

**Submission to the Productivity Commission Inquiry**  
**into**  
**Progress in Rail Reform**

**Commonwealth Department of Agriculture, Fisheries and Forestry - Australia**

**December 1998**



## **Executive Summary**

Agricultural, and to a lesser extent forestry, industries were traditionally among the most significant users of rail in Australia. Despite the cut back of rail services in non-metropolitan Australia and the predominance of road transport today, rail continues to be an important mode of transport for some agricultural industries. The competitiveness, efficiency and quality of rail services all have an impact on the international competitiveness of the industries which use them. As a consequence, the Department of Agriculture, Fisheries and Forestry - Australia (AFFA) and portfolio industries have a keen and ongoing interest in rail reform.

The decade of the 1990s has seen various reforms to Australia's rail system as a result of the introduction of National Competition Policy (NCP), the rationalisation of State rail systems and the privatisation of elements of both Commonwealth and State rail systems. AFFA believes that these reforms have delivered net benefits to portfolio industries. AFFA is of the view that further rail reform is required before portfolio industries which use rail achieve the fullest benefits.

The most pressing reform issues in rail transport today for portfolio industries are:

- . (i) the cost of rail transport;
- . (ii) getting the access regimes right so that they can generate genuine competition between providers of above track services;
- . (iii) addressing network blockages/bottlenecks;
- . (iv) review of lines and terminal sites taking into account their suitability for today's agricultural production; and
- . (v) improving service delivery through increased competition and new investment in rail infrastructure.

Both cost savings and improved service delivery can be achieved through furthering the adoption of access regimes and structural separation of monopoly and contestable elements of rail systems. The processes involved to date in achieving access and structural separation have been time-consuming and expensive. In future more attention needs to be given to achieving the best possible outcome at the lowest cost.

High freight rates are an ongoing problem faced by portfolio industries. Not only do freight rates have to be more competitive, but the mechanisms for setting them need to be more transparent so that users can be confident that they only pay for what they use and are not subsidising other elements of the rail service.

While new government funds are limited in both amount and impact, privatisation is assisting by further improving service provision. There is evidence that a new culture is developing, with a new focus on the customer and market demands, on quality service,

innovation, and, at employee level, some innovative steps at sharing the benefits of reform directly with employees.

There is considerable scope for cost savings and improvements in services to be achieved by introducing changes to the management and operation of rail services. These include improving train running times, increasing track speeds and axle loads, reducing shunting costs, wider use of single person train crewing, ensuring consistent train operating practices across state borders, improving loading/unloading operations, and encouraging the uptake of newer rolling stock.

The costs imposed by regulation are an issue for some operators, particularly smaller operators. A key issue is whether the regulatory regime is appropriate to all levels (for example, to branch lines, compared to busy urban networks) and all types of operations across the rail industry.

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. A new culture and approach which is evident in the privatised railways needs to be reflected in railways that continue in Government ownership. Opportunities exist for the rail and agricultural sectors to work more closely together to identify how they can both benefit from improvements in transport and in identifying new domestic and international markets.

One consequence of reform has been the reduction or withdrawal of rail freight and passenger services from many rural and regional areas, usually leaving business and consumers with fewer transport options. The continuing reduction in services becomes self-perpetuating with fewer people choosing to use the infrequent, and at times less convenient, services that remain.

AFFA believes that where governments choose to retain subsidised passenger rail services in non-metropolitan Australia, they should provide direct funding for these subsidies rather than using freight costs to cross-subsidise these services as has been the case in the past. Such community service obligations should be transparent funded from the budget of the relevant government.

AFFA supports a balanced approach to future rail reform which considers both industry competitiveness and community needs.

## Introduction

The Department of Agriculture, Fisheries and Forestry aims to contribute to rising national prosperity and quality of life through competitive and sustainable agricultural, fisheries, forestry and processing industries. To achieve this the Department works with other Commonwealth and State government departments and agencies, industry and the community to improve the competitiveness of portfolio industries through work in a number of key result areas. These include:

- **increased productivity** - increasing industry output by using existing resources more effectively;
- **enhancing value** - increasing the value of what Australia produces;
- **investment and uptake** - making Australian products and services more attractive to investors and customers;
- **market access** - helping to make overseas markets more open and accessible to Australian exporters and investors;
- **sustainability** - managing our natural resource and resource-based industries so that the needs of the present generation are met without compromising the ability of future generations to meet their needs; and
- **infrastructure** - providing the infrastructure on which Australia's resource-based industries and their communities depend for their viability.

