AUSTRALIAN AUTOMOBILE ASSOCIATION

Productivity Commission's Inquiry into Public Infrastructure

Submission by the Australian Automobile Association

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FIA ACTION FOR ROAD SAFETY

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Introduction

The Australian Automobile Association (AAA) is the peak organisation representing Australia's motoring clubs. The AAA's constituent clubs are the NRMA Motoring and Services, RACV, RACQ, RAC (WA), RAA (SA), RACT, AANT and the RACA. Combined, these clubs represent more than seven million Australian members, and advocate on behalf of all road users.

The AAA appreciates the opportunity to provide input into the Productivity Commission's (PC) review of Public Infrastructure. In the lead up to the 2013 federal election, the AAA ran an advocacy campaign emphasising the need for stronger investment in transport infrastructure and more innovative funding arrangements. The commitments made to important infrastructure projects in recent months are encouraging, however, it is clear that more needs to be done to provide the infrastructure required for a rapidly growing population.

In order to bridge the nation's infrastructure gap it is essential that we consider all available funding options to deliver the infrastructure which will drive growth, improve productivity and generate additional economic benefits for future generations. The motoring clubs thus support the Federal Government's decision to task the Commission with undertaking this review.

As the national representative for the Australian motoring clubs, our contribution to this consultation process will focus on land transport infrastructure.

The Case for Stronger Investment in Land Transport Infrastructure

It is widely accepted that Australia has not invested adequately in its infrastructure. According to Infrastructure Australia, the nation faces an infrastructure deficit of around $300 billion.[1] While this figure applies to various types of infrastructure, it is clear that existing roads and other land transport infrastructure are inadequate or unable to meet capacity.

In recent years, Australia has experienced rapid population growth which has resulted in growing demand for access to our road and land transport infrastructure. There is a significant gap between our growing demand for new roads and public transport and the capacity of the existing funding approaches to deliver this infrastructure.

Strong action is needed to address the land transport infrastructure deficit in order to reduce the effects of urban congestion and deliver improved road safety outcomes.

Reducing the social and economic costs of congestion

As one the world's most urbanised countries, the gap in transport infrastructure is acutely felt in our cities. Congestion is a significant and growing problem, which affects private and commercial vehicles as well as public transportation, particularly in the larger cities. According to the Bureau of Transport and Regional Economics (BITRE), congestion is estimated to cost Australians $20.4 billion per year by 2020.[2]

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[1] Infrastructure Australia, *National Infrastructure Plan*, 2013

[2] Bureau of Transport and Regional Economics, *Estimating urban traffic and congestion cost trends for Australian cities*, 2007

In research conducted by the AAA for its *Motoring Report 2013*[3], it was found that 82 per cent of motorists are concerned with road congestion generally. The high level of concern has been backed up by research completed by our constituent clubs. A recent survey by the RAC (WA) found that on average, Perth drivers spend over three hours a week in traffic. The survey of almost 700 RAC members shows that congestion results in less time spent with family (46 per cent); less time to do something you enjoy (59 per cent); having to get up earlier (44 per cent); and getting home later from work (36 per cent).[4]

Road congestion is also a real concern for businesses. The annual *NRMA BusinessWise Congestion Survey* of nearly 1,000 businesses reveals that over the 12 months to May 2013, traffic congestion had contributed to an increase in fuel costs (59%); an increase in capital and running costs (39%); a slowdown in overall productivity (33%); and an increase in staff late to work (32%).[5] It is clear that congestion is a handbrake on productivity as it interrupts and delays supply chains by affecting the timeliness of goods being brought to the market.

Although there are various policy options which can address the problem of congestion, better transport infrastructure is clearly an important part of the solution. In order to improve productivity and drive economic growth, it is essential that investment occurs into the type of projects which are likely to encourage efficient traffic flows in our cities.

Improving road safety outcomes

Australia also needs to factor road safety considerations into its transport infrastructure investment decisions. The national road toll remains at unacceptably high levels, with sub-standard roads being a significant contributing factor.

In 2012, 1,300 people were killed and more than 30,000 hospitalised across Australia as a result of road crashes. It is estimated that road trauma costs the community $27 billion a year, so it is essential to invest in infrastructure projects which reduce the economic and human cost of road crashes. The AAA's research shows that almost 50 percent of motorists consider road safety to be their primary concern ahead of a host of other concerns.

