



AUSTRALIAN CAPITAL TERRITORY

SUBMISSION TO THE COMMONWEALTH GRANTS COMMISSION'S POSITION PAPER 2008/26: *TRANSPORT SERVICES*

January 2009



IEWS ON THE COMMISSION'S ASSESSMENT PROPOSALS

INTRODUCTION

The 2010 Review has been run as an iterative process between the Commonwealth Grants Commission (the Commission) and the States and Territories (the States) over the course of the past four years. As part of this process, the ACT has provided a number of submissions in response to Staff and Commission Discussion Papers and refined based on multilateral and bilateral discussions with Commission staff and other States. These submissions outlined the ACT's position regarding the validity of the conceptual case underpinning the assessments and the proposed assessment methods.

It is noted that in some instances the position adopted by the Commissioners, as detailed in the latest Commission Position Papers, is at odds to those of the ACT. In the interests of brevity, the ACT has not sought to reiterate the entirety of its previously stated position unless new data or new thinking has been applied. In this context, a lack of objection does not imply support where such support has not been previously stated, and instances where comment has been made on refining a methodology does not necessarily imply support for the broader method itself unless otherwise stated.

As such, this submission encompasses the ACT's views on only major issues.

The ACT supports the continued development of an assessment based on the population in urban and non-urban areas and the different level of subsidy States pay in these areas.

The main points in this submission include:

- **support** for the Commission's general approach despite concerns with lowering the population threshold to 20,000 which may water-down the relative importance of the urban subsidy weights;
- **support** for the consultancy and an examination of the specification of population band groupings and their interaction with the weights and category factor outcomes;
- **support** for not assessing concessions as the data are not reliable nor fit-for-purpose and using alternative proxies for concessional use would be a poor indicator of need; and
- **opposition** to the distinct assessment of freight disabilities using non-urban passenger transport subsidies (an EPC assessment of freight disabilities is requested), as:
 - although the Commission is not inclined to assess a disability for freight subsidies as 'it will be difficult to identify a common policy or reach agreement on what might be appropriate and reliable indicators of disability', including freight expenses in the non-urban passenger transport subsidies expenses equates to an assessment of disabilities; and

- the scope of equalisation is being extended to include Public Financed Corporations (PFCs) and the commercial operations of freight carriers.

URBAN AND NON-URBAN POPULATIONS AS A BROAD INDICATOR OF SUBSIDIES

Population threshold

In response to *CGC Discussion Paper 2007/18-S Transport Services*, the ACT supported the staff proposal to separate State populations into urban and non-urban based on an urban centre/locality (UC/L) size threshold of 50 000, and then to weight these population groups according to the level of subsidies paid.

The Commission now intends to adopt an ‘urban’ population threshold or ‘cut-off point’ of 20 000 persons.

This has significant implications for the transport assessment, and for the ACT in particular given that it is the most urbanised State in Australia. That is, the approach by adopting such a low threshold size of 20,000 appears to water-down the most important aspect of the transport assessment – urban transit. This concern is consistent with information suggesting that rural transport services are relatively minor, as acknowledged by the Commission:

“State involvement in passenger train and bus services in rural areas is relatively small.”¹

Despite these concerns, the ACT is amenable to the approach if the weights for different urban and non-urban population groups, reflective of the level of subsidies paid, are specified correctly. If this is the case, then most of the concerns of the ACT are likely to be adequately addressed.

DETERMINING URBAN AND NON-URBAN SUBSIDY LEVELS

The ACT notes that the analysis undertaken by the Commission in the latest Position Paper demonstrates that subsidy levels increase broadly as urban centre population increases and that higher subsidies are average policy in larger cities.

It is noted that to recognise the differences in subsidy levels but not overly complicate the assessment, the Commission has separated urban centres into three groups:

- 20 000 and 200 000;
- 200 000 and 2 million; and
- above 2 million.

Following this, a placeholder assessment has been based on the subsidy level for urban centres with populations of 110 000, 1.1 million and 3.5 million chosen to represent the average subsidy for each of the above groups. The average subsidies were– 20,000 - 200,000 (weight of 1.0); 200,000 - 2m (2.61) and over (3.43).

¹ Commonwealth Grants Commission, *Disaggregating Expenses*, Staff Discussion Paper CGC 2006/06, paragraph 17, page55.

