



4 August 2005

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Dear Mr Rowe,

REVIEW OF THE RAILWAYS (ACCESS) CODE 2000 – DRAFT REPORT

Thank you for the opportunity to make a submission in relation to the Draft Report of the Review of the Railways (Access) Code 2000.

In general Co-operative Bulk Handling Limited (CBH) is supportive of the Draft Report analysis and the proposed Recommendations and Preliminary Views with one exception. CBH wishes to comment on Preliminary View 2, which deals with the treatment of government subsidies.

Our submission can be found on the following pages.

Yours sincerely,

PP Colin Tutt
General Manager Operations

Preliminary View 2 – Treatment of Government Subsidies

CBH View

CBH believes that any government subsidy, which is directed towards supporting the viability of rail transport for freight, should be dealt with outside the Access Code and the Over-payment Rules. A subsidy directed at supporting the viability of some part of the rail network has the primary objectives of:

- i. assisting rail transport to be competitive with road transport;
- ii. assisting rail transport to meet the social needs of rural communities; and
- iii. minimising road externality costs to the government.

This form of subsidy is different from the subsidies that relate to safety or any potential subsidy aimed at lowering freight rates.

Government Subsidies for Freight Transport on Rail

The WA government has recently announced that it will make a contribution towards the cost of maintaining the Picton to Greenbushes railway to support the use of rail for woodchips and log transport. Discussions have also been taking place with key grain industry participants in relation to the prospect of the government contributing to the maintenance of the narrow gauge grain network.

The focus of these discussions relates to a multi-faceted proposal designed by CBH and ARG Group (the combined ARG / WestNet entity), which has the principal objectives of:

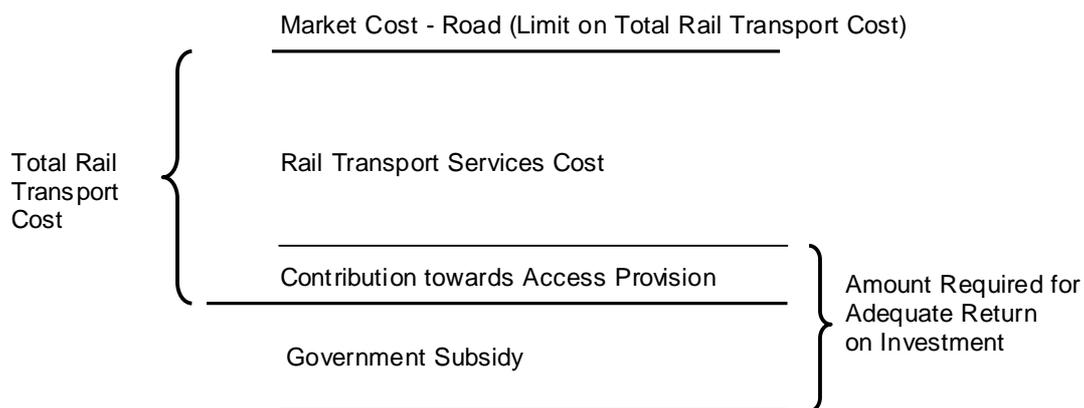
- i. ensuring the long term viability of regional grain lines in Western Australia by maintaining grain on rail;
- ii. creating the most efficient grain supply chain nationally;
- iii. enabling ARG Group to earn sufficient return on investment in order to maintain rail services for grain on the most expansive possible narrow gauge network;
- iv. creating an environment that encourages investment in rail related infrastructure by the industry infrastructure owners; and
- v. securing the long term future of rail as the transport mode of choice through continuation of network pricing principles.

The trend towards subsidisation is recognised in paragraph four under section 4.8.3 of the Draft Report *“Government contributions to the enhancement of the WA rail network appears to be becoming more common, with proposed Government grant funding to assist with upgrades on some branch lines and the interstate network.”* However, the final paragraph in the same section appears to draw conclusions primarily based on Government subsidies for level crossings.

Role of Government Subsidies.

Government subsidies for rail infrastructure maintenance are being considered in situations where the Government's overall policy of supporting the use of rail transport can be facilitated. Subsidies are being considered in situations where market conditions are such that without a subsidy insufficient income can be derived from access charges to enable the long term lessee (WestNet) to achieve adequate returns on investment and, therefore, to maintain services on otherwise unviable branch lines in the medium to long term.

The diagram below depicts the situation. The *Total Rail Transport Cost* that can be charged for both the rail transport services and access is limited or capped by competition in the market from road transport (*Market Cost – Road*). The amount that can be *Contributed towards Access Provision* is the amount remaining after deducting the *Rail Transport Services Cost* from the *Total Rail Transport Cost*. Should the amount available for access provision be insufficient to maintain the railway to the required standard and also provide an adequate return on investment to WestNet, the Government may consider providing a subsidy (*Government Subsidy*) so that both these objectives are met.



Role of Government Subsidy

Government subsidies are likely to be limited to amounts just sufficient to enable WestNet to achieve an adequate return on future investments i.e. a satisfactory Internal Rate of Return for the investment rather than being sufficient to achieve an amount equivalent to the ceiling cost. In other words, the total revenues from access charges and government subsidies are likely to be below the ceiling cost.

Applicability of Access Code & Over-payment Rules

Government subsidies in the form discussed in this submission are aimed at supporting the use of rail transport where market conditions are unfavourable. The amount contributed by Government will depend on the prevailing “effective” rates in both the general market for freight transport and the rail transport freight market. Should there be changes to rates in one or both of these markets then the amount of funds that are

available to cover the provision of access will change, and in turn the amount of Government subsidy is likely to change to reflect those changes. In this situation any changes in the rates and the subsidy level is believed to be a matter for discussion and resolution between WestNet and the Government. CBH believes that, in effect, any Government subsidy relating to network viability is outside the scope of the Access Code.

Over-payment Rules have relevance to the cost of access charges when total revenues exceed the ceiling cost. As discussed earlier, while it is not anticipated that the provision of government subsidies relating to network viability will result in total revenues exceeding the ceiling cost, the principle inherent in the Over-payment Rules is that should the ceiling cost be exceeded then any over-payments are returned to the Operators (and presumably) the contracting parties of the Operators. This principle is not believed to be appropriate when this form of government subsidy is involved. As mentioned in the previous paragraph any adjustments are believed to be a matter for WestNet and the Government. In CBH's opinion, it would be inappropriate to be effectively handing a portion of a Government subsidy to Operators.

In addition and as depicted by the earlier diagram, there is a relationship between the rail transport services costs and charges, and contribution towards the costs and charges of access provision when the extent of any government subsidy relating to network viability is being considered. This relationship is not relevant to the rail transport services market and should have no effect on rail transport competition. From a Government perspective it is likely that the Government would want to encourage rail transport competition and lower rail transport charges so as to increase the amount of funds directly available for the provision of access and hence lower the amount of any government subsidy.

Summary

In summary CBH submits that any Government subsidy aimed at supporting the viability of rail transport should fall outside the provisions of the Access Code. Should the Authority not agree with this view then the following points are made:

- Any Government subsidy that is provided to support the viability of rail transport against road competition is not likely to result in total revenues on the relevant section of the network exceeding the ceiling cost.
- Any funding adjustments will relate to adjustments to the level of Government subsidy and not to access charges to Operators through the use of the Over-payment Rules.
- The Code needs to make the distinction between Government subsidies to support the viability of rail transport and any third party contributions or Government subsidies for other purposes i.e. such as contributions to level crossing standards.