The AAA, through its road assessment program, has examined the safety features of almost 22,000 kilometres of national highway. Our assessment awarded a 'Star Rating' of the condition of the various sections of the road network with 1-star being the least safe and 5-star being the safest. The most recent findings in 2013 found that nearly 40 per cent of the highways recorded an inadequate safety rating of only 1 or 2 stars, while the proportion of five-star roads was negligible.[6] There is clearly scope to improve the safety of existing road infrastructure and make sure new roads meet the highest safety standards.

It is clear that the demand for travel has outstripped the capacity of the existing road and public transport networks. This causes significant congestion on both of these networks, resulting in higher costs to the community and significant impacts on the business sector. These impacts are in part due to the existing transport charging systems. The current process of charging motorists to access the road network and investing proceeds from those charges is characterised by a number of flaws. It is important that the Commission

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[3] Australian Automobile Association, Motoring Report 2013, http://www.aaa.asn.au/documents/reports%2F2013%2F12301_AAA_Motoring_Report_For%20Web.pdf

[4] RAC, Congestion Cutting into Family Time, http://rac.com.au/news-community/news-and-reports/publications/rac-enews/rac-enews-2013/perth-congestion-cutting-into-family-time

[5] NRMA, *Congestion making us sick: NRMA BusinessWise survey*, http://www.mynrma.com.au/about/media/congestion-making-us-sick-nrma-businesswise-survey.htm

[6] Australian Road Assessment Program, *Star Rating Australia's National Network of Highways*, http://demandbetterroads.com.au/uploads/media_items/ausrap-star-rating-report.original.pdf

understands these flaws and their contribution to Australia's current public infrastructure environment.

The Limits of the Existing System of Funding Infrastructure

Under the existing system road users pay for access to roads by delivering revenue to governments through a number of state and federal taxes or charges. State governments acquire revenue by imposing an access charge on vehicle owners in the form of vehicle registration. Other forms of revenue state governments derive from motorists include stamp duty and licence fees. These charges vary across jurisdictions.

Further, through the federal fuel excise, motorists pay a sum of 38.14 cents per litre (cpl) of fuel they purchase. Fuel excise delivers a significant proportion of revenue to the Federal Government and an estimated $15 billion will be raised in 2013-14. There are a number of shortcomings associated with the current system including:

- No direct link between revenue and expenditure on land transport infrastructure
- The system institutionalises cross-subsidisation
- The system manages demand poorly
- Fuel excise is a diminishing source of revenue

No direct link between revenue and expenditure on land transport infrastructure

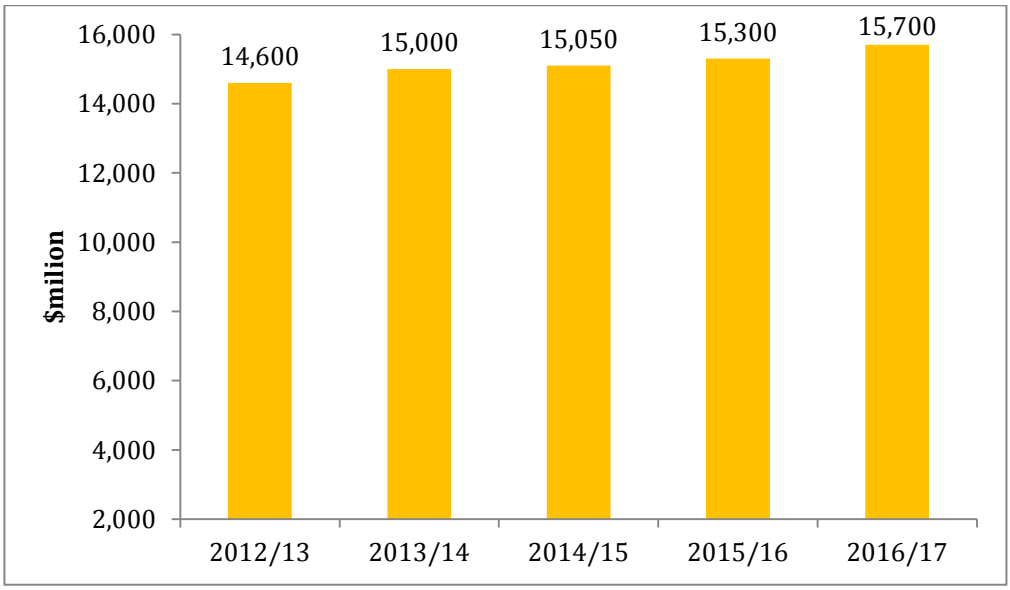
One of the major problems with the existing system is that there is no link between the taxes motorists pay and investment by governments on transport infrastructure. This issue goes to the discussion paper's question: *What are the circumstances that might lead to governments over or under investing in infrastructure?* The AAA believes this particular problem contributes significantly to under investment in transport infrastructure.

