



Transport Asset Holding Entity

Initial assessment of
options

**SENSITIVE – NSW
CABINET**

21 July 2020

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Mr Rodd Staples
Secretary
Transport for NSW
16 Lee Street
Chippendale NSW 2008

Dear Secretary,

We have been delighted to assist TfNSW to inform consideration of the nascent Transport Asset Holding Entity (TAHE).

This is the final draft, superseding prior versions.

Our work considers potential high-level operational models for TAHE, beyond its limited transitional operations from 1 July 2020.

We have outlined two high-level options, which we call:

- 'TAHE Real'; and
- 'TAHE for NSW'.

These models seek to resolve the key organisational and operational challenges, identified during consultations with selected transport officials and rail operators.

Noting the limitations outlined in the Executive Summary of this report, these options are subject to further detailed analysis – and to separate safety assurance review or opinion by TfNSW – during the next phase of work.

Through you, I would like to thank the senior TfNSW and NSW Treasury officers, who contributed their time, experience and insights to our work on this complex issue.

In anticipation, we look forward to continuing to work with you to further refine TAHE's operating model over the coming months.

Yours faithfully,

Brendan Lyon

Partner
Infrastructure & Projects Group

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Executive Summary



Executive summary

Introduction & purpose

This report supports Cabinet's consideration of the long-term operating model for TAHE, beyond its initial transitional existence from 1 July 2020.

Importantly, the risks and challenges examined in this report do not refer to TAHE's initial administrative period of operations, where arrangements closely replicate 30 June 2020.

Rather, this report applies itself to the complex issue of what TAHE and other rail and transport entities do in practice, over TAHE's long operating period.

This report provides initial, high-level assessment of models and does not include any safety or operational assurance, which will be provided by TfNSW in the context of the Cabinet's next consideration of TAHE later in the year.

About TAHE

The NSW state accounts have reported TAHE as a public sector non-financial corporation (PNFC) since 2015, owning all formerly RailCorp 'heavy' rail assets, including trains, tracks, property and other infrastructure.

This budget accounting treatment allows capital grants and depreciation expenses for rail assets to be structured beyond the reported 'surplus/deficit' position reported in the NSW budget each year.

The *Transport Administration Amendment (Transport Entities) Act 2017* created a legislative basis for TAHE, but remained unproclaimed until June 2020, reflecting a requirement to further define what TAHE will do in practice – and how it and other related arrangements can support fundamental transport outcomes.

Budget policy requires that TAHE 'stand up' on 1 July 2020 – but Cabinet has mitigated potential risks by ensuring TAHE's transitional period sees arrangements replicate those in place on 30 June 2020.

Cabinet will consider TAHE's long-term operating arrangements later in the year, with the benefit of deeper analysis and assessment against Cabinet's objectives.

TAHE & accounting standards

Changing accounting standards are a fundamental reason that an agreed TAHE operating model has remained elusive.

In 2014, the relevant accounting standards required a risk/revenue transfer to sustain treatment as a PNFC. This saw TAHE contemplated as a 'passive' asset owner with little practical control over rail – or impact on transport governance and delivery.

The emergence of new accounting standards in 2018 incorporated a revised test of control that may challenge the broader TAHE operating model design and its relationship with the general government sector. This is logically challenging in the context of safe, efficient transport service delivery – and introduces a range of potential challenges, gathered around:

- Control and accountability for integrated, multi-modal customer services/journeys;
- Control and management of access for rail freight customers, including access pricing;
- Control of long-term transport network planning;
- Control, prioritisation and coordination of major projects, including across modes;
- Control, prioritisation and coordination of minor projects, including across modes;
- Control, prioritisation and coordination of O&M funding, including across modes;
- Coordination and prioritisation of capital and O&M funding, including across modes;

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- Coordination and control of transport operations, including across modes; and
- Accountability for safe, integrated service operations within rail.

The history of structural reform in NSW and other comparable railways provide several relevant cautionary examples, where these accountabilities were not effectively allocated.

TfNSW will provide an independent safety opinion or assessment to support Cabinet's consideration of long-term operating models later in the year.

Safety considerations in structural reform of railways

Recent history shows two main drivers for structural change in railways in NSW and comparable global jurisdictions. Broadly, these can be characterised as:

- 1) Structural changes that respond to financial drivers; and
- 2) Structural changes that respond to rail accidents.

For context, a select history of structural change in NSW railways is provided below.

History of NSW railways

1996: Structural separation and corporatisation of NSW railways

- Competition policy sees NSW railways split into four entities, being:
 - **State Rail Authority (SRA):** Passenger rail service operator;
 - **Freight Rail Corporation (FreightCorp):** Freight rail service operator;
 - **Rail Access Corporation (RAC):** Rail network access manager; and
 - **Rail Service Authority (RSA):** Separate operator and maintainer.

2000 - 2001: Special Commission of Inquiry into the Glenbrook Rail Accident

- Following the Glenbrook and other rail accidents, the inquiry found fractured accountabilities had contributed to lax safety and operational performance, recommending:
 - Merge the Rail Access Corporation (RAC) and Rail Service Authority (RSA);
 - Move responsibility for service planning and timetables from RAC to the SRA;
 - Appoint a 'Coordinator General of Rail' to remove interfaces between rail agencies created in 1996;
 - Appoint an independent safety regulator to make rail agencies accountable; and
 - Strengthen civil and criminal accountabilities for safety.

2001: Rail access and track maintenance re-aggregated

- The NSW Government announces a partial restructure of rail agencies, which sees:
 - RAC and RSA are abolished in favour of the new 'Rail Infrastructure Corporation' (RIC)

2003: Waterfall rail accident occurs

2004: All rail services are reintegrated in 'RailCorp', bar safety regulation

- The NSW Government forms RailCorp, reintegrating all functions split in 1996 to address ongoing safety issues;
- RailCorp is an independent SOC governed by a Board; and

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- The independent safety regulator, ITSRR, is formed to separately assure safety culture and performance in rail.

2005: Special Commission of Inquiry into the Waterfall Rail Accident

- The Waterfall inquiry reaffirmed the Glenbrook inquiry findings making further recommendations including:
 - Detailed emergency response training, single point of operational command and direct connections to emergency services;
 - Substantially enhanced accountabilities for risk identification, management and ensuring correct documentation and computerised record keeping;
 - Drive control over safety decisions; and
 - Board accountability for safety.

2009: De-corporatisation of NSW railways

- A desire for greater accountability and control over costs, on-time running, ticketing and other policy and operational aspects sees RailCorp moved from the PNFC to the General Government Sector – constituted as a statutory authority; and
- Reports to Minister for Transport.

2011: Rail becomes controlled by TfNSW

- NSW Government policy sees further change, with Transport NSW replaced in most respects by Transport for NSW (TfNSW); and
- RailCorp becomes a 'controlled entity' of TfNSW.

2013: TfNSW assumes greater control over projects and operations

- All RailCorp functions allocated between TfNSW and two rail operators, Sydney and NSW Trains;
- TfNSW assumes control of capital project approval and planning; and
- RailCorp becomes largely an accounting entity with very limited functions and resources.

2020: TAHE's creation sees corporatisation and structural separation return to NSW railways

- The 'stand up' of TAHE as an independent SOC sees a return of corporatisation; and
- Key issues of functional control and legal accountability subject to further advice, prior to Cabinet decision.

Importantly, the structural models considered in this paper have not yet been subject to any independent safety consideration or assurance.

Independent safety opinion or analysis will be provided by TfNSW's experts, as part of the Cabinet's next consideration of TAHE's long-term operating model later in the year.