Within this framework, AFFA has a number of policies and programs which focus on enhancing the capacity of agricultural businesses and communities to meet emerging challenges and opportunities, encouraging social and economic development in rural areas, and providing a social support system for farming families which is comparable to other community members.

Rail reform and the efficiency, effectiveness and overall competitiveness of Australia's rail systems, including both networks and services, can impact upon these areas, either directly or indirectly. There are significant unresolved issues in rail reform which affect the competitiveness of portfolio industries and the services and infrastructure available to rural and regional communities. In this submission, AFFA aims to draw attention to these and to provide a number of key messages about the reforms which have been implemented to date and identify directions for future reform.

## Rail and portfolio industries

Bulk commodities produced by Australia's primary industries are some of the most important freight traffic for our railways. For example, the grains industry accounts for 8.5 per cent of total national tonnage transported by rail, with wheat producers the major users of rail services. It is estimated that the industry produced 18.5 million tonnes of wheat in 1997-98 (ABARE, 1998) of which 14.8 million tonnes was exported. The

Australian Wheat Board (AWB), on average, moves 11 million tonnes per annum of grain by rail. The AWB has estimated that grain travels on approximately 61 per cent of total track kilometres in Australia.

A number of other portfolio industries use rail to transport their product for processing, and to export and domestic markets. These include the beef industry in Queensland and New South Wales, the sugar industry in Queensland, the export woodchip industry in Tasmania and, to a lesser extent, the wool and dairy industries in New South Wales. The cotton industry is a significant user of rail services for the movement of containerised cotton to port for export. Small amounts of bulk milk are moved by rail to cities for the liquid milk trade. In particular, Sydney receives some milk by rail from North Coast New South Wales locations.

Australian rail systems also carry considerable traffic in containers from centres where sufficient quantities of such traffic is available, mainly the ports and capital cities.

### **Summary of rail reforms in the 1990s**

The 1990s have seen a number of changes to Australia's rail system. Reforms have included:

- . those introduced under National Competition Policy (NCP) including access to track;
- . rationalisation of State rail systems; and
- . privatisations of both Commonwealth and State systems.

#### National Competition Policy reforms

In April 1995 the Commonwealth, States and Territories agreed to implement a package of reforms designed to deliver the benefits which competition, properly harnessed, can bring. The commitments made by governments under NCP are contained in three intergovernmental agreements. As a first step toward fulfilling its commitments, the Commonwealth enacted the *Competition Policy Reform Act 1995* creating two new institutions to oversee the implementation of the package. They are the Australian Competition and Consumer Commission (ACCC) and the National Competition Council (NCC).

Under the NCP, Commonwealth, State and Territory governments agreed to implement seven categories of reforms, of which four are directly or potentially relevant to rail. They are:

- establishing arrangements for access to nationally significant infrastructure;
- processes for restructuring public sector monopoly businesses to increase competition;
- introducing competitive neutrality so that government businesses do not enjoy unfair advantages when competing with private businesses; and
- extending prices oversight to certain State and Territory government businesses.

#### Rationalisation of services at the State level

One consequence of reform at this level has been the withdrawal of rail freight and passenger operations from many 'thin' routes servicing rural and regional areas, following assessment of the financial performance of those services. Typically this has left businesses and consumers with fewer transport options. For example, most regional passenger rail services have closed since the 1960s. In some cases, rail operators have switched the available rail traffic to bus services, sometimes run by the rail operator and in other cases by private bus operators. General freight formerly carried by rail has often been picked up by road freight operators. In other cases, services have been abandoned. The details of rationalisation vary from State to State. As a good deal has already been written about the closure of branch lines in rural and remote areas, we will not repeat that process in this submission.

A high degree of rationalisation has occurred, much of it involving reducing services. Nevertheless, the States continue to express a desire to have a stronger and more efficient rail sector than has been achieved thusfar. In practice, if this is to become a reality, it will only occur after further investment from Commonwealth and/or the States, complete or partial privatisations, or other private sector investment.

