WESTRAIL

Supplementary submission to the

Productivity Commission

Inquiry into

PROGRESS IN RAIL REFORM

May,1999

(1) Key Reform Initiative in Western Australia in the 1990's

In the table 3.5 we believe that there are three reforms missing to complete the picture;

- July 1 1995 Transport of all bulk traffics deregulated.
- 1997/98 Rail Safety Act proclaimed transferring regulation of Rail Safety from Westrail to the Department of Transport.
- 1998/99 Rail Access Act passed and application made to the N.C.C. for declaration of an effective access regime to the Westrail Network.

(2) Performance of the Australian Rail System.

The report notes generally continuing improvement in the productivity of Australian railways although it argues that there is a long way to go before we achieve the levels of efficiency evident in U.S. and Canadian Railways.

We also note that there is to be further work on the Commission's views on productivity before the final report is released.

There are a number of issues we would raise;

(i) Scale Efficiency

We are concerned that the results do not take into account a number of factors that impact on comparability.

For example, the commission itself has raised the question of using locomotive numbers rather than locomotive horsepower in comparing productivity.

It then suggests that this effect may have been diminished by the increasing horsepower of Australian locomotives relative to the U.S. industry but the reality is that the horsepower capacity of U.S. locomotives has increased significantly in the same period.

In 1994 the Australian Wheat Board did an international benchmarking exercise on rail services provided to them by Australian railways.

When comparing tonnes hauled per 1,000 tonnes of locomotive horsepower Westrail hauled 116,000 tonnes compared to Burlington Northern at 43,000 tonnes and the Australian average of 66,000 tonnes.

A second example is the question of track standard. The results of a productivity comparison are easily influenced by the operating standards such as axle load and speed.

These factors are governed by the capacity to invest in infrastructure that is determined by;

(a) the size of the market; and

(b) Government policies and funding initiatives (such as taxation incentives).

Generally the Australian Transport market is thin and there have been few direct Government policy initiatives which favour rail.

A third example is the impact of Government policy on rail and therefore its competitiveness.

For example United States rail operators do not pay diesel fuel excise.

Therefore we need to clearly understand the market environment and adjust input factors for scale before making comparisons.

(ii) Use of nett tonne kilometres as the output measurement.

N.T.K. as a measure of output also is impacted by scale.

Reverting to the Australian Wheat Board study again whilst Westrail achieved 116,000 per 1,000 h.p. of locomotive power it only achieved 22 million N.T.K. per locomotive whilst Burlington Northern achieved only 43,000 tonnes per 1,000 h.p. of locomotive power it generated 53,000,000 NTK's because of the generally longer distance U.S. railways operate.

(iii) Use of on-time running as a performance measure.

Whilst on-time running has been a performance measure for freight railways and continues to be measured by all railways (including Westrail) in a number of cases it does not reflect either the basis of the contract or the best measure of performance.

We accept in intermodal (and particularly interstate) freight that it is critical that freight is delivered on time but it is not the most important and best measure especially in bulk traffics.

Westrail adds value to the performance of the freight task by using total logistics management principles which comprehend the clients total operation.

We have employees operating within our clients business and we understand their needs.

We have clients, for example, where the contract requires a minimum number of times to be maintained in stockpiles.

In our grain business where trains are scheduled differently each day the key performance measurements are tonnes to port in order to meed shipping requirements.

With the grain industry we have developed sophisticated logistic management tools.

The point we are making is the quality of the service delivered and the method of measurement will differ and on time arrival may no longer be valid for much of the railways business.

(3) Structural Issues

(i) High Volume Regional Railways

The Commission sought views on the appropriateness of vertical separation for high volume regional railways.

We note the Commission has suggested that low volume regional railroads should be vertically intergrated but horizontally separated and high volume regional railroads both vertically and horizontally separated.

The position ignores the fact that in most Australian examples the two categories are likely to share common facilities (including parts of the track) and achieve economics of scale from shared overhead facilities such as maintenance facilities.

Therefore, in any consideration of a separation model careful consideration needs to be given to;

(a) diseconomies of scale arising from the process; and

(b) the high costs of interface arrangements.

It is generally considered that the ability to extract monopoly rents arises in the provision of infrastructure which is not economically or practically duplicable.

Whether the provision of that infrastructure occurs in a separated or integrated model the opportunity to extract monopoly rents exists.

Effective access regimes are the appropriate model to prevent this because competition is not possible in this market.

Clearly, Westrail believes that the appropriate model for high volume regional railroads is a vertically intergrated railway with an effective access regime to prevent monopoly rents and provide competition in above rail services.

The Commission has spent some time comparing productivity of Australian railways with the US. Perhaps there is something to be learned from these more productive railways where they are all vertically integrated and do not have regulated access regimes.

(iii) <u>Interstate Network</u>

The interstate network has never been a stand alone network and operates over both exclusive interstate track; parts of the high volume regional railways; and on heavily used urban infrastructure.

Whilst there is continued discussion with respect to the interstate network whatever structural model is introduced will require extensive interfaces and this will create issues for operators.

If, for example, the standard gauge network between Kalgoorlie and Perth come under the control of the (A.R.T.C.) then Westrail and other intrastate operators would be dealing with two Access Authorities (the A.R.T.C. and Westrail).

