

1 October 1998

Ms Helen Silver  
First Assistant Commissioner  
Productivity Commission  
Progress In Rail Reform  
Locked Bag 2  
Collins Street East Post Office  
MELBOURNE VIC 8003

Dear Ms Silver

***Re: Progress in Rail Reform Inquiry***

The Road Transport Forum (RTF) is pleased to provide the following submission to Productivity Commission inquiry into progress in rail reform.

Rail reform is of direct interest to the road transport industry, especially those sectors which are either in competition with rail or may be in competition at some stage in the future.

More importantly, rail is an essential part of the transport industry in Australia with the potential to add significantly to national well being. However, if the reform process is not handled effectively, it also has the potential to absorb significant resources, grossly distort competition and create a net burden for the Australian community.

The Road Transport Forum believes that the views of our industry should be judged in light of seeking to gain the greatest benefits for the Australian community as a whole. This, of course, also includes the security and prospects of individual participants in the road transport industry.

As a matter of principle, both road and rail should serve the community on equal terms. Both sectors should pay their own way, each should be essentially commercially driven, Governments should explicitly recognise and pay community service obligations where they are imposed in the community's interest and neither sector should be subsidised.

Unfortunately, there has been enormous difficulty in achieving the right balance.

In recent years, the unfortunate legacy of powerful, well organised rail interests driving along misplaced Government subsidies seems to have been renewed through a promise of new rail lines being constructed in Australia. Such proposals include the Darwin to Alice Springs project and the even more gravity defying proposal for a line from Melbourne to Darwin via every inland town or village in the interior of eastern Australia.

In the public mind and the mind of some key interest groups, it often appears that there is nothing quite so welcome as an excess of conspicuous consumption of investment in the rail industry.

When this drive for conspicuous investment in icon projects with negligible community benefits is combined with inefficient work practices, Australian railways have often produced a grossly expensive, inefficient and destabilising effect.

In sharp contrast, Australia's privately operated railways have generally been paragons of efficiency and economy, which have served the community extremely well.

### **Rail Subsidies**

One paradox which rail enthusiasts are often unwilling to confront is that excessive subsidisation and lack of real performance expectations (especially the Government owned railway system) has produced an inefficient, moribund and unstable rail industry.

Road transport operators who have been subject to conspicuous Government subsidised competition from rail have justifiably felt highly resentful of the sheer waste of community resources and the wrecking impact on their businesses of unsustainable and unfair competition.

Rail is highly subsidised when compared with the road transport industry. Rail receives over \$800 million per year in Government subsidies<sup>1</sup>. The rail industry also benefits from the injection of large capital sums, such as the \$296 million injected by the Commonwealth Government in 1996/97 to facilitate the sale of the Australian National Railways Commission as part of a \$2 billion package.

Often these Government subsidies are achieved in a number of disguised ways. For example, Queensland Rail and the New South Wales Government system gain extensive massive unannounced subsidies through disguised taxes on the transport of coal. The mechanism works in the following way:

- coal is forced onto rail through either political, regulatory or economic pressure
- rail freight rates are pushed up by Government supported monopolies to generate disguised tax revenues
- these disguised tax revenues are delivered to the relevant rail authorities.

While there have been some attempts to estimate the extent of these deficits and some minimal attempts to reveal these estimates in railway accounts, on the whole disguised tax revenues continue to distort the provision of resources to rail within Australia.

Another favoured mechanism has been either writing off capital expenditures, or not allowing capital expenditures to appear on railway balance sheets. The extent of hidden subsidies extended in this way is extremely hard to assess and represents yet another successful distortion of the market place.

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<sup>1</sup> According to Australian Bureau of Statistics unpublished data, all levels of government provided \$845 million to subsidise rail operations, and a further \$1583 million in capital outlays in 1995/96. Net subsidies paid to Public Trading enterprises between 1986 and 1996 totaled \$7964 million.

## Destabilisation

One of the most difficult problems faced by road transport operators is that rail operators from time to time have entered particular markets in a burst of administratively developed enthusiasm. This has resulted in unsustainable destabilising price-cutting with an enormous negative impact in the short term, which in the longer term fades away.

From one perspective, it might be thought that such destabilising behaviour could be viewed benignly. But it cannot be viewed benignly by those road transport operators who are driven out of business during periods of rail reform enthusiasm - as unsustained price-cutting is usually characterised as capital investment.

Another key to improving market arrangements in transport is to place some additional constraints on the mindless enthusiasm for sinking community funds into conspicuous investment in the rail sector. Often a sure sign that a rail project has very little benefit is that the proponents stand logic on its head and call the costs of the project benefits. Say for example we might be told that the Darwin - Alice Springs railway line is socially desirable because it *“requires X thousand tonnes of steel”* or *“generates Y thousand jobs in the construction industry”*. These are not benefits - they are costs - costs which could be devoted to other purposes which have the potential to return far higher rates of returns to the community.

## A Vision for the Future

With all these current problems, the Road Transport Forum sees that a clear vision for the future is emerging. This vision includes the following key elements:

- Firstly, the operation and maintenance of rail track through a commercially focused body,
- Secondly, open access to rail track by any competitive rail operator,
- Thirdly, the determination of rail access fees in transparent and economically efficient manner, and
- Fourthly, the imposition of discipline on Governments to ensure that community service obligations are in fact directed towards achieving community goals and fully accountable.

This vision for rail parallels in all key aspects the current arrangements that govern the operation of road transport in Australia. To reiterate, road transport operates on the basis that;

- The road system (or track) is provided to the road freight industry on a cost recovery basis by State Road Authorities,
- Access to the road is available to all road transport operators on a payment of user charges,
- The user charges are determined through a transparent and open process overseen by the National Road Transport Commission, and
- Community service obligations (which are extremely rare) are at least, in principal, recognised by Governments.

There are a few remaining impediments to the achievement of this goal over time.

The first and most important is that Governments have proved unwilling to genuinely identify and fund community service obligations. While bodies such as the Productivity Commission have spent a good deal of effort in defining the nature of community service obligations and suggesting ways in which they could be measured, Governments have at critical points effectively refused to contemplate revealing just which groups are being supported by Government funding in the community.

One challenge seen by the Road Transport Forum for both our industry and the Productivity Commission is how to ensure that Governments develop sufficient courage to admit that community service obligations are being provided. Furthermore, Governments need to go the extra step and ensure that community service obligations are not in themselves a disguised form of assistance to the provider - rather than an open form of assistance to the (apparently) intended recipient.

The second is the broader issue of whether the Australian economy can meet the costs of sustaining two world class transport systems. We currently run two systems at less than world standard, with Australia being the loser. Infrastructure investment decisions need to be made against agreed criteria, on the basis that priority should be allocated to those projects that will provide the fastest return. This in turn will create the wealth or funding to do other projects.

This is a difficult question for governments given the emotional attachment to rail and the multi-user flexibility of road. An objective judgement would clearly show rail cannot carry out the task that road transport is able to. The reverse does not apply. These are questions that deserve some examination.

We would, of course, be pleased to address any further issues the Productivity Commission may have in mind.

Yours sincerely

RON FINEMORE

*RTF Chairman*