Case studies

Two case studies have been developed, providing high-level insights to errors in previous reforms to NSW and UK railways in recent decades.

These are found in *Appendix 3 – Safety case studies*.

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ABS classification risk

The genesis of TAHE is rooted in the 2012 notification of the ABS's intention to reclassify RailCorp from being a PNFC to a GGS entity as it did not recover a significant amount of its expenses from revenue, and did not charge market prices for access to its assets. This risk remains present for TAHE, and the operational, organisational and fiscal architecture of the models contemplated in this report seek to mitigate this risk.




Developing agreed objectives

Noting the importance of an agreed position between the Transport cluster and NSW Treasury, our engagement commenced with a workshop to define and agree on joint project objectives, which are outlined below.

Senior NSW Treasury, TfNSW and RailCorp officials were involved in the workshop – inputting to each objective – and agreeing on the wording of each.

These objectives served an important function as a series of 'filters' by which to assess the efficacy and appropriateness of potential long-term operating models for TAHE, and have subsequently been adopted in the NSW Cabinet Submission that governs the next phase of work on TAHE.

Figure 1: TAHE agreed objectives

 Fiscal	 Organisational	 Operational
<ul style="list-style-type: none">• Meet accounting standard requirements, by 1 July 2020.• Sustain the accounting treatment, over time.• Maintain PNFC classification from the ABS:<ul style="list-style-type: none">– For-profit: TAHE– Not-for-profit: ST and NSW	<ul style="list-style-type: none">• Support TfNSW's 'Evolving Transport' long-term operating model• Support a long term model that improves the management of assets, commerciality, and transparency of the use of public funds• Facilitate the integration of networks, services and project planning, across modes and with a customer focus• Allow future reform to rail service delivery models• Account for the TAHE Board's duties and corporate objectives	<ul style="list-style-type: none">• Maintain and enhance safe network operations• Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators

Developing high-level TAHE operating models

TAHE has been under periodic consideration since 2014, with many different potential options and functions considered over that time.

Contemplating a new, independent and statutory entity within a heavily regulated 'live rail' environment is complex and will impact effectively every aspect of transport planning, funding and safe service delivery.

Not surprisingly, this sees a challenge whereby different stakeholders held a different conception of what TAHE might be, once it moves into an operational phase – often reflecting an array of prior TAHE operating model options.

'TAHE Pure'

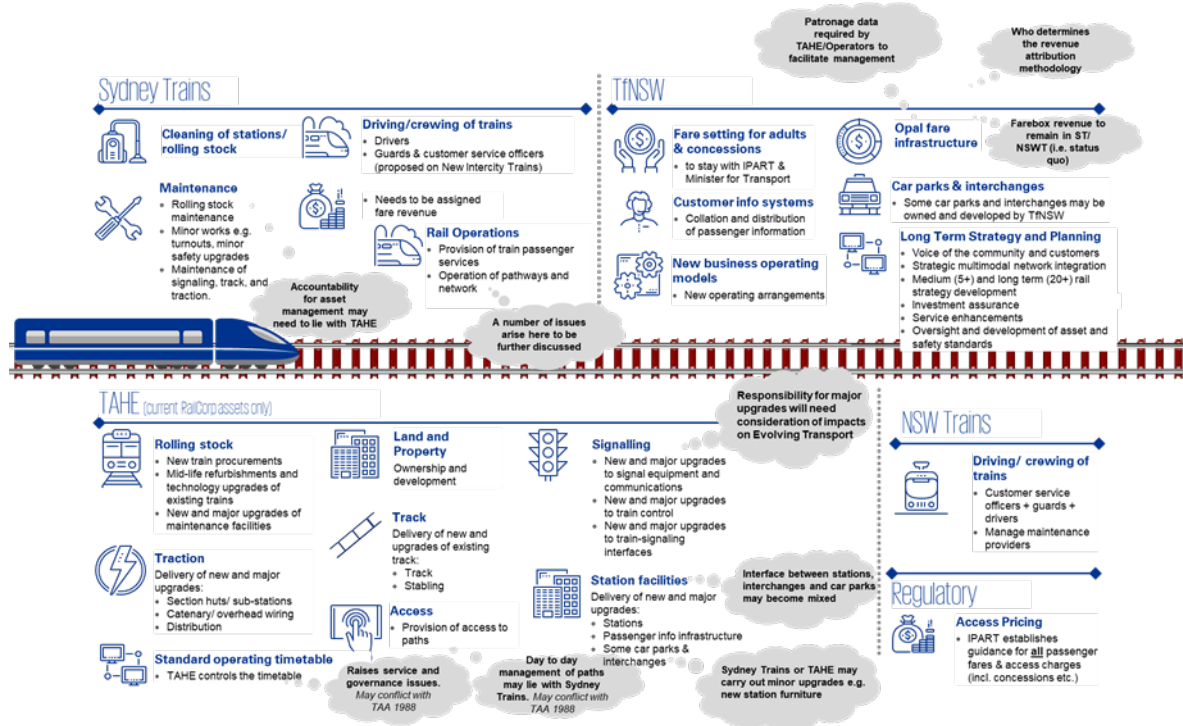
To overcome the challenge of 'multiple TAHEs' across different stakeholders, we developed a purely theoretical TAHE operating model – which we called '**TAHE Pure**'.

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TAHE Pure segments functional roles between TAHE and transport agencies, based on uncustomised and blunt application of the relevant accounting standards to rail transport.

TAHE Pure served as a consistent representation of how the rail sector could operate, once TAHE is fully operational. In this sense, TAHE Pure never formed an option for implementation – but instead served an important role providing a single and consistent basis for rapid consultations concerning policy, safety, operational, planning and fundamental control issues facing TAHE and transport agencies.

Figure 2: Demarcation of key functions under 'TAHE Pure'



Themes identified for resolution in consultations

Asset accountability: Some stakeholders raised the control of asset accountability under a model where asset owners, operators and maintenance are split.

Evolving Transport: Evolving Transport fundamentally seeks to place the 'customer at the centre' of TfNSW's strategy – moving away from mode-specific agencies for road and rail services – in favour of geographic, cross-modal functional alignments. In introducing TAHE, the ability to move capital and investments across modes is unresolved.

Investment decisions (control of capital programme): Prioritisation of investment decisions was raised, particularly concerning the fragmentation of medium and long-term planning.

Interface between operations and infrastructure: There is a lack of clarity on how funds flow from TAHE to rail operators to fund activities such as maintenance and the tension between this and investment decisions on infrastructure.

Operational control: Clarity is needed on who has the power to direct the network. How the standard operating timetable is used and at what level needs to be determined.

Return of capital: The flow of returns, or dividends, to the crown and TfNSW needs to be determined.

Accountabilities of the TAHE Board: Questions regarding the ability of the Board to discharge their duties while there is a disconnect between responsibility and accountability needs to be overcome.

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Access agreements: The price-setting arrangements for existing public transport rail operators (for network access) needs to be determined. Including the constraints on TAHE in setting prices, and balancing this against the need for TAHE to recover its costs over time.

Sustainability of model: The sustainability of the accounting and governance model of trains need to be detailed, including what happens if a Board is set up for rail operators – how the directors are bound and the constraints it operates under.

TfNSW budget control: With uncertain funds flows resulting from TAHE, the issues of TfNSW setting and controlling their budget needs to be determined.

Value for money: How value for money and contestability are achieved under this arrangement needs to be resolved.

Workforce: Where TAHE staff come from needs to be settled, as well as the expected staffing footprint.

Legislative change: The extent of legislative change required is yet to be fully articulated.

