1991, Australian Governments have taken different approaches to reforming the railways. Areas of difference include industry structure, governance arrangements (including the current or intended level of private sector participation) and access arrangements.

Some of the problems raised in 1991 have again been identified as concerns in 1999. In addition, new problems have emerged, particularly in arrangements for access to rail infrastructure and inconsistent safety regulation and operating standards.

The terms of reference for this inquiry direct the Commission to undertake a stocktake of reforms within Australian railways since the Industry Commission's (IC) 1991 inquiry into rail transport. The Commission received a number of submissions from participants providing details of progress made in reforming railways. These included the Australasian Railway Association (ARA), Commonwealth Department of Transport and Regional Services, NSW Government and Queensland Transport.

This chapter describes briefly some of the problems encountered when the IC last reviewed the industry. It also reviews the key reforms initiated since 1991 in the areas of industry structure, governance arrangements, access to rail infrastructure, safety regulation and operating requirements, and heavy road vehicle charging. A full list of key reforms is provided in appendix D.

Investment in railways, while critical to their performance, is not considered a reform in this chapter. Investment is not a reform *per se*, but rather one of the *outcomes* of reform and associated change in the industry. Chapter 2 contains a brief discussion of investment in railways since 1991.

3.1 The 1991 inquiry

In May 1990, the IC commenced an inquiry into Australia's railways. The inquiry examined the institutional, regulatory and other arrangements subject to government influence which led to inefficient resource use, and advised on courses of action to reduce or remove such inefficiencies. The IC released its final report, *Rail Transport*, in August 1991.

Problems and recommendations

Participants to that inquiry identified a wide range of problems with railways in 1991. These included the pricing of rail services (especially the extraction of monopoly rents), service quality, government intervention, investment deficiencies and competitive neutrality between transport modes. These problems are summarised briefly below.

Pricing and monopoly rents

Coal and mineral producers expressed concern about the monopoly of the State railways in hauling bulk commodities and the excessive freight rates imposed. They also expressed the view that the monopoly rents were being used to cross subsidise other rail services. The NSW Coal Association noted:

The coal industry in New South Wales has genuinely been concerned for some time regarding the lack of a commercial approach to the setting of coal freight rates. The SRA [State Rail Authority] has generally used an ad-hoc approach, often imposing 'across-the-board' increases on the industry to meet revenue targets, rather than formulating freight rates in accordance with the cost of providing services. The industry is firmly of the view that this has resulted in freight rates being set well above the level of costs incurred and allowed the SRA, in previous years, to offset or subsidise the loss of other sectors. (NSW Coal Association submission to Industry Commission Rail Transport inquiry, sub. 31, p. 4)

In addition, coal producers highlighted difficulties in establishing the existence and extent of overcharging because of the lack of disclosure of railway costs.

Service quality

Participants were critical of the quality of service provided by government-owned railways. In relation to interstate rail freight services, BHP Transport commented that:

It is the relatively poor level of interstate rail service which is of concern and results in a general preference for the direct, reliable and efficient services provided by road transport. (BHP Transport submission to Industry Commission Rail Transport inquiry, sub. 32, p. 8)

Criticism of service quality was not restricted to freight but applied also to rail passenger services.

Government intervention

The IC argued that many of the problems experienced by rail users were a consequence of government ownership and intervention. In particular, government-owned railways lacked a commercial focus or clearly defined objectives. Governments frequently used railways to promote political outcomes. According to the State Rail Authority of New South Wales (SRA):

... in the past its general level of efficiency, particularly in passenger and [general] freight areas, has been constrained by government intervention and constraints on its employment and investment policies. (State Rail submission to Industry Commission Rail Transport inquiry, sub. 98, p. 21)

In 1991, a number of regulations were in place that restricted the movement of certain commodities to rail (appendix C). Combined with these regulations, governments retained a monopoly position on the provision of rail services, thereby eliminating any competition within railways. Participants were critical of these arrangements claiming that they resulted in inefficiencies and price distortions.

Investment in rail infrastructure

Participants argued that urgent investment was needed in railways, including rollingstock, track and signalling equipment. The condition of these was seen as an impediment to improving the efficiency of the industry.

The IC recognised that deficiencies in the quality of railway infrastructure were present. However, this did not mean that aggregate investment in railways was insufficient:

The Commission is aware of tangible evidence of inadequate capital expenditure in parts of railway systems such as signalling equipment so old as to be unreliable and railway track in need of realignment consistent with modern operating capacities. However, given the total capital expenditure in railways appears to have been at a tenable level, the suggestion is that railways may have suffered from a misallocation of capital expenditure between different segments such as passengers and freight, rollingstock and infrastructure.

