

Chapter 3 Opportunities for participation by the private sector

Introduction

3.1 This chapter considers the second item in the terms of reference:

The opportunities to increase the participation of the private sector in the rail industry.

3.2 Traditionally rail services were provided by the States, although specific purpose railways were built by the private sector from the 1870s onwards, mainly for the transportation of sugar, coal and other minerals. In 1975 when the Australian National Railway Commission (AN) was established, the Commonwealth became involved directly in the rail industry as infrastructure and rolling stock owner. However, it was not until the 1990s after the reforms introduced under the National Competition Policy, that the private sector began to compete as rail freight operators using public sector infrastructure.

3.3 In Australia, private sector participation which, with a few exceptions, was relatively recent in rail, was manifested in the following broad forms. A more comprehensive list of examples may be found in box 3.1:

- One type of involvement was in the provision of rail infrastructure through competitive tendering for design and construct contracts where work was carried out by the private sector but financing and ownership remained in the public sector. For instance A. Goninan & Co Limited has been a rolling stock provider for nearly one hundred years. Recent examples were the upgrades funded under the *One Nation* program (1992–95) carried out by a number of private engineering companies.
- Another form of participation was the outsourcing of maintenance work either on rolling stock or on the infrastructure itself. Again, A. Goninan & Co Limited is a prime example not only for locomotive maintenance in public sector rail but also for a number of private sector rail operators. Another example is John Holland Construction & Engineering Pty Ltd which had been contracted under the *One Nation* program to upgrade sections of interstate infrastructure.
- Similarly, other functions were contracted out, especially when public rail systems restructured, with some of these going to private sector organisations: for example cleaning, catering and marketing.
- A variation was the subcontracting of rail operations. For instance, Northern Rivers Railway as a subcontractor for FreightCorp, hauled flyash on Rail Access Corporation (RAC) infrastructure without having to negotiate its own access as it operated under FreightCorp's negotiated arrangements. Similarly Austrac hauled freight from Griffith to Port Botany.

- Another form of participation was the provision of rail operations through build, own, operate and transfer (BOOT) schemes where construction and investment were by the private sector with some (usually tax) concession during the term of the contract (quasi ownership). At the end of the contract period full responsibility for the rail operation will be returned to the public sector. The Southern Railway–Sydney airport link and the Brisbane airport citylink are examples of BOOT schemes.
- An alternative was the build, own, operate (BOO) scheme where the private operators took full responsibility for the rail operation. An example of such providers is the Skitube in the Snowy Mountains.
- A subset of the BOO scheme was full service provision by private sector operators, usually to fill a void such as the sugar trains, BHP Iron Ore, Hamersley Iron Pty Limited and Robe River Iron Association are also owners of the infrastructure.
- Another form of participation involved private operators who had recently purchased public sector rail operations—Great Southern Railway Limited (GSR), Australia Southern Railroad Pty Limited (ASR) and Tasrail.
- A further variation occurred when private operators chose not to own any of the rolling stock or the infrastructure, choosing instead to utilise the public sector rail services provided by, for example, National Rail Corporation and FreightCorp. However, as the business grows then their participation in rail may expand to include owning rolling stock and running their own trains, although some may lease the locomotives and wagons. Examples of these operations are Specialized Container Transport (SCT), Toll Rail and Boxcar Pty Ltd.
- An unusual arrangement the committee noted was that entered into by Rio Tinto Coal (NSW) Pty Limited (Rio Tinto) and FreightCorp, whereby Rio Tinto purchased some thirty wagons but allowed FreightCorp to use them in return for hauling Rio Tinto coal. Some of the grain companies also had similar arrangements.

3.4 Although the Commonwealth decision to privatise AN opened up further opportunities for investment and ownership of rail operations, previous encouragement had existed indirectly through tax incentive programs. These included the infrastructure borrowings program (Develop Australia Bonds) introduced in 1992 as part of the *One Nation* program but the scheme was discontinued in February 1997. These tax incentive schemes were to facilitate private sector investment in publicly accessible infrastructure such as land transport, seaports, electricity generation, air transport, gas pipelines, water supply, and sewerage infrastructure (Department of Transport and Regional Development 1998, p. 4).