It is not clear how sensitive the category factor outcomes are to the population bands chosen, and how they interact with the subsidies and thus the resultant weights. Changing the specifications of the model, such as by adding or changing the population bands could result in material differences in the outcomes of States. It is requested that the Commission undertake sensitivity testing to determine how robust the outcomes are. This would provide support for the Commission's position.

It is also noted that the transport consultancy will provide advice on the specifications adopted by the Commission in its model, including the subsidy levels, population bands / groupings and weights amongst other things. When these results are provided to the States, the ACT will be in a position to provide further comments on these issues.

ADJUSTMENT FOR CONCESSIONAL USE

The Commission is not inclined to separately assess concession subsidies due to uncertainty about data reliability, although it is still considering the possibility of adjusting the average subsidy paid for eligible concession users.

The ACT considers that concessions should **not** be adjusted for given a lack of reliable, fit-for-purpose data across States. A reliable split of subsidies for urban public transport into Concessions, Pricing and Capital subsidies has not been possible in the past.

Additionally, the ACT does not support the use of concession and health care card holders as a proxy for concessional use as these data are a poor indicator of need. As noted by the Commission in its analysis of State provided subsidy data, despite the ACT having the lowest per capita concession card holder population of the States, the ACT has well above average non-student concession usage.²

ASSESSMENT OF FREIGHT SUBSIDIES

Proposal

In the *Transport Services* Position Paper CGC 2008/26 the Commission has stated that it:

“... is not convinced that a separate disability for non-urban rail freight subsidies is needed. We think it will be difficult to identify a common policy or reach agreement on what might be appropriate and reliable indicators of disability. Assessing a distinct freight subsidy disability would also not contribute to simplification. In the circumstances, the Commission is not inclined to assess a separate disability for freight subsidies.”³

The ACT supports the Commission's decision not to assess a disability for freight subsidies. The reasons for not assessing a freight disability are sound given that:

² *Transport Services* Commission Position Paper CGC 2008/26, page 22.

³ *Transport Services* Commission Position Paper CGC 2008/26, paragraph 72, page 15.

- non-urban rail freight accounts for a relatively small proportion of the transport services assessment - around 8 per cent of the category expenses in 2004-05 and 2005-06;
- in respect to the per capita expenses varying considerably from State to State, the Commission has noted that this may indicate reliability problems with the expense data and/or large policy differences between States;
- it is not clear that States have broadly similar policies for subsidising non-urban rail freight services; and
- often the costs of freight are funded through user charging and the like, as noted by the Commission - “*Freight operations tend to run on a cost recovery basis.*”⁴

The Commission, however, “...will include non-urban rail freight subsidies with other non-urban subsidies and assess them together using non-urban populations.”⁵

Including non-urban rail freight subsidies with other non-urban passenger transport subsidies (population in UCLs of less than 20,000) results in the distinct assessment of freight subsidy disabilities based on non-urban passenger subsidies.

As such, the Commission on the one hand appears to be stating that it will be difficult to reach agreement on what might be an appropriate and reliable indicator of disability for freight, yet on the other appears convinced that using non-urban passenger transport subsidies is a reliable measure of freight disabilities.

It could be concluded that this draft decision is weighted more towards achieving simplicity at the expense of equalisation. It simply has not been demonstrated that non-urban passenger transport subsidies are a reliable indicator of need for freight transport subsidies.

The ACT contends that an EPC assessment for freight subsidies should be the starting point predicated on the basis that disabilities cannot be accurately measured and data are unreliable and/or not fit-for-purpose:

- non-urban passenger transport subsidies do not relate well to freight transport subsidies, for example, the former are provided based on providing transport largely for access and social reasons, while rail freight activity is based on commercial reasons and a significant proportion of the cost is recovered via access charges and the like;
- the non-urban population overstates freight disabilities as railway lines do not run through all non-urban population centres and are generally prominent in specific areas, for example in regard to coal mining, in NSW - Newcastle (Kooragang Coal Terminal and Carrington Coal Terminal) and Queensland, Townsville, Gladstone (RG Tanna Coal Terminal and Barney Point Coal Terminal); South of Mackay (Dalrymple Bay Coal Terminal and Hay Point Coal Terminal) and Bowen (Abbot Point Coal Terminal);

⁴ Commonwealth Grants Commission, *Disaggregating Expenses*, Staff Discussion Paper CGC 2006/06, paragraph 14, page 55.