For the State-owned rail systems, political considerations seem to play the dominant role in determining the magnitude and nature of railway capital expenditure. (IC 1991b, p. 126)

Competitive neutrality between transport modes

A number of participants argued that road users were not paying the full cost of providing road infrastructure. Local councils also highlighted problems regarding the damage heavy road vehicles were causing to local roads, combined with noise and pollution costs incurred by local residents. However, it was also recognised that subsidies were not restricted to road transport. Some participants argued that both road and rail infrastructure were heavily subsidised by government.

Industry Commission recommendations

In response to the problems facing Australia's railways, the IC made 27 recommendations covering areas including governance arrangements, price setting, community service obligations, labour arrangements, traffic regulation, road user charging and open access to railway infrastructure. Some of the key recommendations of relevance to the Productivity Commission's current inquiry are presented in box 3.1.¹

¹The Commission has not detailed the progress achieved on all of the former IC's 1991 recommendations. Instead, it has focused on those key recommendations of direct relevance to its current terms of reference (chapter 1).

Box 3.1 Key recommendations of the Industry Commission's 1991 inquiry

Some key recommendations of the 1991 inquiry into rail transport included:

- railways be fully commercialised through corporatisation, including incorporation under corporations law;
- if governments require railways to provide community services, the conditions of provision should be set out in contracts, the details of which are made public, and include the pre-defined fees to be paid to railways;
- super-normal profits, whether described as 'royalties' or otherwise, should not be obtained via rail freight rates;
- the introduction of road user charges which reflect more accurately the amount of road use and pavement damage caused by all classes of vehicles;
- the removal of all restrictions on the contracting of tasks so that railways can take every opportunity to attain maximum efficiency;
- railways not be subject to government policy constraints that are more restrictive than those applying to private sector enterprises in managing labour resources;
- State Governments eliminate all regulation of traffics to rail, with the possible exception of dangerous goods; and
- owners of railway tracks (whether they be governments, rail authorities or private owners) be required to allow access by other organisations (whether public or private) to operate on their tracks, subject only to capacity being available and negotiation of a commercial agreement which sets the prices and conditions for access.

Source: IC 1991b.

3.2 Factors driving reform in the 1990s

Apart from the IC's inquiry into rail transport, related inquiries and research by other organisations and committees (chapter 1), there have been other factors driving change in the 1990s. They include:

- the continued and increasing competition from road transport;
- the continued pressure on State Government budgets in providing goods and services to the community;
- the pressure on railway freight rates from increasing competition in downstream markets, such as Australia's black coal industry; and
- the implementation of the National Competition Policy (NCP).

Since the early 1950s railways have been subject to increasing competition in freight and passenger markets from road, sea and air transport. In the transport of non-bulk and some bulk commodities, railways suffered substantial losses of traffic to road transport (appendix C). Many of the reforms initiated by Australian Governments are in response to rail's decreasing market share in both freight and passenger markets.

State Governments pay considerable subsidies for non-commercial rail services (chapter 10). They face increasing pressure to achieve the twin objectives of improving services to the community while lowering the level of taxation. One way in which both these objectives can be met simultaneously is to improve the efficiency of service delivery.

Railways and their Government owners have benefited greatly from the growth of Australia's mineral sector. Apart from the increase in bulk traffic providing a renewed life for railways in Australia, Governments have used their monopoly position in rail transport to extract rents from mining companies. However, as described in the Commission's report, *The Australian Black Coal Industry*, Australian coal mines now face increased competition from overseas suppliers (PC 1998a). This, in turn, places pressure on Australian coal mines to improve productivity and lower production costs. As a consequence, the ability of Australian coal companies to absorb excessive freight rates has diminished. The coal industry is seeking further efficiency gains from railways to allow it to be more competitive in its new trading environment.

The forces driving change in railways have been given further impetus by the introduction of NCP. The key elements of NCP are summarised in box 3.2. The NCP package incorporated pre-existing intergovernmental agreements on industry-specific reforms in electricity, gas, water and road transport (NCC 1996a). Although the rail industry is subject to the general provisions of NCP, it is not part of the specific Intergovernmental Agreement (IGA) to implement the NCP-related reforms.² As noted by the National Competition Council (NCC):

Without a national rail reform agreement, the business community, in its attempts to obtain improved service quality and lower prices, has had to rely on the general provisions of the CPA [Competition Principles Agreement] and, in particular, the National Access Regime. (NCC 1997a, p. 142)

These factors driving rail reform in Australia provide a context for examining the reforms initiated across jurisdictions as outlined below.

² An IGA was signed in 1996 which set out principles for achieving a nationally consistent approach to rail safety.

Box 3.2 **The National Competition Policy package**

In April 1995, the Council of Australian Governments agreed to implement a package of measures to extend competition policies to previously exempt sectors of the economy.

The Commonwealth's *Competition Policy Reform Act 1995*:

- amended the competitive conduct rules (Part IV) of the *Trade Practices Act 1974* (TPA) and extended their coverage to State and local government business enterprises and unincorporated businesses;
- created a new section (Part IIIA) of the TPA establishing a national regime for access to services provided by 'nationally significant' infrastructure facilities;
- amended the Prices Surveillance Act to extend prices oversight to State- and Territory-owned business enterprises; and
- created two new institutions — the Australian Competition and Consumer Commission and the National Competition Council — responsible for overseeing and providing advice on implementation of the policy package.

