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TRANSCRIPT
OF PROCEEDINGS

PRODUCTIVITY COMMISSION

INQUIRY INTO PROGRESS IN RAIL REFORM

MRS H. OWENS, Presiding Commissioner
PROF D. SCRAFTON, Associate Commissioner

TRANSCRIPT OF PROCEEDINGS

AT MELBOURNE ON WEDNESDAY, 11 NOVEMBER 1998, AT 9.30 AM

Continued from 10/11/98

MRS OWENS: Good morning and welcome to the second day of the Melbourne hearings relating to the Productivity Commission's public inquiry on progress in rail reform. The first participant this morning is Vicgrain Ltd. Would you like to give your name and affiliation for the transcript.

MR WATSFORD: Thank you. It's Graham Watsford. I'm the chief executive officer of Vicgrain, which is the now privatised grain-handling company bought off the government running 240-odd sites across the state, mainly linked to the rail system.

MRS OWENS: Thank you very much, Graham, for coming and thank you for the submission, which we've both read. My colleagues have paid you a visit earlier in our process. I understand you've just got a few comments that you'd like to make about some structural issues.

MR WATSFORD: Thank you. We've put in the submission but we'd really like to highlight what we see as not so much the progress but the impediments to future progress. I mean, we've seen significant progress in the system and I'm not sure what benchmark we're working off, but there have been some quantum links in progress in the grain industry and therefore the rail industry, and if there is a significant interdependence in Victoria, which I think everyone recognises, given that grain is probably 50 to 60 per cent of the throughput of the rail, for the freight part of the business anyway, and therefore anything that impacts on rail efficiency impacts on grain efficiency and the other way round. Therefore we are vitally interested as an organisation and as an industry, given that we do have 4000 grower shareholders who are also paying the bills for a lot of this, to make sure it is as efficient as possible.

If we look at again some of the history of how the rail system and thegrain system have developed, we've only got to go back about 10 years and there was a significant amount of regulation of firstly the product; secondly, the rail system; and thirdly, the handling system. Whilst that had some economic disbenefits that people might see, it certainly allowed a system which could create an environment where you could invest with some security. Therefore you had certainty because, apart from drought or other impacts, you knew you were fairly safe to get the product.

When we look at even when the handling system and the rail system were within the same ministry within the government, there was this ability to cross-invest, if you like. In fact, if you look at the last major, I think, watershed in Victoria when we had a significant improvement in productivity, it was probably after the result of the CANAC study in the mid-eighties when there was $35,000,000-odd, I think the figures were, spent by our predecessor organisation to improve things like the loop line at Geelong and the siding links and these sorts of things, which led to significant productivity improvements in the total system. You could do that in those circumstances when you had that level of surety.

What we've found now is that we've now had a privatised part of our business and we've had a deregulated rail system, so the handling has been deregulated, the transport has been deregulated but we’ve still got a regulated product sitting over the top of this whole system. We see that as the limiting factor at the moment that is not allowing us to get the full development or the flow-on of the productivity benefits that we still see are required, because there’s no doubt we’ve had this progression, but when we look at the system we don’t just look at rail as being the component from our business, or the grain-handling business, if you like; we look at transport in total. Therefore you’ve got to look at the interface.

If you look at our business, for example, this year, whilst the crop will be down a bit, our first budget figures out of, say, a $3,000,000-tonne movement of grain, 1.6 million tonnes of that product was going to be - its first movement was by road, in a lot of cases to a very near railhead to bring it into the system, but it was a significant amount of tonnage which has a dual relationship, if you like. We’re not convinced that the system as it sits at the moment is necessarily the thing that’s going to create the most efficient mechanism. We’re now seeing a combination of road rates being now very competitive with rail, for example, and therefore the old mix of rail and road we see as probably changing significantly in the future.

There’s no doubt in our minds that rail into our terminal ports is the most efficient mechanism, but we’re not convinced that around the periphery it is the best combination to take it to the nearest railhead, put it on rail and bring it down to the ports. The difficulty we have in trying to sort that out is that, unless you’ve got control over the product, which is again highly regulated, it’s very, very difficult to actually manage that whole situation because, if the reduction of transport costs is not the prime objective of everybody in the exercise, you then don’t lead necessarily to the lowest cost.

So it’s these structural issues that I think we have to address in Australia, not only Victoria, to try and see how we can get this transport more efficient. It’s effectively saying, "Look, we’ve deregulated parts of the business but we haven’t deregulated the total business, therefore we’ve still got some significant impediments to what we think is the necessary progress." We’ve just spent a fairly significant amount of money looking at how we can get a more efficient system within our - we’ve reviewed our old transport system ourselves. Clearly that requires a different level of input in the way that pricing is done and the way all these sorts of things are done in the transport system. For the same reason that people are saying to us, "We want to see your prices unbundled," we need to see the same sort of thing in the transport system.

We have, for example, in our industry or our system significant cross-subsidies between particular areas, and the rail system has those as well. We’ve got to start looking at how we not drive them out but actually identify them and then manage the transport task within that as well. So I think that’s initially what we’d like to say. We think there are still lots of reforms to go and we think there are significant reductions that can still be made, but we’ve got to get a different structure as to how we deal with this whole situation.

MRS OWENS: Thanks very much, Graham. I think you mentioned that what is still highly regulated is the product itself, and I'm not quite sure what that's actually referring to.

MR WATSFORD: In our sense we have wheat, which is - probably 75 per cent of Victoria's grain crop is exported as a concept, through our system anyway.

MRS OWENS: So you're talking about the single desk.

MR WATSFORD: The single desk we've got for wheat and for barley. Probably 60 per cent of the product is therefore regulated. We've probably got the most deregulated state of any state in Australia but we've still got a very high percentage of regulated product. What happens in that sense is if you sell to the regulated marketer, effectively, you've got to buy their freight as well. So the issue from that point of view is that 60 per cent of the market tends to dominate or control what the mechanism is for the transport system underneath that. That's the issue from our point of view, that the benefits that we're seeing - and I don't want to get into an argument about whether single desk - - -

MRS OWENS: No, that's outside the scope of this inquiry.

MR WATSFORD: Yes. But all we're saying is there's a potential cost associated with that. Even though you might be getting a benefit on the other side, it's not necessarily providing the best environment to move forward on transport progress, if you like, in that sense - so leaving the argument of whether it's, as I say, a good thing or bad thing aside.

MRS OWENS: Your submission on page 8 has got quite a nice little diagram about the Victorian situation, where there are contracts between Vicgrain and the Australian Wheat Board and the Barley Board and contracts between those boards and V/Line freight, but you don't have the direct connection. We were talking to the Australian Wheat Board yesterday and they said, "This is now a sort of residual problem for Victoria and it's been resolved in some ways in other states through tripartite agreements." Do you think that's the way it's going to go in Victoria as well?

MR WATSFORD: We think the way it's got to go - whether the other states, our other colleagues, would say it's resolved I'm not sure; we can ask them in the exercise. That would be at least an initial step of getting somewhere. Whilst it's hearsay evidence, our colleagues in South Australia are saying now they're getting a much better relationship because they're dealing directly with the transport operator in a deregulated sense over there. So it may be that just deregulation of the rail system may well facilitate some of the issues we're talking about. We're not sure. But certainly we've got to get a direct relationship between whoever is the storer and the transport operator.

If you look at all of the overseas models, it tends to work in that way and, if you look at the domestic models in the rest of Australia, all of the private storage operators tend to be an integrated business of a truck business and a storage business. That's how they actually develop their business. We're very unusual in the way we've set up in Australia. In fact, the Western Australians have now just launched into their own truck business over there, for example, to try and get some of these synergies to a much greater extent than what they've been in the past. But when you look at the North American or Canadian models there tends to be a significant linkage between the storage and the transport operator.

As I say, we haven't needed that in Australia because we've had this significant amount of regulation which has bound them together. Once we've actually started to pull the pins out of the regulation, we haven't actually worked out yet how to put them back together to get the efficiency driven through the system. Rather than just saying, "Competition in all these areas is a good thing," we've actually got to nut out a better structural way to work this out, and that's where we've been a bit limited. What we're saying is that we've pulled out a couple of the pins and left some of them there. We're in a transitionary sort of phase until we actually get the whole system sorted out. That's really what we're saying: there are still these impediments there to getting an efficient system.

PROF SCRAFTON: Do you think that the sale of V/Line Freight will help the resolution?

MR WATSFORD: Certainly in all the people that we've spoken to as the potential bidders, they are now very cognisant of the issues. We've certainly put in some submission to the government on it and I think they're starting to understand the issues as well. So we are hopeful that that will progress the issue. I'm still very wary, though, that if we want to do something which is contrary to the issues of the party who has got a regulated product on it, it still might not lead to those significant efficiencies that we're talking about. There are some where if it doesn't suit the market purposes it's clear that there's a lack of incentive to actually progress down the path of trying to get the most efficient system. We hope that we'll be able to drive that through, but we haven't been all that successful to date.

PROF SCRAFTON: And in your submission you mention on page 12 the three organisations that you understand are the three main proponents. Is that still the case?

MR WATSFORD: I think there's probably another one now and the hearsay evidence is actually another one on top of that. We don't know who they are though so we believe there's probably four serious ones who have spoken to us on regular occasions. Whilst there was I think a fair divergence of views at the start of that process, I think it's clear now that there is a much greater understanding of the issues in Victoria. I mean, it's not an issue where you can say we'll run block trains or big trains to some of these sites and pick up large lumps of grain and move it in the most efficient form because the market is not like that in Victoria and I think they're starting to get a realisation of that as well. That's why I think what we're saying is that some of these movements might not be best suited to rail alone. They may well be best suited to a more variable or a more flexible type of transport service.

MRS OWENS: Including just taking it on a truck, picking it up in a truck and just taking it straight to port.

MR WATSFORD: I think what we're saying is that there's probably a lot more interim movements that may well be more efficient. When we get down to little parcels of grain, the last 2 or 3 hundred tonnes in a bin, for example, it sits there until the market calls it down. We think from our point of view - and that's very expensive for us and for the transport operator so if they've got to pick up three or four wagons at a time at a site it's a very, very expensive process and we've got to send a crew out to load the train, they've got to send a crew out. There are things such as we think if it was done by truck the one driver could actually do the paperwork and the outloading and those sort of things for these small parcels and get it to one of the more efficient sites. Those small sites might only be 50-tonne an hour elevator capacity. These bigger sites might have 1000-tonne an hour elevator capacity - become very, very efficient mechanisms for rail-based movements.

We don't think that the amount of tonnage that will go to the ports will probably vary dramatically by rail. It's just the total haul. So I think - I mean, we're only guessing because it's very hard to model but there's currently 720 wagons in the V/Line fleet. We would guess you could probably get that down to 400 or between 4 and 5 hundred and therefore get a significant improvement in capital. That may allow us then also to invest in new wagons where we've got significant problems with the current technology for example. So the current configuration, as I say, we don't think is probably at its optimal sort of stage so we think this concept, which is really a continuation of the central receiver point philosophy which came out of the CANAC but it's really got to be now upgraded significantly we think. So there's lots of areas like that that we think are the next phase and hopefully any new owner will be keen to actually sort of move down that path. We're not convinced, but anyway that's what we were trying to pursue.

PROF SCRAFTON: Also in your submission you point out that you keep your own options open; whether this can be agreed upon by the parties or whether it's better to go to a hook and pull arrangement in which you're more directly involved.

MR WATSFORD: Yes, I think our greatest concern there was to make sure there was track access regimes; that you did have the option because the worst thing was going to be if it's sold and then somebody has then recreated the monopoly and doesn't give you any option in terms of the competition. That seems to be in place. I mean, we haven't seen the legislation on it yet but we understand that's in place so it does mean that there will be options there, so that should be - - -

MRS OWENS: Sorry, in terms of these options you've got the hook and pull option that Derek mentioned and you've also got another one where you just do a deal with the successful proponent to carry your grain in its fleet. Which of those options, if you had your choice - I guess it depends on dollars and which one you can do better but would you prefer to run your own wagons or would you prefer - - -

MR WATSFORD: I would much rather not be a train operator, I have to say, conceptually. So I don't want to drive trains but if I have to we would, if we think that's going to create the efficiency. We don't want to necessarily lease the wagons but we will if we have to. We'll look at the technology of a hook and pull. We'd much rather have a sort of interactive contract that said - and assuming they've got a fair or an adequate rate of return on their investment but, "Here is the cost of running that type out of our more efficient facilities," and that might be, I don't know what it would be, 3 cents per tonne kilometre; "and here's the cost of running over the inefficient ones," which is 5 cents per tonne kilometre or 7 cents or whatever the figure might be. We would need to understand that relationship so that we can say, "Where do we now put our investment in the thing?" because what has happened traditionally up to date - because we haven't had this accountability or responsibility within the industry, we've actually made significant investments in the wrong places.

We tend to, because we haven't had this responsibility in there, have pushed our investment back into the acquisition path which is back in the country and we're now at a phase where we're finding that we would be much better off to have a significantly greater amount of capacity at the ports to give more flexibility to the transport system because people are saying to us, "Look, if we could actually store or have more capacity there and run in a different fashion and look at the backloading opportunities, for example, we would be able to give you a much lower rate." Because we've never had that interrelationship, we've actually just put the tonnage where we think it's most efficient for us and then we say, "You just get your stuff there in a just-in-time basis." That hasn't led to - it's a misallocation of capital investment within our business. So again, that's the impact on our business as well that starts to come from not having this relationship sorted out correctly.

MRS OWENS: You've got a diagram on page 6 which shows grain as being about 40 per cent of the freight revenue for V/Line Freight and you say that one of Vicgrain's objectives is to eliminate the cross-subsidisation between the various types of traffic handled by V/Line Freight. What's cross-subsidising what? Is it grain cross-subsidising other things or is it- - -

MR WATSFORD: We tend to believe that. We might be sort of a bit altruistic in our views there but we tend to think that's the case, that there's a lot of product when you look at - it's very hard for us to tell. All we can look at is average rates for handling and we see a significant mismatch, if you like, between grain rates and some other product. We're no exactly sure what some of their distances are though or what the - we tend to think stuff is marginally priced against grain but, look, we don't have enough evidence to say there's a real big issue.

MRS OWENS: I suppose you can compare what the grain rates would be in other states although again, they're not probably strictly comparable because you've got longer distances and - - -

MR WATSFORD: Different geography as well.

MRS OWENS: - - - different geography and we were told yesterday more going for export markets on the west side. So you're not really comparing like with like, but what you're really saying is reflecting a sort of lack of transparency in the pricing arrangements. Is that right? Is that what you're saying?

MR WATSFORD: I mean, it's not an issue that we deal a great deal in, I'd have to say. On the other side of it, there are subsidies which we enjoy the benefit of. Don't get me wrong on this exercise - because there's on-farm pick-up which significantly benefits our system. But we need - because our fear is that somebody is going to come along and say, "That's a subsidy that I can actually put in my pocket." What we want is the transparency to be able to say what is the real cost or what is the real rate of the train operating costs of the system and then if we've actually got to pay the subsidy that's fine; we've got to pay that additional money to get the volume and the throughput, then that's fine. What we can't see is, as you say, this transparency of how we can make a more efficient system when we've got no access to the dollars that are driving the freight and the whole thing.

MRS OWENS: I suppose if you are indeed cross-subsidising other uses of the V/Line fleet, that potentially means that the charges imposed on you are going to be higher than they would otherwise be. That's what the cross-subsidisation would mean, which means that you're less competitive compared with - or rail is less competitive with road and so there's more going on road than may need to otherwise occur. It's changing the relativities between - - -

MR WATSFORD: Yes, I think that's right. I mean, we also have a cross-subsidy out of our system into the rail system as well which we can't work out how to claw back. One of the reasons why they've been able to reduce their fleet, for example, significantly in recent years is because we started to load 24 hours around the clock. We incur significant overtime penalties as a result of that which goes into our charges but because we can't get this relationship right, there's no way of actually recovering that and if we just keep putting our charges up we become uncompetitive as well so it's a very messy situation but it really is - we've got to get to the bottom of that transparency issue otherwise we're not going to generate the efficiency because we can't understand the signals. It may well be the most efficient way for them to operate but it's very difficult for us to understand and, as I say, until we understand it, we can't make the capital investments that may well be necessary to generate greater efficiency in the system. But yes, it does make us uncompetitive in total, with alternatives.

MRS OWENS: Another issue which has been raised - it's a related issue raised by other participants, is just generally the issue of competitive neutrality between road and rail and there's an argument that we don't have a level playing field and that if there were appropriate charges, particularly on the big heavy trucks, you would even it up.

MR WATSFORD: It may be. Look, there's always the issue of road costs and all those sort of things and if we started to pump a lot more onto road, and are they really picking up their fair share, from our point of view we're not sure that's an argument we can ever be involved with. I think that's a social argument and that's fine but it's very difficult for us to make a measurement of - we can only live within a system that says that is the road-based rate or that is the railways rate and take it from there. I'm not sure that if we get involved in the next phase of the argument we would get into a very messy argument which we've got no control over in the exercise but clearly it is an issue. Every time we say that we're going to move to more road, every local council in the state sort of jumps up in arms and they're already at us for road-based funding costs in the exercise, but there is no doubt - but on the other side of it as well, as I say, it's a bit related to that issue - we actually restrict people using roads into the ports because we don't have enough storage there and it's our most expensive storage and we don't want it clogged up. It may well be more efficient to put more storage at the ports and sort that whole sort of thing out. Then somebody has got to sit down and say, "Do we actually want a million tonne coming in by that mechanism or do we want it all restricted to the rail-based movement?"

PROF SCRAFTON: That's an interesting comment, Graham. You mention on page 14 about a role for government and when I first read that I thought in many ways what's happening is reducing the role for government but there are obviously going to be residual issues like this matter of road charging and so on which governments are still going to have to arbitrate or facilitate or work their way through with the industry and the industry being yourselves and the regulatory - - -

MR WATSFORD: I think that's certainly the case. What we've been saying is, if they want to have - I mean, you can't just take it for grain because if they're going to up road rates it's going to affect all the fruit and vegies and every other product. I mean, you can't just single out grain and say it has got to pay more. But you're right, the issue - what we're saying to the governments is if they want to keep it on rail, and that's the most efficient mechanism, it may be that they have got to facilitate or contribute this social contribution to the under wheel costs or the equivalent road-based damage movement, if you like, whatever that may be. That's where I think - that's up for somebody else or the community to decide and say, "Look, we really believe" - I mean, from our point of view rail is the most efficient mechanism of getting grain from our up-country positions to our ports. There's no doubt about that. It's the easiest to control, it's the securest generally and all those sorts of things. So for aggregating grain for ships, you can do it in 8000-tonne lots instead of 20-tonne lots, so it has significant efficiencies there. But the way we're heading is in fact that because road is becoming more and more competitive it's putting a lot of pressure on the system in total. Now, that's fine if that's the way we want to head but somebody has got to nut out that answer at some point in time.