The current model being pursued is an “one-stop shop” model where the ARTC is a clearing house to provide seamless access for all interstate operators.

If the suggested model of the Commission was followed there would need to be similar arrangements entered into to provide seamless access for operators on the regional railway.

Given the critical importance of the urban areas to interstate operators (because of curfews and path limitations such as exist in Sydney) it is always interesting to see that models suggested horizontal intergration of the interstate network never includes dealing with this critical interface.

In any event the extent to which the model effects both market outcomes and operator profitability is largely untested.

The ARTC claims in their submission that vertical separation and an open and robust pricing regime has lead to increased competition in the east/west interstate market. The reality is that much of this competition predates the reforms and that part of the corridor is under the control of a vertically integrated operator.

Westrail believes the proposed model of the ARTC retailing interstate access and providing a one-stop shop is the most pragmatic outcome given the nature and the history of the network.

(iii) Pricing Methodology for Paths

The Commission has sought view on the most appropriate way to price paths.

The simple assumption that paths (i.e. rigid timetables) is the only way to sell access is of interest.

Depending on the business and the market an operator may wish to purchase access to an agreed tonnage or train capacity within a given period (e.g. bulk operations).

In some markets selling paths is not practical as the train service required is not based on paths as much as shipping logistics (e.g. Hunter Valley).

Whilst A.R.T.C. has posted prices for paths that works because its customer base operates in markets with critical close-off and delivery times and paths are important.

We would not dispute the assertion that there should be transparency in the factors used to construct pricing (such as is required by the proposed Western Australian Access Regime) posted prices can extinguish flexibility and innovation.

There also needs to be the ability to differentially price a section of railway based on the market for the goods being carried; and the operational standards and specifications of the specific operations.

Therefore, we do not believe that there is a specific methodology, such as auctions, that will always lead to prices based on the value of the use of the track.

Finally, whilst long term allocation of paths may be seen to limit other competitors entering the market it is the track owners interest to have long contracts to justify the long term investments required and equally operators seek long term allocations to justify their own investment.

(iv) Valuation of Assets

Westrail favours the use of Gross Replacement Value for the methods of valuation as it is transparent and contestable and therefore access seekers can easily judge the extent to which the values are realistic.

Investment in rail infrastructure involve risk because the life of the investment is often longer than the available business contracts and the owner needs to be able to account for asset replacement during the life of the investment.

Alternatives such as DORC can lead to protracted negotiations as to what is the optimum configuration. The benefit of DORC, which is principally alleged to be avoiding ‘ gold plating ‘ or over investment in the infrastructure can be achieved in an access regime requiring demonstration from the owner that the infrastructure is required for the task.

(4) <u>Safety regulation and operating standards</u>.

This subject has been explored by a number of enquires and whilst there are serious issues that need to be addressed but there are also a number of myths and generalisations that are causing confused debate.

The Commission has fallen into the trap of perpetuating some of them.

For example, in box 8.5 you point to different axle loads being permitted at 80KPH on 47-kg rail. That is not surprising as ballast, sleepers, fastenings and maintenance regimes all effect the capacity of the track but that only receives a grudging acknowledgment.

Box 8.1 refers to the radio issue and bemoans the lack of a common frequency and ignores the fact that radio frequency and mode is under the control of the Spectrum Management Agency.

There are essentially three points we want to stress in this area:

- absolute uniformity can stifle innovation and flexibility and out target should be interoperability not uniformity

- the myths and the legends need full and accurate assessment so that the industry can be sure that there is a cost effective solution available (for example you could have a common satellite based radio system today but most people could not afford its operating costs)

- national uniformity for interstate operations could impose significant costs on regional operators who may end up working with two systems

Whilst there are a number of initiatives under way in this area the lack of a rail body equivalent to the role performed by the Road Transport Commission in researching and introducing national standards continues to disadvantage this industry.

On the question of safety regulation we only want to make two comments.

Firstly, there is general agreement in Australia that we should adopt a non-prescriptive compliance based model of safety regulation and good progress has been made in most jurisdictions. Most of the criticism comes from those jurisdictions where there are inspectorial-based regulatory schemes or the compliance-based schemes are being mis-interpreted and inspections are being imposed.

Secondly, there is a good deal of confusion about safety standards imposed under Rail Safety Acts and additional standards being imposed by track owners. The Australian Rail Safety Standard (AS 4292) clearly sets out the parties responsibilities.

(5) <u>Competitive neutrality between road and rail.</u>

It is a pity that this issue is not the first chapter of the report rather than the last.

The major issues have been well identified in the past and include:

- the lack of any framework for long term transport infrastructure planning

- the inequitable investment in road and rail infrastructure stemming from different approaches to analysing the investment which allows Road to pick up socio-economic benefits whilst rail generally doesn't and also with no direct relationship between road use and Road costs

- the inequitable tax treatment of rail versus Road especially the diesel fuel excise

- the lack of a framework to drive the standards change process.

The Federal Government has withdrawn from a direct operational presence and sees its role as creating the appropriate policy and regulatory environment for the transport industry and rail in particular. There is much to be done.

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