There were three intergovernmental agreements in the package:

- the *Conduct Code Agreement* sets out the basis for extending the coverage of the TPA.
- the *Competition Principles Agreement* established principles on: structural reform of public monopolies; competitive neutrality between the public and private sectors; prices oversight of government business enterprises; a regime to provide access to essential facilities; a review program for legislation restricting competition; and consultative processes for appointments to the National Competition Council.
- under the *Agreement to Implement the National Competition Policy and Related Reforms*, the Commonwealth provided payments to States and Territories which gave effect to the intergovernmental agreements, and met reform commitments in electricity, gas, water and road transport.

Source: PC 1996.

3.3 **Reform initiatives**

Railway reforms implemented in Australia since 1991 are described below. They are based on evidence provided by participants and other published sources. Box 3.3 provides a snapshot of some key rail reforms in Australia, while a more detailed list is provided in appendix D. Reforms regarding the deregulation of commodity traffics, the contracting out of activities and provision of non-commercial rail services are discussed in appendix C and chapters 7 and 10, respectively.

Box 3.3 **A snapshot of key rail reforms in the 1990s**

Reforms initiated by the Commonwealth and State Governments during the 1990s have significantly altered the operating and institutional environment in which rail freight and passenger services are provided in Australia. Some of the key reforms are listed below.

Industry structure:

- formation of the National Rail Corporation and Australian Rail Track Corporation;
- separation of the interstate long distance passenger and intrastate freight services of Australian National;
- separation of the former State Rail Authority of New South Wales into four new entities: FreightCorp, Rail Access Corporation, Rail Services Australia and a new State Rail Authority; and
- separation of the former Public Transport Corporation of Victoria into V/Line Freight, V/Line Passenger, Bayside and Hillside Trains (and Swanston and Yarra Trams).

Governance arrangements:

- commercialisation or corporatisation of almost all government-owned railways;
- privatisation of interstate long distance passenger and intrastate freight services of Australian National (Great Southern Railway, Australia Southern Railroad and Tasrail);
- privatisation of V/Line Freight; and
- franchising of V/Line Passenger and Bayside and Hillside Trains.

Access to rail infrastructure services:

- introduction of Part IIIA of the *Trade Practices Act* establishing a national regime for access to services provided by 'nationally significant' infrastructure facilities; and
- introduction of rail access regimes in most jurisdictions.

Safety regulation and operating procedures and standards:

- Intergovernmental Agreement, signed in July 1996, to achieve consistent national rail safety regulation based on agreed aims and principles; and
- signing of the Heads of Agreement on Interstate Rail Reform at the National Rail Summit in 1997.

Industry structure

Most jurisdictions have significantly altered the structure of their railways by horizontally or vertically separating their former integrated rail authorities.³

The Commonwealth

In 1991, the Commonwealth Government owned the Australian National Railways Commission, trading as Australian National (AN). AN owned and maintained track in New South Wales, Western Australia, South Australia, Tasmania and the Northern Territory, and provided the following rail services:

- intrastate freight in South Australia and Tasmania;
- interstate freight in the Northern Territory, South Australia, Western Australia and New South Wales; and
- passenger travel on the Indian Pacific, Ghan and Overland trains.

Since 1991, the Commonwealth Government has both horizontally and vertically separated AN.

In 1991-92, the National Rail Corporation (NRC) was formed under the *National Rail Agreement 1991* to operate interstate freight operations in Australia. NRC's shareholders are the Commonwealth, NSW and Victorian Governments. NRC commenced commercial operations in April 1993.

The formation of NRC took considerably longer than originally anticipated. The NSW Government noted a range of internal and external factors which caused these delays (box 3.4).

Specialized Container Transport (SCT) commenced interstate rail freight operations in competition with NRC in June 1995. TNT (now Toll) followed one year later (sub. DR100).

In 1997-98, the Commonwealth Government horizontally separated and privatised AN's intrastate freight operations in Tasmania and South Australia and interstate passenger services (Indian Pacific, Ghan and Overland passenger trains) (see section below on governance arrangements).

³ Horizontal separation occurs either by product (freight and passenger services) or by geographic area (interstate and regional railways). Vertical separation occurs in railways when track infrastructure and train operations are separated.

AN's mainline interstate track was vertically separated and transferred to the Australian Rail Track Corporation (ARTC). The ARTC commenced operations on 1 July 1998. It has responsibility for management of access and infrastructure maintenance in South Australia as track owner and in Victoria as track manager via a lease agreement. In other jurisdictions its function is restricted to interstate access issues (sub. 74).

