AUSTRALASIAN RAILWAY ASSOCIATION INC

Productivity Commission Inquiry

Progress in Rail Reform

SUBMISSION

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Introduction

The Australian railway network is a significant national asset and plays a key part in the economic well being of the country. Australia's extensive rail system plays a major role in hauling the nation's freight, serving intercapital markets and many important economic regions.

Railways are essential to the nation's economy because they form an integral part of the distribution process for intercapital freight and a range of regional produce and bulk export commodities. Interstate rail operations provide valuable import landbridging between our capital cities.

Principal commodities carried by government railways are coal, grain, ores and minerals, steel, containers, manufactured industrial products and general freight. Private freight railways are used for iron ore in north-west WA and Whyalla in SA, non-ferrous ores in Queensland, NSW and Tasmania, sugar cane in Queensland and a range of traffics in South Australia and Tasmania.

Rail passenger operations provide an essential mass transit alternative to car travel in urban areas; provide car-competitive, cost effective transport to regional and rural centres; and long-distance tourist trains are an integral part of Australia's tourism economy.

Efficiency Improvements in Rail

Over the past ten years, Australia's rail operators have made significant improvements in productivity and cost recovery. Government rail employment has halved, rail freight employee productivity has increased 200% and costs per net tonne kilometre of freight have declined 25%.

Freight haulage has increased more than 36% to over 110 billion net tonne kilometres per year. Rail, road and sea each haul about one third of Australia's net tonne kilometres of freight, excluding pipelines.

The rail freight task comprises around 55% of the combined non-urban rail and road freight task. This consists of all iron ore haulage, 80% of total coal production, 70% of total grain production and 40% of interstate freight. Iron ore, coal and wheat comprise 20% of Australia's exports and are worth $15 billion annually to the nation's export economy.

The interstate rail freight task varies from 70% of east coast to Perth freight to just over 20% of Melbourne-Sydney freight.

All rail freight services are profitable or close to profitable and there is no net cost to taxpayers from government rail freight services.

Government financial support for rail passenger services has declined by 40% and a number of these are now operating profitably. CSO/subsidy payments for rail passenger services are around $700 million per year. Rail passenger employee productivity has increased 90% over the past ten years.

1991 Industry Commission Report on Rail

The 1991 Industry Commission Report on Rail contained a number of recommendations for rail authorities and governments.

The rail reform process that has occurred in Australia's railways over the past six years has resulted in all of the recommendations for rail being implemented by rail authorities. Rail authorities have recognised that change must occur for rail to remain a competitive, viable transport option.

However, many of the recommendations for governments have not been implemented. In particular, introduction of road user charges that more accurately reflect road damage and other externalities caused by heavy vehicles has not been implemented.

The Federal Government has also failed to exempt rail, as an 'off-road' user of diesel fuel, from diesel fuel excise.

Analysis of 1991 Rail Report Recommendations

Recommendation for Rail	Action
Railways be fully corporatised within 3 years	Achieved. Railways have been corporatised or privatised. Westrail is still a Commission. However, it is soon to be privatised.
Open access to rail lines.	Achieved. All States and the Commonwealth have open access regimes in place.
Each rail authority operate its infrastructure network as a separate business centre with accounting separation	Achieved. All rail authorities have either accounting or operational separation for access business units or have accounting systems in place that can readily identify access income and payments.
Outsource to maximise efficiency	Achieved. Track construction and maintenance, locomotive and wagon construction and maintenance, on-train catering and passenger security are some of the functions that have been outsourced.
Increase labour productivity through more efficient work practices	Achieved. Australian government rail employee productivity has increased 200% over the last ten years. Government rail employment has halved over the same period. Multiskilling, wider shifts, split shifts and a range of other initiatives have been implemented to achieve dramatic improvements in labour productivity.
Remove royalties from rail freight rates	Achieved.
Reduce the cost of urban rail services to world best practice within five years	Achieved. Cost recovery from urban rail services averages 40%. This is similar to the New York Subway and the Paris Metro, but lower than Chicago (48%) and Toronto (61%). The overall operating cost of urban rail services in Australia is around $600 million per year. This is a reduction of 35-40% compared with ten years ago. Over that time, urban rail

	employee productivity has increased 90%.
Only retain LCL traffic if it covers marginal costs and contributes to fixed costs	Achieved. Governments now procure LCL traffic through transparent CSO contracts with rail operators
Abolish seniority based promotion and introduce merit based promotion	Achieved.
Introduce salary structures that reflect skills, qualifications and experience	Achieved

Recommendations for Government	Action
Rail receive rebate of diesel fuel excise used for freight	Not achieved. Rail, as an 'off-road' user of diesel fuel, still pays diesel fuel excise. This adds approximately 10% to rail operators' costs. The cost of diesel fuel excise to rail operators adversely affects Australia's export competitiveness for coal and grain and adversely affects rail freight operators competitiveness with road freight.
Introduce road user charges that more accurately reflect road damage	Not achieved. The National Road Transport Commission has introduced uniform national road user charges for heavy vehicles. However, these are not mass-distance based. They do not reflect the difference in road cost recovery from vehicles travelling 'light' or short distances and heavily loaded vehicles competing with rail. The NRTC's road user charges have not been increased since 1992. Proposed updated charges to more accurately reflect road damage caused by the heaviest vehicles are being resisted by governments and the road transport industry. The NRTC has acknowledged that a mass-distance charge for heavy vehicles would

	provide a more accurate level of road cost recovery from these vehicles.
States and territories enable local governments to impose road cost recovery and externality charges on heavy vehicles.	Not achieved. Heavy vehicles cause significant damage to roads and intersections in urban areas. Repair costs to this infrastructure is incurred by local governments. Heavy vehicles in urban areas contribute to road crashes, air pollution, noise and congestion. These costs are paid for by the community.
Local Government contribute to capital and operating costs of new rail public transport schemes.	Not achieved. Rail public transport has the capacity to serve many developing outer suburbs. Local government should contribute to the cost of rail public transport as it does for other infrastructure. Rail public transport benefits local roads by reducing traffic.
CSOs charged against appropriate government budget category	Not achieved. Governments must ensure that the cost of operating rail services is transparent. Where rail services are used by government for social welfare purposes, the cost of doing so must be clearly charged to the relevant government program not the rail operator.
National Accreditation Scheme to recognise rail skills	Not achieved. This is a recommendation of 'Tracking Australia'
Explicit CSOs	Achieved. Rail authorities have in place accounting structures that identify government procurement of non-commercial services for social and environmental reasons.
Remove subsidies to bulk freight within three years.	Achieved.
Trade Practices Act apply to rail authorities and have the power to settle disputes concerning monopoly pricing and track access.	Achieved. The Trade Practices Act applies to rail authorities and dispute resolution through the NCC and ACCC.
Eliminate regulation of traffics to rail and simultaneously introduce appropriate road user charges to cover pavement damage and externalities	Achieved in part. There are no longer any regulations requiring particular traffics to be moved by rail. However, appropriate road user charges to

	cover pavement damage and externalities have not been introduced.