### Privatisations

The privatisation of rail at both Commonwealth and State level has been one of the key economic reforms of the 1990s. A significant step was taken on 28 August 1997 when the Government announced the successful bidders for the former Australian National railway system:

- The South Australian-based passenger operation, comprising the Indian Pacific, Ghan and Overland trains, was sold for \$16 million to the Australian-led consortium Great Southern Railway;
- The South Australian intrastate freight workshops and rolling stock were sold for \$57.4 million to a consortium including US railroad Genesee and Wyoming Inc., Clyde Engineering and Transfield; and
- The Tasrail system was sold for \$A22 million to a consortium called Australian Transport Network, including Tranzrail and Wisconsin Central.

The Commonwealth retains part ownership (with the New South Wales and Victorian Governments) of National Rail (NR) which was formed in 1993 and is Australia's largest rail-based carrier of general and bulk freight, which it carries on the national interstate network. NR earns approximately \$450 million in revenue from customers annually. We understand the intention is that it will be privatised in the near future.

In April 1998 the Victorian Government announced its intention to sell the State's rail freight operations (V/Line Freight Corporation) together with a long term lease from VicTrack over the non-metropolitan intrastate track, signalling and train control. It is expected the rights of other operators to access the track will be preserved.

The Western Australian Government is preparing to sell the freight business of Westrail, that State's rail authority. A special sale taskforce has been set up and is intending to call for expressions of interest by December 1998.

In addition to these asset sales, private investors have been active in putting forward proposals for new Alice Springs-Darwin, Melbourne-Darwin and Sydney-Canberra services.

There are some early indications of improved service following new investment in rolling stock and other facilities. These suggest that privatisation is having a positive impact on service provision. There is also a new culture developing, a new focus on the customer and market demands, on quality service, innovation, and, at employee level, some innovative steps at sharing the benefits of reform directly with employees.

Where rail assets remain in public ownership, the operators should aim to continuously improve efficiency, consistent with maintaining safety and other service standards. Where this leads to lower unit costs the savings should be in part or wholly passed on to users.

#### **Key messages:**

- **Rail assets, particularly those of an 'above-track' nature, need not be owned by governments. Generally, governments should focus on policy and regulatory issues rather than ownership and management of rail assets.**
- **Where rail assets remain in public sector ownership, savings from reform should be passed on to users.**

#### **Reforms affecting portfolio industries**

Reform has impacted both positively and negatively on many portfolio industries and on communities in rural and remote Australia. On balance, we believe that the reforms have delivered net benefits. However, although there has been some progress, the cost of rail transport remains a significant issue for primary industries.

Reforms which have had a direct impact on portfolio industries include line closures and two categories of NCP reforms: access regimes, and the structural separation of monopoly from contestable elements. Portfolio industries have also been affected by reforms to the prices charged for rail transport and by reforms affecting investment in rail by governments and the private sector.

Generally, line closures have had a negative impact on rural and remote communities, while some of the NCP reforms including access and structural separation have resulted in some benefits in the form of lower prices and improved quality of service, albeit at less than the expected rate of benefit.

#### Access regimes



Major infrastructure facilities including rail networks typically have the characteristics of a natural monopoly, meaning that it would be uneconomic for more than one business to build and operate those facilities in the same area. The issue of access is about establishing arrangements which would allow service providers other than the owner to use the infrastructure facility, thereby introducing competition. The establishment of appropriate access regimes is important to portfolio industries because they would allow new rail service providers to use existing track networks introducing competition and, ideally, improved services and/or lower freight rates. This in turn could make Australian exports like wheat freighted by rail to port more competitive.

The Commonwealth and the States have agreed to establish access arrangements and the NCC is tasked with oversight of the implementation of the access component of NCP.

Businesses have three options through which they can gain access to infrastructure. They are:

- . an undertaking, under which an infrastructure operator can make a voluntary undertaking to the ACCC setting out the terms and conditions on which access is offered;
- . a declaration, under which a potential new entrant can apply to the NCC to have an infrastructure declared by the relevant Minister, after which a negotiation of terms and conditions takes place; and
- . by way of a specific State or Territory regime.