Box 3.4 Formation of the National Rail Corporation

The National Rail Corporation (NRC) was formed under the *National Rail Corporation Agreement 1991* (the Agreement) together with Commonwealth and State Government legislation. The formation of NRC was to be achieved in two phases — a transition period and an establishment period.

By the end of the five year establishment period (1 February 1998), NRC was to have been equipped with all relevant assets and operate as a stand-alone entity. However, implementation of the Agreement took significantly longer than anticipated. As stated by the NSW Government:

... implementation of the *National Rail Agreement* has taken considerably longer than expected ... The main reasons for this appear to be the substantial broadening of the rail reform agenda since the company commenced operations. (sub. DR128, pp.23, 24)

Specific factors identified included:

- the moves towards vertical separation of track and train operations, which was not anticipated at the time of formation of NRC;
- some technical difficulties with the identification and transfer of assets; and
- prolonged consideration by shareholders of their obligations to provide the company with compensation payments and railway assets.

While these issues have now been largely resolved, in the interim NRC has also had to contend with competition from other train operators as well as continued competition from road transport.

Source: NSW Government sub. DR128.

New South Wales

The major reform in New South Wales has been the horizontal and vertical separation of the former SRA in July 1996. Previously, all passenger and freight services were provided by the vertically integrated SRA. In July 1996, SRA was separated into the following four agencies:

- Rail Access Corporation (RAC);
- FreightCorp;
- Rail Services Authority (RSA); and

-
- a new SRA.

RAC is vertically separated from train operations and owns the NSW intrastate and interstate rail network.

FreightCorp undertakes freight train operations in New South Wales. Recently, FreightCorp expanded operations into South Australia, carrying coal from Leigh Creek to Port Augusta and NRC won a contract to haul coal in New South Wales.

RSA provides maintenance services to RAC, FreightCorp, SRA and other business clients. In 1997-98, RSA was corporatised and renamed Rail Services Australia. As part of the restructure of the former SRA, it was initially intended that track maintenance services would be made fully contestable by June 2000. However, the NSW Government placed a moratorium on contestable contracting out of rail track maintenance services until July 1999 (chapter 10). The Government has since partially lifted the moratorium by allowing competition for the provision of maintenance services on the Bondi Junction to Waterfall line in Sydney and the Hunter Valley coal lines (some \$65 million in maintenance contracts).

The new SRA provides city and country passenger rail services, and train control to RAC (under contract).

Victoria

In 1991, rail freight and passenger operations in Victoria were provided by the vertically integrated PTC. In 1995-96, the Victorian Government began a process of dismantling the PTC with a view to franchising and privatising different elements of the industry (box 3.5).

In 1995-96 the *Rail Corporations Act 1996* was passed which allowed for the establishment of V/Line Freight and the Victorian Rail Track Access Corporation (VicTrack) as body corporates. V/Line Freight was separated from the PTC in 1996-97 and VicTrack one year later.

VicTrack was initially given responsibility for train control, maintenance and access to Victoria's non-electrified intrastate track (excluding metropolitan tram and train operations). However, part of the privatisation of V/Line Freight involved a 15 year lease over the non-metropolitan intrastate track. As such, VicTrack now only retains landlord responsibilities over this track.

In 1998, the PTC's urban passenger trains and trams, and non-urban rail passenger operations were horizontally separated into five corporatised businesses. They were V/Line Passenger, Bayside and Hillside Trains and Swanston and Yarra Trams.

Box 3.5 **Structural reform in Victoria**

In 1995-96 the State Government commenced a program to reform the provision of rail services in Victoria. This involved the horizontal separation of freight, urban and non-urban rail passenger services formerly provided by the Public Transport Corporation. The new rail organisations created were V/Line Freight, V/Line Passenger (non-urban), Bayside Trains and Hillside Trains.

Associated with this restructure, the Government privatised freight operations while passenger services were franchised to the private sector through a process of competitive tendering.

Freight

The Government privatised V/Line Freight in February 1999. Freight Victoria, a consortium headed by RailAmerica, was the successful bidder, agreeing to pay \$163 million for the freight business. Freight Victoria purchased rollingstock and other assets, and entered into a 15 year lease over the non-metropolitan intrastate track (with certain rights of renewal) (sub. 82).

Passengers

The Government has franchised all passenger services. National Express was the successful bidder to operate Bayside Trains and V/Line Passenger. Melbourne Transport Enterprises was the successful bidder to operate Hillside Trains.

These franchisees have bought rollingstock and have a lease over the track infrastructure. The franchise agreements specify, among other things: passenger service levels; maximum fares at current levels, adjusted for inflation; minimum service levels; and operational performance (including punctuality and reliability, capacity, quality of service and journey times). Contract length, subsidy payments and investment commitments of the franchisees are shown below.