The revenue governments receive from road users is not earmarked for expenditure on the road network. Fuel excise flows through to consolidated revenue, where the process of directing funding to land transport is complex and lacking in transparency. This leaves motorists with little idea of whether (or to what extent) the taxes they pay are being returned to the construction and maintenance of transport infrastructure.

Research conducted by the AAA in 2012 found that around 90 per cent of Australian motorists believed that most of the fuel excise revenue raised should be spent on major road and land transport projects. The reality, however, is that only a fraction of this revenue stream is allocated for this purpose. In 2013-14 it is estimated that the revenue collected from the Federal Government through fuel excise will total $15 billion. This is projected to grow in nominal terms across the forward estimates with a projected $15.7 billion to be raised in 2016-17.

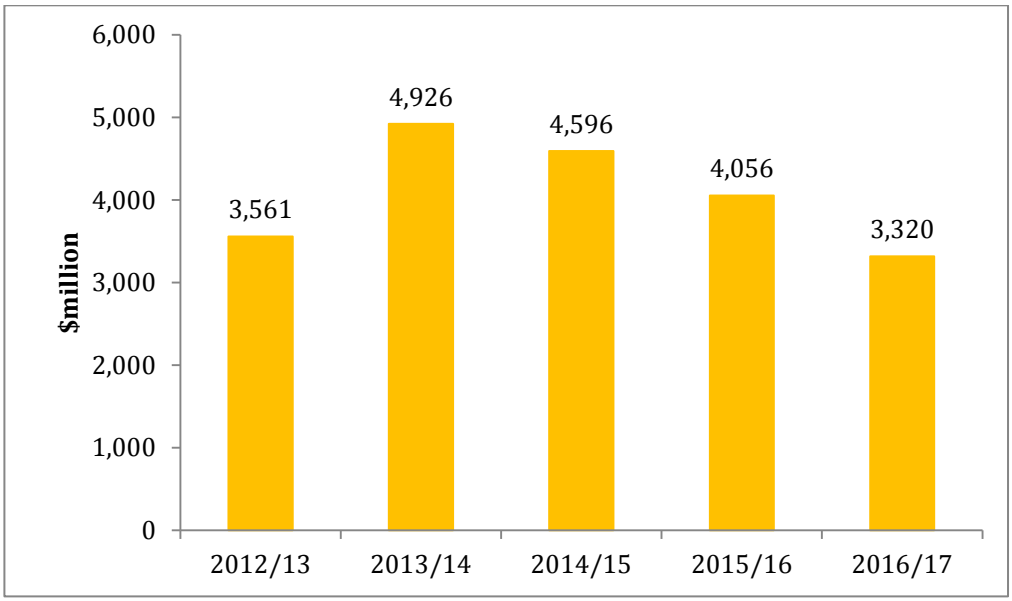
However, Federal Government expenditure on the land transportation in 2013-14 will only be $4.9 billion. This means that for every litre of fuel sold, only 12.6 cpl of the total 38.1 cpl raised will be returned to land transport, less than one-third. The situation is not expected to improve across the forward estimates and in fact spending on land transport infrastructure is estimated to dip to $4 billion in 2015-16 and $3.3 billion in 2016-17.

Fuel Excise Revenue



Source: Budget Paper No. 1, Statement 5, 2013-14.

Land Transportation Funding



Source: Budget Paper No. 1, Statement 6, 2013-14.

The system institutionalises cross-subsidisation

The current system leads to cross-subsidisation as those contributing most to road-related revenues do not always benefit from the new or upgraded roads. The current system does not put a price on externalities such as physical damage to roads, road crashes and contribution to congestion. By not considering external costs, low-impact users (such as a motorist driving in a rural setting) are subsidising high-impact users (such as a motorist regularly driving through a congested city during peak hour).