The Commonwealth and the States are at varying stages in the implementation of access regimes. Most of the work to date on access to rail has involved infrastructure in New South Wales, Queensland and Western Australia. The NSW and Queensland governments have also applied to the NCC to have access regimes declared as 'effective'.

In New South Wales in April 1997 a Task Force formed to represent users of the Hunter Railway Line applied to the NCC for declaration of that service. It sought to establish its case by submitting that:

- the NSW Rail Access Regime was incomplete and inappropriate;
- the terms and conditions of access were neither reasonable nor commercial; and
- the terms and conditions acted to discourage access and competition.

In parallel with the Task Force application for declaration, the NSW Government submitted its rail access regime to the NCC for certification in June 1997.

In September 1997, the NCC accepted the Task Force's application and recommended to the NSW Premier that the Hunter Valley rail line be declared for access.

In November 1997, the NSW Premier rejected the NCC recommendation. The Taskforce appealed against this decision to the ACCC. The appeal was heard in April 1998 and in June 1998 the Federal Court determined a full bench of the Federal Court would hear the case. In October 1998 that appeal succeeded.

In 1997 the Queensland Government established the Queensland Competition Authority (QCA) to administer an access regime in Queensland. In March 1998, Queensland applied the access regime to certain rail services by regulation. The Queensland Government in June 1998 applied to the NCC to have the regime for access to certain rail services certified as “effective”. Queensland indicated in its application that it would be submitting a voluntary undertaking on conditions of access including details of pricing principles, the provision of information to access seekers, and safety requirements.

AFFA believes the proposed Queensland access regime provides a framework for negotiation of the terms and conditions of access which is consistent with the terms of the Competition Principles Agreement. While we welcome this, we believe the regime serves as a framework only, and there is a need to give greater attention to details in addition to general principles. We consider that fair and reasonable access arrangements need to take account of a number of factors including transparency in pricing and decision-making, economic efficiency, and independence.

We note that provisions relating to pricing principles, the provision of information to access seekers, and safety requirements are to be included in an undertaking being prepared by Queensland Rail (QR). QR’s access arrangements may become a benchmark that will be used to determine access fees for other competitor service providers. We note that QR will be prevented from providing access to itself on terms more favourable than the terms offered to a competitor and welcome this critical component to the proposed integrity and transparency of the regime. However, attention also needs to be given to a mechanism that ensures QR’s own access fees are fair and reasonable and do not contain cross subsidisation elements that inflate access fees or restrict access. We note that details on the mechanism for calculating rail freight rates will be provided in the undertaking being prepared by QR.

Transparency is an important factor in assisting companies to determine their cost structure and identify areas where their competitiveness can be improved. Service users can benefit from transparency that separates out the costs of supplying and operating the network. Transparency is also an aid to investors since it can provide greater certainty. A lack of transparency in pricing and price decision-making reduces user confidence in the service provider and provides the opportunity for excessive charging.

While the proposed Queensland access regime does not cover pricing principles in detail, the access regime document does state that industries’ capacity to pay will be considered in determining the prices charged for access. This aspect is one potentially of concern to the portfolio for economic efficiency reasons, as it may give rise to rent-seeking.

Such arrangements could reinforce previous practices that used rail services as a way of extracting economic rent from industry which have led to inefficient investment decisions. There may also be a reduced incentive for service providers (because they are already

receiving substantial profit margins) to improve the efficiency of services for higher paying industries.

The Queensland access regime appears to provide an acceptable framework for negotiations. However, as the outcomes of those negotiations will depend heavily on details to be included in an undertaking being developed by QR, which we are not privy to, it is difficult to make a complete assessment of the arrangements for access to rail infrastructure in Queensland.

Although access has not yet been formally established, the prospect of access has been a factor contributing to reduced prices for rail freight in Queensland.

We are increasingly concerned about the high cost to industry of negotiating access. In the case of the Hunter Rail Access Task Force, \$1.65 million has been spent to date on consultants and lawyers to research and argue the case. This figure is in addition to the cost of companies' staff time spent working on the issue. The issue of the administrative and bureaucratic costs associated with access is an issue for smaller niche operators who can sometimes provide rural communities with a low cost alternative to road transport.