Safety: The safety implications of introducing additional interfaces, and potentially moving away from a vertically integrated model need to be understood.

Developing workable TAHE options

Using these limited consultation inputs across transport agencies, we distilled two high-level operating models for TAHE; with each seeking to address the fundamental challenges posed by TAHE. These options are:

- 1) **'TAHE Real'**
- 2) **'TAHE for NSW'**

These options were tested with key transport officials to understand any new challenges or interfaces created – and to understand where transport outcomes might be improved, under a TAHE operating model.

Each was then assessed against the joint project objectives, and subject to financial analysis using the limited model provided by NSW Treasury.

'TAHE Real'

'TAHE Real' seeks to bring coordination between TAHE and the rest of the Transport cluster through two coordination units relating to infrastructure investment decision making and network operations – two of the major issues raised during consultations. TAHE Real seeks to retain as much of the tenor of Evolving Transport as possible, but recognising the splitting away of rail asset ownership from the Transport cluster.

Accordingly, TAHE Real seeks to mitigate the identified challenges through the creation of two functional alignments – termed as 'coordination units' spanning both operations and capital funding.

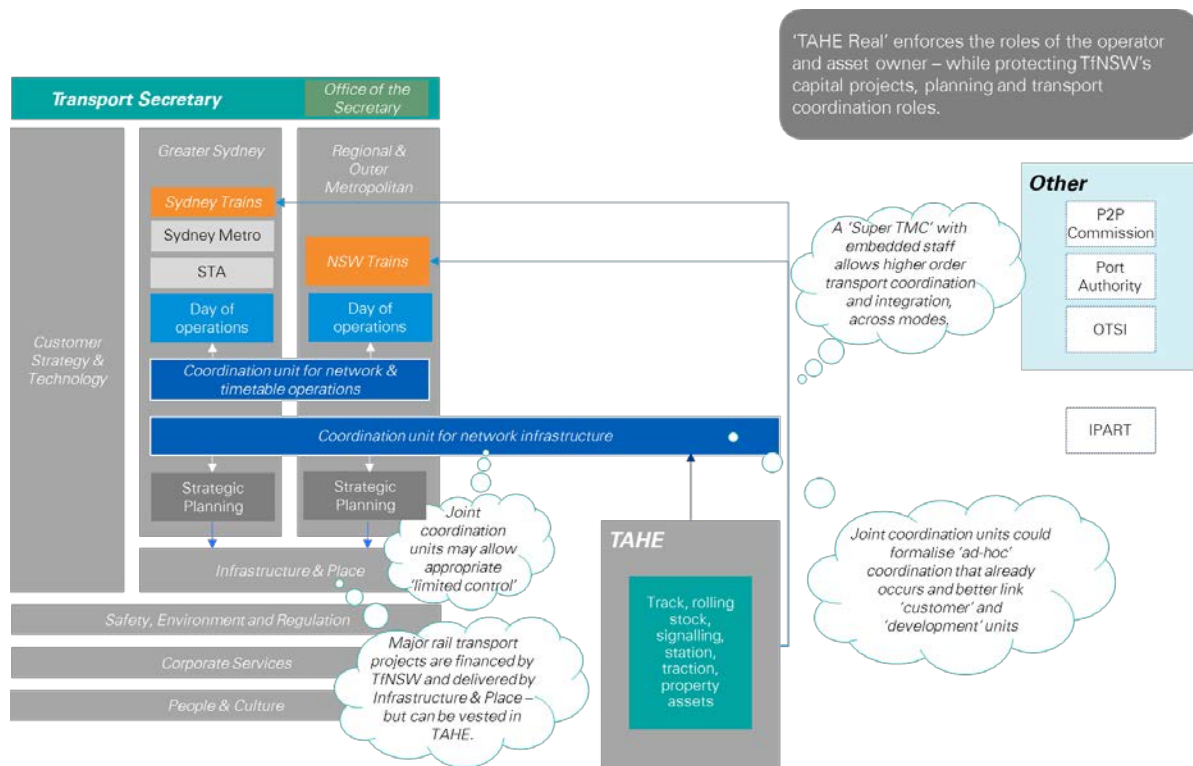
Accounting advice provided to NSW Treasury and the TAHE Board has provided TfNSW with comfort that defined 'business rules' can be used to specify accountabilities and guide outcomes; without risking a determination of accounting 'control' under the relevant accounting standards.

These functional alignments – shown in the blue boxes in Figure 3 below – are contemplated to introduce appropriate business rules to allow coordination in daily operations; and coordination in long-term network and service planning.

Noting the very short time-frame provided for this initial analysis, no work has been done to define what these business rules will cover or how they will operate – which will be the subject of the next phase of work beyond this report.

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Figure 3: 'TAHE Real'



'TAHE for NSW'

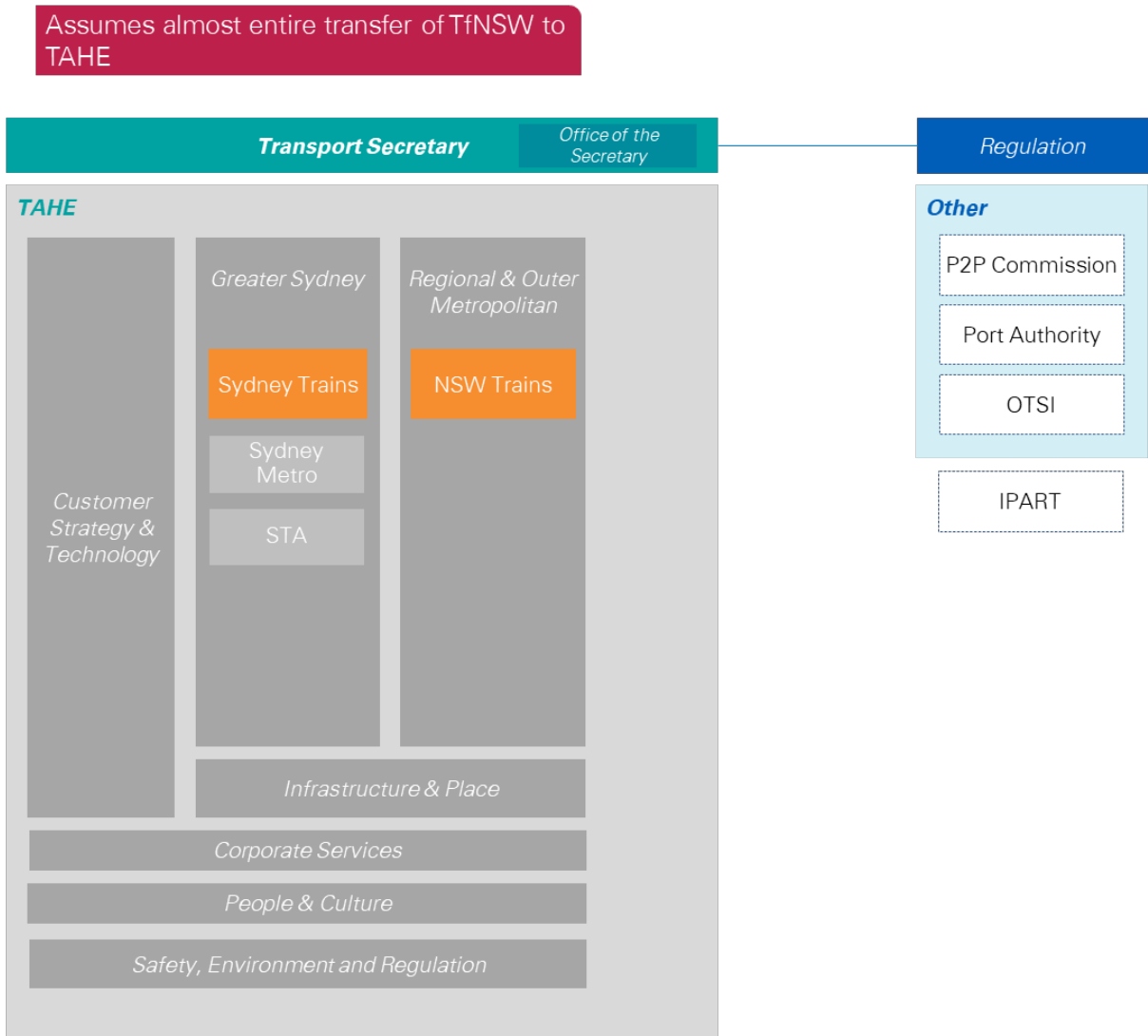
We also developed a second high-level option, which seeks to redress the fundamental challenge of fragmentation caused by TAHE, by including effectively all transport functions within TAHE – beyond independent regulatory functions, that could remain in a vestigial general government sector transport agency.