PROF SCRAFTON: A few years Victoria did in fact go through that sort of exercise, didn't they, when they put some money into standardising some of the branch lines.

MR WATSFORD: Sure.

PROF SCRAFTON: I think serving Portland, wasn't it. They might have to go through that again with the rest - you mention that in your submission too, that they might take a look at standardising the rest of the - or whatever is efficient in the rest of the rail network.

MR WATSFORD: Yes. We've got some - I mean, we've got access to - what we're saying at the moment is we'd like to see standardised into Geelong, for our Geelong facility for example. It would give us access to a lot more market share out of southern New South Wales, we think. Now, again we don't have the costs either way of being able to say, "Well, we think that's a million dollars, therefore we think we can get some benefit out of it." Traditionally we've actually said we resist any - or we're ambivalent, if you like, to standardisation, because we've never seen the benefit sort of side of it coming through. Again I suspect it probably was a short-term view that we should have not taken, sort of thing, but there is a role for the government - whoever is the track owner, and that looks like being the government still, in terms of that whole track availability or track costs, if you like.

MRS OWENS: Just going back to privatisation, I've just got one other issue, which is only a very small one, but you've got a list of improvements in rail performance that you would like to see. We just talked about standardisation, but you talk about Portland and purchasing new wagons and so on. This is on page 14.

MR WATSFORD: Sure.

MRS OWENS: You talk about the increase in the storage capacity at Vicgrain sites and so on. What do you think the possibility is of all that sort of investment taking place if the system is privatised? This is V/Line Freight.

MR WATSFORD: I think there's a much better chance if it's privatised than not privatised. So I think that's a distinct chance. We've been speaking to the various potential owners. Whether we can actually get that into reality, I'm not sure. But I think they have a significant problem with this capital investment within the government ownership structure I think. It was the same problem the old GB had. Whilst it spent money, it's very difficult for them to in fact get that through the whole government-type process. I think there is significant chance - we've just written to the railways and said, "Look, there's a whole range of issues that we need desperately address," which we touch on there for example, in some of them, "where we're incurring a cost which is not being recovered." So we think we will get somewhere. What we're trying to say to the new owners is, "Well, there is potential capital here that you've got to spend," and I think they understand that sort of issue. Whether they actually spend it or not, I'm not sure. We're fairly hopeful that we will get a much better relationship under a privatised structure.

MRS OWENS: I think you need a really clear cut relationship between the new owners and the government, in terms of them sorting out who's going to do what.

MR WATSFORD: Correct.

MRS OWENS: I think part of that is happening with the franchising the urban rail network, because the government is making it clear what their expectations are of the bidders in terms of investment. I'm not sure whether the same is taking place at V/Line Freight. It probably is. I'm not quite sure. But hopefully the more that can be sorted out up-front before the sale takes place and the greater the clarity of who's responsible for investing in the rolling stock and storage facilities and so on, the better it will be for you, I would presume.

MR WATSFORD: Certainly. That's why we've written to the government saying, "Look, these issues are currently live, that we need fixing." Just the gravity feed on lines for example, where we have a significant problem where we've got to pinch-bar wagons up, so we've got to do a manual task to shift rail wagons instead of being gravity fed. It is a significant occupational health and safety for us. I mean, we have had people get injured - the tops of wagons, you know, when we've got people walking along the tops of wagons. We've got people inside wagons doing various duties. There are significant issues like that that we're saying to the government, "You've got to sort these out."

It's unreasonable for a new buyer to come in and say,"All right, you've bought the railways for X million dollars. Now spend 20,000,000 to fix up these occupational health and safety issues." You can't have the occupational health and safety legislation on one hand and try and sell an asset which doesn't comply with it on the other hand and then think that nobody is going to have a problem in the meantime. They're the sort of issues that we are trying to get sorted out with the railways and the government at the moment. But they are very big issues in our - not only our industry, across Australia as well, because it's inherently a dangerous activity. All of the injuries we ever get are generally always related to rail and the transport sort of system. So there are lots of things like that where we think that capital is required, which might not even have a great reduction of costs. It's just going to be a significant issue for us.

PROF SCRAFTON: The experience, certainly in Tasmania, tends to support that view, that if the bids are properly set out then the investment level can be clearly seen by all the parties before the sale takes place. Nevertheless, your comment is still valid: that in the end the new buyer has to make the investment down the line. If his expectations of the performance of the railway is different from what actually eventuates, well, then they might pull their resources back a little too. I mean, I think in the evidence that we were given from the South Australian operator he pointed out that his expectations and what is actually eventuating in some areas is quite different. But nevertheless, I think your generalisation is valid: that the environment is much better for that investment to take place. The experience of the last 10 years has been very mediocre.

MR WATSFORD: I agree.

MRS OWENS: I don't have any other questions. Have you got anything else, Graham, you'd like to say before we finish?

MR WATSFORD: No, I think we've covered all the issues that I think are of relevance or concern to us at the moment, so thanks very much for the opportunity.

MRS OWENS: Good, thank you very much. Thank you for the submission once again. I think the grain issues, like the coal issues, are quite important - to talk to the biggest customers and get that perception on the operation of the rail system I think is extremely important and of great interest to us. So thank you very much for coming.

MR WATSFORD: Thank you.

MRS OWENS: We'll now break for just 5 minutes and resume at 10 past.

MRS OWENS: Our next participant this morning is the Department of Transport and Regional Services. Welcome to the inquiry. Would you each give your name and your position with the department for the transcript.

MR WHALAN: Jeff Whalan, first assistant secretary land transport division.

MS BEETHAM: Robyn Beetham, assistant secretary, rail.

MR WILSON: Andrew Wilson, director rail policy.

MRS OWENS: Good, thank you very much and thank you for the submission which Derek and I have both read. At this stage would you like to make any opening remarks and then we'll have some discussion.

MR WHALAN: Thank you, and thanks for the opportunity to be able to supplement our submission with some comments today. As you would have acknowledged from the introduction, the division that I represent covers land transport - rail and road - and other areas as well. Both Robyn and Andrew are experts in rail. I'm somewhat new to the area but particularly interested when we get into the comments about the extent to which you're looking at the role of rail in relation to other modes of transport and the relativities between those different modes. In terms of our submission and this inquiry, it's interesting stepping back and looking at what's happened since the last inquiry done by the Industry Commission some 7 to 8 years ago.

While those people who worked quite closely to rail believe that there's agonisingly slow progress, as someone new looking at it, there's been quite remarkable progress over that period. So we've had the establishment of National Rail; the separation of the above and below rail operations in Victoria, New South Wales and South Australia and the completion of the standard gauge link between the capital cities; the privatisation of Australian National; the rail summit of 1997 with the agreement by all jurisdictions to work towards the uniformity of operating practices and regulations; the intergovernmental agreement on rail safety; the establishment of the Australian Rail Track Corporation to provide a single point of contact for the interstate network; the announcement of the privatisation of National Rail, Westrail and V/Line Freight; the contracting out of maintenance and capital work programs in Victoria, South Australia and WA.

For example, in the Australian Financial Review this morning you may have seen an announcement by FreightCorp that they are going to start operating between Sydney and Melbourne. So whilst Robyn and Andrew tell me that it's actually a very hard slog, it seems to me that they have made incredibly good progress or the sector has made incredibly good progress over the last few years. We would be happy to contribute further to the inquiry.

MRS OWENS: Thank you for that. Yes, we get different views on the amount of progress. We had the Australasian Railway Association here yesterday and they had actually done quite a useful check list for us. I won't refer you to their submission but they have looked at the progress - I haven't got it here, but the progress that's been made by the rail sector and the progress made by government and they have basically said that all the things that the commission inquiry in 1991 said that needed to be addressed by rail had been done, achieved. Most of the things that government was required to do hadn't quite made it. So I haven't got it and I won't go through it with you at the moment but it depends who you're talking to. Whether we've had a lot of progress or not, it depends who you're talking to and where they fit into the system and whether they like what's happened really.

But it's a very impressive check list that you've just given us. All those things that have been happening, I think probably a decade ago, nobody would have thought that we could have got that far. I suppose it's a matter of, nobody is ever satisfied. We've had the parliamentary inquiry, Tracking Australia, and they have made suggestions in that report, some of which probably you've said in your submission will be addressed by government early next year or sometime next year.

MR WHALAN: Yes, we still haven't put in a submission but will be shortly. What I hear you saying is that there's no disagreement there's been huge progress. There's just a bit of debate about who's going to claim the credit for it.

MRS OWENS: Yes, that's probably the case. I think there are a range of issues which we'd probably like to talk to you today about but there's issues relating to how quickly the access regimes are getting established and how quickly the NCC is dealing with the declaration applications and just the problems with determining policies relating to access pricing. There's a whole range of things that people are still feeling somewhat unhappy about. I think an interesting question that we've been grappling with is the question of the different approaches that have been adopted in different states and which of those approaches works best. You may say, "Well, it's horses for courses," and maybe the different environments say - you know, it might be quite suitable for Queensland Rail to say it's a vertically integrated entity and for New South Wales government to do what they've done in New South Wales with separation and Victoria has done something different. But I think that's probably where I'd like to start and I'd like to just get your views on the different state arrangements. Which of those sort of models do you think is working best? Do you think separation is the preferred model or vertical integration?

MS BEETHAM: I think it is a bit of a case of horses for courses. At the national level where we have the interstate system, we've gone the route of separating track from operations with the objective of facilitating competition on that line. I think some of the reason for that comes out of the history which is characterised by state organisations that were sort of fairly intransigent and not driven by a commercial discipline, as well as competition policy, no doubt, is behind that. But I think that's a reasonable and desirable approach to take on the interstate system. I don't think though that it should be interpreted as meaning that the Commonwealth has any particular aspiration to have a set number of competitors operating on that track. We would look to have competitive forces operating on the track.

So while there are four players there now and others aspiring to participate in that industry, my expectation would be that over time that might in fact rationalise down to possibly maybe one or two players and perhaps some niche players singling out particular elements of the market that they can best serve. But if you're talking about a smaller system such as the South Australian state system or the Tasmanian system, critical mass is no doubt a key factor in whether or not you can meaningfully press for competition. So when we were selling AN, for example, the reason we opted to sell those state systems as integrated systems, was really a reflection of the fact that to endeavour to break them up and to do it in any other way seemed not so commercially viable.

PROF SCRAFTON: In your submission, you comment on the decision to sell Westrail as a vertically integrated organisation, interfering in what I might call the national interest. Would you like to comment on that?

MS BEETHAM: Again, I think, one of the things that the industry has long sought is a single access regime for the interstate system and we worked incredibly hard through negotiating with the states to try to achieve that and we also believe in the merits of it, which is why we were doing it. It wasn't just because industry asked. Having got something that was less than we might have aspired to, we would have liked all of the track to be linked or passed over to the ARTC in the way the Victorian one was, so the Victorian track is now managed by the ARTC in a complete sense. We did get sufficient agreement to provide a one stop shop for access and our concern is that notwithstanding commitments by Western Australia to honour their obligations under the agreement through which the ARTC was established, then in fact there will be an anti-competitive force being exercised or available to the owner of the track. If it's sold as an integrated operation that could distort the achievement of that one stop shop. Andrew too would like to comment, I'm sure.

MR WILSON: I guess in relation to the Western Australian situation, what you will see is a commercial organisation which will buy Westrail and its commercial imperative will be to provide dividends and returns for its shareholders. Its best commercial practices may not be in the interests of generating competition within the interstate which is what we've seen over the last 4 to 5 years and may therefore reverse some of the trend that the Commonwealth would see has been a good trend in terms of generating competition, improving the product that is provided by interstate rail, driving down the price passed on to the customer. Those sorts of trends that we've seen since the introduction of SCT a number of years ago may be thwarted by commercial practice - and very acceptable commercial practice - of an integrated operator who, as I said, is driven by different drives than an infrastructure organisation would be.

If the track were to be passed over to the ARTC under their charter, their only source of income is through revenue, their only methodology of seeking revenue is through increasing the volume of traffic on the railway, whereas a commercial operator who's vertically integrated may be able to maximise profit through not increasing traffic volumes but through other commercial means. I guess we are concerned that that byplay may occur if Westrail is sold as an integrated operator.

PROF SCRAFTON: Thanks for that. But how then would the arrangement with the Tarcoola, Alice Springs, Darwin railway work because the Commonwealth already agreed to give that away. Presumably you don't think the traffic is worth worrying about but I don't want to put words in your mouth.

MR WHALAN: On the surface that's inconsistent, no doubt about that. Your comment is probably a reasonable approach that the east-west line is far more important than the north-south.

PROF SCRAFTON: I think it's probably true, it's just the slightly different policy thrust.

MS BEETHAM: I would say though that what we're endeavouring to do, we are still going through the process of negotiating the arrangements under which that line will be handed over. While arguably it's a spur line and not such an issue, we will be doing all we can to protect the integrity of - - -

PROF SCRAFTON: To ensure that it falls in with the policy that you've described.

MS BEETHAM: That's right, and to maintain open access on the line as well so that others can compete. How successful we are in that is yet to be seen but we're certainly looking to pursue the same principles.

MRS OWENS: But coming back to access regimes, I think what Western Australia is arguing is that they could sell it off as vertically integrated entity and provided you've got a suitable access regime, what's the problem. If they go through the process of getting their access regime certified by the NCC, is there going to be a problem? If they have an adequate access regime that the NCC certifies, isn't that going to be enough?

MS BEETHAM: It will go a fair way but I think I have a certain cynicism about how effectively you can regulate out to anti-competitive practices. They may allow others to operate on that length of line but there are ways - and it's interesting in another context when we were talking about national competition policy and the access provisions of the ACCC and so on applying to South Dynon terminal in a Victorian context. The Victorians are very concerned that the national regime wouldn't be strong enough, that they wanted another one over and above it. So they had a certain concern about the veracity of the national regime. Whether or not they feel they can develop a cast iron one that will prevent anti-competitive practices remains to be seen, but there are much more subtle ways than simply denying someone access to a line but which you can limit their freedom.

MRS OWENS: So subtle ways - for example, scheduling and- - -

MS BEETHAM: That kind of thing. Whenever you schedule your maintenance work, various requirements you might have of other players, that sort of thing.

MR WILSON: Also investment priorities. If you're a vertically integrated operation you'll invest where it will provide the best commercial return for you and that may or may not suit the commercial requirements of other operators. To take an example, you may actually feel that 1600-metre passing loops, crossing loops is the best commercial investment for you, whereas industry is pushing at the moment for 1800-metre crossing loops. Now, that's not likely to happen because you will be operating on the rest of the network as well but it's an example that may occur. I guess I would always fall back to the argument that the road industry had actually said to me and that is, "I wouldn't want to have to run my trucks on my competitor's roads," and that's the basic problem that we see.

There are ways you can affect the operations of a vertically integrated operation which may affect your competitor. We think that it will be far better to eliminate to whatever extent possible that potential and provide an environment in which the above rail, the actual contestable services, are open to competition.

MRS OWENS: Going to the other end of the continent, what about Queensland, doesn't that present a similar problem or not? They're a vertically integrated system in Queensland. They haven't handed over any rail, as far as I know, to the ARTC. They haven't done a Victoria- - -

MR WHALAN: It does beyond Brisbane. The 50 kilometres or so of track to Brisbane is almost neither here nor there.

MS BEETHAM: It's in the ARTC's purview - or it will be. It's declared and is covered by the ARTC. Queensland will cooperate with the ARTC concept, but north of Brisbane, no, they don't let anybody else in. That in act is typical of problems that arise. TNT took them to the ACCC and didn't succeed but nobody else gets in there and they've been creaming off royalties I think from the coal trade and so on and putting a lot of government money in there. But they have not allowed a competition into - they are corporatising but they've opted to run the state system as an integrated one.

MRS OWENS: The ARTC, to get access into these other states - New South Wales and Queensland - they've had to go and seek access through the access regimes, haven't they, or is that- - -

MR WILSON: Formally in New South Wales I believe what will happen is that the ARTC will be recognised within the New South Wales access regime so that ARTC is legally allowed to sell access to the interstate network. At present, RAC is the only body within New South Wales who can sell access to their track. Under the intergovernmental agreement, ARTC is to take over control of the sale of interstate track under an arrangement between the Rail Access Corporation and the Australian

Rail Track Corporation. It will be a contractual arrangement but behind that will be the empowerment through the access regime of the ARTC to sell access.

If we go back to Queensland one step, the Queensland network is a narrow gauge network. The interstate network is a standard gauge network. The traffic on the two don't intersect. Minimal traffic goes from the Queensland network through Brisbane and on to the interstate network. So you're not looking at an enormous volume of traffic. A lot of it goes to the ports, a lot of it goes into Brisbane but not a lot of it goes and continues on to the interstate network. So you'll find, I guess, we've drawn an artificial line through Brisbane where the standard gauge track stops, in one sense, past that point, because of the differences in gauge and we've not pushed the ARTC concept.

PROF SCRAFTON: That has a very sad aspect to it though, doesn't it, that a lot of the potential for a rail on general freight, interstate general freight, is the growth of the coast sort of north of Sydney right up through Queensland. It means that unless somebody tackles that issue, we're giving that traffic to road in the corridor where we would really like rail to be able to capture more of the market.

MR WHALAN: From a distance I think you're right there. It's a pragmatic decision at this point in time, we return to the future of rail and the future development of Queensland and a national network, you're right.

MS BEETHAM: You can in fact take freight up there by train but you have to put different bogies under it and so on, so it's an additional cost, but that's if you could get the right to operate in Queensland.

PROF SCRAFTON: But I thought I saw that Queensland and QR were cooperating to run a through Melbourne, north Queensland train, which obviously shifts containers across under wagons or changes the bogie. I think nowadays it's more switching the containers between wagons. But yes, I mean, I think that's a good point that Jeff makes. It's a long-term issue but it's one that we shouldn't lose sight of if we really want rail to have a future.