3.5 In the 1997 Budget, the 1992 infrastructure borrowings program was replaced by an infrastructure borrowings tax rebate scheme which was capped at \$75 million (1997 prices) per year. Royal assent to the *Tax Amendment Act No 5 (1997)* which enabled the new scheme to be implemented was given in April 1998. Under the new scheme, the eligibility scope for projects was narrowed. Ultimately the scheme will be restricted to land transport facilities. Both BOO and BOOT proposals will be eligible although the projects must demonstrate there is a direct charge or levy on the public. Private sector investors in rail projects may access this scheme and other similar industry incentives.

3.6 These developments focused greater attention on the need to provide effective mechanisms for open, nondiscriminatory access to rail similar to access in other core industries (for example, gas and electricity). In the absence of a national legislative regime specifically addressing rail access, rail users increasingly looked to the provisions of Part IIIA of the *Trade Practices Act 1974* to enable third party access to essential infrastructure facilities. Access regimes which determined charges and pathways can have a major effect on private sector participation. For further discussion on access see chapter 4.

Rationale for private sector participation

Reasons for

3.7 In the 1990s Australia moved towards encouraging greater private sector participation in transport and in the provision of infrastructure generally. The changed attitude to public sector involvement in rail was complemented by a changed view on the role of government, its participation in business enterprises and its exposure to associated risks.

3.8 As the Queensland Department of Transport said in its submission:

In general, international best practice has been characterised by primacy of the commercial objective, private sector ownership and separation of the regulatory function. The introduction of competition between government owned corporations with a commercial focus is likely to lead to significant improvements in performance of the rail industry. The inclusion of the private sector in that competition is likely to lead to even greater innovation and efficiency. (Sub 68, *Submissions* p. 910)

3.9 Transfield Pty Ltd also suggested that the introduction of market pressures could increase the efficiency of rail above and below line through: better rail investment decisions; whole of life analysis; lower costs for the design, construction and maintenance of rail infrastructure; more efficient system usage and integration; better allocation of resources; higher level of project innovation; and more efficient use of rail infrastructure (Sub 97, *Submissions* pp. 1245, 1253).

3.10 Given constraints on government budgets, it was suggested that private sector investment may permit some projects to proceed earlier than is possible with government funding. Therefore, the economic benefits of such projects may be secured at an earlier date and so provide a net benefit to the community. The Skitube in the Snowy Mountains and the Sydney airport–rail link were two examples given in support of this claim (Subs 30, 97, *Submissions* pp. 350–8, 1245).

3.11 Other witnesses maintained that a more competitive environment for transport industries would result in greater efficiency and effectiveness in the rail business. Examples cited included the private railways run by the sugar mills and the iron ore mining companies, and the successful development in New Zealand after Tranz Rail Limited bought the business. In other words—why should governments operate rail when the private sector might do it better? The private sector claimed it would run benefit cost analyses and would ensure that investments would produce profitable returns (Sub 30, *Submissions* p. 350). Public funds could then be spent on social and education programs.

3.12 In the move towards privatisation and potentially greater efficiency, many State rail operations were restructured and corporatised, some in preparation for privatisation. At the Commonwealth level, all of AN was sold in late 1997 and the Office of Asset Sales completed its scoping exercise in NR in September 1997. However, NR's actual sale was placed on hold until the shareholders reach agreement on asset transfer. At the time of writing, two State rail operations were currently being considered for sale: V/Line Freight in Victoria and the WA Government Railways Commission operations (Westrail).