It can be argued that the substantial variations in registration charges between jurisdictions also lead to cross-subsidisation. States and territories levy vastly different registration charges based on vehicle type or size. Some jurisdictions offer discounts for fuel efficient vehicles. The rate in jurisdictions can vary by hundreds of dollars. This results in a situation where motorists using roads in multiple states and territories may benefit or be disadvantaged depending on the variation between the charge in their state/territory of registration compared to the charge in the state/territory of road use.

Furthermore, the system benefits users of fuel efficient vehicles or vehicles which utilise fuels that do not incur the full rate of excise. Drivers of such vehicles pay less than regular motorists despite having the same impact on congestion and road wear and tear. As fuel excise is considered to be a charge levied to cover the cost of road use, it is inconsistent that vehicles which operate on alternative fuels which contribute to road wear, crash and congestion costs are exempt from this charge.

Heavy vehicles exert higher external costs than light vehicles as they do more damage to road surfaces than light vehicles. Yet heavy vehicle operators currently pay less fuel excise than motorists, despite inflicting higher costs on the network. The Henry Review confirmed that charges imposed on heavy vehicle operators did not reflect the wear and tear they caused to roads.

The system manages demand poorly

The discussion paper questions: *Are current systems for raising revenue for public infrastructure services providing appropriate signals for efficient use and for new investments? If not, what scope is there to improve these systems?*

The existing method of charging for road use sends limited signals to users of the network, primarily restricted to paying more or less fuel excise according to distance driven. Under the current system the network experiences congestion during peak travel times, while offering excess capacity during other periods of the day. Although fuel excise manages demand imperfectly, it is a better demand management tool than the fixed charges, such as registration.

Alternative approaches to road user charging may provide the opportunity for decision makers to make use of price signals to efficiently allocate demand to the network throughout the day. Under the current system of charging, users are not strongly encouraged to travel outside of peak times.

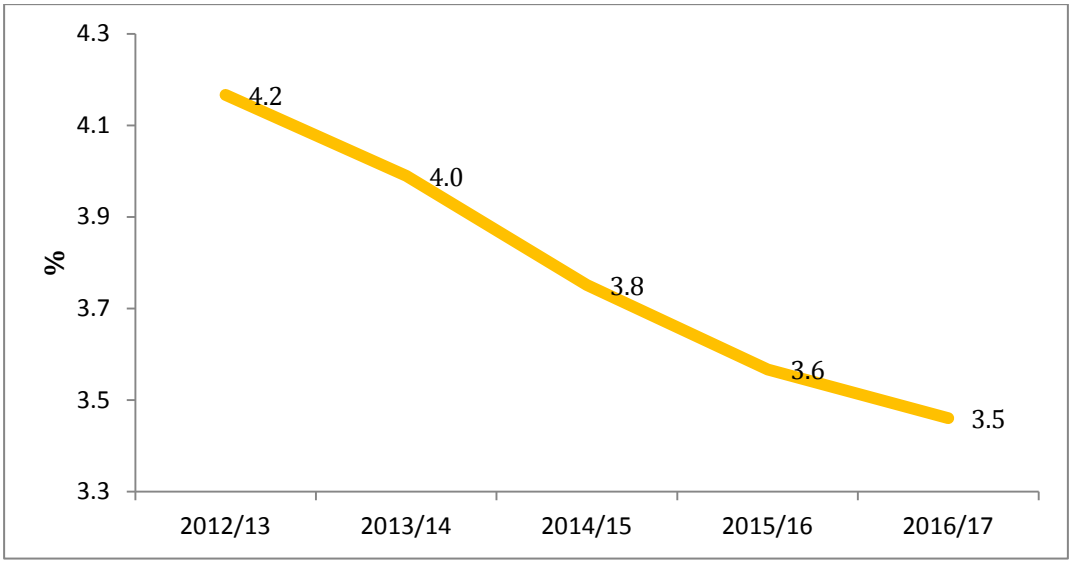
Fuel excise is a diminishing source of revenue

Another problem with the existing system relates to the fuel excise and the fact that it is a diminishing source of revenue. While the fuel excise revenue has been increasing in nominal terms, in real terms it is declining. A general increase over the years in greater fuel efficient vehicles coupled with growth in consumer uptake of alternative fuels has seen the fuel excise decrease as a percentage of the Australian Government's total receipts.