This option is much more fundamental, but done well it would offer an opportunity to substantially increase the transparency and accountability of transport functions, via corporatisation of most or all of TfNSW's existing functions.

Interestingly, this option performed the strongest in NSW Treasury's financial model – and fundamentally addresses coordination challenges by placing TAHE's 'hard border' around TfNSW itself.

Whether this option is feasible or desirable remains to be seen, but TAHE's broad legislation appears to allow broader contemplation of TAHE's end-state – and may provide opportunities to better align TAHE's creation to transport, as well as fiscal policy objectives.

Figure 4: 'TAHE for NSW'



High-level assessment of TAHE models




























All three models have been analysed and assessed against the agreed objectives, to test their suitability for further detailed development during the next phase of work. The results of that assessment are shown in the table below. Keeping in mind that TAHE Pure serves as a device to draw out issues, the assessment suggests that TAHE Real and TAHE for NSW merit a deeper consideration as a part of the further work required to operationalise TAHE.

Table 1: High-level assessment against agreed objectives

Key: Green = likely to meet the objective, Orange = requires further investigation, Red = unlikely to meet the objective

Organisational	TAHE Pure	TAHE Real	TAHE for NSW
Support TfNSW's 'Evolving Transport' long-term operating model	<div></div>	<div></div>	<div></div>

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Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds			
Facilitate the integration of networks, services and project planning, across modes with a customer focus			
Allow future reform to rail service delivery models			
Account for the TAHE Board's duties and corporate objectives			
Operational		Rating	
Maintain and enhance safe network operations			
Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators			
Fiscal		Rating	
Meet accounting standard requirements, by 1 July 2020			
Sustain the accounting treatment, over time			
Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSWTF)			

Initial financial assessment of TAHE models

Scenario assessments using a high-level model (the 'Model'), developed for NSW Treasury, have been undertaken by KPMG to assess the financial impact to government from implementing the identified TAHE options.

The Model incorporates the following simplifications:

- An asset write-down of 50 per cent, incurred upon transfer of assets between GGS and TAHE to reflect that TAHE may not be able to generate sufficient cashflows to justify an asset valuation at depreciated replacement cost.
- A commercial rate of return of 3 per cent on TAHE's assets.
- A return of 90 per cent of TAHE's profits back to the Crown.

The extent of this reduction will vary based on the assumptions around any potential write-down of assets in TAHE (and the resultant reduction in depreciation expense), and the dividend payout ratio. The Model draws upon forward estimates of capital and recurrent expenditure from NSW Treasury's PRIME system.

The financial impact assessment has been undertaken for each option relative to a historical baseline, which assumes that TAHE is not stood up but also *assumes that no changes in accounting standards occur*.

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The outputs are based on a series of assumptions including a transition pathway to a TAHE 'end state' (noting that this is not yet fully defined) where all funds flow and arrangements are fully implemented.

The impact of no policy change

The financial impact assessment indicates that without action, the financial impact associated with the change in accounting standards would be \$1.8b per annum in 2020-21, increasing to \$2.2b by 2026-27. These impacts would continue in perpetuity.

Table 2: Impact on the budget result relative to historical baseline – no policy change (\$m)

	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Change in GGS expenditure	2,000	2,200	2,200	2,300	2,400	2,400	2,500
Change in GGS budget position	(1,800)	(1,900)	(1,900)	(2,000)	(2,100)	(2,100)	(2,200)

The change in GGS expenditure mirrors the change in the budget position, with only a small offset accrued from the recognition of legacy RailCorp revenues being incorporated into the GGS budget outcome.

Financial impact of TAHE Real

The standing up of TAHE has the potential to reduce the general government sector financial impact. The transfer of legacy RailCorp's heavy rail assets to TAHE avoids the impact of the depreciation from these assets falling onto the GGS budget outcome.

However, to sustain this outcome, an increase in GGS expenditure is required to fund the access fee revenues that the train operators, Sydney Trains and NSW TrainLink, would need to pay to TAHE, and possibly CSO payments should the access fee revenues fall short, to sustain TAHE commercially. The Model indicates implementation of TAHE Pure increases GGS expenditure in the order of \$2 billion per annum.

The net impact of these expenditures is eased by the return of TAHE free cashflow back to the Crown as well as National Tax Equivalent Regime (NTER) payments and Government Guarantee fee (GGF) payments from TAHE.

Based on the current assumptions in the Model, these receipts would be in the order of \$800m annually, reducing the financial impact on the Budget result to around \$1.2b annually.

Table 3: Impact on the budget result relative to historical baseline – with TAHE Real (\$m)

	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Change in GGS expenditure	-	1,800	1,800	2,000	2,000	2,100	2,100
Change in GGS budget position	-	-	(1,200)	(1,200)	(1,200)	(1,300)	(1,300)

Financial impact of TAHE for NSW

Under the TAHE for NSW option, the Model encompasses additional revenues including the transfer of the motor vehicle registration taxes, other user charges currently received concerning activities associated with the legacy RMS and all farebox revenue.

The analysis does not consider increases in GGS expenditure that would be expected to implement such a wide-ranging reform and change.

Relative to TAHE Real, the incorporation of other Transport cluster elements, most notably legacy RMS, results in a range of temporary revenue and cost impacts. These impacts dissipate beyond the forward estimates period, with the Model projecting a longer term increase of \$1.2b in GGS expenditure.

Based on current assumptions in the financial model the adverse impact to the Budget Result is in the order of \$0.5b to \$0.7b annually.

Table 4: Impact on the budget result relative to historical baseline – with TAHE for NSW (\$m)

	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Change in GGS expenditure	-	-	(1,700)	(500)	200	800	1,200
Change in GGS budget position	-	-	(700)	(600)	(500)	(600)	(700)

Next steps – refining a long-term TAHE operating model

Following this report and the high-level identified options - based on consultations with a limited number of TfNSW and Treasury stakeholders – a more detailed analysis will follow in the next few months to report back to Cabinet in October.

We will revisit the identified TAHE options and assess any other ‘hybrid’ model(s) that can meet Cabinet’s organisational, operational and fiscal/financial objectives. The next steps include:

- **Safety opinion:** With the constrained timeframe involved in providing the initial high-level advice in this report, the critically important issue of safety has not received the focus required. In developing the detailed models in the next phase of TAHE development, safety considerations will be paramount. Once the models are developed, an expert safety opinion will be sought, and any necessary sign-offs will be obtained prior to any model being recommended.
- **In-depth operational design:** We will work with TfNSW to design and refine clear, real-world operating models for each identified option.