3.13 The committee notes the suggestion that competition and privatisation principles introduced into government operations may force the latter to become leaner and meaner and operate like the private sector, returning money invested to their shareholders—the people. Competition from private operators seemed one way to induce government business enterprises (GBEs) to operate effectively and efficiently, to provide better priced services for Australian industry and Australian people. (*Transcripts*, pp. 607, 610). As was stated in evidence:

If we are going to get a much more improved railway system, we cannot just rely on telling the railways to get to world's best practice. They need the spur which comes from the loss of their business from competition in order to achieve maximum efficiencies. (*Transcripts*, p. 607)

Reasons against

3.14 The potential costs of private sector participation may well outweigh its benefits in some cases. For instance, private sector rail operators may cherry pick route by route and product by product leaving the public sector struggling to provide essential transport network services at a loss, thereby appearing to confirm the inefficiency of public sector rail. Costs associated with involving the private sector may include increased financing costs, transaction costs, guarantees such as no rival public sector developments, promised regional developments, increased user charges, revenue foregone through government incentives, and network usage costs. Examples of these were given by various witnesses (Subs 82, 95, 97, *Submissions* pp. 1130, 1224–5, 1248–52).

3.15 In the context of attracting private sector participation, NR raised the issue of political advantages carrying more weight than benefit costs analysis, citing the proposed Adelaide–Darwin railway which attracted a total of \$300 million from three governments as initial funding when that amount could have helped upgrade Australia's national track (*Transcripts*, p. 1272).

3.16 Privatisation does not necessarily guarantee competition. The spectre of a private monopoly was discussed by witnesses. SCT expressed concern that NR may be sold at a price which could result in 'one large competitor being given an unfair subsidy...a dominant position in the marketplace' (*Transcripts*, p. 756). Exchanging a public monopoly for a private monopoly may not necessarily increase efficiency, effectiveness and competition.

3.17 The Public Transport Union (PTU), the trading name of the Australian Rail, Tram and Bus Industry Union, maintained that 'empirical evidence does not support the argument that private enterprises are more efficient than public enterprises.' (Sub 39, *Submissions* p. 483) Private firms may be inefficient for the same reasons that public firms are inefficient.

3.18 Privatisation may not be the appropriate remedy since a privatised enterprise after a public sector sale may continue to be inefficient. What is required is a complete restructuring to implement policies and management strategies designed to correct inefficiencies.

3.19 Restructuring, however, should be carefully considered and planned. Thew & McCann Pty Ltd argued that one potential drawback to privatisation was the loss of in-house expertise and technical capability, especially with downsizing—a slash and burn restructuring. Downsizing may result in no new young staff being trained. Sometimes people in a new environment tend to be given greater responsibilities without the necessary previous experience. Some decisions may be made in the new entity without any full understanding of possible consequences and implications (*Transcripts*, pp. 605–7).

3.20 Thew & McCann Pty Ltd also considered that:

There seems to have been a willingness on the part of government to accept a view that any involvement by government in public enterprise is by definition undesirable, and that the market economy is intrinsically so perfect that it alone is the key to microeconomic reform...

Indeed, the public could be forgiven for forming the view that our political leaders are quite happy to take the short-term political kudos and economic windfalls from early reform initiatives, without consideration of the long-term socio-economic consequences, since by that time they will have gone from political position and therefore from any public accountability (except to history) for their former actions. (Sub 93, *Submissions* p. 1216)

3.21 The PTU highlighted other aspects affected by deregulation and privatisation. Safety standards and procedures may be undermined and disrupted as cost cutting measures were reconsidered by private sector management after a purchase. Certainly some staff would be retrenched. Many of the tasks which previously were performed by employees may be contracted out as a cost saving measure to enhance efficiency and cost effectiveness. Downsizing may lead to the erosion of corporate memory and knowledge base. Concern was expressed, for instance, about the paucity of experienced signalling maintenance staff, many of whom are in their late forties with few apprentices being trained to follow on in the trade (*Transcripts*, pp. 225–8, 613).

