

IPART CONSIDERS FUTURE CITYRAIL REGULATORY FRAMEWORK AND FARES

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Over the last few years, CityRail's costs have increased by more than the rate of inflation and taxpayers have contributed proportionately more to fund these rising costs than CityRail passengers. For example, since 2001/2 CityRail's costs have increased by 7.9 per cent in real terms, while fares have decreased by 1.4 per cent in real terms, and the proportion of costs funded by passengers has also decreased. This trend is not sustainable, especially when CityRail's costs and investment are projected to rise strongly over the next four years.

The Chairman of IPART, Dr Keating, said that "clearly fares will have to rise, but that rise should be seen to be justified. CityRail passengers should not be asked to pay for inefficient costs, but they should pay their fair share of the efficient costs of the services that they use."

Accordingly IPART is seeking to establish:

- ▼ First, the efficient cost of CityRail's services, based on costs that are consistent with those of best practice operators in Australia, and
- ▼ Second, a fair sharing of those costs between passengers and taxpayers, based on an assessment of the external benefits from CityRail's services that accrue to all members of the community and which should therefore be paid by taxpayers.

In addition, the NSW Government has requested IPART, as part of this fare review, to develop a more comprehensive and robust regulatory framework for CityRail that will in future provide it with stronger incentives to improve its efficiency, and to deliver its services to the appropriate standards for the least cost, for the benefit of both passengers and taxpayers. The current framework is not able to provide such incentives.

To assist it in establishing CityRail's efficient costs, IPART engaged L.E.K Consulting to undertake a total cost review of CityRail's regular passenger services. LEK identified achievable cost savings (or efficiency gains) over the period 2008/09 – 2011/12 that would contain the growth in costs to around 3.5 per cent pa (which is broadly in line with the expected increase in the CPI). These savings would bring CityRail's costs more in line with those of other Australian rail operators, and would reduce its annual operating and maintenance costs by around \$480m per annum by 2011/12 (or by 18 per cent compared to CityRail costs under a business as usual scenario). However, to achieve these cost savings, CityRail would need to undertake additional capital investment of approximately \$800m over 4 years.

To assist in establishing the appropriate proportion of CityRail's costs to be funded by passengers and by taxpayers, IPART engaged CRA International to assess the value of the external benefits that accrue to the community from reductions in road congestion, greenhouse emissions and road accidents as a result of CityRail services.

Economic modelling of traffic data flows by CRA International indicates that the value of these external benefits is currently around \$1.6b a year, and will increase to around \$1.7 – 2.0b a year over the period 2008/09 – 2011/12. This represents around 70 per cent of the efficient costs of providing CityRail services over this period. Given this estimate of the external benefits of the rail system, IPART's preliminary view is that it may be appropriate for passengers to fund around 30 per cent of CityRail's total costs by 2012.

However, after considering the impacts on the affordability of fares and the level of patronage, IPART's preliminary view is that fares should increase by between 20 – 30 per cent in real terms over the next 4 years.

In the past, IPART has made one-year fare determinations for CityRail. For the 2009 determination, IPART's preliminary view is that a four-year fare determination is preferable. By establishing CityRail's revenue requirement on a sound basis for the next four years, CityRail will have greater budget certainty, which will better allow it to plan ahead, and it should make CityRail more accountable for delivering the services required by the Government within its agreed budget. A four year price path would also allow CityRail more time to establish management programs that can deliver any cost savings implied by the fare determination.

A longer determination period similarly provides government and taxpayers with greater certainty about the extent to which CityRail will require government funding over time, and CityRail passengers with a better indication of how fares will change over time.

IPART has also examined the structure of CityRail fares to establish whether changes to the basis for pricing distance-based fares, peak and off-peak fares, and periodical fares could lead to more efficient use of the CityRail network, more efficient investment decisions, and increased equity between different groups of passengers.

IPART invites submissions on its discussion papers by 18 July, 2008. IPART will release its draft fare determination in September 2008.

For further information, contact: Michael Keating – IPART Chairman

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Background

IPART today released two discussion papers which consider improvements to the CityRail regulatory framework - the first paper (*Determining CityRail's revenue requirements and how it should be funded*) focuses on the total costs associated with providing CityRail services and discusses what portion of these costs should be recovered from passengers through fares, and what portion should be funded by taxpayers through government subsidies. The second paper (*Deciding on the structure and level of CityRail fares*) focuses on how fares should be structured to encourage efficiency in the use of the CityRail network, equity between different users of CityRail services and promote efficient investment decisions.

The discussion papers can be downloaded from IPART's website at www.ipart.nsw.gov.au or obtained from Andrew Hall on (02) 9290 8435. The following consultant's reports can also be downloaded from IPART's website:

- ▼ *Review of CityRail's total costs*, L.E.K. Consulting
- ▼ Value of CityRail externalities and optimal government subsidy, CRA International.