Issues for the Inquiry

Industry Structure and Competition

Australia's government railways have undergone significant reform in the past six years.

Competition policy has resulted in the Commonwealth and some States establishing separate rail infrastructure entities and generally these bodies have been required to adopt "commercial" style accounts that include full accounting for capital investment and capital stock. Access regimes have also been established as separate business units within vertically integrated railways.

Government rail authorities have been corporatised and, in some cases, separated into freight, passenger and track authorities.

The former Government owned Australian National Railways Corporation had a separate track access unit to oversee open access to the interstate standard gauge network in South Australia.

Australian National has now been privatised into separate freight and passenger businesses. However, the track access unit remains government owned as the Australian Rail Track Corporation (ARTC).

The ARTC now manages access to the interstate standard gauge rail network throughout Australia.

In NSW, the State Rail Authority has been split into four separate corporations. These manage track access, track construction and maintenance, freight services and passenger trains. A number of private freight operators now have access to NSW tracks.

In Victoria, the Public Transport Corporation's metropolitan operations have been re-structured into four stand-alone train and tram businesses in readiness for privatisation.

V/Line Freight Corporation, which provides linehaul freight services throughout Victoria, is in the process of being privatised with a 15 year lease over the non-electrified network.

In Western Australia and Queensland, the rail systems remain vertically integrated, profitable, government owned business enterprises with responsibility for their entire operations. However, the Western Australian government intends to privatise Westrail.

New Operators

Private rail operators are playing an increasing role in Australia's rail freight and passenger task.

Competition reform and open access to government railway infrastructure has resulted in private companies offering freight and passenger services over government owned track.

Three private operators have entered the interstate freight market using government rollingstock and train crews over government owned track.

Specialized Container Transport and Toll Holdings offer services carrying general freight and containers between Melbourne and Perth. These two services are operating very successfully. They have lowered rail freight rates by over 40%, saving the WA economy over $100 million.

Shipping stevedore Patrick offers an export container service between Melbourne and Adelaide. This service provides valuable landbridging between those two cities. It enables shipping companies to take advantage of more frequent sailings to and from Melbourne, reducing their holding costs.

In a semi-private operation, NSW government owned FreightCorp has recently reached agreement with Rio Tinto to use that company's own wagons to run coal trains out of the Hunter Valley. GrainCorp in NSW has entered into an agreement with FreightCorp to operate grain trains on lightly used NSW branch

lines. Under the arrangement, GrainCorp will crew its own trains using FreightCorp locomotives and wagons.

Open access in NSW has also seen the entry of Austrac operating general freight trains out of the NSW Riverina area to Sydney and Melbourne. In northern NSW, Northern Rivers Railroad has entered into an agreement with FreightCorp to operate some of its freight services.

In Victoria, private operator Great Northern Rail Services undertakes shunting duties for the National Rail Corporation in Melbourne, while another private operator, Rail Technical Support Group, undertakes shunting and other maintenance services for Australian National's "Overland" passenger train.

Rail passenger services are also being privatised.

The former government owned long distance passenger trains "The Ghan", the "Indian Pacific" and "The Overland" were sold to a private operator in 1997. Privately run passenger trains also operate between Melbourne and Warrnambool and Melbourne and Shepparton and in NSW between Moss Vale and Wollongong.

In addition to these existing privately-operated passenger services, the Victorian Government intends privatising all urban and non-urban passenger services. Non-urban passenger services will be put out to individual tender, while the metropolitan rail network will be split into two systems and the tram network into four systems.

The objective of splitting the metropolitan train and tram system into four franchises is so the rail operators can be benchmarked against each other and the tram operators can be benchmarked against each other. It is hoped that competition by benchmarking will produce optimum service levels at least cost.

All these services indicate that there is no 'right' model for rail industry structure. Competition and open access to rail facilities can be provided within vertically integrated railways or through separate track access providers.

Community Service Obligations

Governments have an obligation to procure non-commercial rail services where these provide economic, social or environmental benefits to society. These contracts are no different to governments procuring any other goods or services.

However, procurement of these services must not disguise inefficiencies. These services must be managed commercially by rail authorities, but with transparent CSO payments from government.

Australian rail operators presently receive CSOs for the provision of urban and non-urban passenger rail services and for some rural rail freight services.

Australia's railways play an important role in providing passenger services, particularly in urban areas. Australia's urban and commuter railways generate significant social benefits by providing an efficient mass transport alternative to cars, helping to reduce road congestion and accidents, fossil fuel consumption and greenhouse gas emissions, particularly in urban areas.

Urban Rail

Australia's urban rail networks are vital to urban transport systems.

Urban rail services improve urban amenity by reducing the environmental impact of cars in urban areas. These services are the most efficient way of moving large numbers of people with minimal environmental impact.

Urban rail services will always require government financial support. This support is justified because of the enormous economic, social and environmental benefits these services provide. These benefits include less land use required for transport, reduced road congestion, lower road construction and maintenance

costs, fewer car parks, fewer road accidents, reduced pollution and greenhouse gas emissions from cars, less energy use and greater mobility for disadvantaged groups and people without cars.

These benefits flow through to the whole community, not just public transport users.

Urban transport systems around the world, including roads, are subsidised by governments except for some Asian transit systems. Hong Kong, for example, has a transit cost recovery of 136% due to the city's high population density and the ability of the system to capitalise on increased land values along its route.

CSO/subsidies to urban rail systems represent 65 cents per week per person in Australia. This is just one tenth of the cost of congestion, air pollution and noise attributable to motor vehicles.

Urban rail services are 2.5 times more energy efficient than motor cars and twice as energy efficient as buses. The contribution of urban rail transport to Australia's total greenhouse gas emissions is negligible, including power generated for electric services and diesel powered services. By contrast, urban motorists cause 5% of Australia's total greenhouse gas emissions.

Australia's urban rail services kept 365 million car journeys off urban roads in 1996/97 saving 2 million tonnes of greenhouse gas emissions.

There will always be an obligation on Governments to provide CSO payments to urban rail passenger operators because of the huge social and environmental benefits they provide.

However, there may be particular groups for whom urban public transport is provided as a form of welfare. CSO payments for these groups must be clearly identified in rail operators' accounts and charged against the relevant Government department.

Non-urban Passenger Services

Non-urban rail passenger services have an important role linking major regional centres with capital cities (eg Warrnambool-Melbourne, Canberra-Sydney) and are an integral part of Australia's tourism and hospitality industry.

Commuter rail services must receive continue to receive Government CSO payments so that fares can be set at a level that entices commuters out of their cars. These services reduce pressure for bigger roads and more car parks by providing fast comfortable, car competitive transport alleviating road accidents, air pollution and urban road congestion.