⁵ *Transport Services Commission Position Paper CGC 2008/26*, paragraph 72, page 15.

- they imply that all the entire non-urban population in UCLs of less than 20,000 are serviced by freight rail – this is not the case;
- they do not reflect that a range of mineral and agricultural products are transported by road - the road network is significantly larger than the rail network and reaches much more of the non-urban population;
- it does not reflect the relative reserves of the commodities and need for bulk transport that may be located in certain rural population areas, again thus applicable to only a proportion of the non-urban population.

A further unintended consequence is that by assessing freight disabilities, the scope of equalisation has effectively been extended to include Public Financed Corporations (PFCs) and the commercial operations of freight carriers.

The government funding of significant components of freight carrier activities are similar in intent to business development expenses which are intended to promote, attract and grow business activity. As such freight activities are akin to economic development expenses:

- Several freight providers are now providing commercial activities far beyond their State boundaries, which from an equalisation perspective, could be characterised as non-core government activities that should not be equalised. For example, Queensland Rail (QR) launched QR National in 2005, and since then has made several large acquisitions, such as the purchase of West Australian-based freight haulier ARG for \$446 million. This deal secured 70% of the contestable bulk market in Australia and builds on QR's position as the nation's number one coal and bulk freight transport provider. ⁶
- It remains unclear what subsidies are being paid by State Governments to their freight PFCs, and the policies underpinning the payments. The fact that freight operators are making substantial profits and paying significant dividends to State Governments is of concern in terms of any proposal to assess needs for freight subsidies. For example, QR's:
 - net profit for 2004-05 was \$173.3m (with a dividend of \$193.1 million paid to the Queensland Government); ⁷
 - 2005-06 profit of \$82.2m (dividend of \$68.5m); ⁸
 - 2006-07 profit of 183.2m (dividend of \$151.5m). ⁹

The Commission has previously indicated that identifying the drivers of economic development expenses is problematic and that development expenses generally vary considerably between the States and are highly policy influenced.

At the Commission-Heads of Treasuries meeting in November 2007, the Commission is on the record as stating that while economic development disabilities may exist, considerable judgment would be needed to identify the economic development

⁶ QR Annual Report 2005/06.

⁷ QR Annual Report 2005/06, page 92.

⁸ QR Annual Report 2006/07, page 78.

⁹ QR Annual Report 2006/07, page 78.

expenses and the disabilities to apply to them.¹⁰ This position regarding considerable judgment is consistent with the stated view of the Commission in the position paper regarding freight disabilities:

“We think it will be difficult to identify a common policy or reach agreement on what might be appropriate and reliable indicators of disability. Assessing a distinct freight subsidy disability would also not contribute to simplification. In the circumstances, the Commission is not inclined to assess a separate disability for freight subsidies.”¹¹

In this context, a separate EPC assessment of freight expenses is recommended. To do otherwise could see a number of jurisdictions cross subsidising other jurisdictions with freight operators that have the capacity to pay large economic development type dividends to their respective governments.

This application would be consistent with the Commission’s finding that:

“Given the high degree of uncertainty about how to define and reliably measure economic development and how to define the disabilities associated with it, we do not intend to differentially assess business development expenses.”¹²

SCOPE OF CATEGORY EXPENSES

The Commission has noted that several non-transport related groups, such as ‘Pipelines’ and ‘Communications’ are included in this assessment. The expenses represented around 2 per cent of the category in 2005-06.

While the ACT supports the Commission’s view that it does not need to change the composition of the category expense standard, the ACT supports other States’ concerns that the inclusion of this data may result in an over / understatement of the category factors for the States depending on their circumstances.

As this is the case, the ACT supports including non-transport related expenditure within freight expenses and assessing this component EPC.

¹⁰ *Services to Industry* Commission Position Paper CGC 2008/27, paragraph 23, page 5.

¹¹ *Transport Services* Commission Position Paper CGC 2008/26, paragraph 72, page 15.

¹² *Services to Industry* Commission Position Paper CGC 2008/27, paragraph 25, page 5.