#### **Key messages:**

- **Any pricing mechanism for access should be publicly transparent, fair and equitable.**
- **The process of determining access arrangements has been time-consuming and expensive. In future more attention needs to be given to achieving the best possible outcome at the lowest cost.**
- **Although access has not yet been formally established, the prospect of access has been a factor contributing to reduced prices for rail freight in Queensland.**

#### Structural separation of monopoly from contestable elements

Structural separation involves splitting a monopoly into smaller, separate entities. In rail this might involve separating track provision and maintenance and signalling from the operation of locomotives and wagons. The potential benefit lies within the contestable parts of the former monopoly, where the new competitive environment may result in lower prices and/or improvements in service quality. There are two potential advantages to portfolio industries from structural separation of rail systems. These are:

- . clearer, more definitive charging systems - this reduces the scope for cross-subsidisation between operating units, which we understand continues to occur, so the user can see what they are being charged for; and
- . the introduction of competitive pressures for improved services and lower prices.

Under NCP, governments are not required to pursue structural reform, but have agreed to a set of principles to ensure that business structure issues are considered before any privatisation or introduction of competition into public monopoly markets.

The New South Wales Government has implemented such a structural separation in its State Rail Authority (SRA). On 1 July 1996, the NSW Government structurally separated the functions of the SRA into four separate entities:

- the SRA, previously responsible for almost all aspects of the State's rail infrastructure and services, became primarily a passenger railway operator, made up of City Rail, Countrylink and a passenger rolling stock maintenance group;
- the Rail Access Corporation (RAC), responsible for managing track, and providing operators with access to facilities in return for commercially negotiated access charges;
- the Freight Rail Corporation (FreightCorp), a State owned commercial freight rail operator; and
- the Railway Services Authority (RSA), a statutory authority which supplies rail infrastructure (track) and rolling stock goods and services including maintenance, construction and repairs to the railway industry in general.

AFFA notes that, unlike New South Wales Government, the Queensland Government has not established separate organisations for providing the 'below track' infrastructure and the 'above track' freight carrying service. While we do not necessarily consider this structure problematic, any structure must ensure that decision-making, particularly in the area of pricing, is transparent and independent (at arms length) and also seen by stakeholders to be transparent and independent. This will provide users with more confidence in the decision making process and the application of non-discriminatory pricing.

#### **Key message:**

- **AFFA supports the separation of contestable from natural monopoly components of rail service provision.**

#### Pricing

High freight rates are an ongoing problem faced by portfolio industries. In 1993 the Queensland Government announced significant reforms to freight rate arrangements. As part of these reforms:

- QR became a corporatised body on 1 July 1995;
- all new contracts negotiated by QR since 1992 have been on a strictly 'commercial' basis and existing contracts will be renegotiated on that basis as they expire;

- contracts extending beyond 2000 will be given the option of renegotiating in that year; and
- from 2 September 1993, two freight rate formulae - CPI minus 0.6 or CPI minus 0.3 - have applied to existing contracts, with pre-1992 contracts already on that basis.

These reforms have recently been superseded by Queensland Rail announcing on 4 October 1998 that Queensland rail freight charges would be frozen for 1 year to provide relief, in an effort to cushion the effect of the Asian financial crisis. AFFA welcomes this announcement and supports any relief for rail freight charges.

The negotiation of a commercially acceptable rail freight rate is a critical factor in the development of regions such as the Carpentaria-Mt. Isa area. AFFA encourages changes which will improve the competitiveness of the rail industry, thus reducing freight costs and delivering transport and handling efficiencies for portfolio industries.

**Key message:**

- **Where rail infrastructure and services are provided in a monopoly environment, pricing should be transparent, reflect adequate return on investment and determined at arm's length from governments.**

General rail reform issues

While the portfolio considers access arrangements, structural separation and pricing to be the main areas in which reform is required, there are a number of more general issues associated with the management and operation of rail services which could benefit from reform. Reforms in these areas could deliver cost savings and improvements in services.

Industry has identified such areas to include:

- improving train running times;
- increasing track speeds and axle loads;
- reducing shunting costs;
- wider use of single person train crewing;
- ensuring consistent train operating practices across state borders;
- overcoming network blockages;
- improving loading/unloading operations; and
- encouraging the uptake of newer rollingstock.