Contract details for rail passenger franchises

<i>Franchise</i>	<i>Contract length</i>	<i>Subsidy in 2000-01</i>	<i>Subsidy in final year</i>	<i>Investment</i>
	Years	\$m	\$m	\$m
Bayside Trains	15	83	(19)	640
Hillside Trains	15	91	25	490
V/Line Passenger	10	78	46	165

Source: Victorian Department of Treasury and Finance, pers. comm., 23 July 1999.

Queensland

Queensland Rail (QR) remains horizontally and vertically integrated in providing passenger and freight services in Queensland. Reform of QR has focused on improving the financial arrangements between QR and its Government owners, internal restructuring of QR's operations as well as allowing for access to the QR track network.

In 1997-98, the Network Access Group was established in QR to deal with access issues.

Western Australia

Westrail currently remains horizontally and vertically integrated in providing passenger and freight services in Western Australia.

However, as discussed in the next section, the Government is intending to privatise the freight operations of Westrail. If the privatisation occurs as is currently intended, then the freight operations of Westrail will remain vertically integrated but horizontally separated from the provider of urban passenger services.

South Australia

In 1991, the SA Government provided urban passenger services through the State Transport Authority (STA), while intrastate and interstate freight operations were undertaken by AN.

In 1994-95, the STA was restructured into:

- TransAdelaide, which assumed the operating functions of the former STA; and
- Passenger Transport Board, which undertakes the planning, regulatory and purchasing functions for public transport in Adelaide.

Currently, TransAdelaide provides urban rail passenger services under contract to the Passenger Transport Board (there is no tendering for the service).

Tasmania

In 1991 freight services were provided by AN (no rail passenger services were provided). In addition, Emu Bay Railway (owned by Pasminco) transported zinc. In 1997-98, the Commonwealth Government horizontally separated the freight services provided by AN as part of the privatisation of Tasrail (see below).

Governance arrangements

Since 1991, a number of reforms introduced by governments have focused on making railways more commercially focused. In some instances railways have been privatised or the provision of the rail services required by government has been franchised to the private sector. For railways that remain in government ownership, commercialisation or corporatisation models have been adopted aimed at replicating many of the commercial incentives which apply to private firms.

The Commonwealth Government sold AN's intrastate freight and interstate passenger services to three separate operators in 1997-98. Australia Southern Railroad and Australian Transport Network (Tasrail) purchased the intrastate freight operations in South Australia and Tasmania respectively. Great Southern Railways now provides long distance passenger services linking Perth, Adelaide, Alice Springs, Sydney and Melbourne.

The NRC and ARTC were corporatised on establishment and incorporated under the Corporations Law (table 3.1). The Commonwealth Government has also announced its intention to sell its share of NRC.

Table 3.1 Governance arrangements of government-owned railways

<i>Railway</i>	<i>Statutory Authority</i>	<i>Commercialised</i>	<i>Corporatised</i>	<i>Incorporated under Corporations Law</i>
National Rail Corporation			✓	✓
Australian Rail Track Corp.			✓	✓
State Rail Authority (NSW)	✓			
FreightCorp (NSW)			✓	
Rail Access Corp. (NSW)			✓	
Queensland Rail (Qld)			✓	
Westrail (WA)		✓		
TransAdelaide (SA)			✓	

In New South Wales the Government has corporatised FreightCorp and RAC. However, the Government did not corporatise SRA which remains a statutory authority with its objectives specified in the *Transport Administration Amendment (Rail Corporatisation and Restructuring) Act 1996*.

The Victorian Government has privatised its intrastate freight operations and is the first Australian Government to franchise the provision of passenger services (box 3.5).

The Queensland Government corporatised QR in 1995-96.

Westrail was not corporatised. Instead, the WA Government decided upon a commercialisation program that included many of the principles of corporatisation. However, the Government has announced its intention to privatise the freight operations of Westrail as a vertically integrated entity. The proposed legislation allowing for the privatisation of the freight operations of Westrail was being debated in the Western Australian Parliament in mid-1999. The Government is yet to announce a decision regarding passenger services (sub. 60).

Access to rail infrastructure services

In April 1995 the Commonwealth, State and Territory Governments agreed to establish a national competition policy, and to work cooperatively on competition issues within their jurisdictions. As part of these reforms the *Competition Policy Reform Act 1995* introduced Part IIIA into the *Trade Practices Act 1974* creating the National Access Regime (box 3.2 and appendix F). This established an overarching national regime through which businesses can seek access to nationally significant infrastructure services that are not covered by another regime (such as state-based rail access regimes).

Since then there have been significant changes in the institutional arrangements with regard to access to a range of important railway infrastructure services.

Four applications from governments (NSW, Queensland, South Australia/Northern Territory and WA) have been made to the NCC to consider the effectiveness of their regimes and recommend it be 'certified' as effective under the national regime (appendix F). The NSW, SA/NT and WA applications are still under consideration. Queensland withdrew its application in February 1999 and subsequently applied to the Queensland Competition Authority to have it deemed effective.