MRS OWENS: Just coming back to these arrangements that are going to be negotiated between ARTC and Queensland and New South Wales, is that happening now? Maybe we should ask the ARTC but - - -

MR WILSON: Yes, it is happening now, and the best person to ask would be the ARTC this afternoon. I can give you second-hand information in terms of where they're up to and the intent, but they would be able to answer the questions much more fully.

PROF SCRAFTON: One policy-related aspect, though, that I think is worth drawing to your department's attention, is that some of the people who have made submissions to us have pointed out that one of the weaknesses with the arrangement is that if you want to make an interstate haul that does not involve only the sort of inter-capital routes and so on, you then do get caught up in the state regime as well. I think the example that was given was a fairly unlikely one but it illustrated the case. I think it was given to the House of Reps too - grain from, say, the Victorian network into Port Kembla. Without going into the detail of it, the question was, would it be possible to contemplate the ARTC being able to negotiate for a service, in effect, rather than a route - you know, rather than a section of track. That's a sort of broader policy-related issue. If we ask the ARTC they will just say they aren't allowed to do that now. I just wondered whether or not that had ever been contemplated or whether it was all just too hard.

MS BEETHAM: I think two things. One is that the idea was to get the ARTC up, give it a clear focus, and it was hard enough to get to that, and I do mean it was difficult to get to that. If we had given the ARTC, originally, powers to engage in commercial businesses like that, actually providing rail services, there were people within the Commonwealth bureaucracy who would have been concerned that it was another AN arising from the ashes, sort of thing. There was a real concern that we were genuine about what we were claiming to be endeavouring to achieve.

The other thing I think it's worth saying is that you need to walk before you can run. We're still very much in the formative stages of this national access regime. It has got to prove itself and get some runs on the board. Depending then on the psychology of the industry and government, perhaps one might want to look beyond that. But at this time there's no intention to - we'd sooner see commercial providers provide those sorts of services.

PROF SCRAFTON: Thanks for that. I guess that's true. You have the difficulty of getting governments to sign up, and then not only to sign up but to actually live up to what it is they have signed up for. I guess that's right. But I draw it to your attention because submissions have drawn it to ours and said, you know, "It doesn't help us because we have to negotiate with more than one." Let me say that the most extreme example was somebody drawing to our attention you have to negotiate with three organisations to get from one side of Broken Hill to the other, which is a very extreme example. It is an indication of the complications that we are building into the system in order to develop what we believe will ultimately be a sort of seamless system.

MS BEETHAM: Let me say - and I don't think there's any problem in my saying so - that while we have focused on the interstate, which is where the Commonwealth powers dwell, that we do have some quite draconian constitutional powers in relation to rail. We would aspire to perhaps the example being set by the ARTC as being so attractive that we might persuade others to sort of come on board in terms of their intrastate operations. That's a grand dream. But certainly in terms of the work we're doing to improve the uniformity of the operating environment for rail, while we can only do it in relation to the interstate track, strictly speaking, we expect a flow on, and it doesn't make sense for the states to have something different in the way of communication system to that which industry and governments have agreed ought to apply in the interstate system. So there would be trickle-down there. I would like to think that might happen on access, but that's a pipedream I suspect.

PROF SCRAFTON: No, I think it's a good description of - a lot of people say, you know, the Commonwealth should provide leadership in some of these areas. It's a very easy thing to say but it's a very difficult thing to actually implement on the ground. I think that the access example you've given is a good one; that people are happy for you to give leadership as long as you don't tread on what they regard as their area. So walking before you can run is obviously the way to go. Thanks for that.

MRS OWENS: Yes, quite a lot of the operators have said, you know, it's fine to have the international access regime but if we don't just do interstate services, increasing we've got - FreightCorp is going to be coming to Melbourne. You've got them going into other states and doing intrastate business in other states, as well as interstate. So they've still got umpteen stops along the way, you know, to negotiate the access in different places. So we still haven't totally resolved the issue.

MS BEETHAM: No, we haven't, but I think as those competitive pressures build - you know, if I'm FreightCorp I've got to deal with, in the old world, Victoria and South Australia - sorry, what would have been AN and WA. The incentive is there to get some sort of one national place where you can get your access rights, because the people who buy Westrail are going to want to operate interstate too. So again - to me it's commonsense that a national one-stop shop is the way to go. Those sorts of pressures are going to increase I think, as more people play.

PROF SCRAFTON: One of the encouraging things I think that has been put to us: that in terms of the railway operators, the state boundaries have already gone, or are fast disappearing.

MS BEETHAM: Yes.

PROF SCRAFTON: You know, the expression "intrastate" and "interstate" is really somewhat irrelevant, and people have put to us that we should now think in terms of national, regional and so on - local, rural and urban transport. So you have these different sort of classifications. However, those traditional state boundaries are being recreated with the - whether it's the access regime - and I think we can be, in light of that earlier discussion, reasonably optimistic about the progress that might be made there. But also in the case of the regulatory, the technical and safety regulatory regimes, those states boundaries seem to be being reconstructed.

MR WILSON: In terms of the access regime, it's a legal situation. Unless the states agree to transfer control of interstate - I'll talk of the interstate network here - the interstate network into the ARTC, actually physical control rather than just sale of access, the ARTC cannot apply an access regime to the state's track. That means that the access regime in New South Wales and Western Australia and Queensland will be different to the access regime in South Australia and Victoria. So I guess it's a question of we have every intent to try and put in place a single access regime. At the moment there are impediments to that. Similar with the regulatory regimes: we have every intent of unifying or having a more uniform, regulatory and operational environment, but there are currently impediments to it.

PROF SCRAFTON: Could I just ask you a factual question on this national network or interstate network. In your submission you give - I think at one point you state categorically that you know clearly what you mean by that. But is that agreed by everybody, what the national network is?

MR WILSON: The interstate network is as agreed in the governmental agreement of November 1997, signed by all transport ministers.

MS BEETHAM: That comprises the links between the state capitals and the ports. That was described.

PROF SCRAFTON: What about these alternative routes in New South Wales then? They're nodding, are they?

MR WILSON: The alternative routes through Cootamundra?

PROF SCRAFTON: Yes, Cootamundra.

MR WILSON: Cootamundra to Parkes.

PROF SCRAFTON: And then the other one.

MR WILSON: The northern one?

PROF SCRAFTON: Werris Creek or - it's just not clear to me. You know, you see maps and - - -

MR WILSON: I believe the detail of the tracks - and I'm not exactly certain - but I believe that the detail of the tracks will be laid out between the arrangements between ARTC and RAC.

PROF SCRAFTON: Right.

MS BEETHAM: The map which you may have seen does include some of those links from Sydney inland through - or the various approaches to the line to Broken Hill.

PROF SCRAFTON: And nowhere in Tasmania or - - -

MR WILSON: No.

MS BEETHAM: No.

PROF SCRAFTON: That's a curious anomaly too, given that there's a national highway in Tasmania. Again I presume it's a bit like the Alice Springs to Darwin railway.

MR WILSON: Well, I guess the interstate - at the time we were developing this, the interstate network - - -

PROF SCRAFTON: Was the standard gauge.

MR WILSON: Yes, standard gauge firstly, and also, we were in the process of selling the Tasmanian network as an integrated operation.

PROF SCRAFTON: Right.

MR WILSON: There's no connection between the two.

PROF SCRAFTON: It's also true on the highway too.

MR WILSON: There is no connectability.

PROF SCRAFTON: Well, I only mentioned it because it was drawn to our attention by the Tasmanian government and I'm sure they've mentioned it to you. I wanted it on the record that I actually - - -

MR WILSON: There is also less likely to be competition on that network.

MRS OWENS: Just because of size?

MR WILSON: Yes. If you take the financial or the commercial history of the Tasmanian rail network, you have a situation where it has been propped up for a long period of time. It's unlikely that in the short term in particular that it could sustain more than one operator.

PROF SCRAFTON: And the access regime would take care of the rest anyway.

MR WILSON: And the concept behind the interstate network and the establishment of ARTC was the promotion of competition on the interstate network.

PROF SCRAFTON: Yes, and with this emphasis on the standard gauge.

MR WILSON: And it flows through that the one doesn't marry the other. It's a case where roads are slightly different to rail.

MRS OWENS: The Neville inquiry - the report refers to a declared interstate network, the national track, which I presume is your - - -

PROF SCRAFTON: That's what you're - - -

MS BEETHAM: Yes.

MRS OWENS: That's what we're talking about.

MS BEETHAM: Do you have that map? Should I pass you a copy?

PROF SCRAFTON: We've got it somewhere I think.

MRS OWENS: Yes, and they also talk about tracks of national importance.

PROF SCRAFTON: Yes, that was really what was confusing us a bit.

MR WHALAN: They don't currently exist.

PROF SCRAFTON: Right.

MR WHALAN: That's a proposal: just as in the road area, where there's a national highway and roads of national importance, that the Commonwealth government ought also be involved in tracks of national importance.

MRS OWENS: As soon as you have tracks of national importance you also then could conceivably have a financial responsibility on the part of Commonwealth to invest in those tracks of national importance. I suppose there's a incentive for the Commonwealth not to declare tracks of national importance. Would that be right?

MR WILSON: There may or there may not be.

MS BEETHAM: As Jeff outlined earlier, we have not yet put recommendations to government on - a response to that - nor has it responded. How receptive they might be to the notion of tracks of national importance is not yet clear. But we certainly - at the time of trying to establish the ARTC, funding was a real issue, and funding constraints will always be a limitation on the Commonwealth. There is - you're right - that the minute we start to talk about rail of national importance that there would be an implicit assumption I think that the Commonwealth would at least contribute something toward the funding of the upgrade.

MRS OWENS: And the warning bells will start ringing, I would presume.

MR WHALAN: Yes, and maybe we just put the two sides of the argument to you. One side, as Robyn mentioned, is that once you open up the question of tracks of national importance it's hard to decide where that ends in terms of - you know, does it mean one, does it mean three, does it mean five. So you do open yourself up to a great deal more financial pressure, no matter what criteria you set.

The alternative argument would be that there are a number of other areas of track that are of national importance. I mean, we talked earlier about the coastal Queensland route. Some people would argue that getting more competition between ports would mean that you would argue to make track between northern New South Wales and the Queensland port a track of national importance, and you will be able to think of a number of other example.

MRS OWENS: Well, I think the obvious one is Sydney. Getting a freight route through or around Sydney you could define as a track of national importance as well.

MS BEETHAM: Well, the freight route through Sydney is already part of the agreement on the ARTC. New South Wales have undertaken to designate a dedicated freight route through Sydney. Some of the $250,000,000 program is likely to be spent in New South Wales on elements like that.

PROF SCRAFTON: The way you described it earlier, Robyn, also the track to the port would also be already included, would it - the way you described that network. In any case, there's a fairly encouraging comment on page 13 of your submission, where you talk about joint funding proposals in which different parties are involved - you know, maybe private sector. I think the example you give here are state governments and the private sector, so that in getting most effective use of this investment these techniques are more likely to generate a result which is acceptable to all parties, than simply pushing for the Commonwealth to pay, if I could use that as an example.

MR WILSON: I think there's no argument that the 250,000,000 that the Commonwealth has allocated is a panacea to the whole of the interstate network and nobody would accept that, and we don't. One of the concepts behind the 250 has been that it can be used to lever additional funds from areas that will benefit for particular investments. As you've said, the Commonwealth is often called on for a leadership role. That often means in other people's eyes the Commonwealth funds it all, but we see a role for those that will benefit from the investment in contributing to the investments. That may hopefully leave enough funds that rail will see a considerable improvement in the performance of the infrastructure.

PROF SCRAFTON: The other thing that was a very interesting one was you mentioned that the consultants' analysis on where best to spend that money and whatever else that can be leveraged as a result of it were extension of crossing loops and upgrading of control systems, which tends to tie in with all of the other policy things that we've talked about. But how do you sort of manage that when you have this other priority for facilitating these high-profile projects, like spending a lot of money between Sydney and Adelaide? I should point out that our terms of reference don't require us to look at these because, as you mentioned, there's the Smorgon committee already looking at - - -

MR WHALAN: You mean Adelaide and Darwin?

PROF SCRAFTON: Or any of these high profile - I guess the extreme one is the Melbourne to Darwin, 10 billion or whatever it is. It should go a long way in doing a few crossing loops and fixing up the existing track. One of the things why we are not concerned with these big projects, one of the things that will affect our consideration, will be the way in which investment over the next 5 to 10 years can be sensibly reconciled, not only between - the point that you spoke about, Jeff, but also within the rail network itself, and you people have a lot of experience of trying to cope with this issue. I don’t know whether you want to say anything about it or not.

MR WHALAN: We find ourselves probably balancing some different interests here. There’s a nation-building interest, which is slightly different from the transport policy interest and the federation fund is an element of that. As you know, the concept of the federation fund is about nation-building projects and trying to work with state governments about projects which they give a priority to. So I guess through my eyes the Darwin-Adelaide railway line is an example where what we are trying to do is to integrate both some transport policy decisions about good investment in rail and the extent to which you can get private sector involvement together with a federation fund project where a territory, a state and the Commonwealth have agreed that they’d like to make a non-commercial in some way contribution from a nation-building point of view. So there is some tension between those two ambitions and our challenge is to integrate them.

PROF SCRAFTON: Thanks for that. It’s a good example because it is a difficult task that you’ve got, determining where the national interest lies and the fact that that national interest will not be represented all the time in always quite the same way. I mean, in your own submission you talk about how the Commonwealth has to change direction in its feeling about what it should be doing in relation to railways, and I guess that’s part of it. I guess the real test is whether it’s a good investment but, as you say, your job is only to facilitate.

MRS OWENS: I think there is an issue which some of the submissions that we’ve had raise in connection to these high-profile projects, and that is whether in the future they may jeopardise the other, more mundane, investment from taking place. We recognise that those projects will have a potentially significant private sector contribution if they’re found to be viable, but I think there’s a feeling that if those projects go ahead it takes the pressure off the Commonwealth or the states or whoever to do other sorts of necessary investment in the existing network. Is that something that’s come to your attention?

MS BEETHAM: Certainly we’ve heard suggestions made to that effect. Some people have done sums and said, "You’ve put 300,000,000 into Alice-Darwin. If you put that into the interstate track you could do a lot more." We acknowledge that that’s a fact but from our own point of view, from a transport policy point of view, we don’t see the fact that that money is going there relieves in any way our desire to try to continue to increase investment in the interstate track. Going back to the question Derek was asking about balancing, our own view, I guess, would be that if we had some certainty about funding you could better manage it in terms of an ongoing program and that would help.

One of the things that makes the task more complex is to have - we had the One Nation program, which was sort of a short, sharp dollop of money, shall I say, and now we have a 250,000,000 program. In a perfect world that would be regularised in such a way that you could plan to do certain things, at least on the interstate track which we've currently determined between Commonwealth and state ministers we will focus on. But that obviously is an issue for budget priorities and we can only do so much.

MR WHALAN: I think the bottom line here is that the 300,000,000 would not otherwise be available for rail investment if it weren't for the nation-building aspects of that money.

PROF SCRAFTON: It's a hypothetical issue here. I guess just again perhaps the people who raised it in their submissions probably recognise that. I think it was more or less effectiveness, and particularly in relation to your own examples, where they are not sort of high-flying projects that this money is going into, but the cost-effectiveness of them has been demonstrated by a consultant to be far better than some of the alternatives. Yes, that's good.

Just staying with that issue of certainty, do you think that the privatisation process that's taken place will assist in developing that investment certainty in the future? Some of the people who have appeared before us have tended to feel that it is a good idea because, if you get a number of privatised railways with a clear investment program of what they're buying into, that will help all the parties involved. Do you think that's right? Is that your experience? Do you think that will occur?

MR WILSON: I certainly think that the move from government-supported railways or government-run and operated railways to commercial entities with a focus on delivering a product to a customer rather than running a railway will give you a much greater chance of success within the rail industry. I'd attest that you wouldn't get many arguments from anybody in that. I also think that it will give you a great deal more certainty in terms of the investments where those companies feel that they can generate a greater commercial return will be. That will then split the difference between commerciality ends and where government support may even come into it. You'll certainly create a great deal more certainty on the commercial side of life than you will on the government side of life.

MRS OWENS: I'd like to talk just very briefly about your vision. You've got a section on page 14 about future directions and the Commonwealth's vision for interstate rail. I know that you have a responsibility for the interstate systems, but I'm wondering why we don't have a vision which looks overall at the rail system as a whole. Should somebody have a vision for the whole of the rail system and, more broadly, the land transport system? I think you know where I'm heading. I'm heading towards a land transport corporation or whatever you want to call it and the proposals for that. But do you think that the vision should be broader on the part of the Commonwealth.

MR WHALAN: I'll kick off. Our primary responsibility is interstate, so there we have a clear mandate for a vision. I guess notwithstanding that our vision would go further, and that would be that we, together with the states, could have an integrated view for the future of rail across Australia.

2 MINUTES' SILENCE OBSERVED IN RESPECT TO REMEMBRANCE DAY

MRS OWENS: You were saying that perhaps you could be getting together with the states to develop a broader perspective.

MR WHALAN: Yes. Just one last comment, and that is that my view is that that Commonwealth-state approach ought to be ideally an intermodal approach. That's my view.

MRS OWENS: I know it's a bit unfair to ask you, because it's one of the Neville reports recommendations. They recommending developing a national land transport commission, but I understand there has been some work going on in this direction.

MS BEETHAM: Yes. I'll comment on that. There are two or three points I'd like to make. One is that, while I think everybody thinks that a vision is a very worthwhile thing to have and that we ought to be working within some sort of broadly-agreed policy framework, achieving that has proved incredibly difficult over the many, many years because of statehood, the different orientation. The Commonwealth is more preoccupied with interstate and with freight. The states have passenger services, and they put a lot of priority and funding into those. So in some senses there are opposing objectives.

Another factor I think is that very often when people talk about the Commonwealth having a vision they really need more money. There's a difference in what people do mean about a vision too. The way we've described it in our submission is a sort of broad objective of a basically self-funding industry, not ruling out the Commonwealth or some government support but a basically commercial operation to generally underpin it rather than substitute for commercial discipline. There are others who want to have a very, very specific plan. They'd like to see almost lines drawn on a map with railways of national importance and roads of national importance and a Commonwealth commitment to actually make sure those are funded.