We will define the functional specification of each TAHE option – what each option controls, owns, decides and operates – and design the business rules needed to meet the operational and organisational objectives determined by the Cabinet.

- **Detail organisational design:** TfNSW is mid-way through the most fundamental change to transport operations and governance in NSW’s history; through ‘Evolving Transport’.

Evolving Transport fundamentally seeks to place the ‘customer at the centre’ of TfNSW’s strategy – moving away from mode-specific agencies for road and rail services – in favour of geographic,

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cross-modal functional alignments. Without careful consideration and customisation, TAHE would have consequences on the Cabinet's agreed cluster-wide structural and service reforms.

With the functional and operational structure and resourcing of TAHE resolved – and initial 'business rules' developed under each option, we will define the resource profile (e.g. resourcing need and the implications of each model on budget, investment, and the existing entities such as TfNSW) and implications of each option and their alignment with 'Evolving Transport'.

- **Robust financial modelling and impacts:** the next phase of work will provide a more sophisticated financial model which will allow the capability to understand the impacts on various PNFC and GGS entities – and the likely fiscal impacts.

This means that the development of a detailed and robust financial model, including a DCF, is a foundation stone of our approach. This model will allow TfNSW and NSW Treasury to have confidence in articulating the financial impacts of each option.

- **Extended stakeholder consultation:** All the above steps will be undertaken in conjunction with extended stakeholder engagement across every step of the process to inform and uncover any potential problems or opportunities ahead of Cabinet in October.

Limitations to our work

This work provides initial, high-level observations and has faced a number of timing and informational limitations that will be resolved in the next round of work to advise the NSW Cabinet. Key limitations impacting this report include:

- **Financial model:**

Limitation: Due to the urgency of this engagement, we were limited to using the very high level financial model developed by NSW Treasury; which includes simple assumptions, hard coding and a range of other limitations.

Resolution: In our next scope of work we will develop a sophisticated financial model for TAHE to better understand its impacts on the NSW Budget and TfNSW.

- **Draft accounting advice:**

Limitation: This initial high-level option analysis has been undertaken in advance of the completion of key accounting advice, being led by NSW Treasury. This means that several key aspects remain unclear at this point.

Resolution: We understand that complete accounting advice will be provided by the end of July 2020, informing the next work on the operating model.

- **No safety assurance.**

Limitation: As a safety regulated industry, any operating model will require a high level of assurance that the chain of accountability is maintained. The analysis in this paper has not had the benefit of any safety opinion.

Resolution: TfNSW will provide appropriately qualified personnel to provide an opinion on safety matters to satisfy Cabinet's questions in this area.

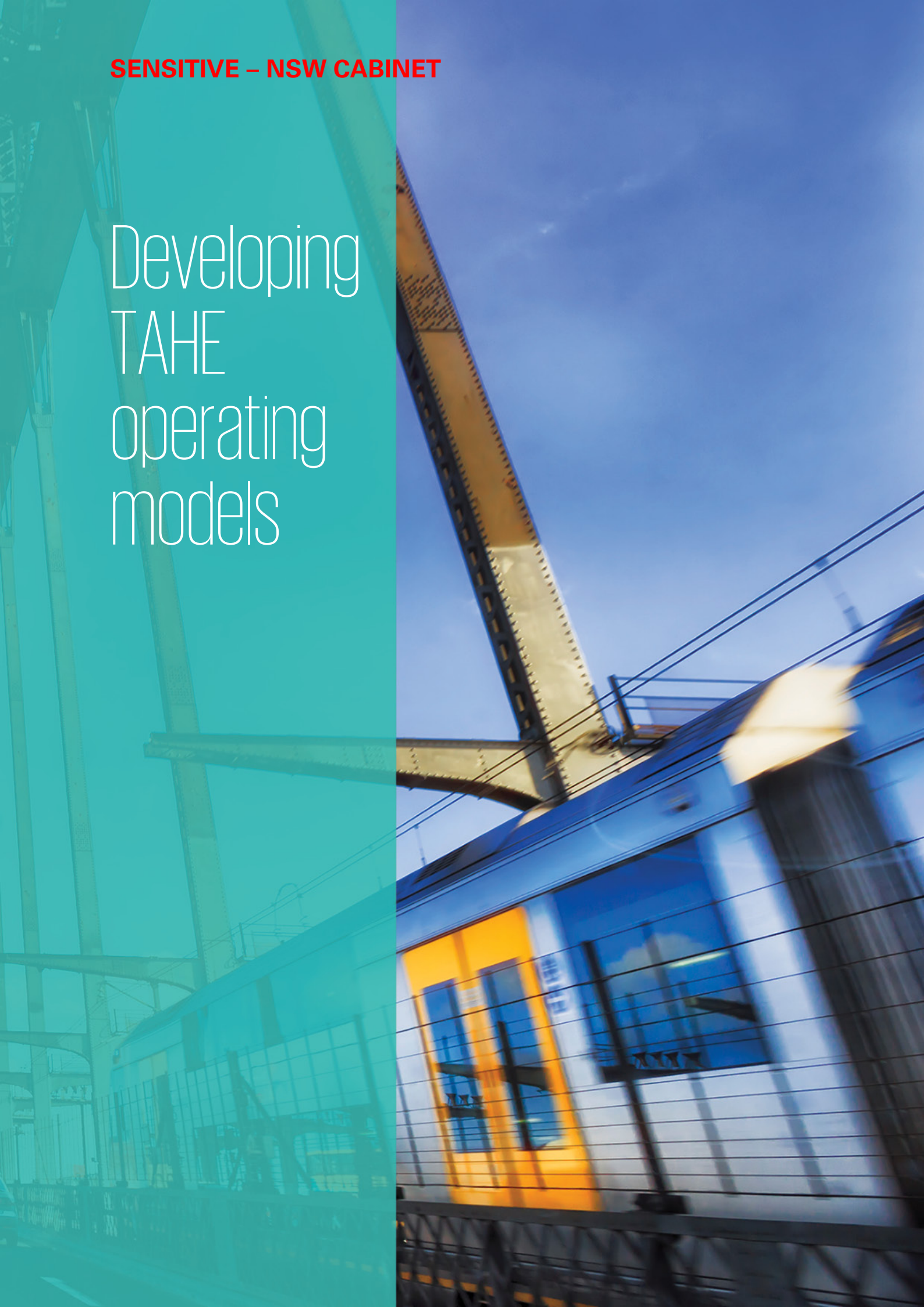
- **Limited consultations:**

Limitation: The limited time allowed for this engagement and the sensitivity of the subject matter meant that we had limited access to very senior stakeholders across TfNSW and its agencies, in some cases limiting the granularity of inputs.

Resolution: With the benefit of more time and the proclamation of TAHE, our work will benefit from deeper insights and broader perspectives – allowing a more thorough interrogation of TAHE operating models.