In several instances train operators and track owners have reached commercially negotiated agreements, without recourse to formal mechanisms. According to the Tasmanian Government the privately-owned, vertically integrated Tasrail and a number of other operators have reached commercially negotiated access agreements even though no formal access arrangements exist in Tasmania (sub. 81, p. 2).

Other operators have negotiated access agreements under state-based regimes. In New South Wales, Austrac is providing agricultural freight services in the Riverina region and NRC is providing coal freight services in the Hunter Valley. New private operators (SCT, Toll Rail and Patrick) are providing services on the interstate network.

In some cases, potential operators have been unable to gain access under suitable terms and conditions and have consequently sought access through the declaration provisions of the National Access Regime (chapter 7).

The Australian Competition and Consumer Commission (ACCC) has not received any undertakings for rail. However, the ARTC is developing an industry code to take to the ACCC covering access to that part of the interstate network it owns (trans., p. 570).

Safety regulation and operating procedures and standards

Since the IC's 1991 inquiry, the Commonwealth, State and Northern Territory Governments, and industry have undertaken several joint initiatives to improve rail safety regulations and operating requirements (appendices D and G and chapter 9).

The first major step occurred in 1993 when the Australian Transport Council (ATC), comprising Commonwealth, State and Territory Ministers, endorsed a report, *A National Approach to Rail Safety Regulation* (ATC 1993). The report concluded that consistent rail safety regulation was required, particularly for interstate operations.

An IGA was signed in July 1996 by Commonwealth, State and Northern Territory Ministers setting out guidelines for the establishment of a safety accreditation system for interstate operations and stating that all parties would make legislative provision for accreditation and mutual recognition.

The next significant initiative took place in September 1997, when Commonwealth and State Ministers signed the Heads of Agreement on Interstate Rail Reform at a National Rail Summit. Among other things, the parties agreed that there was an urgent need to reform interstate rail.

By the end of 1997 the issues had been prioritised and the principles for reform agreed on. The Standing Committee on Transport (SCOT), as the main advisory body to the ATC, established a Rail Group to facilitate rail reform and advance uniformity of regulations and operating procedures and standards. The Maunsell report (Maunsell 1998) provided a detailed assessment of the safety and operational issues that needed to be addressed and implementation options.

The SCOT Rail Group established a number of Working Groups to address the priority tasks for action identified in the Maunsell report. The Rail Safety Committee of Australia (RSCA) was formed in 1998 specifically to address safety

issues and an Industry Reference Group (IRG) was established to develop nationally consistent standards and operational requirements.

In April 1999, the ATC agreed to SCOT establishing an independent review of safety arrangements and the establishment of a national non-statutory body to facilitate and coordinate implementation of uniform operational requirements (ATC 1999).

Relevant reform in the road industry

An important element in rail's ability to compete for business with road transport is the level of heavy road vehicle charges (chapter 10). Since 1991, road charges for heavy vehicles⁴ has been addressed primarily through the activities of the National Road Transport Commission (NRTC).

A key objective of the NRTC is to introduce nationally uniform or consistent road transport policies, laws and standards. Reforms implemented include a national registration scheme for all heavy vehicles, uniform technical and operating standards, and nationally consistent road charges for heavy vehicles.

Between July 1995 and October 1996, Commonwealth, State and Territory Governments introduced national heavy vehicle charges based on the First Charges Determination prepared by the NRTC in 1992. In 1998, the NRTC proposed a revised set of charges for heavy road vehicles.

3.4 Problems identified in 1999

Although the rail industry and governments have undertaken a range of reform initiatives aimed at improving the efficiency of railways, a number of problems identified in 1991 still remain. In addition, new problems have emerged.

Problems remaining from 1991

Several problems identified in 1991 have been raised by participants to this current inquiry. In particular:

- the need to improve the commercial focus of government-owned railways further, removing remaining impediments to achieving this objective;
- inadequate investment in rail infrastructure;

⁴ Road vehicles heavier than 4.5 tonnes.

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- the lack of competitive neutrality between train operators and between transport modes, particularly road and rail; and
 - whether railways still extract monopoly rents from coal companies through coal freight rates.

Commercial focus and government involvement

For government-owned railways to fully realise their potential in Australia's transport system they need to have an appropriate commercial focus. This requires that railways:

- pursue only purely commercial objectives (including the commercial provision of services to governments); and
- be responsive to market opportunities and requirements.

To achieve a commercial focus, it is important that railways have:

- the flexibility to make timely decisions (investment and operational);
- the ability to form strategic alliances, mergers or joint ventures;
- access to capital; and
- no undue restrictions on input choice.

Underpinning this approach, railway management should be subject to performance-based systems of rewards and sanctions similar to those prevailing in the private sector.

The Commission received considerable evidence indicating that government-owned railways have not achieved an appropriate level of commercial focus. This situation was largely seen as a consequence of the objectives and restrictions placed upon railways by governments.