I think there's a philosophical difference, too, about what we mean by a vision. A third point I would make is that the notion of a Land Transport Commission I think has some merit. Our own view is that we would be better to get a Rail Transport Commission first and get rail in an even tidier position before we embark on that sort of thing but even if one was successful in having a Land Transport Commission to try to pursue the intermodal approach, there's an issue for government in delegating to a statutory corporation the role of determining national policy. I think even if you got a Land Transport Commission, it might be able to advise on national priorities and make some judgments about A versus B in terms of approaches but it's ultimately the governments that have to work out what their vision for the nation is. It's not something you can give a commissioned body to do for you.

PROF SCRAFTON: And people draw the parallel with the model of the Road Transport Commission but one thing that the Road Transport Commission does not do is to get on the investment side and the big issue that we face with a lot of participants, including yourself, is getting that right, isn't it?

MS BEETHAM: But just as we commission Booz Allen and Hamilton, for example, to do some work on what might be the most cost effective way of spending the budget we have for rail infrastructure, you might be able to ask a Land Transport Commission to do some modelling, come up with some findings on a road versus rail solution to certain problems and implications of changes in fuel excise or mass limits or whatever but the judgments have still got to be political ones made by ministers.

PROF SCRAFTON: And the evidence of the old Commonwealth Bureau of Roads, which did that for roads, was that if you do the job too well and governments don't like the outcomes then the organisation disappears and you start again. So I think those are useful comments but obviously you in your own intergovernmental machinery are working through a lot of these things which brings me, Helen, to - we don't want to take too long but you've given some excellent attachments at the end there which tell us where you are with all of these groups and committees. I wonder if we could just ask you in general if you would either confidentially or on the record if it's appropriate just keep us in touch in the next few months with where these groups are going. Some seem to be making very good progress; others don't seem to be.

MS BEETHAM: Absolutely no problem. We're hopeful of making some real yards with some of the work we're doing and I think there is a good will within industry to help bring about the sorts of changes we're pursuing. In fact, they're very heavily involved in a lot and are funding it jointly with the Commonwealth. So the scene is well set and as we make these changes and get agreement we'll be wanting to broadcast them to everybody so I will be very happy to put them on the record.

PROF SCRAFTON: Thanks. The ones that are of particular interest to us is the competitive neutrality issue obviously and in your paper of course the big issue is - you talked about a long-term issue for us. We don't have a long time to consider it but perhaps we could talk to you about that particular topic separately later. Another one is this barriers to private investment although according to your report that one doesn't seem to have made a lot of progress but we'd like to be kept in touch with that one.

MS BEETHAM: That one we're looking to have brought to a reasonable head fairly soon. There are two ways in which that work is being progressed. One was as a task undertaken by the department under the aegis of the rail group. A survey of a small number but nevertheless very significant players in the rail industry was conducted and we have the results and they're to be written up and submitted to rail group. At the same time the Smorgon committee, which was established by Bob Mansfield, is looking at the much broader issue of facilitating private sector investment and they too are doing some work. What we're looking to do is both complete the work Rail Group initiated which is writing it up, but also take advantage of that and integrate that with some of the work with the Smorgon committee so that there will be two sets of findings, as it were, coming out.

PROF SCRAFTON: Great, thanks. The third one is the one that we've already mentioned, the proposal - these alternatives about a Rail Commission or a Land Transport Commission. In fact, you must be pretty - I think you're not suggesting you've got a draft of that because it's got to go to ministers in December, I think.

MS BEETHAM: There is a draft paper in circulation and the current expectation is ministers will consider that issue and we hope make a decision on it on 4 December.

MRS OWENS: So it may be one of the things we don't have to look at if a decision is made but you never know in this game.

MS BEETHAM: No.

MRS OWENS: I won't hold you up any longer but is there anything else you'd like to say before we break for morning tea?

MR WHALAN: Thank you for providing us an opportunity and we're very happy to provide you with some information out of session on those three things you raised.

MRS OWENS: Good, thank you very much, and I think we would like to come and visit you at some stage out of session as well. Thank you for coming this morning. We'll now break for morning tea and we'll resume at quarter past 11.

MRS OWENS: We will now resume. The next participant this morning is Rio Tinto. Would you please give your names and affiliations with the company for the record.

MR CUSACK: Good morning. I'm Barry Cusack, managing director in Australia for Rio Tinto.

MR McMAHON: Peter McMahon, general manager business development for Pacific Coal, which is Rio Tinto's company in Queensland managing it's coal interests.

MRS OWENS: Good, thank you, and thank you both for coming this morning and for the submission, which we have read. I'd like to also just take this opportunity to thank Rio Tinto for the other submissions that you have made to other inquiries that the commission has conducted. At least, the Industry Commission conducted an inquiry recently into the coal industry. I know you were active participants in that and we were fortunate enough to speak to your colleagues in Perth, Hamersley Iron, 3 weeks ago. We're very appreciative of the interest you have taken in this inquiry and our last inquiry and for the time you've given us, so thank you for that. We have read your submission and we have a number of questions we'd like to ask you, but in the meantime would you like to make some opening comments?

MR CUSACK: Thank you, and thank you for the opportunity to contribute to this study. We are aware of course of those previous studies that you mentioned, and particularly on black coal, which does address many of the issues that are also canvassed today. We certainly hope that through your research and analysis the need for an acceleration of rail efficiency in this country can be achieved.

We acknowledge the submission by Malcolm Richmond of Hamersley Iron and support his submission to you in Perth. We also support the submission to the inquiry of the New South Wales Minerals Council, which is entitled Progress in Rail Reform for Coal Transport in New South Wales. Peter, with me today, represents our Queensland coal interests, who haven't separately made a submission, as I understand. So he can canvass those issues.

The process of implementation of the Hilmer reforms was intended to be undertaken cooperatively between the Commonwealth and state governments. In practice, however, the lead has been taken by the Commonwealth, with different states progressing at different rates. In the field of rail reform, politics has impeded the delivery of reforms. As our submission says, the agreement on competition principles reached in April 1995 gave a wide discretion as to how reform should be executed. The contradictions of many aspects of the process have been identified. For example, responsible ministers can basically ignore a recommendation to the National Competition Council by refusing to act. This is what occurred following a request that the Hunter railway line system, which services our coal, be declared in April last year. Of course, subsequently there have been court cases and a finding in favour of the New South Wales Minerals Council 1 month ago. In New South Wales the transport minister has responsibility for the four rail organisations that are a result of disaggregation of the system, and that of course leaves some residual potential for conflict.

Where there has been political drive to achieve reform, it has often been the central agencies in the states that have taken over the process, such as in electricity and gas. This is probably because of the substantial revenue gains to state treasuries from reform and privatisation. It's disappointing, when potential savings accrue to the private sector rather than the public sector, that the same time and attention and will to reform is not apparent. Comparisons can be made between road transport reform and rail reform. The emphasis on road transport can in part by explained by the assumed direct links that its costs have to prices that are passed on to domestic consumers. Improvements in road transport are perceived to result in benefits being passed on to the public through things such as lower food prices in regional and rural areas. There is not the same political constituency for rail reform, as the benefits accrue to producers who export and the benefits to the Australian community are more indirect through the balance of payments.

These sorts of problems were recognised in the Hilmer report, and there was provision for the Commonwealth to act unilaterally where there were important national interests at stake. For many stakeholders there's been a call for one overarching government agency with responsibility for land transport as a whole, road and rail. There might be some merit in this approach. Without going into the details of road versus rail transport, the implication for Rio Tinto of this country's preoccupation with road transport has been that little political will has been devoted to the issue of improving rail transport. As our submission states, although rail reform has been on the agenda of the Council of Australian Governments since the early 1990s, there has been no specific agreement between governments as there has been for areas such as electricity, gas and road transport.

For Australian mining, the land transport of mineral products is a key element of competitive position. This is particularly so for the bulk commodities such as iron ore and coal, where transport from mine site to export wharf is a significant proportion of the landed cost to customers at point of purchase. As international competition intensifies with the consequent real-terms decline in product price, all elements of the value chain come under cost scrutiny. Fortunately, the iron ore producers of Australia have been able to meet this challenge and remain competitive, not only in Asia but in more distant markets such as Europe. This has been achieved at Hamersley Iron through relentless pursuit of efficiency. Initially this focused on individual elements of mining, processing and transport. More recently, substantial gains have been achieved by the smarter optimisation and integration of the whole value chain.

The analogy I use for this is the shift in manufacturing that probably took place 15, 20 years ago when unit operations were linked to the Canban or just-in-time integrated manufacturing systems. This enabled manufacturers to achieve flexibility in meeting customer needs and built-in quality as well as substantial efficiency gains. Similarly, Hamersley Iron is freeing up substantial capital, manpower and management by adopting those principles. To achieve this it is essential that the whole value chain is optimised both for quality control and efficiency. Flexibility of scheduling and short cycle times are essential elements to maintaining productivity and quality. The costly buffers that have in the past been used, such as large stockpiles - they were used to compensate for poor performance - have been removed. This of course makes the whole system interdependent in real time, and I hope therefore you can see why we regard rail as the most critical element of that production process.

Australian coal exporters have only recently felt quite the same competitive cost pressures, and they've been working hard to unwind the uncompetitive practices that were entrenched when they were considered an essential domestic service. Your commission has done excellent work in examining this question and Rio Tinto coal companies have been leaders in tackling change, and I'm pleased to say with some good success. However, the cost of transporting coal in both New South Wales and Queensland has not shown the improvements expected from competition policy reform. That's not to say nothing has happened, but the pace of change and the delivery of outcomes is frustratingly slow, and commitment to reform has to be seriously questioned. There is ample evidence to support this: the lack of transparency in pricing; overinflated valuation of assets; no issuance of operations protocols after 2 and a half years; despite recommendations to declare, no action; and customers being excluded from an appeals process.

For Hunter Valley coal exported via Newcastle, rail has been a bottleneck. When demand for product is strong, exporters have seen queues of ships and we have had to pay demurrage on waiting ships because they haven't been able to be serviced by rail. This is particularly galling where we believe we're paying over the top through monopoly rent and overblown costs and at the same time we're suffering through lack of ability to service our customers. I'll leave Peter to comment on Queensland. Suffice to say it's no better a picture.

In our submission we've made a number of recommendations for your consideration as desirable actions to address our perceived deficiencies. Just let me say in summary I think it's appalling that the outcomes of Hilmer to date are minuscule and somewhat cosmetic improvements to the uncompetitive aspects of the eastern states' coal freight and yet a threat to weaken the world benchmark performance of Hamersley's integrated railway. I don't believe that's in Rio Tinto's interests, and it's not in Australia's interests. Thank you.

MRS OWENS: Thank you.

MR McMAHON: Just some brief comments specifically in relation to Queensland. As an overall comment, our major concern is that the current approach is really designed to make it as difficult as possible for customers or potential third party providers to evaluate any competitive alternatives. We've gone into some detail in the submission with some specific issues. Really four points I just wanted to raise as introductory comments for noting. The first one is the lack of structural separation of Queensland Rail. We have a situation where an access unit is being established within the same management organisation and reporting to the same chief executive. That's a concern to us. We've got slow progress in relation to the development of the access undertaking, limited consultation, and that's not going anywhere fast.

The industry has found it impossible to date to obtain any information at all on asset valuations. By contrast, Queensland coal producers have been able to obtain asset valuations for other public infrastructures such as the courts that we deal with, and the government-owned corporation there has made balance sheets available. Queensland Rail have made no information available. Another issue there in relation to that on asset valuation is complete lack of clarity on treatment of use-funded assets. The industry in Queensland put a lot of money into rail assets in the eighties and nineties and there's been no clear process for how that's to be treated.

The final point I wanted to make is that there is an inability of all customers to get from Queensland Rail a breakdown of the freight rates into the access charge and the hauler's charge, and that makes it very difficult once again to evaluate any competitive alternative. So by way of introduction they're the issues. The submission goes into them and others in more detail.

MRS OWENS: You've actually raised a lot of quite serious issues, I think, and I know you've only got a very limited time with us, so I think we'll have to be fairly selective in what we talk about. I think one of the things that you mentioned, Mr Cusack, at the beginning was you were talking about the - there's been very little political will to look at rail. I think over the last year or so things have changed, but it may not be changing in the direction that you may think is appropriate. There has been a lot of political interest in new major projects, as you're probably aware, and maybe that has become a bit of a distraction, but that has been at very much the national level rather than the state. But there has been quite a lot of activity going on in New South Wales in terms of restructuring. I think the first thing I'd like to ask you is which of the two regimes that you're dealing with directly for coal, New South Wales and Queensland, would you find the least unsatisfactory?

MR CUSACK: Well, let me say there's clear problems with Queensland, as Peter has mentioned. There really has been very little change in the structure of Queensland Rail and there has been very little open dialogue about how they're intending to implement change. In New South Wales the situation is different. Yes, they have created the four entities. But in terms of outcomes, this hasn't yet achieved the desired changes. So we regard it as somewhat cosmetic at this stage. The intention seems fine. The concept of separating the rail access corporation out from the operator for freight and the passengers.

When they did look like doing something, there was the question of tendering for maintenance of infrastructure. In January they went out and said, "Yes, we've already got the 12 regions, we're starting the process, we're going out to tender for this," and a month later the government stopped it. Why? You know, that's what I mean when I say there's no political will.

MRS OWENS: I think they're going to resume it, though, aren't they?

MR CUSACK: Yes, but we built Hamersley a railway, two towns and a mine and a port in 19 months. Here we are over 2 years down the track and nothing has happened.

MR McMAHON: Can I just make one comment on that. From our perspective I think structural separations are necessary but not sufficient condition to reform. So we would prefer that Queensland followed the same approach. However, as Barry said, there are still problems once you get that step. But until you get that step, the chances of getting to a competitive outcome in the end I think are fairly minimal. So we would certainly prefer the New South Wales model to be adopted. Then it comes down to issues of, you know, how you value assets, what's appropriate rates of return. So the devil is in the detail in the access codes but without separation you've got no hope, is our view.

MR CUSACK: I was just going to say, when you ask us to say which is preferred, the question for us really is the fact that we don't think either has done anything significant and we are really are left with Hobson's choice, to answer your question.

MRS OWENS: Have you got a better idea of how you would structure it? Is there a preferred model?

MR CUSACK: I think the model that New South Wales have followed is a reasonable model for assigning accountabilities, provided that they actually led to some actions that created efficiencies. I mean, we've got much the same people acting in much the same ways, and that says to me there hasn't been a real fundamental change of culture that is focused on delivering efficient outcomes.

MRS OWENS: Could you get that, do you think, by actually privatising all the entities?

MR CUSACK: I think leave alone the infrastructure and look at the rest. Yes, probably private has been shown in other areas to deliver great efficiency gains. I don't see any reason it couldn't in this area, and that could include the maintenance aspects of the rail and the signalling etcetera.

PROF SCRAFTON: I think Peter's comment about the models is very interesting because in New South Wales the one newcomer that came in, Barry, was the guy who ran the RSA. He was the one who wanted to contract out everything and he was immediately closed down. It was a good example of Peter's comment, about it's not enough. You know, you separate out but you have to corporatise properly and let the organisations run themselves. The evidence is that the governments in both Queensland and New South Wales are still not prepared to do that, whereas at least if you privatise, you know, unless you have something in the contract or the sale process, once you've privatised, well, then it is up there in the market. So maybe that is the next step.

Could I ask you, just in relation to Helen's question, though, do you notice anything different about performance? You know, is the delivery to you, as a user, any better in New South Wales or Queensland? I think in your submission you talk about, in New South Wales, the turnaround times. That's not the expression, is it?

MR McMAHON: Or cycle times.

PROF SCRAFTON: Cycles times - you believe they're 50 per cent slower than they ought to be. Is that also true in Queensland or do you get better performance in Queensland?

MR McMAHON: You've got longer hauls in Queensland so there's some advantages there; probably less mines. So there are some different characteristics.

PROF SCRAFTON: Right, so it's not so simple.

MR McMAHON: I'm not totally familiar with all the operational details of New South Wales. I think overall the performance is fair to reasonable in Queensland. However, as in most situations without the threat of competition, it gets to sort of a cosy point. At the moment those customers that are keen to bring in some sort of competition, in other words to make some elements contestable, don't have any processes to actually push that. So what we've seen I think is Queensland Rail have made what I'd call the easy gains. They're conscious of the threat of competition so they're offering, for example, lower freight rates to a lot of the customers, long-term contracts. Basically they're trying to lock them in and keep everybody else out. So they're giving the easy bits first up. But until you've got real competition you don't get that - you know, the drive for improved productivity.

MR CUSACK: Could I just pick up that point. I think there has been some improvement. I don't want to say there hasn't been. There has been some improvement in focus. The Hunter Valley has a - almost a hundred different products go through that port, so it's not an easy comparison with someone who has a much more simple system. So I can only say that in time, yes, FreightCorp has cooperated better and recognised more the needs of the system. Certainly the manager of the Port Waratah Coal Services, which runs the port facility, said that FreightCorp are now easier to deal with on his needs. But in terms of delivering anything like the efficiencies we see in other rail systems in this country and overseas, there's a long way to go.

PROF SCRAFTON: Yet it seems to me that it's not enough to encourage the mine owners to want to try to run their own railway, in the same way as you do with the iron ore railways.

MR McMAHON: In our case, for example, we're not particularly interested in running our own railroad. It's a different situation, because we do have multiple users. What we want is a system whereby if we're not happy with the structure or the freight rates that has been put on the table by Queensland Rail, we have a clear, transparent system for evaluating an alternative and making a decision as to which way we go. At the moment we don't have that right to make that decision. But running our own railroad is not something that's on our agenda.

MRS OWENS: But are the rates higher or lower in Queensland than New South Wales, or the same?

MR McMAHON: It's a little bit difficult to make a lot of comparisons. It's probably a little bit lower but a lot of that has got to do with the fact they're longer hauls.

MRS OWENS: So you come back to the problem then - - -

MR CUSACK: And easier terrain. But in terms of - you know, one of the greatest things I think for the iron ore producers was to manage their rail, because it was so integrally tied up with the delivery of the quality reliability, which is the distinguishing feature in competition. I have often said it was the greatest argument we ever lost, whether that should be private or government, because it has certainly delivered today, you know, real benefits to the iron ore industry in Western Australia to have the private systems. Of course, although the total tonnage might be the same across, say, Hamersley as down the Hunter, it's slightly different. In the Hunter you've got many, many producers. So you know, each running their own system is not logical.

PROF SCRAFTON: Yes.

MR CUSACK: But getting the efficiencies out of running the system - there's a lot to be learnt.

PROF SCRAFTON: Not even running the system as a collective? That was investigated a few years ago, wasn't it, or you had a - and still do probably - that Hunter Valley - you called it rail cooperation.