The below graph shows that the decline is expected to persist in the short-term and by 2016/17 it is projected that it will be less than 3.5 per cent of total receipts. The decline is also set to persist over the long-term with a study by the CSIRO indicating that the revenue collected from the fuel excise will decline to 33 per cent or one third of its current value by

2050.[7] While fuel excise may provide sufficient returns over the medium to short term, the Commission should consider revenue sources over the longer term, particularly as Australia's population is forecast to maintain its strong growth in the decades to come.

Fuel Excise as a Proportion of Total Receipts



Source: Budget Paper No. 1, Statement 5, 2013-14.

New Approaches to Infrastructure Funding

A new approach to funding land transport infrastructure is clearly needed if we are to bridge the gap between our growing demand for new roads and the capacity of existing road infrastructure. A strong commitment to infrastructure investment should not be compromised by the current challenging fiscal circumstances.

Australia is in desperate need of a better long-term plan for transport infrastructure. It is clear that we can no longer rely on the existing process for infrastructure development and funding. The drip feed approach to annual budgets has failed and will not deliver the significant long-term infrastructure projects and improvements needed for Australia. The creation of Infrastructure Australia (IA) was a step in the right direction, and the current effort to reform the advisory body is a positive development. One of the most important changes to IA is the requirement that the agency develops a 15-year infrastructure plan for the nation, which is to be revised every five years. This and the other reforms to IA should improve the strategic planning of nationally significant infrastructure projects.

It is critical that there is a greater degree of transparency of project evaluations, particularly cost benefit ratios. In addition, it is important that post evaluation measurement of cost benefit return is conducted as this will inform future decisions by comparing actual benefits to those predicted at the evaluation stage of the project.

Although the current fiscal constraints should not dissuade policymakers from providing important funding for infrastructure, there is no doubt that we need to adopt more innovative methods of funding, financing and delivering infrastructure projects. The discussion paper

[7] Graham PW, *Projecting future road transport revenues*. CSIRO, 2012

asks: *What alternative funding mechanisms for public infrastructure should be considered in this inquiry?* The AAA believes that we should utilise all available options, including:

- Better use of the revenue from motoring taxes and fuel excise
- Appropriate user charging
- Reinvestment of the proceeds of the sale of existing assets
- Strengthening the risk assessment of new public private partnerships
- Considering the benefits of reduced road trauma in road funding decisions
- Establishment of a Transport Infrastructure Fund
- Other options

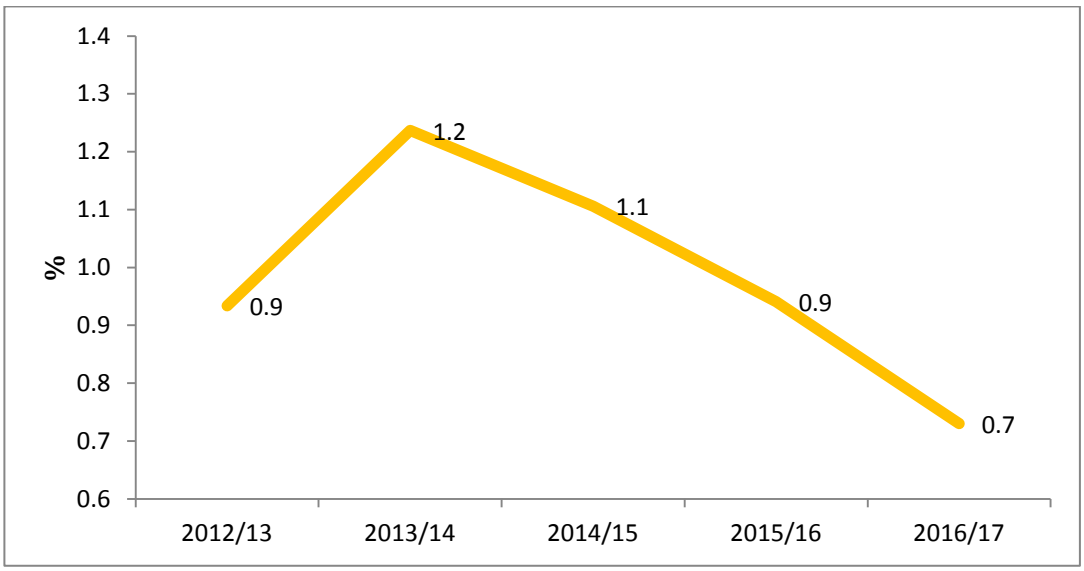
Better use of the revenue from motoring taxes and fuel excise

Each year, motorists pay billions of dollars to the federal, state and territory governments. At the federal level there is a significant shortfall in the level of funding directed to road and land transport infrastructure relative to the amount of revenue raised from fuel excise.