For example, one V/Line passenger train carrying 400 people between Geelong and Melbourne keeps 320 cars off the parallel freeway, saves 2,800 litres of fuel and 6.5 tonnes of greenhouse gas emissions and reduces congestion and car parking problems in Melbourne.

Non-urban tourist rail passenger services, some of which are private commercial operations, are part of the overall tourism experience to varied parts of Australia for thousands of people each year. These trains are able to carry hundreds of people to a range of destinations and provide a vital link in the viability of many tourism ventures.

Provision of CSOs to long-distance rail services is justified in many instances for regional economic benefits or to target particular groups. However, these payments must be clearly identified.

Rail Freight Services

For environmental, road safety or economic reasons, some rail freight services receive CSO payments. These CSO payments are warranted where there is a justified community benefit. However, government procurement of these services must not prevent a rail freight operator from operating these or other services commercially.

Access Regimes and Regulation

Access Regimes

Open access regimes to facilitate access to rail lines are now in place in all States and the Commonwealth. Rail reform has now seen the Australian Rail Track Corporation (ARTC) given sole responsibility for negotiating track access, pricing and conditions for access to the interstate rail mainline network.

As well as managing track access, the ARTC will coordinate mainline rail investment decisions and encourage greater private sector involvement in the rail industry.

The ARTC owns the interstate mainlines in South Australia, having inherited them from its predecessor Australian National's Track Access Unit. ARTC is leasing the interstate standard gauge track in Victoria from the Victorian Government.

It was intended that ARTC also lease the interstate standard gauge line in WA from Westrail. However, that track is now to be included in the sale of Westrail.

ARTC will negotiate access to interstate track in WA through WA's third party access regime. In NSW and Queensland, ARTC will negotiate interstate track access with the Rail Access Corporation and Queensland Rail's Network Access Unit respectively.

The ARTC is a significant step forward for the Australian rail industry. Prior to its creation, interstate rail operators had to obtain track access agreements from the various state track regimes before they could operate trains. This posed an additional administrative barrier to entry onto the rail network

Regulation

Establishing a national system of track access also provides the opportunity to standardise the plethora of state based regulations presently governing interstate rail operations. There are presently 22 train control systems operating on the interstate mainline network and 8 radio communication systems. Each state requires rail operator compliance with different safety and accreditation standards.

Historically states developed their own operational standards because they owned and managed all track within their borders (except for Tasmania and South Australia where their rail operations - other than in metropolitan Adelaide - were ceded to the Commonwealth in 1975). These different standards have adversely affected interstate rail operations. These regulations govern a range of rail activities ranging from complying with different safety regimes and accreditation requirements to different radio and signalling systems. The time required by rail operators to comply with these requirements must be minimised through harmonisation of regulations between states.

The ARA considers that harmonisation of regulations affecting interstate rail operations is equally as important as single management of track access to interstate rail corridors. Harmonisation must extend to items that ensure that rollingstock, communication systems and other systems and procedures can be used as widely as possible throughout Australia and that loading gauges vary as little as possible between states. As far as possible, there must be uniform rail operating standards throughout Australia.

The harmonisation of technical standards is consistent with the conditions of the Inter-governmental Agreement on Rail Safety and AS 4292. The Inter-governmental Agreement on Rail Safety came into effect on 1 July 1996 following agreement by the Commonwealth, State and Territory Ministers for Transport**.** The Agreement provides for a national approach to the regulation of rail safety by a system of safety accreditation of owners and operators. The Agreement was primarily reached because of the increasing use of publicly owned rail track by private operators under the Hilmer competition reforms and the need to accredit those operators as safe rail operators in accordance with relevant rail safety standards.

A key element of the Inter-governmental Agreement on Rail Safety is the mutual recognition between accreditation authorities of accreditation based on Australian Rail Safety Standard AS4292. However, the rail safety regulators are not applying consistent conditions for accreditation as determined by the IGA.

State-based regulatory regimes remain a barrier to entry into rail operations. Despite their excellent safety record, rail operators are subject to a vastly more complex and costly regulatory regime than road operators. Notwithstanding a common Rail Safety Standard AS4292 and an Inter-governmental Agreement (IGA) that embraces the principle of mutual recognition, twenty or more sets of state based operating rules and regulations still exist.

The IGA on Rail Safety was intended to provide an easier path through the mutual recognition process but in practice, safety accreditation is proving to be a difficult and costly process. In particular, interstate operators face substantial costs in complying with different state requirements including accreditation fees that must be paid to each state jurisdiction irrespective of mutual recognition.

The "one stop shop" approach for rail safety will have significant benefits for the operator in streamlining their accreditation process and is supported by the ARA.

Developing and implementing uniform standards is critical in eliminating inconsistencies for rail operators and in enabling a more "seamless" rail transportation system.

Competitive Neutrality

The ARA considers that the concept of competitive neutrality is the single most important factor affecting the future development of the rail industry in Australia.

The National Competition Policy Report by the Independent Committee of Inquiry in August 1993 makes the following statement :

> "Differences in regulatory and other requirements imposed on firms competing in the one market may distort competition and hence undermine market efficiency."

The Hilmer Report on National Competition Policy (1993) stated

> "Government businesses should not enjoy any net competitive advantage by virtue of their ownership when competing with other businesses."

Firms should compete on the basis of their relative intrinsic efficiencies, without any net competitive advantage arising through ownership. Government enterprises should be subject to the same regulatory and financial regimes as their private sector competitors. Similarly, private sector firms competing with government enterprises should not have regulatory or financial advantages over their public sector competitors.

This was recognised by Federal, State and Territory governments in 1993 when agreeing to develop a national competition policy.

One of the principles agreed to was:

> "As far as possible, universal and uniformly applied rules of market conduct should apply to all market participants regardless of the form of business ownership."

The National Competition Council reinforced the principle of universal and uniform rules applying to the market by stating that introducing a competitively neutral operating environment for government businesses can deliver a range of benefits, including "more efficient pricing leading to resources being allocated to their best uses" [1]

However, the present transport operating environment is far from balanced with major anomalies in infrastructure funding, regulations, taxation and access pricing between road and rail.

The following table indicates some of the regulatory differences applying to rail and road.

Road/Rail Score Card

PARAMETER	ROAD	RAIL
One stop shop for access	✔	✘
Consistent access price	✔	✘
National standards	✔	✘
National accreditation	✔	✘

- One stop shop for access: a truck registered in one state can operate freely in any other state, whereas an interstate rail operator requires safety accreditation plus track access agreements from each state to operate
- Consistent access fees: interstate trucks pay a flat national charge and do not require access contracts; rail operators must negotiate access contracts and pay access fees that vary between states
- National standards: national operating standards apply to interstate trucks regarding road regulations, speeds, load limits etc, whereas rail operating standards vary within and between states
- National accreditation: once accredited in one state, a licensed truck operator can operate in all other states; interstate rail operators must obtain accreditation for safety, competency, etc from each state, all of which add costs and delays to start up.