Participants indicated that governments did not set purely commercial objectives for their rail authorities. As argued by Australian Transport Network:

Governments give more weight to non-economic factors, they are risk adverse owners limiting the business' growth potential, and they lack in-depth knowledge of the business. (sub. 25, p. 2)

Some argued that government-owned railways could be more responsive to market opportunities and customer needs. Great Northern Rail Services stated:

When GNR is approached by existing rail clients looking to change providers, it is often not the cost that is the compelling reason. The reasons put forward are:

- attitude;
- lack of flexibility; [and]
- lack of concern for client needs. (sub. 46, p. 6)

With regards to interstate freight operations, the CRT Group argued:

... NRC adopted an autocratic attitude towards customers in terms of what they would carry, freight rates and attitudes to the other rail systems. In short they were not customer service orientated. (sub. 20, p. 4)

The need for stronger commercial focus was summarised by the Department of Agriculture, Fisheries and Forestry:

The rail industry needs to put more focus and energy into identifying new freight opportunities, meeting market and customer needs, and developing themselves as part of the total logistics chain. (sub. 84, p. 3)

The Commission also received evidence that government-owned railways are unable to achieve a stronger commercial focus due to the restrictions placed on them by governments. NRC raised issues relating to flexibility in decision making and the ability to form strategic alliances, mergers or joint ventures:

Under public ownership all of those sort of changes in the corporate boundaries and structures are extremely difficult. If, for example, one — as a company like ours — were to attempt to purchase a freight forwarder or enter into some tight alliance with a freight forwarder, that would require shareholder approval and that shareholder approval could take months to get. In the meantime, the moves that we wanted to take would be all over town and they would be effectively blocked by all those people whose interests were adversely affected by it. (trans., p. 1002)

The Victorian Government raised problems of access to capital:

Across Australia, potential rail investors face an industry which is characterised by the problems highlighted in the draft report, including:

- inadequate investment where it is needed (that is, it should be directed by market forces and not driven by supply), and
- lack of commercial discipline. (sub. 118, p. 4)

The problems associated with government ownership and involvement were summarised by the NSW Minerals Council:

The reality is that Governments do interfere with the operation of Government-owned railways, often to the detriment of their economic and operational efficiency ... (sub. 39, p. 29)

In addition to the issues surrounding government ownership, NRC (sub. 117) also highlighted problems regarding complex and inconsistent regulatory regimes, a lack of competitive neutrality (especially between road and rail) and limited competition in some markets served by government-owned railways as further impediments to a stronger commercial focus.

The need to improve the governance arrangements between governments and their commercial entities has been highlighted in various reports and inquiries. The IC's (1994b) report, *Urban Transport*, recommended that moves to corporatise government rail authorities be continued and extended. Chapter 7 discusses further government and private sector participation in railways.

Investment in rail infrastructure

Many participants argued that the rail industry cannot achieve its full output and employment potential due to a lack of investment in the industry. ARA stated:

Progress in rail reform has been severely hampered by inadequate infrastructure investment. (sub. 51, p. 13)

And NRC:

The poor quality of infrastructure used for interstate rail operations increases the cost of rail operations and affects service quality. (sub. 53, p. 12)

Investment in transport infrastructure has also been examined in a number of other reports since 1991. In 1994, the National Transport Planning Taskforce found, among other things, insufficient evidence to support a case for a substantial increase in the current overall level of transport infrastructure spending. However, the Taskforce did find that infrastructure investment decision-making and funding was highly segmented by mode and by level of administration and was not considered on a nationally consistent basis (NTPT 1994).

The House of Representatives Standing Committee on Communications, Transport and Microeconomic Reform undertook an inquiry into the role of rail in the national transport framework in 1998. Its report, *Tracking Australia: An Inquiry into the Role of Rail in the National Transport Network*, recommended that the Commonwealth Government invest \$750 million to address the worst deficiencies

on the national track within the next three years and spend a further \$2 billion over ten years from 2001 (HORSCCTMR 1998b).

A Rail Projects Taskforce was established in August 1998 to evaluate how governments could better facilitate viable major rail investment proposals developed by the private sector. The report from the Taskforce, *Revitalising Rail: The Private Sector Solution*, recommended, among other things, that the Commonwealth Government accelerate the existing planned capital expenditure of \$250 million and spend an additional \$470 million on the national track by June 2002. However, the Taskforce also recommended that this funding should be conditional on State Governments achieving identified reform measures (RPT 1999).

Chapters 7 and 10 discuss investment issues in railways.

Competitive neutrality

A number of participants considered that government-owned railways do not compete for business on a competitively neutral basis with private operators. In addition, debate and complaints by both rail and road operators regarding competitive neutrality between them indicates that this is still an issue.

Many submissions from the rail industry argued that heavy freight vehicles are not paying the full cost of providing road infrastructure. Conversely, other participants argued that rail is heavily subsidised compared to the road industry.

Chapter 10 discusses the main reforms needed to promote competitive neutrality between train operators and between transport modes.