AFFA considers that every effort should be made to resolve these issues. Most are the responsibility of rail service providers and users, although government may have a role to play in encouraging change. Increasing track speeds and axle loads and encouraging the uptake of newer rollingstock may also have implications for investment in rail infrastructure and services.

There is scope for improvement through the development of long-term strategic partnerships between transport providers and customers. 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. This is already occurring to a limited extent. For example the cotton industry is achieving efficiency gains by locating storage facilities in low-cost regions. International experiences with private sector injection are that reforms of this type are clearly delivering benefits to all the stakeholders. However, this new culture and approach which is becoming evident in the privatised railways needs to be reflected in railways that continue in Government ownership.

Opportunities exist for the rail and agricultural sectors to work more closely together to identify how they can both benefit from improvements in transport and in identifying new domestic and international markets. In this respect New Zealand is leading the way with the recovery of freight previously lost from rail to road, in extending their role as a transport manager for the total logistical needs of their customers, and actively working with their agricultural customers to identify new marketing opportunities and transport solutions, both domestically and internationally.

### Investment in rail

The need for more investment in rail transport systems was confirmed in the recent Neville Committee report. That report included three recommendations involving injections of Commonwealth funding: the first of \$750 million to be invested in the national track over three years, the second of a further \$2 billion over ten years for rail infrastructure of national importance, and the third a once-off Commonwealth grant to standardise communication equipment and safety operations.

Recent privatisations have created opportunities for increased private sector investment and AFFA supports this means of attracting much-needed new investment. That the private sector has been active in proposing new projects including the Alice Springs-Darwin and Melbourne-Darwin routes is evidence that the environment for investment in rail is improving.

However, new rail infrastructure is sizeable and costly. If left entirely to the private sector, new rail investment may not occur because of externalities, different risk preferences or because of the length of time the investment takes to generate returns. Thus, there may be instances where governments should be involved in rail infrastructure provision. In those cases where new investment is publicly funded, governments should consider the investment in the light of its other budgetary and policy priorities. Proposals to spend government funds should be in the national interest and will also need to be considered in

a consistent long-term cost benefit framework that accounts for all costs and benefits, including social and environmental.

AFFA believes that by adopting a national approach to rail infrastructure it may be possible to open up new regions and industries. A high percentage of this rail freight would be, as existing freight business is, carried on intra-state networks and caution must be taken to ensure there is no undue emphasis on investment in the inter-State lines. For this reason, an approach which concentrates on overcoming the bottlenecks and blackspots in the intra-state networks should be considered when funds are allocated to projects.

**Key messages:**

- **Investment in the non-monopoly elements of rail should be privately provided, unless there are very strong reasons for government involvement.**
- **Government has a role in infrastructure provision in limited circumstances where private investment is not forthcoming due to externalities or other forms of market failure, or for strategic industry development reasons.**
- **Extensive cost-benefit analysis should be used as a basis for deciding whether government should invest in infrastructure projects.**

When Australia's road and rail transport systems are compared, it is apparent that there is a considerable difference, in favour of road, in the levels of investment, both public and private, in the two types of infrastructure. The high level of investment in road infrastructure has improved the cost and quality of the service provided by road transport operators, while rail has not had the benefit of the same level of investment. As a consequence, the efficiency and competitiveness of rail have been adversely affected. For example, on some routes containers cannot be double-stacked because of the height restriction imposed by certain bridges and tunnels.

**Key message:**

- **The imbalance between investment in rail and road infrastructure justifies additional government investment in rail infrastructure, particularly where private investment is not forthcoming or significant externalities exist.**

A systematic and reliable analysis comparing the taxes and charges paid by road and rail transport is beyond the scope of this submission. However, we note that the Government's tax reform package includes measures which are expected to improve the absolute (if not the relative) competitive position of rail. The implementation of the new tax policy is an opportunity to put in place a more consistent and equitable approach to road and rail transport taxes and charges.