There are a number of areas where regulations are more onerous for rail than for road operators. The cost implications of these regulations needs to be assessed to evaluate their impact on rail and road economics.

Such regulations include :

- Non uniformity of state safety regulations, which imposes extra costs in complying with different state requirements and constitutes a barrier to competition
- Investigation of rail accidents is more onerous for rail than for road accidents and the cost is borne entirely by the rail operator. Road accident investigations are not paid for by road transport operators.
- Regulatory creep - road transport operators are able to take risks such as exceeding mass and dimension limits and driving hours with a relatively low risk of penalty. Rail operators have to ensure regulations are adhered to through operational controls
- Dangerous goods regulations are stricter for rail than for road. For example, a rail tanker carrying flammable material is called a “pressure” vessel and must be constructed of metal that is least 10-15mm thick. A road tanker carrying the same material is called a “non-pressure” vessel and requires the metal of the tanker to be only in the order of 5mm thick. Given rail’s superior safety record to that of road, the requirements for road should be at the same standard.

The following is a comparison of access requirements for rail and road networks:

RAIL	ROAD
• variable, state based access fees	• fixed national registration and licence fees
• fuel tax (variable)	• fuel tax (variable)

• mass distance charge	• no mass distance charge
• safety accreditation by Inter-Governmental Agreement	• uniform safety regulations
• 22 sets of state based operating rules and regulations	• near uniform operating rules - traffic signals, speeds, rest breaks etc
• various speeds and axle loads	• generally uniform loads limits
• 8 radio communication systems	

The anomalies within the rail mode and inconsistencies between the rail and road modes has led to inefficiencies in the transport economy and increased cosats for consumers.

Rail's payment of a road user charge through diesel excise is completely indefensible and has persisted through a total lack of political will to fix the problem.

The marked difference in the cost of access to the transport network puts rail at a severe cost disadvantage and affects the viability of a number of services and corridors.

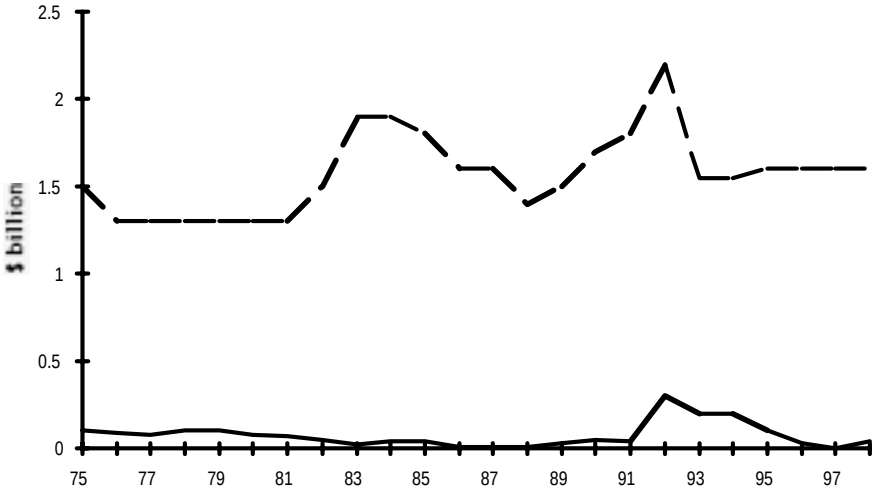
Funding

Progress in rail reform has been severely hampered by inadequate infrastructure investment.

Between 1975 and 1998, the Federal Government has spent $34.5 billion on roads. About half this has gone into the National Highway System and Roads of National Importance.

Over the same time, the Federal Government has spent only $1.8 billion on mainline rail infrastructure.

Federal Rail and Road Funding



Due to poor funding, Australia's rail industry is struggling to rise to the challenge of delivering 21st century service on 19th century infrastructure.

The rail industry recognises the economic importance of the national highway system. However, governments must develop integrated land transport strategies and apply consistent investment criteria to rail and road projects. Rail and road projects must both be assessed on economic, financial, social and environmental grounds rather than the narrow commercial approach that is presently applied to rail.

The rail industry is not seeking preferential treatment: it seeks the same approach as given to roads.

In 1995, the National Transport Planning Taskforce identified over $3 billion worth of expenditure required on Australia's interstate rail network by 2015.

The findings of this report were echoed in 'Tracking Australia', the report of the Federal parliamentary rail inquiry. 'Tracking Australia' recommended:

> **In addition to the $250 million committed to the Australian Track Corporation, a further $750 million be allocated over three years for investment in the national track. An additional $2 billion should be invested over ten years from 2001 in rail infrastructure of national strategic importance.**

An example of the benefits of improved rail infrastructure is the Brisbane-Cairns line.

This line has been upgraded by Queensland Rail at a cost of $590 million. The upgrading work involved extensive curve easing, installation of heavier rail and concrete sleepers, replacement of timber bridges and improved signalling and communications systems. The upgrade increased locomotive and wagon productivity by 30-40% and decreased maintenance costs by 20-30%.

To address the need for investment in Australia's interstate mainline rail network, an integrated land transport policy needs to be developed by the Federal Government. The role of each mode and its contribution to Australia's transport needs must be properly assessed and appropriate levels of funding allocated to each mode to ensure that the nation's transport system operates as efficiently and economically as possible. The National Transport Planning Taskforce identified the need for long-term strategic assessments of Australia's transport infrastructure to ensure funds are targeted where they will produce the greatest benefits.

'Tracking Australia' recommended that a more integrated approach to transport infrastructure investment be developed. 'Tracking Australia' recommended:

> **The Commonwealth establish a National Land Transport Commission to provide:**
>
> - **advice to the Government on a national transport plan; and**
> - **recommendations to the Government on the allocation of funds for rail and road projects on the strict basis of highest benefit cost ratios, which address all relevant externalities, such as accidents, congestion, pollution, greenhouse gas emissions and noise.**
>
> **Further, the Commonwealth give higher priority to land transport infrastructure investment within total budget outlays than is presently the case.**

Comprehensive evaluation criteria would see some rail projects considered as road projects because of their benefits to the road network in terms of reducing congestion, pollution, road accidents etc by getting traffic (passenger or freight) off roads onto rail. In other words, the positive social benefits that are attributed to road projects are equally attributable to rail projects.

Diesel fuel excise

Rail operators' payment of diesel fuel excise is inequitable and discriminatory. This tax costs rail operators approximately $170 million per year, increasing their costs by an average of 10%.