MR CUSACK: Yes. Well, see, Port Waratah is run as a port as a collective. I can tell you it's not always easy though.

MRS OWENS: But would you be interested in that, if that opportunity arose?

MR CUSACK: I think there could be potential there. We would see some difficulties where there are large producers who have a lot of long-term customers to service and small producers who tend to put more spot cargoes in. There is always enormous potential for conflict in that. So the mechanisms for controlling those decisions have to be fairly clear at the outset or it ends up in a finger-pointing exercise. But I think a commercial provider of freight, according to fairly transparent rules; whether it's owned by the coal companies or owned externally is less important to us.

MRS OWENS: The access charging methodologies in each of the states - have you got any knowledge of those? I think there are slight differences in the way they determine the charges. You seem to be supporting the New South Wales approach more than the Queensland approach; at least that's more explicit. I wasn't quite clear from the submission as to whether you actually did support discriminatory pricing or whether you would prefer some sort of other approach.

MR CUSACK: Certainly we don't think that there's a fair basis for pricing the service. The way in which they have evaluated return on assets double-dips and is way over the top.

MRS OWENS: This is on the replacement costs method of - - -

MR CUSACK: Replacement cost, plus building in inflation into a nominal rate of return, and the rate of return itself is a pretty sweet rate of return for the sort of risks associated with that business. I'd like some of that. So we think that the actual pricing is flawed, and you know, there is admission that there is a monopoly rent component which is being unwound. The basis for what was monopoly rent and what was genuine cost of service is not clear. There's a lot of opaqueness in this. The mechanisms for pricing appeals - customers are excluded. Only freight providers can appeal. None of these are truly what you would call commercial behaviours. So although we might see something of elements in New South Wales of the way in which the freight and the operations are separated from access to the monopoly facility, the outcomes again are pretty inadequate.

MRS OWENS: So you're still suspicious about the monopoly rent.

MR CUSACK: Absolutely.

MRS OWENS: You think it will still be there after the year 2000.

MR CUSACK: Well, I guess it's in the eye of the beholder and we're standing and looking from a different aspect. But without some transparency in it, we can't sort out what's genuine monopoly rent, what's genuine returns and what's just inefficiency.

MR McMAHON: Just a comment now. I think the fact that it is very difficult in our case, for example, to obtain assets valuations from Queensland Rail in itself suggests there's maybe something to hide there, in terms of monopoly rent. I mean, if there was transparency and we knew the asset valuations and we knew the methodology and we can apply our rate of returns, it's fairly easy to work out whether they are or are not making a monopoly return. If they won't tell you anything, it's virtually impossible. So their silence in itself is an indication I think as to the point Barry is making.

MRS OWENS: Maybe in New South Wales at least some of this will come to light when the IPART review that is taking place now reports. So some of it may become more transparent.

MR CUSACK: We're hopeful. We've been pushing for some IPART benchmarking all along and we're disappointed it's taken this long. But let's be hopeful the process is thorough to do that.

MRS OWENS: Can you get involved in that sort of process? I suppose you could put a submission in.

MR CUSACK: Yes. We don't necessarily - we're not assured that we will be taken notice of in that. We can only hope that by providing information of quality and behind which we can stand and which we can open the books, that that will be part of the review process.

PROF SCRAFTON: One problem is the way in which the recommendations of such independent reviews can just be ignored. At least the House of Reps committee did make a recommendation that you have a reverse onus test there. If the government - the premier or the treasurer, in the case of the Commonwealth, does not respond, then the recommendation would stand. I mean, what we have heard up to now and reading the House of Reps conclusion, I think there is a general feeling out there that the need for independent review and recognition of the findings of that independent review does need reform. So maybe that might only be a small area but it's one that may be removed, although equally other parties, for instance, pointed out that these processes are incredibly slow.

MR CUSACK: Yes, I agree. I still remain hopeful that there are forces out there trying to drive the original objectives forward but, yes, the pace.

PROF SCRAFTON: The other point you made - and it's related a bit to that - is the way in which in some areas of reform it has been driven by central agencies by premier and cabinet or treasury or whoever it might be. In Melbourne, the railway reform is a function of the treasury, so at least that has been moved at arm's length from the interested agencies. But I do think those two things together are very important. You need a measure of independence in the advisory process to government, that if your advice is coming from an interested party, such as the Department of Transport, even if it's good advice it isn't going to move very quickly and it may just sit on the minister's table for evermore.

MR CUSACK: I would say in the matter of coal freight, treasury is not a disinterested party.

PROF SCRAFTON: Yes. So you do at least need the independent review agencies whether - as you said, the extent to which their recommendations might be taken on board. It seems incredibly bureaucratic. You have all these organisations like the Productivity Commission, if it comes to that.

MRS OWENS: We're not bureaucratic.

PROF SCRAFTON: But if you don’t have them the situation is worse. You’ve just got to accept the fact that if a process is not working in the way that you’ve described - and described very well. I mean, I endorse Helen’s comments. I think the submission is just superb. But you have to keep beating the drum and you have to hit everybody in sight until you get a listener and you get those reforms taking place.

MR CUSACK: Let me say it is not an easy process. These are complex questions. So it is expected that things will take time but we’re just not seeing the will to drive it and knowing how complex it is and even if you do it efficiently, what length of time it would take, we’re really frustrated that here we are 2 years down the track and we haven’t seen a real push.

PROF SCRAFTON: One example you gave - I think Peter mentioned it - that you do in fact have good relations with the ports in terms of getting costs and yet not with the railways. But are the ports part of the same portfolio?

MR McMAHON: In Queensland, all our coal goes through the port of Dalrymple Bay which is owned by Ports Corporation of Queensland. For example, we’ve recently been negotiating charges for that port, in effect access charges. The Ports Corporation of Queensland gave us the balance sheet and the earning statement for that operation out of all of its accounts, handed them over to us as part of the negotiations, said, "That’s what we’ve got it in the books at. Here’s the assets, liabilities," and we’re able to sit down and discuss the asset levels, the methodology and the appropriate rate of return. That’s the sort of information we’d like to be able to get from the railways; so far with no success.

PROF SCRAFTON: But it’s a government corporation. It’s the same thing. I mean, you wonder why that situation would be allowed to prevail. It’s in your mutual interest, it’s not as if - obviously it’s head to head as parties but it’s in your mutual interest to develop a port and to develop the business, and the same applies to the railways.

MR McMAHON: Probably the difference has been here we weren’t going to build another port.

MR CUSACK: Yes, I think it is true that the ports have got a customer focus. I think that’s partly because perhaps they don’t have so many customers to satisfy. The Hunter Valley is mainly a coal rail, so it probably doesn’t apply quite so much there. But the ports tend to see their business as allied to volume growth of the business and competitiveness looms large in that and they are much more prepared these days to benchmark themselves and then run it. So we have seen a difference between those two.

PROF SCRAFTON: I think we should mention, Helen, that the benchmarking of rail is a very important aspect of the Productivity Commission’s function. I mean, it is difficult but it must have been difficult for ports to do it too. But one of the problems is you can in fact hide behind the benchmarks if you do it in a way which is not valid -

statistically valid - and the integrity is not there. I think a bit of that has - in some of the information that we've been given you can see that there is a rubbery area there behind which one can hide, but it's not that great. I mean, if you don't want to compare your railway with a class 1 US railway, well, find a class 2 that has similar characteristics.

MR CUSACK: I agree absolutely that if you have got a spread of data you start to form a view much more clearly than arguing about what's in and what's out of a fair comparison - one on one. I think we benchmark ourselves all the time and we learn lessons from it and adjust. I think what benchmarking can do, instead of being absolutes that, you know, there are 2 or 3 cents a tonne if you did this. You say, "If we did this we could improve. We think it's of this order," and then find out and it tells you what you ought to start working on.

MRS OWENS: I think what's interesting about our exercise is that we're doing it at all. I mean, if these entities were commercial entities, which they are meant to be, they should be doing it just as a matter of course. We should have no problem going out and getting data because they should all be collective. But then they would probably make it commercial-in-confidence. The fact is that there's not a lot of benchmarking being done within the states - even between states - to see can we do thing better, as far as I can see. So I think that's quite interesting. Look, I'm really aware of the time and I know you only had half an hour to spend with us but some of the issues you have raised have been picked up in our black coal report which hasn't yet been released, I'm afraid. It went to government on 3 July this year and it one of the reports that is still awaiting release. I think the other issue that we didn't really come back to was the issue we discussed with Mr Richmond over in Perth which was the Hamersley issue. We didn't really come back to that.

But I think what I'd like to say on that is that one of the reasons you might want to introduce more competition onto a private line is to ensure that there is greater competition in the market. To ensure that there's greater competition you have to be convinced that that other mine wouldn't go ahead with that railway line. I'm not totally convinced. We have spoken to Robe and they have said that they will go ahead regardless and the investment decision has been made and if they don't get access to the Hamersley line they will do their own thing anyway. So I'm not quite sure what the competition issue is there, so that's my view which I probably shouldn't be expressing at this stage.

MR CUSACK: I think if there is any element of introducing a new competitor with a walk-up start then they will compete at a lower price level in the market than would otherwise be the case. The way in which prices internationally are set for iron ore, it's generally the one person who sets first, sets the price for everyone.

MRS OWENS: So your price goes down to meet the market.

MR CUSACK: Everyone's price goes down. The world measures itself off the Japanese steel mills benchmark price. I'd like you to do a study of that.

MRS OWENS: You could go and say could they do it. I think that's all. Do you have any other questions?

PROF SCRAFTON: No, I think it's very thorough. We haven't got time to talk about them but I think it's worth commenting on the next steps that you put in which we found particularly useful. We get a lot of comments, we get a lot of useful stuff from people but very few are prepared to put down in writing what they think ought to happen and we appreciate that. If we have any questions maybe we could just come back to you and to some of your colleagues on some of these because there's an enormous amount of stuff there and maybe as Helen said, once the black coal report is out there maybe a sort of follow-up and we might just do that out of session, if that's okay with you.

MR CUSACK: We'd certainly be happy to you. I mean, there are a lot of next steps there. I think they're pretty simple. None of them are rocket science but some of them may need further discussion and we'd be happy to do that.

PROF SCRAFTON: But collectively they represent a lot of reform, to go back to your introductory comment. The agenda is all set up, you know, whether you're writing in your words or in the existing law, it's the time and the cost and the process which is at issue here.

MR CUSACK: Yes, absolutely.

MRS OWENS: We will be doing our own version of next steps and I think this will be a very useful input into that. We will end up with a report which will say, "Where do we need to go from here?" So we appreciate getting a few signals along the way. Is there anything else, Mr Cusack or Mr McMahon, you'd like to say before we finish?

MR CUSACK: No, I would just encourage your report to be timely and let's hope that it doesn't sit for a few months' post-report till release.

MRS OWENS: We have no control over that.

PROF SCRAFTON: That's the very point we made earlier.

MRS OWENS: There will be a draft report in April which we have a bit more control over because we release that. But we have no control over the final report.

MR CUSACK: I understand. But it's part of our being anxious to see this process move forward.

MRS OWENS: Good, thank you very much. We will now break for lunch and we will be resuming at 2.15 with the Australian Services Union.

(Luncheon adjournment)

MRS OWENS: The next participant this afternoon is the Australian Services Union. Would you please give your name and your position with the union for the transcript.

MR McLEAN: Thank you, madam chair. My name is Greg McLean. I'm the assistant national secretary for the Australian Services Union and our union is a fairly active union in the railway industry.

MRS OWENS: Thank you and thanks very much for the submission which we got and we've both read it over lunch so it was quite good because you had attached to it other parts of the Australasian Railway Association submission so we had already read so it was a nice easy read for us. Thanks for coming and I thought just before we started, if you could just give us some idea of the sorts of members you've got that are involved in the railway industry.

MR McLEAN: If I could, starting with that point of the membership which we have in the railway industry, as outlined in our submission, the ASU has been involved in the railway industry for probably around about 100 years. It would be known in its previous name prior to its amalgamation as three unions. One was the Municipal Employees Union, the other one the Municipal Officers Association and there were a number of other unions that fell into the section as well as the Federated Clerks Unions. One of those unions was ATOF, the Australian Transport Officers Federation, and ATOF has been active within both the railways area and also the shipping and transport industry for some years. Predominantly it has grown out of the realm of supervisors and salaried officers. It would represent people that had traditionally worked within office areas, foremen-type people, supervisors and many of the supervisory technical and semi-technical skilled operations within the railway industry and as the industry has changed the membership has probably changed to reflect that as well by some of those classifications appearing or disappearing as industries grow and change.

We are a union that's also active in other areas of the transport industry which are in both the shipping industry, as I alluded to earlier and of course the airlines industry. We are actually the largest union, for instance, in the Australian airlines industry but we don't represent pilots, flight attendants or ground engineers but the people - the customer service officers at airports, the check-in clerks, load controllers and administrative sales types people in core centres. So we've got a very broad range within the transport industry but probably predominantly fixed amongst the salaried para and professional groupings.

The areas that we would like to point out to the commission is we have been involved in a number of reform areas within the micro-economic reform target groups if we want to use that term which have in the start, both under the previous government and also the current government, been three target areas of which we understand to have been telecommunications, electricity and transport. Our telecommunications involvement is probably fairly marginal. However, our involvement in the railway industry, the transport industry category, and also the electricity industry - we are principal unions in the electricity and also in the railway industry in the eyes of the Australian Council of Trade Unions and that's the highest status that any union can have within those industries. We're a union that's here to stay in the industry.

The ASU has worked with many employers, both private and public sector, in the reform of electricity and rail industries. We are not afraid to deal with the issues of reform and I would describe it at some stage as our views have been pragmatic and I think have been well-balanced. Our major area of concern of course as a union is in respect of the standards of living that our members and employees within the industry have. That is of course supporting the standard of living for the individuals and also of course their families. So issues that have traditionally been developed within contracts of employment being the common real contract of an award or an enterprise agreement, superannuation and those other conditions are paramount concerns to ourselves.

We also, as I alluded to earlier, have worked with employers trying to achieve the best results for companies and that's a part of the way in which our union operates. We believe that our membership's long-term standard of living and success lies with us working for the success of the industry. However, that's not to be at the expense of some of the core responsibilities, we believe. We are opposed to the issues of contracting out and that is on a number of areas, principally because of the attacks upon conditions and rates of pay that are often found when employers change hands or work is held by way of competitive contracts.

We also hold grave concerns for regional Australia where quite often the contractors that would compete for work or take work away would be contractors that are, to use the term, out of town, so to speak. We all see what happens when jobs are lost to a town, the town's growth slows, it stagnates and then we have pressures upon the town to maintain infrastructure services such as schools, hospitals and roads, where they may be in demand to go to perimeter areas of capital cities, for instance, the movement of hospital beds and such. So we are a union that is extremely active in regional Australia, probably predominantly from our local government base but also the history of rail and how it has been decentralised and has had employment opportunities in regional Australia.

The ASU is a member of the Australian Railways Association and you'll find within the report that we make extensive reference to the submission of the ARA and we were quite pleased with the standard of that document - - -

MRS OWENS: So were we.

MR McLEAN: - - - as a member of the organisation, and we have of course taken steps to convey our views to the organisation which, as you know, represents industry players and we're quite proud of the fact that we're involved in an association that represents the players throughout the industry where we can work together for common good. The submissions from the railway association also deals in some detail with some good points, in particular its comparison between road transport costs and also with the question of that being compared to rail. We notice also that timely within the ARA's report there's a reference, I understand, to the GST and its possible implications for transport and the difference that would make for rail compared to road transport.

Many of the core issues of the railway industry and its ability to move large amounts of freight and service public transport needs are of course well-documented by organisations such as the ARA and I don't believe it's worthwhile proceeding into those issues this afternoon. We do draw the commission's attention to two particular conventions on page 5 and page 6 which we hold quite high which are the ILO conventions in respect of employees being able to organise and participate to gain the best benefits for themselves. We also, as I pointed out earlier, seek to represent those members and believe that ILO conventions that talk of employees' rights are very timely and they are issues that the commission should consider. In other words, not just consider domestic pressures but where there are international charters that fall upon the Productivity Commission, we would expect those to be taken on board. I'vegot no doubt that the commission from time to time would look at views put forward by the World Bank, IMF and other international organisations. We would of course draw your attention to secretariats of the United Nations, in particular the ILO conventions, when it comes to issues affecting employees.

Our three major points at the end, if I could perhaps just read those for the record because they are the salient points in our duty of care.

MRS OWENS: Please do.

MR McLEAN: The first one is the ASU registers our concerns with the inquiry, that in many instances where private operators have acquired previously state or federally-owned resources, the change of ownership has been constantly used to undermine the wages, conditions of work and the general working environment of employees. Point 2, we call upon the commission to support such legislation to be enacted that provides protection for employees in regards to the maintenance of award standards in employment conditions and that it is mandatory for new operators in the field to negotiate these conditions with relevant unions at the transmission of business stage and therefore through collective agreements in the form of award of enterprise agreements.

Just on that point, I notice that there are similar provisions exist within the European Union, under I think it is the CHUPI - I'm not certain of the spelling but I think it is the CHUPI Act, that provides for the transfer of conditions of employment for employees at the time of the sale of business. There is a time window on that but it does provide for a settlement period at least to commence the operations and we notice that there has been extensive reform in the movement from public sector ownership to private sector ownership within the European Union and that perhaps is an example for the commission to consider the rights of employees when businesses are transferred.

Point 3 of course you probably would have heard by other organisations. The ASU seeks an opportunity to comment on the Productivity Commission's report reference to the above items. So we would look forward to having an opportunity to comment on the report of the commission once it is available and we would of course request that a copy of that be mailed to us at the first possible opportunity. The ASU is willing to answer questions this afternoon and if there are any issues that I cannot answer or you think require additional detail, I would be only too happy to take steps to arrange for any additional information or issues that you would like raised that I can't answer, that information to be forwarded to you as a matter of urgency once we've convened today.

MRS OWENS: We would greatly appreciate that. Thank you very much and thank you for those comments. I'll just address that very last point that you made in relation to getting access to our report and providing comment. We would be delighted if you had a look at the draft report and the process is that we'll be putting out a draft report before Easter and you will get one as a matter of course as a participant in the inquiry and there probably will be aspects of that report that you will want to look at. We're going to be spending time looking at issues such as benchmarking between what's happening in Australia with overseas systems and we'll be looking at issues such as what has been happening with productivity, what has been happening with job losses and so on. So I think there will be a range of issues that you and your members will be interested in, in that report. So we would be very, very happy if you were to put in a second submission at a later stage.