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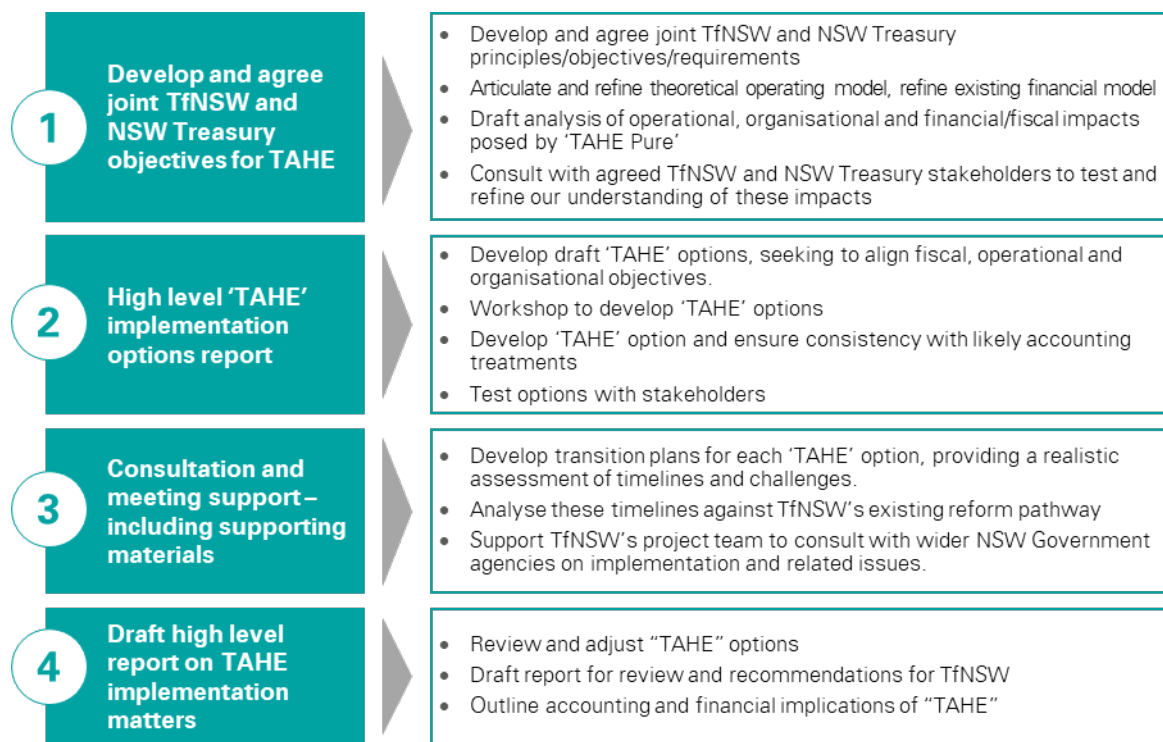
Developing TAHE operating models



Our approach

During this initial rapid assessment, our approach targeted getting agreement early on objectives, developing the high-level options to test the objectives against, consulting with stakeholders to test the options, and then delivering this report. Figure 5 below provides detail on our approach.

Figure 5: Our approach



Given the time constraints, and the sensitive nature of this work, our initial consultations were targeted and narrow – focussing on transport. We sought to speak with the most critical stakeholders, who would allow us to test the options and draw out the salient issues. These consultations included:

- Elizabeth Mildwater (Deputy Secretary, Greater Sydney, TfNSW);
- Peter Regan, (Deputy Secretary, Infrastructure and Place, TfNSW);
- Fiona Trussell (then Chief Transformation Officer, TfNSW) and Anne Hayes (then Deputy Secretary, Corporate Services, TfNSW);
- George Roins (legal counsel, TfNSW);
- Peter Crimp, (Executive Director, Sydney Trains);
- Brenda Hoang (Chief Finance Officer, TfNSW); and
- Peter Perdikos (TAHE Project Director, TNSW).

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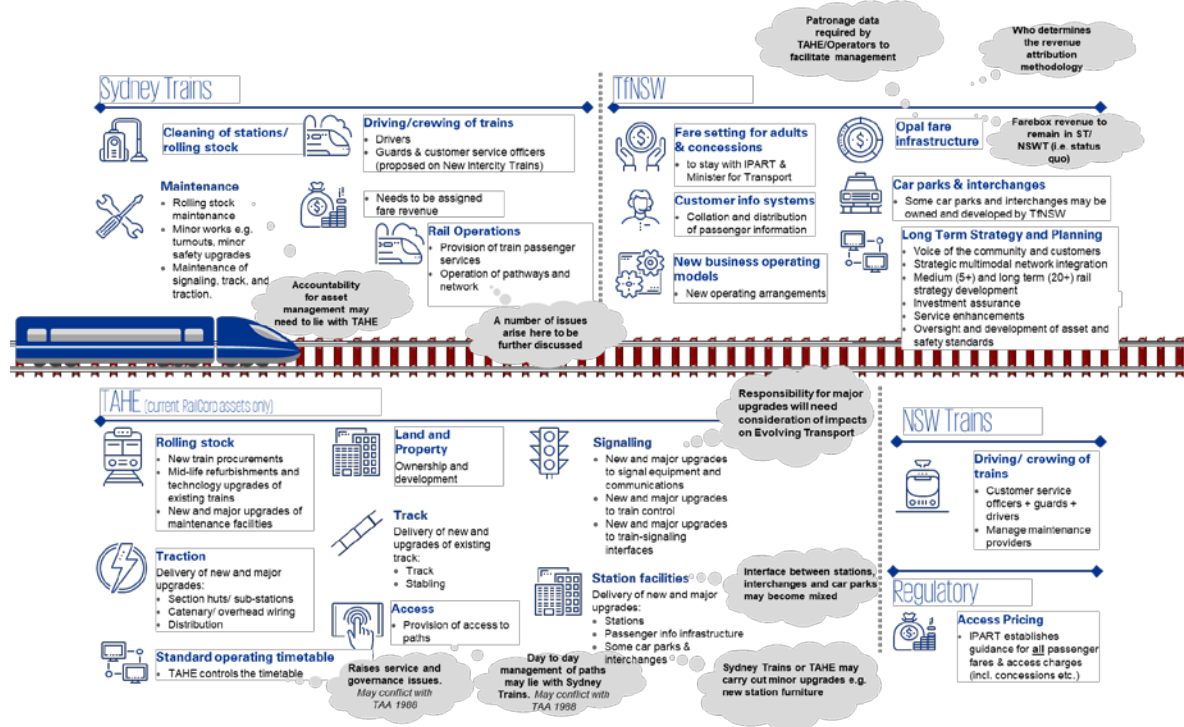
TAHE Pure'



What is 'TAHE Pure'?




'TAHE Pure' is a functional representation of a 'pure' or non-customised application of TAHE, shown in Figure 6. This functional representation has been used to undertake consultations to identify areas of concern for core stakeholders in transport.

Figure 6: TAHE Pure



Functional description

Figure 7: Functional description of entities

 'TAHE Pure'	 Transport for NSW	
<ul style="list-style-type: none"> Governed by a fiduciary board and legislation; Owns all 'RailCorp' assets (e.g. trains, tracks, stations and land etc.); Controls access and pricing for rail operators; Controls the capital funding of rail projects; Embedded on the coordination unit for network infrastructure; and Controls land and may control property development. 	<ul style="list-style-type: none"> Long-term planning; and Sets customer fares (no change). 	<ul style="list-style-type: none"> May need a fiduciary board; Operate rail services, stations etc.; Undertakes minor maintenance activities, funded by TAHE; Collects passenger fares; and Pay TAHE access charges.