In 1982, the *Diesel Fuel Taxes Amendment Act* abolished the diesel fuel excise exemption scheme and introduced the present rebate scheme for "off-road" users of diesel fuel. However, the definition of "off-road" user was narrowed to exclude activities such as railways, coastal shipping and manufacturers. As a result, Australia's rail operators since that time have paid the same level of diesel fuel excise as road users even though rail operators are "off-road" users of diesel fuel.

Rail operators may only obtain the diesel fuel rebate where there is beneficiation associated with a haulage task, that is value-adding or processing before export. The iron ore railways in north-west WA and some government railways hauling mineral and primary produce are examples of this practice.

Other "off road" users of diesel fuel (farmers and the mining industry) obtain annual fuel excise rebates totalling $1,400 million per annum. Even Japanese long line fishing boats in Australian waters manage to exploit a loophole to obtain over $90 million per annum in fuel tax rebates.

Rail operators are frustrated that part of their fuel excise is nominated as an 18 cent per litre road user charge.

This iniquitous tax costs Australia's government railways approximately $90 million per year. The proposed $250 million Federal Government mainline rail investment program over four years from 1998-99 will be far outweighed by the approximately $340 million in road user charges that government railways will pay over the same time.

Paying diesel fuel excise, particularly the road user component, is not economically efficient.

In 1991 the Industry Commission report *"Rail Transport"* recommended that railways should not be required to pay fuel excise on diesel used for freight purposes on the basis that the price of export commodities would be adversely affected.

This finding was further supported by a 1994 Industry Commission report *"Petroleum Products"* which said that the 18c/litre road user charge should not be levied on rail and that road user charges **applied to rail would distort transport decisions**. The report recommended that the diesel fuel rebate scheme apply to rail freight, noting that none of the diesel fuel excise paid by rail is returned to rail, but that some of it is used for roads.

The Industry Commission in its 1994 report *Petroleum Products* estimated that extension of the diesel fuel excise rebate to all rail operators would result in a net increase in Australia's GDP of $120 million per year and Australia's balance of trade would improve by $40 million per year. Export volume would increase by 0.19 % per year.

The net annual increase to GDP of $120 million includes economic benefits across a range of sectors as well as that arising from modal shift to rail. Coal producers could benefit by $20 million per year and producers of wheat and other grains could benefit by $40 million per year. Operators of diesel powered rail passenger services would save nearly $25 million per year.

Costs of access to the transport network

In the financial year 1996/97, the National Rail Corporation carried 16.9 billion tonne kilometres of freight and paid $117 million in track access fees to various state authorities to do so. Had the same amount of freight been carried by road, 3100 B-double trucks would have been required with a road access fee of $17 million in registration charges. The cost of road access is 15% of the rail access fee. These fees do not include fuel costs and its associated road user charge.

In 1995, the National Transport Planning Taskforce estimated taxes and charges as comprising 16.6% of road freight operating costs. At the time, no charges applied to rail operators, but taxes were estimated to comprise 16.5% of rail operating costs of which 12% was diesel fuel excise. Track access charges applying to rail operators have now increased rail's taxes and charges by 25%-30% to over 40% of operating costs, two and one half to three times that of road.

This disparity is caused by inadequate road cost recovery from heavily loaded, long distance articulated trucks, rail's principle competitor for long distance freight haulage.

The Swedish Government, which pioneered the separation of infrastructure and operations in 1988, has now abolished track access fees for rail operators. These fees cost rail operators nearly $100 million per year. The Government has recognised that these fees placed rail at a disadvantage with road and has now levelled the road/rail playing field.

Abolition of the fees will result in increased rail competitiveness, enabling rail to compete for passenger and freight traffic on an equal footing with road operators.

Road user cost recovery

There is substantial evidence that long distance road freight operators are not paying their full costs of road use.

The argument that road users pay their way has been analysed by the Bureau of Transport and Communications Economics in the paper titled "Review of Road Cost Recovery" - Occasional Paper 90, 1988 and found to ignore two important issues :

- the appropriate allocation of revenues and costs among vehicle types; and
- the level of cost recovery by vehicle type

Allocation of road costs is vital to developing appropriate road user charges. Cars are responsible for 81% of vehicle kilometres and only 0.1% of pavement loading (ie road damage), whereas articulated trucks are responsible for 12% of vehicle kilometres and 67.3% of pavement loading. A rigorous road user cost recovery scheme is necessary to ensure that each class of road user contributes to its share of road construction and maintenance.

The 1988 BTCE paper allocated avoidable road costs among road user groups. The report found that articulated trucks failed to recover their avoidable pavement cost by $750 million per year. This cost under recovery translated to $18,000 per year for the average six axle truck and nearly $50,000 per year for the heaviest vehicles. The report noted that the shortfall from this vehicle group was still large even if such things as sales taxes, customs duties and stamp duties were included. Although that work is now nine years old, its findings are still valid, particularly the principle of allocating road costs to different classes of users.

The more recent 1997 BTCE paper 'Taxes and Charges' in Australian Transport – A Transmodal Overview' commented that present road user charges mean that there will be under-recovery of pavement damage costs for vehicles which are over the average weight at the expense of those below the average.

As well as damage to road infrastructure, society must also bear the "external" costs of road use including crashes, crash trauma, pollution and congestion.

Articulated trucks under recover their road use costs because truck road access fees, unlike rail access fees, are not mass-distance based. This deficiency in articulated truck cost recovery causes more freight to be travelling by road than would be the case if competitive neutrality applied to road access pricing

Present Road User Charges

Road user charges were developed by the National Road Transport Commission (NRTC) in 1992 and were based on the average vehicle in each class in 1991. Road access charges developed by the NRTC combined an "access charge" and a "mass-distance" charge into a single fixed annual registration fee and an 18c/litre road user charge. All road users of diesel fuel pay this charge, but the NRTC acknowledged at the time that a mass-distance charge may be more appropriate for heavy vehicles. In any case, the 18c/litre component of diesel fuel excise cannot presently be considered a "road user charge" since rail pays it too.

Combining an "access charge" and a "mass distance" charge into a fixed annual charge that does not vary with mass or distance assumes that all vehicles can be attributed the same amount of road costs. This is not the case. **Road pavement damage is not linear, but varies with the fourth power of the axle load** - a 10% increase in axle load will increase pavement wear by 1.1 to the fourth power.

Allocating costs using average vehicle mass is inappropriate because virtually no vehicles travel at the class average mass. **The use of average mass and distance for six axle articulated trucks leads to major distortions in truck road access pricing.** It underestimates the cost of road damage attributable to articulated vehicles travelling at over the class mass average. Road user charges based on class mass

averages discriminate against lighter, short distance vehicles both between vehicle classes and within a class of vehicles. Lighter vehicles travelling short distances subsidise heavier vehicles travelling longer distances: those vehicles in direct competition with rail.