3.22 In contrast to this move is Queensland Rail (QR), where a project to provide work for its skilled tradesmen resulted in a joint venture with the London based Venice Simplon-Orient Express to develop the Great South Pacific Express as a deluxe tourist train (*Transcripts*, p. 487). The \$35 million train was built in the Townsville Railway Workshops by more than 94 QR tradespeople and 30 trades assistants. Apprentices developed skills to produce Victorian and Edwardian decorative techniques in polished wood, embossed mirrors and parquetry. These skills were being passed on to the next generation of workers.

3.23 In this context, it is worth noting that QR's investment in its work force training has been paralleled by a substantial program of investment in rail infrastructure. In its submission to the inquiry QR noted that it is halfway through a ten year \$5.5 billion investment program which to date has included improvements to the narrow gauge mainline, and an extension of the urban network to the Gold Coast (Sub 40, *Submissions* p. 497). This investment, in human resources as well as fixed assets, has been made possible by QR's business operations (generating an annual turnover in excess of \$1.8 billion), demonstrating that a public sector rail operator can be both innovative and commercially orientated.

Figure 3.1

[New map to go here showing location of proposed new projects]

Box 3.1 Opportunities for the private sector

Examples of private operators

- SCT: Melbourne–Perth rail freight service three times a week
- Toll Rail: Melbourne–Perth rail freight service twice a week
- West Coast Railway: passenger trains Melbourne–Warnambool
- Hoys Roadlines: Melbourne–Shepparton rail freight service
- Northern River Railway: flyash and cement in northern NSW and proposed tourist scenic train
- Sugar mills: sugar trains in Queensland
- BHP coal and steel products: trains in Port Kembla (NSW)
- Iron ore trains in Pilbara (WA)
- A. Goninan & Co Ltd: design and construction of rolling stock
- John Holland Engineering & Constructions Pty Ltd: infrastructure design, upgrades and maintenance
- Skitube in the Snowy Mountains (NSW)
- Austrac: shortline Griffith–Port Botany rail service
- Joint venture by QR and Venice Simplon-Orient Express to develop the Great South Pacific Express as a deluxe tourist train
- Transfield and others: Sydney airport link and Brisbane airport link
- Australia Southern Railroad: intrastate freight in SA
- Great Southern Railway: Ghan, Indian–Pacific, Overland passenger lines
- Tasrail: intrastate freight in Tasmania
- Railroad Technologies has prototyped roll on–roll off intermodal freight system— to start by early 1999 on Melbourne–Sydney corridor

Proposed private rail systems [see figure 3.1]

- Alice Springs–Darwin
- Melbourne–Darwin project
- Canberra–Sydney high speed train
- From Surat Dawson Basin (Sudaw) to port (Qld)
- Perth–Kalgoorlie high speed train

Proposed sales

- Proposed sale of Optima Energy (coal lines to Leigh Creek, SA)
- Proposed sale of V/Line
- Proposed sale of NR
- Proposed sale of Westrail

3.24 As Charles W. Hoppe said:

There appears to be a common belief around the world that the solution to the problems of government-owned railways is privatisation, as if privatisation were a magic wand that makes railway deficits turn into profits, indifferent service into customer satisfaction, and bureaucratic employees into entrepreneurs...

The reality, rather than the theory, is that corporatized, state-owned railways are often managed as well as their private sector counterparts except for the distractions which government ownership tends to overlay on management. Privatisation of railways makes sense as long as it streamlines the decision-making process so that the focus is on the customer, not on internal, bureaucratic debate. (Sub 110, *Submissions* pp. 1491–2)

3.25 In the context of privatisation, the committee notes issues to be considered include:

- changed attitudes to public sector investment and participation in business enterprises and its exposure to associated risks;
- belief that market pressures through competition could make rail more streamlined, efficient and cost effective; and
- costs associated with privatisation and private sector participation.

3.26 However, the committee accepts that there are advantages of increased private sector participation. In saying this, the committee believes private sector participation does not mean the total withdrawal of the public sector. The important focus for the rail industry is to increase its effectiveness, efficiency and utilisation so that Australia's transport needs may be met in the best possible way.