Issues with 'TAHE Pure'

Table 5: Issues needing to be resolved before TAHE implementation

Issue	TfNSW perspective	Rail Operator perspective
Asset accountability: Some stakeholders raised the control of asset accountability under a model where asset owners, operators and maintenance are split.	Maintaining vertical integration is key, particularly from a safety but also from an accountability point of view.	The rail operators need a mechanism, or level of assurance, that crucial maintenance will occur on assets they are not accountable for but rely on for safe operations.
Evolving Transport: The ability to move capital and investment across modes is unresolved.	Evolving Transport is the core strategy for TfNSW. The ability to deliver multi-modal, customer-centric transport operations must be maintained.	Clear direction is required on how rail operations will coordinate with other modes under a TAHE model
Investment decisions (control of capital programme): Prioritisation of investment decisions was raised, particularly concerning the fragmentation of medium and long-term planning.	TfNSW needs to retain control over medium and long term network planning.	Prioritisation is important to rail operators primarily concerning crucial network maintenance vs more commercially attractive investment by TAHE.
Interface between operations and infrastructure: There is a lack of clarity on how funds flow from TAHE to rail operators to fund activities such as maintenance and the tension between this and investment decisions on infrastructure.	Clarity on how TfNSW fits within this interface is needed, including what level of control they can exert.	Rail operators will need certainty on network maintenance investment.
Operational control: Clarity is needed on who has the power to direct the network. How the standard operating timetable is used and at what level needs to be determined.	TfNSW will require the ability to direct the network when needed, including retaining control of the standard operating timetable.	Rail operators ultimately need to have a level of control over their operations. How timetabling works under the TAHE model needs to be further articulated.
Return of capital: The flow of returns, or dividends, to the crown and TfNSW needs to be determined.	In the context of funds flowing back to TfNSW (for network planning etc.), this need to be determined.	With rail operator paying TAHE for rail access, the flow of funds (for maintenance etc.) back to the network from TAHE needs to be clear.
Accountabilities of the TAHE Board: Questions regarding the ability of the Board to discharge their duties while	The extent to which TfNSW can put constraints of TAHE actions needs to be clear.	Accountabilities on rail operations, in particular regarding safety, need to be determined.

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Issue	TfNSW perspective	Rail Operator perspective
there is a disconnect between responsibility and accountability need to be overcome.		
Access agreements: The price-setting arrangements for existing public transport rail operators (for network access) need to be determined. Including the constraints on TAHE in setting prices, and balancing this against the need for TAHE to recover its costs over time.	TfNSW's role in access arrangements needs to be articulated, including any role in price regulation and governing access agreements.	The price for network access for rail operators cannot be prohibitive to operations. How this access charge will be paid for by the operators will need to be clarified.
Sustainability of model: The sustainability of the accounting and governance model of trains need to be detailed, including what happens if a Board is set up for rail operators - how the directors are bound and the constraints it operates under.	The governance role TfNSW plays within these models needs to be robust and defined.	The PNFC status of rail operators needs to be maintained. Any fundamental structural changes need to be understood before implementation.
TfNSW Budget control: With uncertain funds flows resulting from TAHE, the issues of TfNSW setting and controlling their budget needs to be determined.	Funds flow to TfNSW under a TAHE model needs to be determined so that TfNSW can set their internal budget. Disruption to this during a transition period could result in disruptions to service delivery.	Any flow-on impacts from TfNSW budget control issues for rail operators need to be understood.
Value for money: How value for money and contestability are achieved under this arrangement needs to be resolved.	How TfNSW is expected to ensure public funds are achieving value for money need to be documented.	The expectations on rail operators regarding procurement guidelines and expenditure of funds needs to be well understood.
Workforce: Where TAHE staff come from needs to be settled, as well as the expected staffing footprint.	The extent (if any) to which TfNSW staff will be transferred to TAHE needs to be detailed.	Any impact to rail operator staffing from the TAHE implementation also needs to be detailed.
Legislative change: The extent of legislative change required is yet to be fully articulated.	TfNSW needs an understanding of any legislated accountabilities that will be transferred.	Rail operators need an understanding of any legislated accountabilities that will be transferred.

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TAHE Pure: Objective assessment




Table 6: TAHE Pure vs agreed objectives

Key: *Green* = likely to meet the objective, *Orange* = requires further investigation, *Red* = unlikely to meet the objective

Organisational	Rating
Support TfNSW's 'Evolving Transport' long-term operating model	
Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds	
Facilitate the integration of networks, services and project planning, across modes with a customer focus	
Allow future reform to rail service delivery models	
Account for the TAHE Board's duties and corporate objectives	
Operational	Rating
Maintain and enhance safe network operations	
Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators	
Fiscal	Rating
Meet accounting standard requirements, by 1 July 2020	
Sustain the accounting treatment, over time	
Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSW)T)	

'TAHE Pure': Organisational objectives

Table 7: TAHE Pure vs agreed organisational objectives

Organisational	Rating
Support TfNSW's 'Evolving Transport' long-term operating model	
Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds	
Facilitate the integration of networks, services and project planning, across modes with a customer focus	

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Allow future reform to rail service delivery models



Account for the TAHE Board's duties and corporate objectives



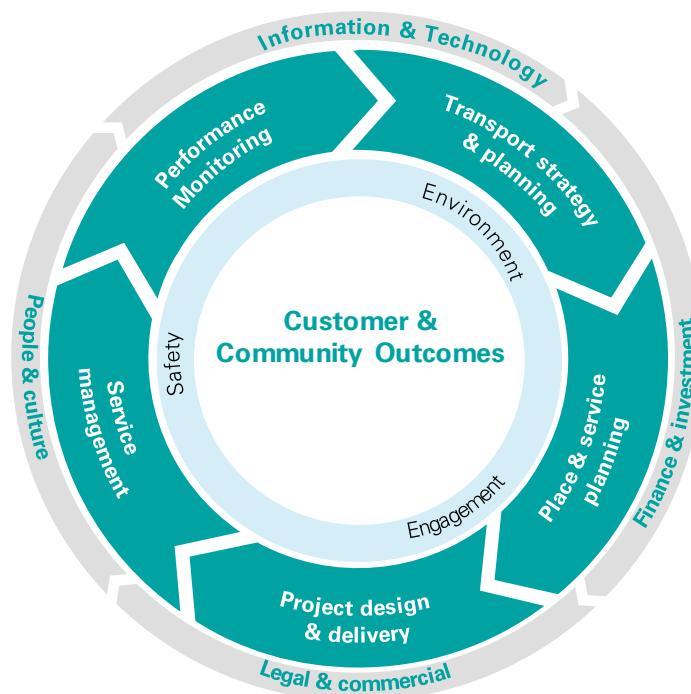
Does 'TAHE Pure': Support TfNSW's 'Evolving Transport' long-term operating model?

No.

TAHE Pure is inconsistent with 'Evolving Transport', with TAHE Pure's effect the separation of control and accountability of rail; while Evolving Transport is fundamentally seeking to drive alignment, integration and higher-level coordination across all modes for capital and operating costs and performance.

In practice, Evolving Transport is seeking to create accountabilities for integrated mobility (Figure 8) and fulfil the role of 'placemaker' responsible for integrated land use and transport planning to activate public spaces, corridors and networks for the benefit of the community.

Figure 8: Macro-Level TfNSW Value Chain



Does 'TAHE Pure': Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds?

No.

The hypothetical TAHE Pure has the potential to fragment accountability for the management of assets; development and exploitation of commercial opportunities and may reduce transparency and accountability for the allocation of public funds to rail infrastructure projects.

TAHE's fiduciary structure and control of the reinvestment of access fee revenue flows to the network sees a functional disconnection of asset management accountability and practical separation between the funding and the network.

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One of the key challenges of the TAHE model overall is the requirement to demonstrate a 'pathway' to profitability.

TAHE Pure is most unlikely to improve the management of assets; noting that it creates a firm structural separation between the rail operators, transport policy and management, and asset investment decisions.

Does 'TAHE Pure': Facilitate the integration of networks, services and project planning, across modes with a customer focus?

No.

TAHE Pure envisages the ceding of control over the standard working timetable to TAHE, which would require legislative changes to the Transport Administration Act 1988. This would run the risk of repeating the modal independence over service planning; a structure that frustrated the early 2000s attempts at integrated ticketing (ERG).