The case for mass distance charging

Mass-distance charging for heavy articulated vehicles provides a more accurate measure of the true contribution that these vehicles should make to their total road costs. This view was supported by the Industry Commission as far back as its 1991-92 Annual Report. The Commission stated:

> "Annual fixed charges are not efficient because costs vary with the distance travelled and mass of the vehicle. The result is that some vehicles - the heaviest travelling long annual distances - will meet less than 20 per cent of their attributed costs. Charges for heavy vehicles that reflect costs they impose are essential to ensure best use is made of the nation's road and rail infrastructure, and that industry location decisions are appropriate in terms of minimising the overall cost of economic activity. Differences between recommended charges and road-related costs are greatest for vehicles competing with rail. The (NRTC) charges, as recommended, will therefore potentially distort the long-haul freight market as rail reform takes effect... "(p197-98)

The NRTC also acknowledges that road user charges based on vehicle averages are not the most efficient charging mechanism. In its document, "Heavy Vehicle Charges : The Second Generation" - February 1995, the NRTC commented (emphasis added) :

> "All the road use data used in the charging process are averages for a vehicle class. These averages conceal differences in the use made of the road system by individual vehicles. **This is one argument for a mass-distance charge that reflects differences in the operating mass and the distances travelled by individual vehicles.**
>
> The differences between costs and charges may be accentuated if trucks that operate at masses higher than average also travel distances higher than average. Any such vehicles are also likely to be newer, with better than average fuel efficiency, so that their contribution to costs via the Road Use Charge (diesel excise) will also be lower."

The most efficient way to rectify cost under recovery from articulated trucks is to impose a mass-distance charge on these vehicles to supplement the fuel excise and registration charges. The ARA submission noted that this would "differentiate more accurately between vehicles causing most of the road damage and will achieve full and consistent road cost recovery from long distance articulated vehicles without penalising other road users."

Other road users presently subsidise heavy long distance articulated vehicles. Such vehicles should be subject to a mass distance charge to reflect their road use costs.

This conclusion was also reached by the Federal Government's recent report into rail 'Tracking Australia'.

Recommendation 12 of 'Tracking Australia' is:

> **The committee recommends that the Commonwealth develops a more consistent, equitable approach to transport infrastructure charges to ensure competitive neutrality between modes.**

Application of mass distance road user charges

A mass-distance road user charge for articulated trucks has applied in New Zealand since 1978. The charge is based on cost attributable to the various categories of vehicles and are calculated using the fourth power rule. Articulated vehicles require licences based on how far they will travel and what their maximum load will be. The licence fee depends on the axle configuration spreading the load. The result is that in

New Zealand, the heavier articulated trucks are charged around 3-4 times what they are charged in Australia.

The New Zealand Ministry of Transport is currently examining future land transport pricing strategies. The strategies are examining a wide range of matters including road pricing, road maintenance, road funding, environmental impacts of road use, road congestion, private sector involvement in provision of roads and road safety. Part of the reason for examining land transport pricing options was that road user charges were last reviewed in 1984 and might now be inefficient.

Five options were developed for future land transport pricing strategies. The options were subject to public consultation.

The commercial options being considered, with support of the NZ business community, include:

- a time/weight/distance/location road user charging regime
- road pricing to provide a return on equity on new works
- policies to internalise (paid by the user) or influence externalities, including congestion. The options note that these policies would only be required if externalities persisted despite efficient road pricing
- a neutral road management regime, encompassing accountability and performance aspects and the pursuit of safety and environmental goals
- more involvement by the private sector in the provision, management and funding of road services
- an appropriate regulatory regime to enable competition and prevent monopolist behaviour
- transferring local authorities' and Crown road assets to commercial enterprises owned by the state and local authorities

The proposed New Zealand approach to commercialising roads is strongly supported by the ARA. A road user charging regime based on time/weight/distance/location and including congestion pricing is the most effective way to ensure competitive neutrality applies to road and rail access pricing.

For rail to fulfil its potential in the national transport network as an efficient mover of long haul freight, a more efficient system of road user charges for articulated trucks needs to be implemented without further delay, particularly with the continual increases in truck size and weight.

New Zealand has shown that sustained reform in the transport sector resulting in a more commercial approach through mass distance charging for road freight operators, has removed major distortions from the transport economy and allowed rail to increase it's market share.

Taxation Reform

Fuel Excise

The Federal Government's proposed tax reform package further tilts the playing field in favour of road.

The proposed GST and reduction of fuel excise to 18 cents per litre will benefit users of road and competing rail freight services. There will be a reduction in costs for both modes.

However, the proposed GST will also increase the price of rail and road outputs. Rail, for example, loses its sales tax exempt status.

The net effect of replacing present taxes and charges with a GST is an increase in rail's costs of 6.1% relative to road. This is a significant impediment to the progress of Australian rail reform.

The greater gain to road transport from the Coalition's tax package results from the larger proportionate reduction in fuel excise for road compared with rail:

- fuel excise for heavy trucks will drop from 43 cents per litre to 18 cents per litre, a reduction of 58%
- fuel excise for rail will drop from 35 cents per litre to 18 cents, a reduction of 49%

The nine-percentage point differential in favour of road compared with rail will have a significant competitive impact. A substantial amount of freight now on rail in all interstate corridors intrastate will transfer to road. The proposed increase in heavy vehicle mass limits will aggravate this transfer.

For the farm sector, the National Farmers' Federation estimates that retention of an 18 cent per litre fuel tax on rail will increase the cost of grain transport by approximately 80 cents per tonne. Nationally, this will add $24 million to grain growers' costs.

Retention of an 18 cent per litre fuel excise for rail and road as part of the Coalition's tax package is completely unjustified. The 18 cents has been determined by the National Road Transport Commission to be a road user charge. Applying it to rail is inequitable and discriminatory. The Coalition's tax package must exempt rail from the 18 cents per litre fuel excise as it does for other off-road users of diesel fuel.

If the18 cents per litre is not a road user charge, then it is a fuel tax. If it is a tax, then a road user charge must be introduced to cover the costs of road use in the same way that rail pays an access charge for use of the rail network.

Rail Tourist Services

The Coalition tax package will adversely affect operators of rail tourist services.

The tax reform package proposes that overseas tourists who pre-purchase travel within Australia will be exempt from the GST if their domestic travel is by air. There will be no GST exemption for rail or bus fares.

This anomaly will severely affect rail's competitiveness in the domestic tourism market. For example, a one way first class ticket between Sydney and Perth on the*Indian Pacific,* one of the world's great train journeys, would increase by a massive $126.

The total amount of GST collected on long-distance rail fares for inbound tourists would be approximately $2.5 million, based on 1996/97 patronage.

Imposition of the GST on fares for long-distance rail travel by 'inbound tourists' when air travel in the same circumstances would be exmpt from the GST would inevitably damage rail business serving the tourism market in competition with airlines.