I thank you for this submission because there are a number of important issues that you have raised but you're raising issues from a different perspective from a lot of our other participants and we need to get a balance into what we're thinking and what we're writing and I think - you can look at issues such as job losses in two ways. If you're the operator of a railway you can look at job losses and say, "This is very good. We're getting greater productivity into our operation and we can reduce charges to users." If you're the union or you're members or other people working in the system that loses their jobs, it's a different story. So we need to get some understanding of what impact this has had on people. As you say, there's the regional impact. There's also, I would assume, a very significant impact within urban areas as well because there has been - well, I'm a Melburnian and you only need to look at what has been happening over the last 7 or 8 years in terms of going to driver-only trains, losing jobs on stations and guards. I know some of these aren't your members but these are jobs that have been in the system that are no longer there.

But you talked on page 2 of the submission about contracting out and competitive tendering. I think one of the problems that we have with some of the statistics that we're getting in terms of productivity measures is it's looking at the original - the operator, the government operator - and saying, "Well, jobs have gone there," without actually building in the jobs that may have increased at the contractor end or with a private operator if there's been more private operators coming into the system. I don't know whether you have looked at that issue of what is the net job loss in this sector.

MR McLEAN: There's probably a few issues there and if I could start again with - as you point out on page 2 of our submission, the opening paragraph, which reads:

> The ASU is supportive of industry reform that guarantees real long-term employment for the union's members and greater employment opportunities job growth for the broad Australian society.

I think if we look at micro-economic reform in some ways it's probably delivered on the bottom line, so to speak, with the contracting out issue to one side. It's delivered on the bottom line insofar as we have seen benefits to the reform process. We've seen particularly, say, the highlight of maybe looking at electricity industry, where in New South Wales for instance we've seen prices drop from $39 a unit down to 22, 25 dollars, spot prices, down to $10, but we also saw the spot price jump to $1000 a unit in November last year when there were some problems with some Victorian operators. So there are some witches and glitches in the system.

The reforms that we're now seeing is - governments are demanding to see increased productivity in the organisations that they are directly responsible for and also those ones that they are indirectly responsible for. Corporatisation is probably a classic example in New South Wales, where separate government business enterprises have been set up outside of the Public Sector Management Act and those businesses, in particular the distribution industry, are returning significant profits to the New South Wales government.

On that, I note that there's reference in our submission on page 3 to Auckland electricity industry. Most parts of the Australian electricity industry have a substantial number of what are called cable jointers. These are employees that have normally come through either a semi-skilled or a skilled area and are very sophisticated in joining pieces of wire together that allow electricity to flow down them. The joints that they perform are very, very complicated issues. Most authorities in New South Wales, including its smallest one, Advance Energy, would probably have 20 or 25 cable jointers working for it. Auckland Energy had none. During their reform process they actually had to import their labour from Australia and the people that made money out of that was the New South Wales state government who happened to own the corporatised identity called Energy Australia that performed the contract in Auckland. So the New South Wales taxpayers made a few dollars directly out of the Auckland electricity crisis.

MRS OWENS: A new export industry.

MR McLEAN: It is, actually. Australian workers are these days - many of them within the electricity industry - their employers hold passports for them and they're kept on callouts, to be sent anywhere throughout Asia - this is public sector ones, corporatised identities - to go and repair cable joints. It's not uncommon for them to put bids in for work to be undertaken in other parts of Asia, as well as Europe. We are developing a substantial amount of expertise.

One of the areas that we are concerned about is seeing expertise move out of some of these organisations if the reform process is not undertaken correctly. In other words, there's a movement of people to leave the organisations and then we find the bottom line looks nice but then when the crunch comes, we can't deliver.

MRS OWENS: Does that mean - I mean, potentially in the rail sector you're saying, "People could leave and we won't get them back, we lose those skills," and then eventually we could be doing an Auckland and importing people?

MR McLEAN: Well, you could face that, but you can also find yourself in a position that some of that work could be done internally by some of those companies. The services are contracted out and the contracting company becomes one specialist organisation that may provide services to many and the opportunity for some of those services to have a technical expertise to be developed. Some of those companies won't do it unless there really is a market there for it.

I suppose research and development does suffer under any form of changes where we see a movement from public sector traditional services, the gold-plating of the system so to speak, when we move to more a competitive market-based system. There are some things that happen when you increase the bottom line.

The concern we have is that some of those skills are lost and are never replaced. People leave organisations and companies decide not to perform that work. They may in fact re-employ those people working for contractors some weeks later after they've picked up redundancy packages. You've got to question the value of that to an organisation as it progresses through. There have been examples I suppose in the UK during some of their privatisation, where the whole company, workers and all, were moved across. That's an issue I suppose that needs greater consideration.

The job migration can also have effect too, where we can see an area, or a city for that matter, having particular jobs and expertise and then the contractor no longer being based in that area. If we were to take a regional centre, we might take, say, Newcastle in New South Wales, where there is a rail manufacturing area up there that I understand there has now been a downsizing of some of that rail infrastructure. You may find that as time goes on that the expertise in some of those rail industry jobs are not in Newcastle any more but they're in Sydney.

There are even broader and blunter examples of that with some of the lower level skill areas, where you may find cleaning companies for instance where the jobs used to be based in this region. The jobs are now somewhere else and in other regions. In fact some towns in regional Australia - I notice from a report that was commissioned by the Australian parliament, published May this year I think - I actually have a copy of it up the back.

MRS OWENS: It's all right, you can tell us later.

MR McLEAN: Published in May this year, the House of Representatives I think had an inquiry into productivity reform and social costs, I think, that were associated with it. There were a number of organisations - I note some of the Queensland regional organisations raised specific concerns about job migration. I think one of them was - a certain service was no longer provided locally but it needed to be provided from another city and unless the job was of a certain magnitude, people would not be interested in going there.

MRS OWENS: Greg, I should just interrupt at this stage and tell you that the commission is actually doing another inquiry, in parallel with this, on looking at competition in the bush and looking at the regional impacts of that. You might be interested in getting the details about that particular inquiry. So there will be a very strong emphasis on some of these issues that you're raising with us now.

MR McLEAN: I must admit, I'm pleaded to hear that. There may be other people in my organisation dealing with that, but I'll certainly ensure that I speak to the officers of the commission today before I leave. Thank you for that. The other issues that we see arising from that - I'm not certain whether I've answered your question there or not but I think - - -

MRS OWENS: While we're talking about skills, there is the question - there's two aspects relating to losing skills. You lose people altogether or you get this shift or migration of people from one area to another, and they both have different ramifications. In terms of the first one, from your perspective has there been any attempt to try and address the issue of skills formation? I mean, has there been any effort to develop training programs for people in this industry?

MR McLEAN: The ASU has been extensively involved in the development of industry training accreditation boards. Our principal areas of involvement there have been within the electricity industry, the water industry, and local government.

MRS OWENS: But not rail?

MR McLEAN: I think there has probably been - because of the large-scale changes going on with rail - I think some of the reform in respect of training issues may be lagging a little bit behind. We often find that training is seen - well, it has been our experience that training and accreditation is quite often pushed by the public sector, and the private sector picking it up in the short term. The value to training reform by way of industry training accreditation I think within the public sector tends to look at long-term goals. Within the private sector there is now an immediate push for the bottom line, that, "Does it add to the balance sheet this year? Does it add to our short-term profits? Is it a luxury we can afford?"

I think that's a legitimate concern for anyone these days, particularly if you look at the programs that Australia has had over the years, where we had no formal sort of apprenticeship systems until the end of the Second World War. The training within industry that commenced then, the move to formal apprenticeships in the sixties, now the traineeship concepts and in addition to concepts, the industry training accreditation and the movement of recognition from one industry to another, the development of new apprenticeships - I am quite amazed at the similarities between traineeships and new apprenticeships between, say, Australia and the United Kingdom. It's quite amazing, the similarities that the two countries are going down.

We believe there is a necessity for rail to plan long term, for boththe retention of those jobs and also to pick up skills that can be used as an export industry. I noticed from a recent private trip to the UK a bit of amazement in respect of the standard of their rail industry at the moment, to find that the English rail system is now fair game for jokes and banter on national television by national politicians and senior politicians and cabinet ministers of the government. I notice their discussions and views in respect - which I suppose I'm going to expect - are more regulation to take place within the UK, and I think European railway industry. I think we'll see regulation as being the solution to what was previously achieved by way of pushing the public sector in a certain direction. I think regulation needs to be an issue considered these days when there's both private sector and public sector players involved in the industry. The more important the industry, perhaps the more important the regulation and the ongoing watchdog mechanisms that are established to keep the industry playing field level and transparent.

MRS OWENS: I think there's been a bit of a problem in this industry in relation to regulation in that the operators and others have said, "Well, if anything, there's some overkill in terms of some regulation, in that each state has got its own regulatory system and then overlaying that are some national arrangements as well," and there's not a great degree of uniformity. So I acknowledge what you say. I think if you move down the track of having greater private sector involvement, what you need to make sure you've got in place are appropriate regulatory framework - and it's not just private involvement, it's changing the structures, and that's what has been happening in Australia.

MR McLEAN: I suppose that if you look upon what's taken place in Australia in the last 10 or 12 years we'll probably see a movement from what you might call the state-based organisations to more nationally focused and nationally-based organisations, and I suppose it's raised the question of the blurring of the state borders.

In some respects there are substantial similarities between that and the changes that have been taking place, say, within the European Union. We are, after all, talking about one country that's the size of Europe and we're talking about really regulations that in some parts of the world are five countries or seven countries. If you look at some of the regulation that's been able to be achieved, I think by way of, say, even the electricity industry, some of the issues that have been signed off there, whilst they haven't been perfect there has nevertheless been some attempts to create some national regulatory frameworks that even the industry has said are needed. However, in saying that, there are then some issues that will clearly remain state prerogatives, such as occupational health and safety or WorkCover issues, as we would call them, and I notice that at the moment there's an inquiry going on in New South Wales in respect to the reform of safety regulations for the rail industry, and that includes quite a number of areas. I notice that recently there was something similarly done in Western Australia, I think in respect of testing of drivers - I mean, testing by way of alcohol and drugs and things.

So I think there probably is a necessity for some national regulation to be put in place, and I think during the restructuring of national rail there were some remarks made by the New South Wales Minister for Transport, Carl Scully, about wanting to see a number of issues or raising the issue of some employee-type related matters that again need to be thought about. I would think it's probably an area that there's going to be a need for greater consultation in the form of regulations between the states. There are some of those regulations that will clearly have an impact upon the business community, and I suppose you need to look at how they can be best channelled in, and then there will be some other areas that my union will also have an interest in, but they may not necessarily be the same ones that certain companies that are pursuing other issues may have an interest in.

But when it comes to the opportunity to deal with regulations, I think anyone that's involved in the industry, be it an employer or be it a union, would probably be interested in establishing one set of regulatory arrangements for the industry, and I think as time goes on, with the introduction of private sector players in the industry, private sector players, particularly if they've come from the USA or from Europe, will find it rather interesting to have to comply with different levels of regulation for different states.

MRS OWENS: They're already here and they're already saying there are problems, and I think they find it all a bit puzzling as to how we can have so much.

MR McLEAN: I do know in respect of some of the issues, such as occupational health and safety, job retention, career development and also the traditional industrial areas, our union finds that itself dealing with the employers, and in some respects it would be I suppose simpler for a national-based industry or an industry that's attempting to develop a national focus to have some national regulations and an opportunity for the players in the industry, be they the employers or, for that matter, be they the beneficiaries, I assume like Woolworths or Holden's or someone else, and also the unions to have an opportunity to have an input into the regulatory framework.

PROF SCRAFTON: Greg, could I just go back to this business of contracting out and the impact of real reform on regional Australia. Would the Australian Services Union have any sort of local examples that you could let us have, ones that really are regional offices, reported to you - problems that you've been involved in resolving in cities like Bendigo or Port Augusta or Newcastle, the one that you mentioned, or regional cities in Queensland and so on? It would be useful for us just if you had a newsletter or something that maybe had a few case histories in there, if we could take a look at that.

MR McLEAN: Okay. I'll have to get that information to you, of course, but would you consider that you are after examples of the reform - the industrial path, or are you after that plus job losses and regional effects?

PROF SCRAFTON: All three. I don't want to make it sound like a big imposition but it seems to me that the way you've been talking about it, you've had a lot of experience in this area. It would be interesting to us to see that. I would like to ask you also a very general question about it. In your experience does it always result in job losses or pay levels being held down? Are there any good stories or any good companies, good reform examples that you or your organisation might want to point us to?

MR McLEAN: I think there are probably good examples in all industries when you move from what has been a traditionally sort of service-based culture to a customer-focused system. However, there's sort of a short-term bottom line where the new players in the industry need to be able to justify to their shareholders their investment and show the profit that comes out of that. All too often that results in the short-term directions of downsizing, contracting out and consolidation of business as opposed to fragmentation and regional development. I'm not aware of too many good stories that I can relate today.

However, I am aware that in the movement from public sector authorities there are good public sector authorities and there are bad public sector authorities, and I think for a trade union movement the industrial relations climate or the industrial relations approach taken by an employer, be it in private or public sector, is the most important issue. I have seen public sector authorities that have been inept, backwards, foolish or downright arrogant and confrontational or showing scant regard for their employees, then I have seen other employers willing to work very closely with employees, develop consultative mechanisms and take some of the more progressive steps, and I think there probably would be some good examples of that taking place.

There would also I think be some examples of some individual specific reforms for what might be called enterprise agreements for specific jobs and tasks. For instance, there may be a core set of employees working for a particular company; there's a specific job coming up that has substantial time lines associated with it and the award or principal employment agreement that those employees work under does not provide the flexibility that may be needed for that particular job. Some organisations I've seen develop individual workplace flexibility agreements within a framework of a safety net of an enterprise agreement, for instance.

I haven't seen too much of this in the rail industry, but I've certainly seen this in the electricity industry, where you start from an all-encompassing rigid award system, moving to a removal of what is no longer current to a more user-friendly award or enterprise agreement that provides a solid safety net, providing some avenues for flexibility, and then having what are called workplace flexibility documents that allow flexibility within certain constraints that are signed off by the union and by the employer after voting by a particular sectional group of employees. I know employers that have found that process to be far more efficient than attempting to negotiate an enterprise agreement for a particular area and lock the unions out.

I've seen some classicexamples of that within again principally the electricity industry, and the union's major concerns have been to maintain the core issues for employment for employees - the traditional ones of long service leave, annual leave, the things that really form the basis of your standards of living, and then to provide some flexibility on top of that.

MRS OWENS: But we're not seeing this in rail, you say?

MR McLEAN: I haven't seen that so far in rail. I'm aware of some of the new companies that have started up in New South Wales, the new corporatised identities, where I think there was previously the one public sector authority where there are now three. I hear from some of my colleagues of some good movements being made in two of those, and I've been at negotiations where I've sat down with the players from those three companies. Without going too far, I would regard one as being rigid, narrow-focused and the blinkers on and sheerly out to play political games, if you want to use that term, sort of questioning the union's right for issues; where I've seen two other areas where the employer has said, "Fine, let's just get on and do the job and let's work with people," and legitimately include the unions in those processes.

That goes on in other parts of the world. The consultation in the rail industry in Germany through works councils, through Europe now with the European works councils now spreading throughout various industries, be it electricity, be it water, be it rail, and having large consultation, where we find that unions are working with employers to achieve goals. We see a place for that. We don't see we have a luxury to play the old traditional games of confrontation. An example of that is at the moment Integral Energy, a New South Wales corporatised energy company, is now publicly in the bidding to buy a privatised Victorian energy company. They're putting the package together quite well. They have sought support from the entire New South Wales trade union movement through the Labour Council to assist them in the bid for that process.

Those sorts of issues where people can work together we regard as a very practical way to go. Whilst there is no doubt that the reform process will see jobs disappear, will see redundancies occur, our sort of preferred method is to see redundancies occur after consultation, where employees make dedicated, dignified decisions to move on, if that's the case. There is no point in having an employer go out and pick out a certain number of employees to be made redundant without consulting with the broad workforce, for that matter, because 3 weeks later they might find Mary Jones or Freddy Smith was going to leave them anyhow, and the last person you want working for your company is the person that doesn't want to be there.

If you have consultation, I believe, with the union movement and also consultation with your employees and establish credibility and respect as a good working relationship, you can certainly pick up that little extra edge that will help you succeed. I have seen that achieved in a number of organisations. I would say it reflects probably upon what latitude the board of an organisation will give the CEO, and it reflects greatly upon the sort of culture and the sort of vision that a CEO has for an organisation and whether he wants to work with people or not. I regard that as a very strategic issue for a company to take these days.

MRS OWENS: I've just got one last question. We talked about the EU and the act that provides for transfer of conditions of employment, which I'd like to get more information about if you wouldn't mind. But are you aware of what's happening in Victoria with the franchising arrangements and whether there have been any efforts made in that context to ensure that the employees' conditions are maintained when the different sections of the industry are franchised?

MR McLEAN: I know that there's been an argument over a number of awards in this country about transmission of business clauses that have actually assisted in that process. I'm unaware of the detail of which that's been done in Victoria, but I can certainly get some up-to-date positions to you.

MRS OWENS: You may not be able to. I don't know whether there has been a lot of consultation with the unions - I would presume there is - but you're probably in a good position to find out.

MR McLEAN: I can certainly find out for you and have that passed on.

MRS OWENS: Thank you very much. Thank you, Mr McLean, for coming. We would appreciate it if you could get those additional bits of information that we've asked for. Have you got any other comments you'd like to make before we break?

MR McLEAN: No, I haven't, but if there are any further issues that arise after I leave and the commission seeks clarification on it, we would hear from you.

MRS OWENS: Thank you very much. We'll just break now until quarter past 3.

MRS OWENS: The next participant this afternoon is the Australian Rail Track Corporation Ltd. Would you please give your names and positions with the ARTC for the transcript.

MR MARCHANT: David Marchant, chief executive officer.

MS McMILLAN-HALL: Denise McMillan-Hall, strategic business manager.

MRS OWENS: Thank you very much for coming and thank you for the submission. We've received other material from you from time to time as well and we're very grateful for that, so thank you. We have read the submission and we'd be happy if you would make some opening comments.