Opportunities

3.27 As indicated in the introduction, many opportunities for the private sector to be involved in the rail industry exist. Private operators may be consultants, contractors, managers, buyers of franchises, partners in joint ventures, outright purchasers or providers of outsourced services—cleaning, catering, marketing, ticketing, manufacturing, maintenance or rolling stock. Furthermore, the private sector may be involved in BOO or BOOT schemes. Examples of opportunities for private rail operators are found in box 3.1 and discussed throughout this report.

3.28 Transfield Pty Ltd pointed out that governments need to provide the leadership and set the agenda for private sector participation. Private sector investors require certainty and clearly defined profit opportunities:

If we can establish a taskforce where people genuinely look into that and create the definition of what is to be done, from then on we will go to the next step down and say, 'How can we produce it and how can we deliver it?' (*Transcripts*, pp. 1208–9)

3.29 Private sector commitment and willingness to be involved leads the committee to conclude that the rail industry is still viable and attractive to the private sector, subject to the national track being upgraded to an acceptable standard. The committee supports private sector participation in the rail industry since this seems a logical way to imbue the rail industry with innovation, new technology and funds.

3.30 Private sector participation provides the rail industry with stimulation and challenge by forcing public sector rail to reconsider its approaches, strategies, future plans and corporate policies.

Infrastructure

3.31 The committee is aware that there are other opportunities additional to the examples listed in box 3.1. For instance, the Commonwealth is interested in attracting the private sector to invest in rail infrastructure. With the exception of the private rail lines in NSW, Queensland, WA and Tasmania, investment to date in rail infrastructure has largely been by the government (*Transcripts*, p. 493). However, interest is certainly there from the private sector. What the private sector requires is an indication that government is prepared to provide an atmosphere of some certainty. For instance, GSR said:

...there has to be commitment on behalf of government to really reform the rail process. Once private sector operators like us see that, we will start spending money. I have \$14 million to spend. I want to spend some of that on the Overland. Once I see the government committed to fixing that track, I will start spending money on my train and making a dollar from it. So the government has to be involved in that process, not only in fixing up those issues but in further investment. That will in turn leverage private investment. (*Transcripts*, p. 928)

3.32 NR in discussing private enterprise participation and public funding of rail projects argued that decisions to encourage increased private sector participation should be made on a logical assessment of how Australia's transport industry would benefit—namely there should be true benefit cost analysis. It cited as an example the commitment by three governments to put a combined \$300 million into the proposed Adelaide–Darwin railway project as an enticement for private funding and questioned why priority was assigned to that project (*Transcripts*, p. 1272). Private sector participation should be carefully justified and rationally supported. NR suggested that:

...inquiries such as this have really got to get to the heart of infrastructure investment in the national land transport infrastructure...Is it [investment] arrived at by a logical assessment of where this country's transport industry will gain economic benefit from infrastructure investment? (*Transcripts*, p. 1272)

3.33 Private sector participation in maintenance and upgrades on a contract basis already exists in both public and private rail. NR itself contracted a number of engineering and construction companies to help create the national standard gauge track under the *One Nation* program in 1992–95. RAC increased private sector participation recently when it tendered NSW rail infrastructure maintenance work internationally and attracted a number of international tenderers (*Transcripts*, pp. 1177–8).

3.34 There is scope for private sector participation in the building and upgrading of railway stations. GSR spoke to the committee about the unsatisfactory nature of some rail stations, especially their impression on tourists who are travelling on the Indian–Pacific or on the Ghan (*Transcripts*, p. 912). The committee believes that private sector participation would provide improved facilities at railway stations as shown by the recent architectural award earned by the newly opened Homebush Station which will also be used during the Olympic Games as the main rail station for spectators. NSW is also experimenting with the construction of

privately owned stations as part of the new airport rail link. At the end of the concession period, the stations will be handed over to the NSW Government (*Transcripts*, p. 1207).