**Key message:**

- **The implementation of the Government's new tax policy is an opportunity to put in place a more consistent and equitable approach to road and rail transport taxes and charges.**

## **Effects on competitiveness**

Except where services have been withdrawn altogether, reform has generally had a positive impact on the competitiveness of agricultural and forest industries. However, some impediments to competitiveness remain. There are a number of industries whose competitiveness is constrained by the present state of rail transport in Australia. Where an industry requiring bulk transport does not have access to cost effective rail services, it is at a disadvantage, even though road infrastructure may be in place. For example, high transport costs translate into lower overall returns to wheat growers and impact directly on the competitiveness of Australian growers in world markets. It is also worth noting that delays and inefficiencies in moving grain may impose additional up-country storage costs on growers. These costs can be high with estimates around \$2/tonne/month. Transport costs impact on the AWB's business and so it is a priority to seek to achieve improved efficiency to lower costs.

Some of these issues are being addressed by service providers in Western Australia and Queensland by the upgrading of country branchlines, old locomotives being upgraded or replaced with new units, information technology being used to ensure resource utilisation is optimised, and closer working relationships being developed with customers than previously experienced.

Information provided by AWB Ltd suggests that whilst rail charges have fallen, road is increasing its share of AWB Ltd's business, especially with domestic customers. Road transport offers better service because of the direct delivery from the farm to the end user and the truck driver is able to assist with truck loading and unloading. Experience has shown that the government owned railways have been unable to effectively respond to the new competition.

## **Some negative consequences of reform**

Although the evidence to date is largely anecdotal, the effects of reform have generally been positive. However, there have been some negative consequences too. These have mainly involved reduced choice for users of rail in rural and regional Australia as a result of line closures or reduced services.

### Reduction of non-profitable services

As a general comment, the Australian rail system has transformed itself in recent decades from a general carrier receiving and delivering goods at stations in many large and small communities, to a bulk carrier focusing on the movement of large quantities of commodities such as grain.



The movement of general freight, fertiliser, livestock, wool, fruit and vegetables, which were once major components of rail traffic in rural areas, has virtually ceased because of the flexibility and lower cost of road transport in handling smaller consignments at irregular intervals. Rail has focused on its natural advantage of moving large volumes of produce between two fixed points such as from wheat terminal silos to the ports.

In the forest industries, rail services have been perceived as inflexible in providing services and rail has been substantially replaced by road transport although in the past rail and private tramway, combined with coastal access, was the main conveyor of timber.

Bulk petroleum fuel, an input in many agricultural and forest industries, is still transported to a substantial degree by rail to major regional distribution points. However, this traffic is increasingly shifting to road as competition increases the range of marketing options available in the petroleum retailing sector.

The only services continuing to offer rail transport of cattle are from Western Queensland to coastal meatworks and from Central Australia to Adelaide on the Alice Springs line. An occasional container of refrigerated meat may be hauled in a number of States, but the volume of this trade is not high as road transport has taken much of this trade.

Almost no wool is carried by rail from country areas to the selling centres. Some containerised wool may be moved to the ports after sale and dumping.

The impact of reduced services is greatest for producers of high volume low value commodities such as grain which do not naturally lend themselves to road transport. It is these producers who are most affected by line closures as they are then faced with the less efficient and more expensive option of road transport.

**Key message:**

- **There appear to be short term considerations impacting on decisions to reduce rail freight services that run counter to the long term comparative advantage that rail holds in regard to movement of relatively high volume/low value bulk commodities. Service planning should be encouraged in future to take a more strategic account of the rail industry's underlying economic strengths/advantages over road transport.**

Reduced choice in rural and regional areas and the definition of Community Service Obligations (CSOs)

Strong local communities and access to appropriate physical and social infrastructure, including transport, in rural and regional areas are vital to the ongoing viability of Australia's agricultural and forest industries. Twenty-nine per cent of Australia's population lives outside major metropolitan areas. The Department has a major responsibility to consider the interests of rural and remote communities and works to ensure that these communities have the infrastructure they need.

One consequence of reform has been the withdrawal of rail freight and passenger operations from many rural and regional areas, usually leaving business and consumers

with fewer transport options. With regard to passenger services, most regional rail services have closed since the 1960s.

Regional passenger rail services today exist only for larger towns such as Dubbo and Albury in NSW, Charleville, Longreach and Mt Isa in Qld., Bunbury and Kalgoorlie in WA and Bendigo in Victoria. Most rail passenger services, both rural and metropolitan, in Australia run at a considerable revenue deficit. Because of this, their future is constantly under review. It also appears to be easier to close down regional services than metropolitan services because of the smaller numbers of passengers involved. It should be noted that the continuing reduction in services becomes self-perpetuating with fewer people choosing to use the infrequent, and at times less convenient, services that remain. Reducing services also changes the externalities associated with rail services and, where these are positive, local councils may face higher road maintenance costs as a consequence of reduced rail services.