MR MARCHANT: Essentially I wasn't going to talk what the ARTC is about. I mean, that's all the background material. Basically, our submission is premised on the basis that the best productivity gain that could be made is to actually put the industry on an even platform with road and sea and to do that by getting tax equations right, whether it be fuel taxes and infrastructure tax framework, given that the industry actually pays for access and in fact makes a contribution towards the capital where some of its competitors don't. In fact that would be the most significant gateway to allow the industry to start to develop on its true economic footing, rather than being reliant on government capital subsidies and infrastructure all the time because that scares the private sector off. Relying on government for your capital and investment actually is an impediment rather than strategic gain.

Essentially getting the equation right for the investors to feel more confident about investing in industry would actually produce a better overall result than just pouring money in infrastructure all the time. Secondly, responding to industry demands for more and more infrastructure money without getting the economics of the industry right by actually getting it on an even footing. The way people are looking at the industry at the moment with the rah-rah about the new generation of rail doesn't necessarily reflect the reservation some new operators have about investing in the industry while their competitors are government-owned entities which have deep pockets and economic drivers. Essentially those competitors will not invest significant capital until they know what the shape of their retail competition is going to be.

So the faster the government-owned entities - National Rail, V/Line Freight and Westrail - are sold, the more likely you'll get a much more significant interest than what the market really can produce. People will not take those sort of entities on when they have deep pockets and don't necessarily have the same drive to not make significant losses. The real point of the exercise in the end was to point that in the east-west market, Melbourne to Perth, where there has in fact been the introduction of competition, more particularly in the last couple of years, we've seen a number of things happen, one of which is significant freight rate reductions in real dollars which has been good for the customers and good for the market development. Secondly, we've seen the slide of market share at least stabilise without necessarily growing, but stabilise between road, rail and sea. Thirdly, we've actually seen the beginning of segmented markets. We've seen the beginning of niche marketing rather than just common carriage railways.

Some of those players that are on the track now are actually players who have developed specific targeted markets and play to those markets' needs, rather than just holding themselves out as common carriers. That sort of segmentation is in fact going to be good for industry and good for the economy because effectively it provides a segment that relates to the market customer needs, rather than treating all customers as the same shoe size. When you go to one national monopoly government framework, it's not possible necessarily to segment. You actually go for the best economies of scale rather than market responsiveness. The attached graphs that we put on the submission were aimed to actually give a bit of a picture.

MRS OWENS: They don't come up well in the photocopy.

MR MARCHANT: They're much better in colour.

MRS OWENS: Yes. Have we got an original here? We have this problem with the attached graphs that they look like that.

MR MARCHANT: Could I hand you over those coloured ones.

MRS OWENS: You don't need them?

MR MARCHANT: I'm going to share Denise's in a second. Hopefully they're the same. If I can just quickly take you through them because the reason we gave them is to give a bit of a picture of some quantifiable issues about the rail industry because one of the things about road and rail is that there isn't a lot of data about market shares and market segments. At least on the east-west corridor there's a history of at least some data and there's at least a history of what the trends are. I'm concentrating on the east-west corridor because effectively it's the only corridor where there is actual competition and it's only new, it's not bold and strong, it's relatively new and cautious. But what you see is actually a consistent level of improvement both in transit times, on-time delivery and reliability.

The debate in the rail industry against its competitors isn't necessarily about price. Price rail is generally at this point of time per unit cheaper. The question is its transit time and its reliability to end users. Effectively they become the heart of the issue about improving interstate rail and transit time reliability. The only time price becomes a factor is if you predict ahead what the effect of the GST and the diesel tax is, where in fact road and rail are treated the same at 18 cents a dollar and you have a first time, a reversal, where the economics are - given they're treated equally and yet the benefits go to road, that effectively you get a marginal unit price advantage going to road again because road doesn't pay an access charge and if they're treated the same on tax grounds, on the only area that's supposed to be an off-road tax but somehow hits rail, you actually get a situation where rail's price advantage from its economies of scale and unit price is in fact reversed, not by any economic criteria but by a badly targeted tax criteria.

So this equation could change dramatically in the next couple of years to in fact produce an event where rail becomes price disadvantageous to road in any corridor, let alone this lack of timeless and reliability vis-a-vis road in certain senses. But the point of the graphs were to actually show and give some picture of the last few years of the productivity improvements taking place in the industry. On the second graph you can actually see a breakdown of what's called "healthy and unhealthy trains". Healthy trains are those trains presented to the track on time and which remain on transit time through the journey. Unhealthy trains are those that for some reason or other are not presented on time or are closed off during the journey because of an incident. Effectively, we have much more detailed graphs about what creates the incidents but what you do have is the beginning of a new trend that on healthy trains presented on time, reliability is now getting up to 95per cent. That is quite different to air reliability or road reliability. It is in fact quite a significant improvement against the image of rail being always late and always out of time.

But that's qualified by the basis that that's the presentation of healthy trains. The second line, the blue line, shows an improvement on on-time exit, regardless of what happened on its entry into the system. Where the yellow one shows on-time exit of unhealthy trains, the blue line shows the on-time exit of all trains, including those trains that are unhealthy. So you're seeing an improvement taking place in the operators of track in the ARTC area, where in fact they're helping trains that are presented off time, out of time, getting them back onto time, because in the end, as I said, reliability and timeless are at the heart of the issues.

The third graph is actually a bit of a breakdown of what's happening in the market and it shows in fact the market share changes. We've asked that this be kept confidential because effectively it actually does indicate who's doing what in the market and it is in fact information that I'm not sure these players would like to be generally known. But we thought it was worthwhile showing how the market segment is changing with competition. The first observation of that is that the principal player who was a former monopolist has changed market share but I wouldn't assume for that that the others have actually picked that market share up. The history is that rail was losing market share on the east-west corridor to road and sea until the last 3 or 4 years and now it's stabilised.

Some of that loss of market there has not necessarily been substituted by the other players because some of the other players are actually niche players at specialist markets that were not carried by rail before. The point I was really trying to portray is that very early in an open market, new entrants have come in and the market is beginning to segment, to the benefit of customers and to the benefit of the industry as a whole, by better market approach. They've actually brought innovation in with regard to how they go about doing business. Three of them are not common carriers, they are carriers aimed for niche markets. One of them packs its trains individually, each carriage, to get the best yield per unit. Another one is a wholesaler who actually distributes from one warehouse to another of their own. The third one is a semi-common carrier but with niche markets.

They have actually presented different market presentations. In each case they haven't invested a lot. They've hired most of their stock or they've leased most of their locomotives. They haven't put large capital on the table yet. That may be because they want to see whether the market is sustainable or it may be a rational choice of saying, "Whilst the big operators were competing with the government-owned and have deep pockets, we're not going to put a lot of our capital at risk and end up finding they're prepared to take masses losses to steal the market from us." So while there's people calling for significant private sector investment, in the rail industry the private sector is going to be cautious about investing a large amount of capital in a marketplace they don't see as even.

But in those that have played in it for very little entry cost, they have actually started to segment and grow. The north-south corridor - Melbourne, Sydney, Brisbane - does not have that competition as yet in that form, although I've got to say in the last few weeks, two new operators have entered the north-south market and as of this week, a third one has entered with a regular daily service, all of which we're trying to promote because our objective is to promote competition to actually create greater transactions and volume. Effectively that's what we're trying to do. That was actually to give you a bit of a picture of what's starting to take place.

The last of the graphs gives you a bit of a picture of what the corridor changes have been on the areas we measure. You will see on the first one that the interstate via Wolseley, which is via Melbourne, has got a growth curve on it which is incremental but long. The second one which is via Broken Hill has actually dropped off and that's mainly come from a redirection through Melbourne. That effectively was mostly affected by a major flood in February 97 which took a little bit of courage about that network out and because National Rail in particular were looking at getting a better unit value by locking up with Melbourne traffic. The Alice Springs line has stayed reasonably steady and via Parkeston which is effectively the Western Australian connection has remained reasonably steady.

What we'll see in the next 12 months is the Broken Hill line will curve, it will start to go back up because there's now traffic being encouraged back across that line. But it at least gives you a picture of the change of market interests that have taken place as people reconfigure, because you actually have had, during the last 12 months and continuing obviously in the next 12 months, a significant rationalisation by the major player and that rationalisation is also creating opportunities for new players. So effectively that's what we were basically outlining the submission with, but with a whole range of much more colourful words than I've used now.

MRS OWENS: More colourful graphs for us as well. It's nice to be actually able to see the graphs. Thank you very much for that, David. Denise, do you want to make any other comments on top of that before we ask you some questions?

MS McMILLAN-HALL: No, that's fine if you want to go ahead with the questions.

MRS OWENS: You made a distinction between the north-west and north-south corridor. I think in the submission you talk about the east-west as being - you call it the Commonwealth network. What is it exactly that happened in the east-west corridor that led to this different pattern of activity occurring?

MR MARCHANT: Firstly, the east-west corridor was deliberately opened up for competitors to enter the market and the pricing regime and the framework around it was made transparent and active efforts were made to introduce competitors into that market. Effectively, it was a transparency and the active desire to open up the market to competition which led to the result.

MRS OWENS: This is the active desire by the Commonwealth government at the time or by whom?

MR MARCHANT: It was the Commonwealth government at that time and it was a deliberate strategy to open up the market. Another reason for that was that AN was going to be sold and part of that sale process was a small freight business plus a passenger business so the setting was placed to actually provide the ingredients for more than one operator to operate on the system and to provide the ingredients for people to have confidence that they could actually grow their market or at least try to. So what happened is you had an open access regime put in place. If you add a separation of the access provider from AN's freight business, that separation was aimed to try and drag it into a framework where it could be transparent and build confidence in operators to know that they would be treated with reasonable independence and that they could have some reliability that there wouldn't be deals done for one player better than another, or advantage, because they were government or non-government or otherwise. And you had a pricing regime that was established to try and induce market growth.

MS McMILLAN-HALL: There was a fundamental difference when Track Access came into being in 1995. As an access authority it took a different approach from other access authorities in that it chose to have a pricing system which was openly published to all operators, so all operators operated off the same pricing schedule which was available to anybody that wanted to see it. This is in direct contrast to the other access bodies which had confidential agreements with each operator and nobody was really certain what prices each was working on. What that did was it gave the operators confidence in their competitive position, as opposed to other people's competitive position and really made it a level playing field which people could compete on.

PROF SCRAFTON: Is the ARTC continuing that policy?

MR MARCHANT: Yes, we just established our first round as a company from 1 July, price issuing. In fact the board has actually reduced the price by 2.5per cent to actually just send a message to the market that as a corporatised entity or in a company form it's not going to actually attempt to try and get into monopoly rent framework. The six principles have been very clear. We want transparency. We want a situation where the cost basis of it is clear, it's not commodity driven; that in fact we're not going to choose when it is based on the commodity product. We're not going to guess what the commodity is. We're actually going to deal with it based on transaction and volume because they have moved to a situation of actually producing a concept that we're in the business of selling time, like pathway, and that effectively we will move our goalposts to actually achieve that market commodity base and that may mean improving timeliness and reliability by actually enabling higher axle loads or greater speed.

If that can be translated into volume of traffic then we can put that back into the maintenance regimes to actually build the market up. So it's a market-based attempt but it's transparent, it's published, it's able to be broken down into units of categories of trains rather than categories of commodities and the terms and conditions are in fact visible to all. Lastly, there is not one deal available to one, it is available to all. Some other things we've added into that, apart from that, is we've actually added some new concepts, such as in peak periods. In the future we may have to look at auctioning pathways to enable the market to dictate highest and best use rather than trying to guess at other frameworks. Secondly, we've introduced a concept that people who own pathways do not have to be an operator. They can only be operated by an accredited operator but a purchaser of services could actually hire a pathway and then put the operations out to tender to an accredited operator.

Thirdly, a person who owns a pathway can trade the pathway during the terms of the contract. They can assign it, either temporarily or permanently to a person on the same terms and conditions. Fourthly, we put the market on notice that we will do spot pricing in our down times to see what the elasticity of the market is to demand, and to see if we can actually try and get better utilisation of the down periods. So we're actually moving to try and path on our systems as more of a commodity base, not suggesting that there's going to be a big trade in second pathways but to give more flexibility and transparency and power to the owner of the pathway over the owner of the asset primarily and to actually enable choices between highest and best use to be in the hands of the person who has acquired the right of the pathway. Therefore to put a floor and a cap on our conduct in pricing because those very things actually produce a situation where the market has a capture around what our pricing terms are by actually auctioning gives a cap framework in peaks. Spot pricing actually gives a core framework and assignability actually means that if someone assigns at a lower marginal framework they will actually put pressure on our pricing if it's too high. It gets traded off against other competing choices.

Hypothetically you could have someone who is able to substitute between road and rail and if our prices - that's not hypothetical, that's real - are such that it actually puts a capping on our path prices, because they can trade that out on assignment to get the benefits of the road discount and a marginal cost benefit on the bit assigned; it may not be 100 per cent and actually be better off and also put pressure on us in a market sense. So we're actually trying to get a lot more market dynamic involved in the way we think about our pathways and our pricing. The fruit of that we'll see in the next couple of years. There is another reason for why we've done that. The pathways that exist are historical. They have been chosen by the monopoly operators who are up for sale. We want to provide some flexibility that the other players can actually have a go at some of those pathways in the future because in the end it's your relationship between getting to your customers that becomes quite critical to those players. We want to be able to get some more flexibility in pathways to enable new market entrants not to be held to ransom by previously monopolised government-owned pathways that are now in private sector hands and we want to try and free that up.

Conversely, we've put in provision such as if we don't use the pathway seven out of 12 times, the pathway is surrendered to us to trade.

MRS OWENS: So it's a use it or lose it arrangement.

MS McMILLAN-HALL: Yes.

MR MARCHANT: Exactly, but on a basis that if you give them assignment rights, if you give them an ability to lease pathways or put a hold over pathways, then you could get a market behaviour where someone blocks out the best pathways and doesn't use them. So we actually want to keep the market behaviour from anybody who has got deep pockets who decides that he's going to block everybody out. So we've tried to come in with, I think, innovative ways of getting market open to some fairness without relying on a regulator who in the end will never beat those people that have outsmarted the market. A regulator can deal with extremes of pricing and they can deal with extremes of behaviour but there's more ways to skin a cat than extremes and when a market is very sensitive on times and reliability, you need to put sensitivities in there to enable the behaviour of the players to be more open and flexible.

PROF SCRAFTON: Could I just ask, Denise, how does this operate or is that over the total network or is this only over what I might call now the network that you own?

MR MARCHANT: Our terms and conditions at this point only operate over the things we own or manage. We have a lease over Victoria. We have the ownership, for better or worse, of the old Commonwealth AN track and we're attempting to negotiate access and exclusive agency rights with New South Wales, Western Australia and Queensland. We are also trying to develop an industry code for interstate access which, regardless of whether we're the track owner or manager, those access codes must comply with the industry code. Whether that's successful or not, we'll see what the participants in the other states do, but we're seeking to try and put an industry code to the ACCC on behalf of the interstate rail track owner industry which actually comes in alignment with the principles that we're moving on but doesn't make them absolutely explicit for each state.

On the other hand, we're attempting to do an exclusive agency all leasing arrangement with New South Wales and Western Australia to provide a seamless service approach on which we can sell paths on what may be their asset, of which they may still own and operate but we have an agency right. We're in the middle of interesting discussions in attempting to pursue that, even though each state has agreed in the inter-government agreement to provide that very end. Sometimes the detail and the art of the principle aren't necessarily always in alignment but it's only early days. You've got to expect people are going to be a bit (indistinct)

MRS OWENS: I was wondering how long it's going to take to get these agreements in place. Is it proving difficult or are you having success?

MR MARCHANT: Let's say that the interests of all the players are not always in alignment and - - -

MRS OWENS: You'd be surprised if they were, wouldn't you?

MR MARCHANT: It would be entertaining if they were but sometimes less entertaining if they aren't. To a large degree it's about incentives and disincentives. We're attempting to, on behalf of the mainland state governments, come up with a seamless interstate network without necessarily having to own it all, although that's not an option we discount but we don't necessarily have to do both. But let's face it, that competes in time and path with intrastate services and there's a trade-off there that has to be managed and thought through. In some case interstate services are a pain in the neck to those operators but for various reasons of power, privilege or some other notional concept, they would rather not surrender it than surrender it, even though it's a pain in the neck financially or it's not their main financial gain. We're working through those issues as best we can. In the next few months we'll either come to a rational conclusion of that or we'll come to an irrational one. It has been 20 years that governments in Australia have been trying those gigs.

MRS OWENS: Are there more problems in certain states than others or are they all being equally difficult?

MR MARCHANT: No. Western Australia has made a policy decision to consider selling its rail freight operations and initially indicated that would include the track so the discussions there have been more about policy framework and the rest. They've always indicated they intend to honour the IGA in some form and we're trying to constructively do that but we're also having detailed discussions there with regard to some of the concepts of regulating operators. Vertically integrated operations have a place in certain markets but they can be actually killers in competitive markets. At some point there was consideration obviously in Western Australia, a view that a regulator could protect the competitors in the market against the conduct of a vertically integrated operator.

I think there's probably a wiser view now that regulators aren't that insightful on a day-to-day basis to be able to give that protection to the maximum degree possible and although that may be appropriate in some rail environment markets, in a market where you've got four players competing, of which timeliness and reliability are critical, price is reasonably close because they compete in that framework, it is very easy for an integrated operator, inadvertently or otherwise, to provide a situation where some of its competitors trains become regularly unreliable. If they're regularly unreliable they tend to lose customers. And regularly unreliable can take place from a whole lot of inadvertent things such as the owner's trains taking precedence at crossings or things like that and that may not even be a policy thing. It might just happen that way on a regular basis.

In those markets that would be a significant impediment and would bring undone the whole of the last 3 years in the express corridor. It would undo the small gains being made in opening up market. I think there's a better understanding that the ingredients in the rail industry are not ones where you simply regulate price and there is no regulator smart enough to in the short term pick up the behaviour traits of reliability and timeliness issues and be able to give it the wisdom of Solomon, resolve them in short periods of time. We're dealing in an industry which can change operators and movement very quickly.

PROF SCRAFTON: I think that last comment is particularly important. Even if Solomon was in charge as the regulator, he's got to be able to operate in a very short period of time. There's no evidence to date that that is happening. In fact, a lot of participants have pointed out to us that the philosophy or the theory under which they are operating in this reform process, that's fine, but the practise is proving to be far from satisfactory.