Partnership

3.35 QR has a number of above rail projects with the private sector and believes that these joint ventures encourage private sector investments (Sub 40, *Submissions* pp. 514–15). Foxboro Australia Pty Ltd (Foxboro) also drew attention to public and private sector partnering opportunities whereby the two sectors could combine and offer their complementary expertise and services to Australian and international projects. Foxboro believed that government support and/or involvement would make the proposal more attractive overseas, especially in Asia. This belief was supported by evidence from the Australian Railway Industry Corporation Ltd (ARIC) which talked of the secret of success as being 'the coat of arms—that they are seen as government railways, efficient and effective railways—that works well in Asian market—and are not seen as another consulting or contracting company' (*Transcripts*, p. 1104).

3.36 Foxboro was also interested in providing its integrated control systems, which it had marketed and installed successfully in Hong Kong to the Australia rail industry (Sub 94, *Submissions* p. 1222; *Transcripts*, p. 616). It believed that there was also advantages to be gained from joint ventures in Australia, especially when the public and private sector partners bring complementary expertise to the project (*Transcripts*, pp. 617–8).

Impediments/incentives

3.37 In the 1990s, many of the opportunities available to the private sector meant the private sector had to seek the funding itself, do the benefit cost analysis and manage the interface between the various suppliers and construction entities. The private sector, then, had to absorb market risk whereas previously it was contracted to the public sector which provided the funding. Therefore private sector participation provided some protection for the public sector, in that the debts were incurred by the private sector. Examples of these type of ventures are the Skitube in the Snowy Mountains, the Sydney–Canberra high speed train proposal and the proposed Melbourne–Darwin Railway 'where a private company by its own initiative creates an infrastructure project' (Sub 95, *Submissions* p. 1224).

3.38 Macquarie Bank Limited was of the view that 'world best' delivery of Australian rail infrastructure required private sector participation. However, the private sector required certainty and reliability which were best introduced by a national regulatory framework, similar to the regulatory environment for road transport. 'Private rail operators who view themselves as potential entrants in the market indicated they wanted track access charges that are simple, affordable and transparently set.' (Sub 30, *Submissions* p. 359)

3.39 Macquarie Bank also urged that a 'strong case exists for offering a more generous rebate scheme to private sector investors in Australian rail.' (Sub 30, *Submissions* p. 361; *Transcripts*, p. 356) In giving evidence, Macquarie Bank indicated that:

There is no shortage of investors in the infrastructure industry in Australia; it is all a question of price. There are investors there who will put money into transactions if they are going to provide a return—and we are not talking about a super return here, we are talking about a return that is higher than a government bond but lower than the normal equity market.... There

is no shortage of people who want to invest in this stuff. The question is: what is the price?
(*Transcripts*, p. 357)

3.40 The committee heard sufficient evidence to support this view. However, one impediment was the poor condition of the national track. The committee heard that many investors wanted to see the present infrastructure upgraded to a level that would enable private investors to make a return. Rail operators then may be willing to consider contributing to the maintenance of the system they were using (*Transcripts*, pp. 357–8).

3.41 QR mentioned other possible impediments which could arise when governments attempt to attract private sector participation. These included cross jurisdictional and other issues such as native title, land acquisition, environmental concerns and heritage issues (Sub 40, *Submissions* p. 500). Given current sensitivities regarding some of these matters, the committee believes that the Commonwealth and the State/Territory Governments need to develop suitable proactive strategies in order to provide an atmosphere of certainty required to attract private sector participation.

Economic benefits and costs

3.42 As noted elsewhere, industry reforms, increased pressure on public rail entities and public spending in general have all created opportunities for greater private sector investment and participation in rail services and infrastructure. To some extent, this development has been accepted by governments, policy makers and industry exponents. This attitude was largely reflected in the evidence taken by the committee. However, the one area that would most benefit from private sector investment is rail infrastructure.

3.43 Macquarie Bank outlined a number of benefits it maintained would derive from private sector participation in Australian infrastructure funding.