The Federal Government needs to dedicate a greater portion of its motoring-related revenue to investments which will deliver the land transportation which Australians deserve. The below graph shows the estimated share of federal spending which will be dedicated to land transport infrastructure between 2012-13 to 2016-17. The proportion of spending peaks at a mere 1.2 per cent before declining over the forward estimates to less than 0.7 in 2016-17.

This level of spending is unlikely to significantly bridge the transport infrastructure gap. Although it is critical to attract private sector capital for major projects, public sector spending also has a role to play. The country faces a difficult fiscal situation, but governments should differentiate between general debt used to fund deficits and debt which enhances productivity by paying for infrastructure. Funding critical infrastructure is a good investment likely to provide long-term public benefits and the use of public debt for this purpose should be treated as an investment in the nation's future.

Land Transportation as a Proportion of Total Spending



Source: Budget Paper No. 1, Statement 6, 2013-14.

Appropriate user charging

The discussion paper touches on the issue of user charging and poses the questions: *What costs and benefits should be taken into account when considering the suitability of user charging for public infrastructure? What impediments exist to the wider application of user pay funding arrangements for public infrastructure, and how does this differ for different infrastructure types? How could such impediments be addressed?*

It is important to note that motorists using motorways in Sydney, Melbourne and Brisbane already pay direct user charges in the form of tolls. While toll roads are not suitable in all situations or locations, it is clear that critical projects such as Melbourne's East West Link and Sydney's WestConnex will only likely proceed by attracting private sector involvement through the use of tolls.

The AAA believes that it is appropriate to begin a debate on our future road funding options, including the potential for a more direct system of user charging. However, the AAA is concerned that motorists already pay more than their fair share in motoring taxes and charges, and the perception that motorists will be asked to dig deeper into their pockets is a major impediment to winning public support for a wider system of road user charging.

For this reason it is crucial that any reform seeking to implement a broad based system of direct road user charging needs to be a methodical, open and transparent process. To win the support of motorists it will be critical that the case for change is clearly laid out and the benefits of reform are properly explained. Road users will be more likely to accept direct user charging if they see tangible results through better infrastructure and improved congestion and safety outcomes.

A road user charge should only be implemented as a part of genuine reform of taxation on motorists and should not be imposed on top of the existing fuel excise charges. The AAA believes it is important to begin a constructive dialogue on the merits of such a reformed system. However, our position has always been that any reform of motoring taxes, charges and fees should be revenue neutral and ensure that there is no net increase in the overall cost of motoring.

Reinvestment of the proceeds of the sale of existing assets

Another option for governments operating in a challenging fiscal environment is funding infrastructure investment through the use of proceeds from asset sales. The discussion paper raises this issue through the following questions: *What is the scope for further privatisation or 'capital recycling' of existing government assets to fund new public infrastructure? What principles and processes should guide these decisions, and what tradeoffs need to be taken into account? To what extent could widespread use of this approach create incentives for governments to over invest in infrastructure irrespective of efficiency considerations?*

Asset sales are not always popular with the electorate and the AAA does not intend to suggest which if any public assets should be sold. However, recycling capital from existing infrastructure into new projects is increasingly being seen as a viable option. Recently, the New South Wales government earmarked $5 billion it received from its sale of Port Botany and Port Kembla for new infrastructure including the first stage of the WestConnex transport project.

It is also important that the potential for state governments to recycle capital from asset sales is not hindered by fears of lost revenue. Currently, state-owned enterprises pay state governments the equivalent of corporate tax as a means of ensuring competition. However, when an asset is sold the states forgo this payment as the new private enterprise is bound to pay corporate tax to the Federal Government. This disincentivises state governments from proceeding with asset sales.

It is thus encouraging that the Federal Government has recently raised the possibility of making an incentive available which would allow states to continue to receive this revenue. What is particularly encouraging is that the incentive will be conditional on the state government using the proceeds of the sale to invest in infrastructure.

The AAA reiterates that is does not take a position on which if any assets should be sold off, however, we welcome the fact that various options to fast-track infrastructure investment are starting to emerge.