MR MARCHANT: Regulators can deal with extremes of behaviour. Subtlety of market behaviour which actually does dictate end results, is something that a regulator will never capture until a long period of time of evidence which by that time the damage has really and truly been done. You're better to set up the economic incentives of the players to achieve your long-term goals. If your economic achievement is to grow competition in a market, if that's your objective and if the market is large enough to sustain competition and in fact will grow with segmentation, then in fact you should set the rules up to achieve that end.

Therefore you set up the rules that if you want open access in a competitive environment, you separate the monopoly part of that market which is the track, and you make sure the person who is operating that has the economic incentive to increase volume in traffic, regardless of whether it's interstate or intrastate. It's irrelevant. It's about time and volume and the smaller segments used are just as good as larger segments for that. As long as they're not an operator competing above rail, their whole life is based on what they can do about getting volume and traffic over, you can then set reasonable (indistinct) oversight about their price but you know their economic incentive is to ensure their customers meet their ends for them to actually sustain return on their capital and their risk. In that sort of market, that's a reasonable rational outcome.

If you're looking at a small contained market, Tasmania, where the market size and the ability to move from one market mode of transport - rail to other or substitutes is easy and flexible - and the base market which rail could normally take for granted is so small that it's unsustainable to keep a rail operation going, then you're looking at a different market behaviour and market outcome. If you're looking at an urban passenger system in say Perth or Adelaide, then you're really asking people to bid against what level of government subsidy they're in and you'd ask them to take the track and the rail risk because otherwise all you're going to have is two people for the government subsidy, the track owner and the rail owner, if in fact it's one market and you actually put the risk on them. If you're in urban Sydney, hypothetically, you could break that up into three markets, because you can make three cycles out of it, but you would want the track and the above because in the end the customers in that market don't have much choice. Individual personal passengers don't have a lot of market choice in a big infrastructure investment. Bit cargo careers and freight investments do have choice. They have market power.

So I mean, you're dealing with different market segmentations. The market theory changes, depending on size, shape of market, and ability to choose, and transparency. Rail is part of the transport industry. It's part of logistical modes. It's not an industry that's owned. It's not an end in itself. But it is in very separate marketplaces. The behaviour and the incentives you put in those marketplaces should reflect the differences in the marketplaces. Not one shoe fits all.

PROF SCRAFTON: I just have one follow-up, if I could. You mentioned about the incentives to improve the viability of the operators but of course, for you there's a commercial incentive to ensure your own viability, isn't there? You mentioned earlier in your introductory comments that you didn't really see the corporation being an organisation that is perpetually topped up by government grants of one sort and another, so you have to ensure your own viability.

MR MARCHANT: The only way I ensure my own viability is to grab a volume of traffic. I can't take monopoly pricing positions or I'll lose a volume of traffic anyway, because the substitutes are too easy in the market that I'm in. In the north-south corridor, anything I do to grow market is going to be good. I mean, let's face it, it is a pathetic market. But that's mainly because it is segmented in its management and segmented in the way it's operated. While ever it remains segmented, it will be a deadly operation, because it's facing competition with issues such as Sydney passenger services and coal services in New South Wales in particular. While ever they are treated all the same, we're going to have problems. If we separate those market issues out and segment the market, we'll move faster.

But the bottom line is the rail industry has a habit of saying, "What we need is more and more government money." Now, I'm not suggesting government shouldn't invest in rail but more and more government money isn't the solution to growing a rail industry. It is only a method of assisting the solution. The solution is, get the economic rules right and the rail industry should survive with or without some government assistance, should survive on its economic merits in an open market framework. Treat it with some reasonable amount of fairness with regard to the way the tax and charges systems work.

I'm not suggesting there shouldn't be access charges. I actually think there should be. I think that's a way to treat the capital well. I'm suggesting they should be offset by the other taxing systems which their competitors don't pay, so that the net effect is reasonably neutral as distinct to the individual tools of policy. It is possible the industry looks too quickly at just asking government to pour money out for infrastructure on track, when in fact the best benefits will be when both parts, above and below, look for incentives to actually improve the game overall. While ever they're like mendicant states, saying, "Just pour more money out of us," they're going to scare the sugar out of those people who have got the money.

PROF SCRAFTON: I think that is a very important point. You made it in your introduction: that if you want private investment, the investors want certainty. They don't want to be a mendicant industry, in effect. This is not a philosophical - -

MR MARCHANT: Well, the governments may look good and compassionate in giving money out, and I welcome the money and the more of it the better, but the reality is if you are so much reliant on the economics of the industry - on them pouring money out year after year in a discretionary way, it's a risky investment. But getting the tax tools and charges right between the transport modes - because in the end that is the market, it's a range of transport modes - getting those principles right, using different tools of policy such as diesel fuel rebate framework, but I'm not just thinking about that. I'm also thinking about infrastructure rebates, because in the end, if you're asking private sector to invest in the rail infrastructure in substitution, then the road infrastructure does not have that investment in that form.

Governments pour money at roads. Getting the economics right with regard to the externality costs and those things, so that in fact the equation is right, then you can use different tools of taxing and charging policy to at least get the net benefit and the net disbenefit right between the modes, even though you may use different tools of taxes and charges. Then let the market work out its best economic effect.

At the moment government taxes and charges and infrastructure spending policies are dictating outcomes and they're dictating outcomes in an uneconomic and unsustainable model process. I mean, you get money thrown at things based on externality costs which are unproven and yet in another industry, in which externality costs are proven, are not recognised when people invest. So I'm basically arguing, don't keep on looking at big dollar infrastructure investments as the only equation. Get the economics of the taxes and charges principles right and you'll find the private sector will build confidence in those things which they think are economic.

They might not build an Alice Springs to Darwin railway but they might actually help overcome the problems of getting through Sydney and getting rail traffic on the north-south corridor, which has huge volumes, of which the investment on the highway system - which will be clogged up again in the next 5 years - could have been substituted by some of that stuff going on rail in a fair economic sense, because rail could have made an incentive to make it happen without governments pouring billions of dollars at it every year, as they do at road. But, you know, you say you want private sector investment. Well, get the rules right.

MRS OWENS: There are some in the private sector, however, who say, "We are not going to invest until the government" - and it's usually the Commonwealth government - "gets the infrastructure up to a certain level. It has been allowed to run down. There are all these things need to happen. We'll be happy to invest but we want it brought up to scratch." What do you say about those sort of arguments?

MR MARCHANT: Yes. I, like everybody else, would like something for nothing if we can get it. I suggest there are a number of rail operators in the private sector who genuinely would like the infrastructure improved but secondly would say, "Look, we could work on that infrastructure if they could just get the rules right and let us have a go, and it will improve because our volume and the rest will help make the money to get the track improved." It's not a chicken and egg. Both things can roll together. I think there are very few real private sector investors who are interested in this investment area who are going to hold back on the basis that they're going to wait until the government gets all the infrastructure right. If they wait for that, come 2020 they will still be waiting. Governments never get all the infrastructure right. That's one of the reasons why governments are looking to put infrastructure investments in a blend between public and private partnerships. If anybody is waiting for the government to get the infrastructure right, they ought not to be in business anywhere.

MRS OWENS: Some of the competitors on the east-west corridor didn't wait. I mean, there has been a lot of complaints about the state of the track, for example, between the border and Melbourne.

MR MARCHANT: There has been.

MRS OWENS: But you still find, as you mentioned at the outset, that there has been more competition on the east-west route than you've got on the north-south route.

MR MARCHANT: Well, let's look at this. I mean, we've set ourselves a target of taking 1 hour of transit time off the Melbourne-Adelaide corridor by March next year and taking a second hour off by December. Quite frankly, we'll achieve that. We'll achieve that with or without government investment, because effectively we can see that we can get some market development by risking some of our capital against it. The bottom line is that if we can grow the market, we'll make the investment as well. The point I'm trying to make is that in the end it will be a blend of government and private investment but unless you get the tax and charge structure right, even if the private sector wanted to invest, they wouldn't.

Some market players are prepared to take that risk and they're prepared to take a risk on a north-south corridor if we can free up the way we manage it, to assist them to get on there and have a go. They don't have to go through five accreditors in Australia about their safety rules. When a truck driver goes to one states, it's recognised everywhere. They don't have to pay safety charges to every state to just get in the game and have a framework. They don't have to go through three different organisations just to get access into one piece of corridor. I mean, they're the things that frustrate them more than the state of the track, because they actually know that the state of the track will improve if it gets better utilised.

The north-south corridor is the only consumer sitting there, is NR and a passenger train owned by the New South Wales government. I mean, there's really not a great incentive to improve it, is there, because they're all in the club, aren't they. Effectively, the more of them that get onto it, the more likely that the improvements will take place in reality, both by the track owner and by the benefits of the economic gain becoming clearer. I'm like an American rail operator. I'd rather own a monopoly in a competitive market. I'd rather come in and say, "I wanted an integrated railway for sale, thanks, rather than a separated one, because I'm used to that and I like regulating this because they never send an industry broke." That's why I like it, not because it's good for competition. It actually ensures protection for shareholders. No regulator sends a market broke. Same with the private sector investment infrastructure - "Yes, I'd rather government did it than me, sure" - so would I. But it'snot real.

PROF SCRAFTON: But maybe the government investing is partly responsible for the very problems you've been describing, that people have become used to the fact that you let things fall apart and then you complain, then the government comes in with a patch-it program but nothing ever really improves.

MR MARCHANT: The proof of the pudding is that most of those things, maintained properly, would never have got to the state they are. The reason they get to the state they are is that government own government monopolies. I'm not having a go at governments. I mean, what I'm truly saying is that because in fact they're in singular integrated frameworks in which government is taking all the risk, the government has a massive number of competing demands on its resources, it will trade off a short-term demand in maintenance in this area against the public hospital demand up the street, and rightly so.

But in the end those trade-offs come to an end. When people are taking market risk with their own capital they recognise the value of husbanding it, because in the end they can't afford the crunch factor - and then sunken infrastructure investment. You're dealing with a long-term investment cycle, of which you actually never get to historical replacement costs if you replace it because the U-curve keeps on moving out and out, right.

It's one of the interesting differences between the economics of track ownership and above rail ownership. Track ownership is a long-term sunken investment - very different economic driver to above track. Economic life - 25 years for a loco at most, and carriages around that - different economic investment. They can trade the carriages and locos overseas or to another market overnight. Not much value for a second-hand track. Not many people will actually get much economic value out of it. The easements aren't big enough to put anything decent on it, including a road, so the substitution costs and the land value don't go too hard.

So the economic incentives are quite different. So they are for government. Better to deal with the short-term issue than the long one. So maintenance actually falls away while those dynamics aren't there. So the very thing they complain about has been brought about by the very system that they actually would like to solve it. But that's the entertainment of changing industries.

PROF SCRAFTON: This is the last question, I promise, from me, Helen.

MRS OWENS: You can have as many as you like.

PROF SCRAFTON: I just want to clarify one thing. About the industry code that you mentioned and taking it to the SEC, is that similar to the electricity undertaking, so that the ownership really doesn't matter.

MR MARCHANT: Yes.

PROF SCRAFTON: It's a matter of pricing the network.

MR MARCHANT: Well, it's about setting a framework for rules of not only pricing but mechanisms of access.

PROF SCRAFTON: Right.

MR MARCHANT: Recognising Queensland has an integrated system with different competing demands, they've got an access regime for Queensland which differs ideologically than what ARTC's view of the market would be. What we're trying to do is if we aren't able to get leasing arrangements or otherwise, at least try and set a policy framework around which it's consistent. Now, in the end, whether that industry code goes ahead or not will depend on whether we can get the industry on side. At this point in time in principle they're in agreement with me. What we at least have got at this point in time is a consensus about key performance indicators between rail operators and track owners - six characteristics measured across Australia and by individual operator, dealing with both track quality, train quality, reliability and timeliness, and some other issues which I'm happy to forward to you.

PROF SCRAFTON: Yes.

MR MARCHANT: There has been consensus around that draft. You know, regardless, it might at least make the industry transparent to all players. So even if we don't get the code up, we might at least get the key performance indicators up.

MRS OWENS: That's better than nothing.

PROF SCRAFTON: Yes.

MRS OWENS: Can I just look to the future - and I know you've only just got off the ground - but you have a potential life span of 5 years, if I understand it correctly, or at least you're going to be reviewed in 4 to 5 years' time. Have you got any sense of what could or will happen at that point? I know this is early but it's a matter of where is this system going. You talked about the regulatory barriers to entry, if you like, the concerns that private operators have got that they have to deal with umpteen regulatory regimes and - - -

MR MARCHANT: Each of those are being addressed by industry working groups to try and cut through those barriers. What we're providing is hopefully a facilitation effect of that. We're not a regulator. We're just a humble track owner just trying to get a bit of business.

MRS OWENS: I understand that. But I think one of the other barriers is the concern that new operators have got about having to find their way through different access arrangements.

MR MARCHANT: Yes, absolutely.

MRS OWENS: That's why I'm really asking you about the future. We talked to the department this morning, and it's a question of how do you deal with that problem. Is there a potential to have one access system in Australia?

MR MARCHANT: For interstate?

MRS OWENS: Inter and intrastate.

MR MARCHANT: I think there's a potential for a common access regime for interstate in the short term. I think there's a great potential by mid-next year. We should be able to come to a common Australia-wide interstate access framework and a singular point of entry on common rules by mid-next year, subject to everybody working through the issues that we're working through. On intrastate, my personal view is that what happens on the interstate sets a benchmark which then helps thinking about getting more commonality anyway and, quite frankly, except for large commodities like coal and the rest that may go to short haul routes, whatever is dictated on the interstate will end up becoming common on the intrastate anyway because it will be a common movement of goods that eventually takes place. So I think one actually follows the other inevitably, even if the individual players in the market want it or don't want it. I think that will inevitably happen.

We've indicated to the market that we're happy to enter contracts for longer than 5 years. We'll do that with our shareholders' approval. In Victoria and otherwise we're negotiating leases which are 5 years but able to be renewable for 5 plus 5, making 15 years, otherwise we can't raise capital to invest in the Victorian exercise. It's very hard to get 5-year capital on sunken investments. So we're actually acting as if we'll be longer than 5 years on the basis that's the way to build confidence in the contracting and the market. Now, if at the end of the 4-year review the Commonwealth and the states come to a view that the thing hasn't worked, the contracts will still be in existence and we'll have to review our framework. If they want to sell it to some independent party, that's cool.

So effectively what we're doing is trying to develop the interstate market, and the proof of the pudding and where it should go from there should be reviewed in 4 years' time. It may be, sell the entity to a non-rail operator and keep the theory going but in different hands than government. It may be that it has achieved its objective and its commonality and we just learn to segment it again, or it may be that it continues in its present form or some mix of the same.

In the end we're trying to give confidence to the market, though, that we'll contract for longer periods than the 5 years, and we'll actually try to invest in capital in those places we're leasing on terms for longer than 5 years, because that actually gives a value to whatever the outcomes are in year 4 of review anyway. You don't have to be the same entity to keep the contracts and you don't have to be the same entity. If you can build confidence that that's the direction, it really doesn't matter who owns the entity except if it's an integrated entity which actually act in contradiction to the very objectives you're trying to achieve. So we're not spending a lot of time worrying about what will happen to an organisation in year 4 or 5.

MRS OWENS: I wasn't implying that you would. I just- - -

MR MARCHANT: But I'll be interested in reading the Commonwealth's answer this morning.

MRS OWENS: We didn't ask them that question in that way, but we were talking more about this problem of the operators that are going intrastate and interstate still having to deal with a number of access regimes.

MR MARCHANT: Sorry. Let me answer the question a different way then. We're saying - and this is one of the definitional problems we have in a state in particular - that if a train's origin and destination goes across a state border it's an interstate train and it can drop cargo off intrastate if it likes. But if it's origin and destination go across the borders, that should be interstate.

MRS OWENS: You've just clarified something for us that we didn't understand, so thank you.

MR MARCHANT: It's on the interstate network. There was a problem in a particular location about that definition because they're saying, "It should only happen if - if it changes its train number at Albury and becomes a new train in Wodonga that shouldn't happen." Our view is that the interstate train should be treated like international airline operations. It's about origin and destination, not about individual stop-off points. Therefore the rules should be so common to the players, because of that origin-destination rule, that they can actually deal with one player. If in fact they're generally going from Cootamundra to Sydney they don't need to come near us, but if they're generally going Sydney, Cootamundra, Broken Hill, Perth, then they ought to just come to us and do one way.

That definitional problem is the heart of one issue in one state, because the more you artificially create it to enable gaining - Sydney to Albury and a new one, Wagga-Melbourne, or Sydney to Tweed Heads and then a separate one from Coolangatta to Brisbane or vice versa - any one of those things - all you're doing is just gaining systems and you're in fact attempting to actually provide economic results which are transparent and which actually only achieve simplistic parochial objectives; they don't actually get you anywhere. So the heart of our problem in one area has been that very definition.

We've taken the view that we should act in similar conceptual terms to the international airline industry because they cover these sorts of problems on a regular basis and they have a very clear definition agreed by every nation as part of IATA, that it only counts on the designated origin and destination of the plane; doesn't matter what they drop off and pick up in the meantime.

MRS OWENS: I could talk to you for about another half an hour on the airline industry because some of the proposals you've mentioned about auctioning pathways and so on are starting to sound very familiar to me because I've just finished an inquiry into international air services agreements. I was just going to ask you a quick question before we finish. That auctioning arrangement has started or is- - -

MR MARCHANT: No, we're holding off until after the sales of the major government entities, but we're putting in our terms and conditions - we've said to the market, "We're not going to go near that until the playing field is clearer and then you all know that you've got a fair go at it." What we're trying to do is give confidence to the non-government investors that are in the market that they won't be blocked out - - -

PROF SCRAFTON: By government operators?

MR MARCHANT: By government operators, and effectively this is the way we'll go about freeing up systems. I mean, we are actually cleansing our pathways now. People who haven't operated those pathways, even though they may have a conditional path, we'll free-up to try and get new pathways into existence.

MRS OWENS: Good, thank you.

PROF SCRAFTON: Excellent. I've got nothing to be explained.

MRS OWENS: That was very interesting and it was an excellent discussion, so thank you for that. Have you got any other comments you'd like to make before we close today?

MR MARCHANT: No, I've caused enough trouble already.

PROF SCRAFTON: No, it's excellent.

MRS OWENS: We'll now close today's proceedings and we resume tomorrow morning, on 12 November, at 9.30 am.

AT 4.18 PM THE INQUIRY WAS ADJOURNED UNTIL
THURSDAY, 12 NOVEMBER 1998

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