- Private sector financing (debt and equity) will greatly assist the government in identifying and selecting the most urgently needed rail infrastructure projects, and will thereby enhance the efficiency with which limited public sector funds are allocated.
- Private sector financing will significantly shorten the time frame and costs associated with rail infrastructure project completion, by introducing market discipline and practices to project implementation.
- Equity funding by the private sector will provide a much needed impetus for the introduction and resulting innovation of new technology in rail infrastructure construction and management.
- Given prevailing public sector policy of fiscal consolidation, which constrains funding available for infrastructure development, private sector financing will allow important rail infrastructure projects to proceed earlier than would have otherwise been possible (Sub 30, *Submissions* p. 350).

3.44 In some cases these benefits are already being realised but on a limited scale. In addition, it is important to note that private sector investment in public use rail infrastructure may also be associated with a number of costs to the community. In brief, costs may arise where Commonwealth or State Governments make available physical or financial resources to encourage private sector development of rail infrastructure.

3.45 The most obvious examples are the provision of public land for privately developed rail infrastructure or the provision of financial incentives (tax concessions or subsidisation) to encourage private sector investment. For instance, the Pilbara iron ore rail services have been built by private sector investments paying peppercorn rents for the easements on public land (Sub 108, *Submissions* p. 1471).

3.46 Private sector investment in rail infrastructure may also result in increased borrowing costs, which may be passed on to service users through higher access charges or the need to finance or publicly 'bailout' potential operating deficits. This argument is premised on the notion that governments generally are given a lower rate of interest on borrowing than the private sector due to government's higher credit rating (HORSCCTMR 1997, p. 104).

3.47 Further potential disadvantages associated with private sector investment in rail infrastructure are increased transaction or administrative costs. For example, these costs could include resource use involved in drawing up and monitoring contractual agreements, processing approvals for plans and project work, or the time taken to negotiate and complete transactions (HORSCCTMR 1997, p. 104).

3.48 Given the emphasis on integration and intermodal efficiencies, the committee believes that it is important to focus on the overall transport strategy when considering individual transport investment projects. Otherwise there is a likelihood that rail projects may depart from the integrated national perspective which should be part of the national transport strategy. The committee therefore believes that individual projects whether publicly or privately funded should not proceed without adequate consideration of the effects on other transport modes, the ways modes may be integrated and the environmental impact.

Size and number

3.49 Evidence was given to the committee on the possible optimal size and number of private operators. Some argued for complete deregulation so that the market forces could determine the ultimate mix. Others favoured large scale operators who would have low unit costs, in contrast to the overseas experience where small operators were unable to achieve the volumes and thus could not compete effectively. Such evidence suggests that Australia's population and market are not large enough to sustain more than two or three major players in the medium term.

3.50 Tranz Rail a private monopoly in New Zealand has been cited as an example of what an effective and efficient rail industry should be. Tranz Rail argued strongly for privatisation without competition and maintained this could only be achieved by large organisations:

The problem...with an orientation that would perhaps result in an artificial stimulus of competition on the rails is that it flies in the face of railway economics and economies of scale, which is very important in our industry. The operator that will have a low unit cost is a large scale operator. You can Balkanise the freight operation and have a number of small operators, all of whom would be competitive between themselves but would be relatively high cost units because none of them would be achieving the volumes that result in low unit costs. So they would have difficulty competing with the highway. (*Transcripts*, p. 160)

3.51 Tranz Rail cautioned against 'some kind of unnatural promotion of competition on the rails beyond what the competitive marketplace would produce on their own.' (*Transcripts*, p. 160). As an example of 'unnatural competition' Tranz Rail cited an artificial attempt in the UK to create competition with three rail operators. The three had now collapsed into one which was operating effectively. Similarly the USA once had hundreds of medium sized railways many of which had now disappeared as the level of business fell. Both these experiences were very costly exercises (*Transcripts*, p. 170).