Employee Housing

The Coalition's tax package will continue to impose Fringe Benefits Tax on housing for rail employees in mining areas.

Where housing is provided to employees of mining companies in remote areas, the Tax Reform package proposes that the benefit to employees be FBT exempt.

This exemption will apply to the rail operations staff of railways which are owned and operated by mining companies, but not to rail operations staff of stand-alone railways performing the same task.

This anomaly should be removed from the Coalition's tax package by extending the FBT on employer-provided housing to employees of railways where they are principally engaged in the carriage of outputs from the mining industry.

FBT on Rail Passenger Fares

The Coalition tax package does not address the anomaly of different rates of Fringe Benefits Tax applying to employer provided cars and public transport fares.

The Fringe Benefits Tax applying to motor cars as part of salary packages is approximately 10% of the vehicle's purchase price. The FBT applying to a public transport ticket is approximately 95% of the ticket price. This policy creates a significant disincentive for companies to include public transport fares in salary packages and encourages greater use of motor vehicles.

Policies favouring motor cars over public transport contribute to the significant social and environmental costs of motor cars. Up to 40% of peak hour traffic is company cars.

Lowering the FBT applying to public transport fares to that applying to cars will provide an incentive for companies to include public transport fares as part of salary packages. This is consistent with the Federal Government's greenhouse reduction strategies. One of these strategies is to: *develop salary packaging arrangements which are neutral with respect to employee choice of transport.*

The Business Council of Australia views current FBT arrangements as inequitable in a range of areas. The Council says, "the current design of the FBT has no basis in economics and owes everything to political pragmatism". (BCA paper on Tax Reform Options, September 1997).

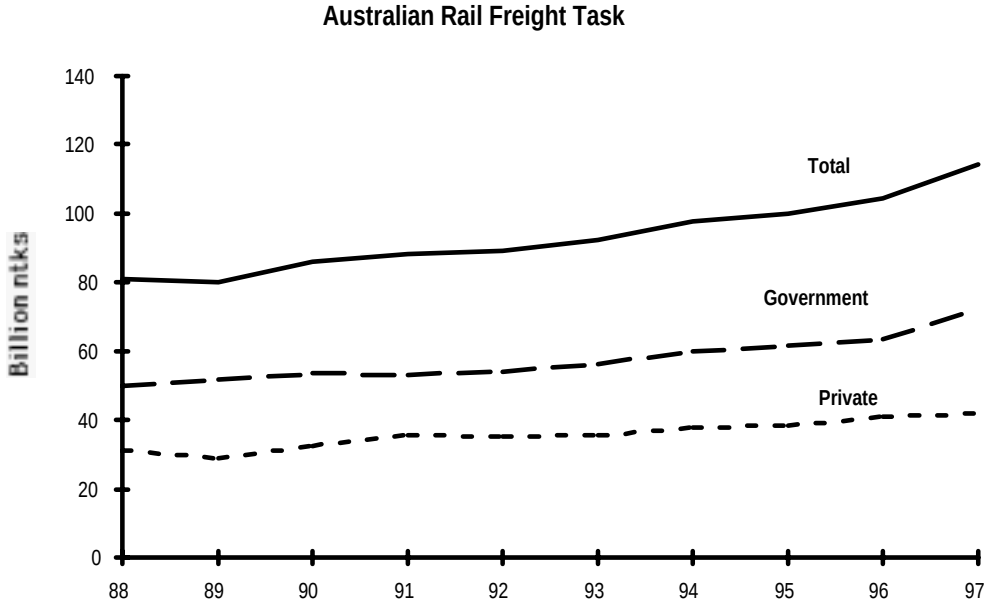
The Coalition tax package must ensure that the FBT rate appplying to employer provided cars and public transport fares is the same.

Performance of the Australian Rail Industry

The performance of the Australian rail industry has been continually improving over the past decade.

The total rail freight task increased 36% from 81 billion net tonne kilometres (ntks) in 1987/88 to 110 billion net tonne kilometres in 1996/97.

Government rail ntks increased 37% from 50 billion in 1987/88 to 68 billion in 1996/97. Private rail freight ntks over the same period increased 35% from 31 billion to 42 billion.



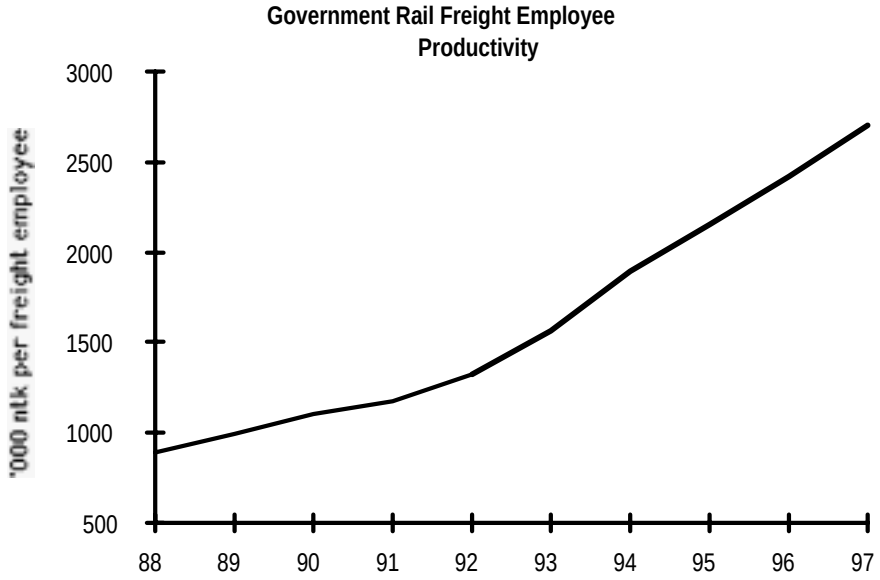
Government rail freight operations are now profitable or close to it. There is no net cost to taxpayers from Australian rail freight operations.