In the past, infrastructure pricing policies have been used in order to meet broader policy or social goals. This has led to cross subsidisation between rail users, usually from bulk commodity users to passengers. This can impose unnecessary net costs on society as industries are unfairly penalised through having to pay inflated prices to subsidise these broader policy or social goals. The resulting higher rail costs adversely affect the competitiveness of firms in the affected industries and result in resource misallocation.

To rectify this situation, CSOs should be clearly defined in a contract between a rail transport provider and government, and identify what market segments or railway lines are to be supported and why. The government and society would be able to assess whether the benefits from any CSO justify its cost or whether social/equity objectives could be met by other means.

If the funding for CSOs does not come from the Budget, an unfair burden is placed on the rail carrier, putting it in a position of being unable to compete with any new carrier that does not have CSOs. Investment distortions associated with profit-earning sectors of business supporting loss-making sectors will be avoided if areas funded by CSOs are clearly identifiable. The portfolio supports CSOs being transparently funded from the Budget.

#### **Key messages:**

- **Where governments consider that target groups (such as the aged, the disabled or remote communities) require subsidisation for the cost of using rail transport, these costs should be separately and transparently funded from the budget of the relevant level of government.**
- **Where rail services are rationalised, reduced or cut-out altogether in rural and regional areas, communities should be provided with alternative services to replace those lost. If replacement services cannot be provided commercially, there may be a role for government to subsidise such services or to require they be provided as a Community Service Obligation.**

## Conclusions

The most pressing reform issues in rail transport today for portfolio industries are:

- . (i) the cost of rail transport;
- . (ii) getting the access regimes right so that they can generate genuine competition between providers of above track services;
- . (iii) addressing network blockages/bottlenecks;
- . (iv) review of lines and terminal sites taking into account their suitability for today's agricultural production; and
- . (v) improving service delivery through increased competition and new investment in rail infrastructure,

The cost of rail transport is an ongoing concern, felt most acutely in industries like the export wheat industry.

The process for negotiating access to nationally significant infrastructure, including rail, has been time-consuming and expensive. Although some applications for access have been resolved, those involving rail have been caught up in long negotiations over pricing principles.

We concur with the statement of the Productivity Commission in the issues paper that "it is of some concern that such a long and expensive process is needed for governments to apply competition policies adequately to their enterprises, especially when such policies offer clear State and national benefits".

In the service delivery area, we recognise that rail has inherent strengths and weaknesses and that when compared to road transport, rail is highly competitive for some tasks and less competitive than road in others. Notwithstanding this, there remains a need to improve service delivery generally.

One way this can be achieved is through increased investment from governments and the private sector in rail infrastructure, and the case for more government and private investment in rail transport systems was confirmed in the recent Neville Committee report.

While new government funds are limited in both amount and impact, privatisation is assisting by further improving service provision. There is evidence that a new culture is developing, with a new focus on the customer and market demands, on quality service, innovation, and, at employee level, some innovative steps at sharing the benefits of reform directly with employees.

Although service provision is improving, 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. A new culture and approach which is evident in the privatised railways needs to be reflected in railways that continue in Government ownership.

Opportunities exist for the rail and agricultural sectors to work more closely together to identify how they can both benefit from improvements in transport and in identifying new domestic and international markets. In this respect New Zealand is leading the way with the recovery of freight previously lost from rail to road, in extending their role as a transport manager for the total logistical needs of their customers, and actively working with their agricultural customers to identify new marketing opportunities and transport solutions, both domestically and internationally.

We believe that the introduction of reforms in the management and operation of rail services will yield costs savings for portfolio industries and should be pursued.

Rail continues to play an important part in the competitiveness of many of Australia's agricultural industries, a number of which generate significant export income for Australia. It is still a significant employer in rural and regional areas and has an impact on the quality of life of rural and remote communities. AFFA believes that, in general, continuation of a balanced rail reform program, as outlined in this submission, will deliver significant benefits to industries and communities in non-metropolitan Australia.