3.52 Charles W. Hoppe, Inc echoed this view:

...it is probably more effective to establish a single strong rail network carrier (with rail niche carriers having access, as necessary, to keep the network rail carrier 'honest'), than to attempt head-to-head rail/rail competition by network carriers—the resulting 'price wars' would no doubt lead to disinvestment (and disengagement from the market). (Sub 110, *Submissions* p. 1493)

3.53 Elsewhere in the evidence QR and the WA Government Railways Commission (Westrail) were cited as being excellent examples of how integration ensured effective and cost efficient railways. The committee noted that with the exception of NR, NSW rail systems, and GSR, most of the rail systems involved above and below rail operations. The committee also noted the argument that disaggregation enabled the resultant rail entity to specialise and improve without being distracted from the main game. Examples of disaggregated rail organisations were those in NSW—RAC, FreightCorp and State Rail Authority (SRA). Certainly, a disaggregated rail industry would reduce the perceived conflict of interest where a rail operator may be inclined to deny access to a competitor (*Transcripts*, p. 1282). This latter issue is of some concern to the committee and is discussed in chapter 4.

3.54 The committee notes the many arguments proffered in support of integration or disaggregation on the size and structure of the organisation and explores these in chapter 5.

Safeguards

3.55 As discussed at various points in this chapter, the committee considered it essential that agreements for private sector participation be transparent and more accountable. However, it was difficult to assess the level of risks and the extent of guarantees being undertaken by government, and the resources provided by government to ensure the success of private sector participation.

3.56 In its report *Planning not Patching*, the committee quoted evidence from the Industry Commission:

Risk, and particularly uncertainty, has been ameliorated by governments through the inclusion of *material adverse effect* clauses in BOOT contracts. This notionally transfers some of the cost of risk to the public in the form of a loss of flexibility—a loss of *option value* that potentially increases the cost of transport infrastructure in the future.

Currently governments do not make available the assessments that form the basis for the decision to use a BOOT scheme in preference to other forms of finance and contracting ...

[NSW and Victoria] do not provide the information required to allow independent scrutiny of the government's decision—thereby weakening accountability. (HORSCCTMR 1997, p. 118)

3.57 The committee considers that any participation from the private sector in rail projects should be transparent and open to public scrutiny. The committee considers that the Commonwealth in consultation with States/Territories should develop procedures to ensure government accountability for, and public scrutiny of, agreements to involve the private sector in rail projects.

Conclusion

3.58 The committee considers that private sector investment and participation in the rail industry have the potential to benefit the community—a more commercial outlook, greater competition, enhanced efficiency and cost-effectiveness. Increased private sector investment may free public funds for investments in other projects. However, the committee has also noted that several witnesses cautioned that private sector participation does not automatically produce greater effectiveness and efficiency nor guarantee competition.

3.59 The committee supports the use of competitive tendering for publicly funded rail projects whether they are for design, new construction, upgrades or maintenance. Infrastructure investments should be viewed from a comprehensive intermodal perspective so that assessments are made in terms of the most efficient and appropriate solution.

3.60 Many opportunities exist for the private sector to be operators, initiators, joint partners, managers, contractors or outright owners. The Commonwealth role is to ensure the regulatory framework and the national strategy support the best outcomes.

3.61 The committee supports greater transparency in agreements for private sector participation in rail projects. Greater transparency in such agreements should make those involved more accountable for the risks assumed by government and the resources provided by government. The outcome should be a better transport network across the nation.

3.62 Given the emphasis on integration and intermodal efficiencies, the committee believes that it is important to focus on the overall transport strategy when considering individual transport projects. Otherwise there is a likelihood that rail projects may depart from the integrated national perspective which should be part of the national transport strategy. The committee therefore believes that individual projects whether publicly or privately funded should not proceed without adequate consideration of the effects on other transport modes, the ways modes may be integrated and the environmental impact.

3.63 The committee's bottom line may be summed up in the following way. It does not matter in the end whether it is the private sector or the public sector which ensures that the rail industry is developed to the extent where it may take an appropriate role in the wider transport network. The important issue is that rail infrastructure is upgraded and the whole rail industry is able to develop its potential. Many have spoken of rail as the transport mode for the 21st century. Australia must ensure its rail industry is not still languishing in the 19th century.