Strengthening the risk assessment of new public private partnerships

It is widely accepted that in order to address our infrastructure requirements, we need to encourage stronger investment from the private sector. The discussion paper has asked: *What are the costs or weaknesses of PPP models? Should the risks associated with PPPs be shared appropriately between governments and the private partner?*

Unfortunately, in recent years a number of road projects funded through Public Private Partnerships (PPPs) have failed due to insufficient patronage levels. Failures have largely been attributed to unrealistic forecasting of traffic levels and the related problem of the private sector being burdened with a large portion of the risk for road projects.

It is important that we strengthen the risk assessment of new PPPs and ensure that private sector investors are not unnecessarily discouraged by the difficulties encountered with some recent projects. Rigorous project selection processes which include peer reviewed economic and transport modelling should be adhered to. The government should also accept more of the patronage risks associated with these projects.

One example of how the burden of risk is being weighted toward the public sector is the current plan for delivering the WestConnex project. The New South Wales government has endeavored to fund the first stage of the motorway and will seek private sector investment to finish the project. In a departure from the traditional model, patronage levels will be established before private investment is sought. The state government taking on the initial risk will provide the private sector with the ability to invest in a lower risk and more attractive asset.

Another issue the inquiry paper has asked: *Is there any evidence of government policies or regulation impeding private sector participation in the provision and financing of infrastructure projects?* The Commission should address the need to remove the barriers to competition in the procurement of PPPs. It is often suggested that bidding costs in Australia are excessive and that the process of awarding contracts is time-consuming and characterised by red tape. This serves to restrict new entrants from entering the PPP market. Bidding costs in Australia can be up to 45 per cent higher than in comparable countries such as Canada.[8] Stronger competition resulting from lower bidding costs should improve the value for money for the governments involved. Maximizing competition in the procurement process for PPPs is

[8] KPMG, *PPP Procurement: Review of Barriers to Competition and Efficiency in the Procurement of PPP Projects*, 2010

critical, particularly as Australia will need to increasingly draw on the private sector to bridge the current infrastructure gap.

Considering the benefits of reduced road trauma in road funding decisions

It is estimated that road trauma costs the community $27 billion per year. Reducing this figure through infrastructure investment has the potential to reduce the strain on other portfolios within the Federal Budget, such as the health sector. While infrastructure project evaluations often specify safety as a goal, the inputs used to calculate safety benefits are often inconsistent when compared to the inputs used by other government portfolios.

Currently, two key inputs - discount rates and the statistical value of life - may not be accurately evaluated when considering road infrastructure projects. Discount rates vary across government portfolios which places inherent preferences on different project types. Similarly, valuing the statistical value of life differently has the potential to lead to an inefficient allocation of funding between portfolios.

Projects across all portfolios which focus on improved health outcomes should use the same project evaluation parameters, in particular, the statistical value of life and discount rates.

The AAA's road assessment program has identified safer roads investment plans for the nation's national highways. Our analysis shows that an investment of $4.7 billion would save 36,000 lives and serious injuries on our highways over a 20 year period. This represents a modest investment over 20 years and will prevent a large number of crashes, reducing part of the social and economic costs of road trauma.

Establishment of a Transport Infrastructure Fund

The Commission should consider the merits of establishing a national transport infrastructure fund. Such a fund would help to ensure that long term funding arrangements are put in place for projects of national significance. This would allow Australia to overcome the short term, drip feed approach which is a characteristic of annual budgets.

Other Options

The AAA believes that the above list of approaches should all be considered by the Commission in its inquiry. Nevertheless, we believe that all options should be on the table in deciding how to fund and finance public infrastructure. There may be scope to evaluate developer contributions framework for securing contributions from land developers. The AAA also welcomes proposals to introduce new arrangements for infrastructure bonds in Australia, while other mechanisms, such as utilising the increased land value from the provision of infrastructure projects can also provide a potential source of funding.

Concluding Remarks

Australia has suffered from years of underinvestment in its land transport infrastructure. Congestion is harming our national productivity, while road crashes result in adverse social and economic outcomes.

We thus welcome initiatives to accelerate investment and make progress towards closing the nation's infrastructure gap. It is vital that a strategic long-term plan to deliver our

infrastructure is put in place. It is equally important that governments and private sector participants are equipped with a broad suite of innovative measures to help fund and deliver this badly needed infrastructure.