Monopoly rents

The NSW and Queensland Governments have begun phasing out identified monopoly rents on coal freight charges. However, mining companies still appear unconvinced that governments have (or will have by the end of the planned removal period) removed the entire monopoly rent component on coal freight charges. Rio Tinto noted:

While reductions or potential reductions in rail charges are significant, although offset to a degree by royalty rate increases at least in Queensland, there is concern that the new charges still contain a monopoly rent component. This concern has been aggravated by the manner in which the methodology for calculating the charges has been introduced. (sub. 58, pp. 6-7)

And NSW Minerals Council commented:

There has been a reduction in the explicit monopoly rent paid for access for coal haulage as it is phased out in four equal steps (in \$/tonne terms) to zero on 1 July 2000. There is no indication that all monopoly rent is being phased out, as the calculation of monopoly rent was not transparent. (sub. 39, p. 25)

The issue of monopoly rents on coal freight was addressed in the Commission's (1998a) report, *The Australian Black Coal Industry*. The Commission found that while the phased removal of identified monopoly rents had improved the efficiency of rail pricing and encouraged improved performance by railways, the pace of change had been slow. In addition, the Commission found that the setting of freight rates for coal by government enterprises in New South Wales and Queensland was not transparent. A set of principles and practices need to be developed in each State which generate efficient prices and provide the coal industry with confidence in the fairness of prices (PC 1998a).

In investigating access pricing for the Hunter Valley coal network, the Independent Pricing and Regulatory Tribunal has recommended the asset valuation methodology be changed and that the pre-tax real return on these assets be reduced to 8 per cent (1999c).

Chapter 8 discusses the pricing of rail services further.

Problems emerging since 1991

In addition to the problems raised in 1991, new problems have arisen with regard to access, and safety regulation and operating requirements.

Access to rail infrastructure

Train operators and mining companies are critical of current access arrangements being implemented by governments. Problems identified include a lack of transparency, complexity and inappropriate implementation. The criticism of access arrangements extends to both intrastate and interstate networks.

With regards to the interstate network and operations of the ARTC, SCT commented that:

The original concept of the ARTC appeared to be a vast improvement on what was in place at the time but in reality what we now have is nothing more than a token gesture of reform in this area. (sub. 37, p. 1)

The NSW Minerals Council was highly critical of the development of the NSW rail access regime:⁵

The Regime was developed with no public consultation whatsoever. The Regime does not comply with the Competition Principles Agreement. (sub. 39, p. 7)

A similar view was also presented by the Queensland Mining Council in the course of the black coal inquiry.

The need for governments to introduce seamless and effective access to rail infrastructure was reported in the Commission's *Stocktake in Progress in Microeconomic Reform* (PC 1996).

Chapter 8 considers the role of access in promoting efficiency improvements within Australia's railways.

Safety regulation and operating procedures and standards

The establishment of the NRC and entry of private operators has highlighted the fact that each jurisdiction had developed (historically) its own safety regulations and operating procedures and standards. These inconsistencies can be an impediment to efficient interstate rail operations and to entering rail markets in different jurisdictions. While progress has been made in improving the situation, many in the industry have indicated that more needs to be done.

Chapter 9 and appendix G discuss the processes currently being undertaken to address the remaining problems and suggest further reform measures.

Overall assessment of reform to date

A number of important reform initiatives have transformed the structure and operation of railways since 1991. There is greater participation by the private sector through the privatisation of some government-owned railways and the entry of new private operators. Both government and non-government train operators now specialise in the delivery of rail services in particular freight and passenger markets. In some instances, particularly on the East-West corridor, private and government operators directly compete with each other.

⁵ The NSW Government (sub. DR128) strongly refuted the claims by the NSW Minerals Council arguing that the regime, or an aspect of it, was subject to extensive public consultation on seven occasions.

In response to these reforms, participants acknowledged that prices have fallen and the quality of services improved.

However, some reforms have taken several years to be implemented fully and do not appear to have been as effective as initially envisaged. As a consequence, many of the problems raised in 1991 have yet to be fully resolved, while new issues have arisen.

The NSW Government (sub. DR128) noted a range of transitional issues, relating in particular to the establishment of access arrangements, harmonisation of safety regulation, the formation of the NRC and the NSW structural reform program. These slowed the process both in New South Wales and nationally.

The reasons for the apparent lack of progress are diverse and in part reflect Australia's complex system of government. Commonwealth, State, Territory and Local Governments all influence the development and operation of railways. In railways, perhaps the greatest influence continues to be exercised by State Governments through their ownership of railways and policy responsibilities.

Reforms in the 1990s have transformed the structure and operations of Australia's railways but progress in some areas has been slow.

The following chapter examines the performance of the Australian rail industry in the 1990s and in comparison with railways in other countries. This information provides a context for evaluating the effectiveness of the changes since 1991 and considering further reforms that may be implemented in future.