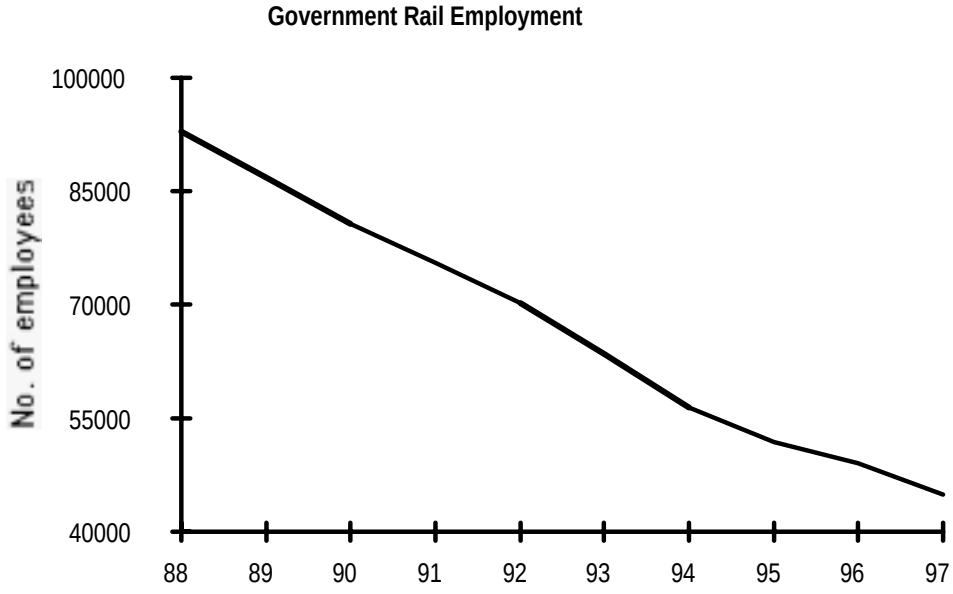
The National Rail Corporation has turned around a business losing $300 million on interstate freight operations to near break-even in just five years. This clearly indicates the extent to which Australia's rail operators have implemented productivity and efficiency reforms.

Remaining rail deficits are almost entirely attributable to urban and regional passenger services for which there are significant social and environmental reasons for their government funding.

Total rail operating deficits are now approximately $700 million per year excluding track access payments and costs of capital.

The productivity of government rail freight employees has increased 200% over the past decade from 900,000 ntks per employee in 1987/88 to 2,700,000 ntks per employee in 1996/97. Over that time, government rail employment has halved and costs per net tonne kilometre have declined 25%.

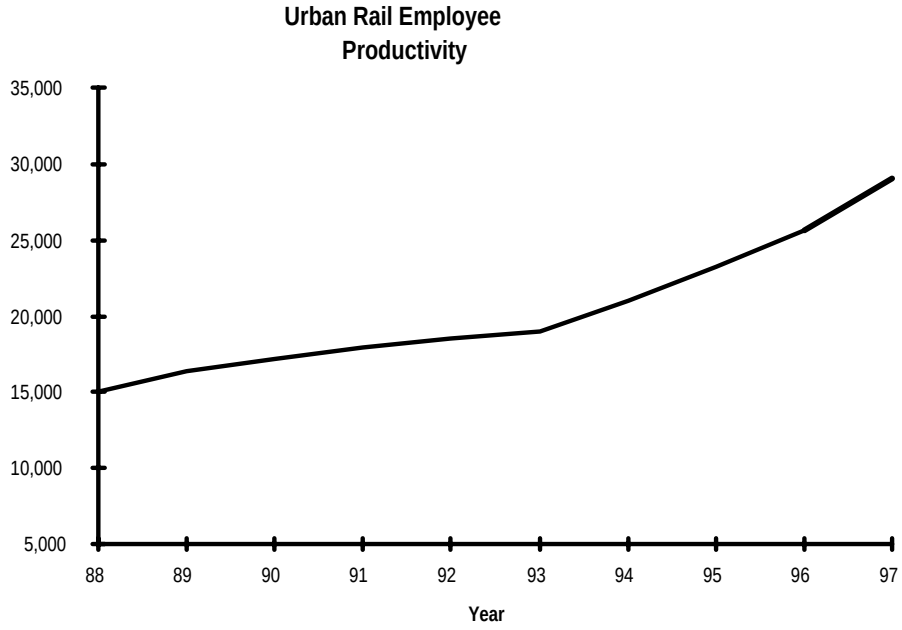




Comparison with overseas railways is difficult because of a range of different factors. However, Australia's freight railways are generally comparable to mid-size, Class 2 US railways. Comparison with these railways shows that Australia's railways rate at similar levels for employee productivity and equipment utilisation.

Australia's urban rail systems have demonstrated their commitment to reform through significantly improved employee productivity and operating practices.

Urban rail employee numbers have declined 40% in the last ten years from 26,000 to 16,000. In that time, urban rail employee productivity has increased 90% from 15,000 journeys per employee in 1987/88 to 29,000 journeys per employee in 1996/97.



Cost recovery on Australian urban rail systems averages 40%. This is similar to the New York Subway and the Paris Metro, but lower than Chicago (48%) and Toronto (61%).

These improvements have enabled governments to reduce their level of support for urban rail operations by 35-40% compared with 10 years ago to around $600 million per year. However, the cost of Trans Adelaide's urban rail services and some NSW CityRail services is increased by diesel fuel excise. These operators are "off-road" users of diesel fuel, but are unable to claim the diesel fuel excise rebate. In TransAdelaide's case, this increases operating costs by 3.5%.

Conclusion

Rail transport plays a major role in moving the nation's freight by moving over half of the combined rail and road non-urban freight task. Rail transport is also an integral part of Australia's major cities by providing an efficient mass transit alternative to cars. In doing so, rail transport contributes significantly to reducing the impact of road transport on the community in terms of road damage, accident costs, pollution, greenhouse gas emissions, noise and congestion.

However, much more could be achieved by Australia's railways if State and Federal Governments implemented competitive neutrality policies to correct the present regulatory and financial imbalance between rail and road transport.

Rail freight transport is subject to a vastly more complex regulatory regime than road freight operators. Access to the interstate rail network typically requires negotiating up to five access agreements and there are different rail operating and safety standards applying in each state.

Rail is also at a disadvantage financially with road. Rail operators pay diesel fuel excise, including a road user component, even though they are "off road" users. This is a discriminatory tax against rail. Government funding for mainline rail infrastructure has been significantly less than for comparable interstate highway improvements. Road cost recovery from heavy articulated trucks - rail's principal competitor - is severely deficient.

Millions are being spent on urban road networks while urban rail systems are being subject to rigorous cost cutting policies and lack of investment.

All these factors combine to tilt the transport playing field strongly in favour of road.

The Australasian Railway Association recommends that State and Federal Governments implement the following major measures to redress these imbalances:

- Federal and State Governments develop integrated land transport planning policies
- Federal and State transport Ministers establish a National Rail Highway and fund as Tracks of National Importance
- Federal and State Governments evaluate rail and road projects on the same criteria taking into account financial, economic, social and environmental considerations including greenhouse emissions
- Rail operators be eligible for the diesel fuel excise rebate
- A mass-distance charge be applied to articulated trucks to ensure that road user charges match road costs
- The GST tax package must exempt rail from the proposed 18 cent per litre diesel fuel tax
- Federal and State Governments establish “Transport Funds” from which funds for rail or road projects are allocated
- The Federal Government develop a comprehensive mainline rail investment program
- Federal and state transport ministers must cooperate to achieve the harmonisation of rail regulations, safeworking, operations and communications standards between states.