While the basis and direction of long-term network planning are established in the Future Transport 2056 and Sydney's Rail Future, TAHE Pure's control over expenditure decisions sets the scene for substantial divergence at a project prioritisation level.

There is also a potential for the objectives of TAHE Pure to misalign potential service or customer-focused reforms; for example, the conversion of an extant rail corridor to 'metro' operations would serve to reduce TAHE Pure's asset base, budget and control – potentially setting the scene for misalignment.

Does 'TAHE Pure': Allow future reform to rail service delivery models?

Yes.

TAHE Pure requires either public PNFC customers and/or private rail operators, meaning that service franchising could occur within the TAHE Pure scenario.

Does 'TAHE Pure': Account for the TAHE Board's duties and corporate objectives?



No.

One of the principal challenges of TAHE Pure is that the creation of unfettered and normal director's duties could conceivably sit uncomfortably astride operational or policy requirements.

Their duties to safeguard the best interests of the corporation (and not the shareholder) set the scene for conflict in a range of areas.

Operational

Table 8: TAHE Pure vs agreed objectives

Operational	Rating
Maintain and enhance safe network operations	
Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators	

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Does 'TAHE Pure': Maintain and enhance safe network operations?

Maybe.

Under TAHE Pure the ability to maintain and deliver safe network operations is potentially compromised by misaligned objectives, fragmented accountabilities and the practical disconnection between investment need and capital allocation by TAHE's Board.

This sees misaligned objectives between TAHE, the asset owner and procurer; and the operators, responsible for maintenance and operations – where investment or procurement decisions could potentially detriment the ability to maintain the network safely and efficiently.

Does 'TAHE Pure': Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators?

No.

TAHE Pure contemplates control of the standard working timetable; access charges and slots; the prioritisation of rail projects; and the money needed to fund them.

Read together, this sees TfNSW unable to control where, what or how capital is invested; or even control its costs through rail subsidies which will effectively be set by TAHE's timetabling powers.




Similar to maintenance and safety, operational performance is related to the asset maintenance and renewal programme, which could be compromised given commercial conflicts between TAHE board and the operators. One example of the illogical accountabilities could arise in a context of capital prioritisation disagreements between TAHE's board and Sydney Trains.

If Sydney Trains were unable to achieve a safe level of funding to maintain infrastructure, remedies including speed limitations, service reductions or at worst service suspensions would be a logical response – reducing the productivity of the timetable and overall transport network and diminishing the ability to satisfy customer requirements.

Fiscal

As previously outlined, TAHE Pure represents the future state of what would happen if TAHE was implemented 'as is' without due consideration for 'on the ground'.

Table 9: Fiscal objectives

Fiscal	Rating
Meet accounting standard requirements, by 1 July 2020	
Sustain the accounting treatment, over time	
Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSW)T)	

The three objectives have a level of interdependency and have been addressed separately to assist with high-level evaluation in the context of this report.

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Does 'TAHE Pure': Meet accounting standard requirements, by 1 July 2020?

Yes – based on completion of current work.

This objective refers to the need to address the potential risk presented by the new accounting standard applicable in 2019-20 i.e. the new revenue standard (AASB 15). In the context of rail, this means ensuring that farebox revenue remains with rail operators.

We understand that such activities are well progressed, and as such, this objective is likely to be achieved regardless of which TAHE model is selected. Accordingly, this objective is "Green" in the case of a hypothetical TAHE Pure model. That said, it is critical that these key activities are finalised and in a way that continues to support the achievement of the objective.

Does 'TAHE Pure': Sustain the accounting treatment, over time?

Maybe – subject to further work.

Sustaining the accounting treatment requires:

- Maintaining any mitigations implemented to address the potential risk posed by new accounting standards; and
- Ongoing progress towards implementation of a for-profit PNFC TAHE, which supports the maintenance of PNFC status and current treatment of equity injections into RailCorp/TAHE by the General Government Sector.

More specifically, activity regarding new standards entails:

- Structuring TAHE arrangements relating to TAHE to effectively mitigate any risks currently presented by AASB 1059 and AASB 16 (and by any other future potential changes to reporting frameworks); and
- Supporting current and future accounting positions and treatments with robust evidence to satisfy stakeholders, including the NSW Audit Office in future years (as well as any other AASBs issued after the date of this report).

An example of structuring is that the operating licence needs to continue to be carefully developed to appropriately balance the desired operational oversight and protections of the TfNSW with the need for TAHE to be able to discharge its legislated functions, with a view to accounting outcomes that align with the State's fiscal strategy.

Demonstrating progress on TAHE implementation for 1 July 2020 entails:

- Proclamation of TAHE as a SOC, creation of a corporate constitution, and establishment of a majority independent TAHE Board, in accordance with the SOC Act;
- "Switching on" TAHE via an operating licence, thereby allowing decisions relating to the operation of TAHE to be made by, or under the authority of the board, in accordance with the functions and authority conferred on it by the operating licence; and
- Commencing the transition to the application of the NSW Treasury's Commercial Policy Framework to TAHE.

Simply put, TAHE has to be "stood-up" by 1 July 2020 to satisfy this objective. On 1 July 2020, TAHE will be implemented under a Transitional Operating Model, and this approach provides flexibility to accommodate a final TAHE business model, based on a preferred option. The TAHE Transitional Operational Model replicates current RailCorp operations to the greatest extent possible.

In future years, ongoing progress, reflective of the final operating model, will be required.

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Does 'TAHE Pure': Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSW)?

Maybe – subject to future developments.

To satisfy this objective, TAHE Pure will need to ensure that TAHE, Sydney Trains and NSW Trains are all PNFC entities, with TAHE required to demonstrate a transition pathway to for-profit status.

The criteria for PNFC status is set out within the Australian Bureau of Statistics 2015 publication 'Australian System of Government Finance Statistics: Concepts, Sources and Methods' (ABS GFS Manual). A principles-based approach is applied when determining whether an entity satisfies PNFC criteria. PNFC classification requires all of the following:

- Limited GGS intervention;
- Determination that an entity is a market producer; and
- Confirmation of an entity being a separate institutional unit in its own right (which is assumed to exist and not explored).

Because the ABS adopts a principles-based approach as it examines factors relevant to PNFC classification, there are no bright lines for individual criterion or indicators.

Having regard to the PNFC criteria, there are various attributes of any TAHE model scenario that indicate continued work will be required to ensure the PNFC criteria of the relevant entities.

Sustaining the required ABS classification of each of the relevant entities will require significant focus to continue to demonstrate that GGS intervention in TAHE is limited. Demonstrating that retained rights of TfNSW's are protective in nature and/or pre-determined will support this outcome, as will application of Treasury's Commercial Policy Framework. It will also be important to demonstrate a pathway to increased TAHE commerciality.

Limited GGS intervention

"Limited Government intervention" in this circumstance can be considered partly analogous to the accounting concept of 'control' under AASBs. 'Control' is defined as a practical ability to exercise decision-making rights. However, the definition of control excludes:

- Protective rights, commonly retained by Governments to protect the public interest (e.g. ensure safety); and
- Pre-determined rights e.g. setting up a desired outcome.

If TAHE is deemed to be "controlled" by TfNSW, it could be seen as having a higher level of GGS intervention, thereby placing the risk on its PNFC status. Under TAHE Pure, it is assumed that TfNSW control is limited, thereby increasing the likelihood that this objective can be sustained over time.

The extent of government support can also constitute government intervention. Community Service Obligation (CSO) payments are a form of Government funding paid to government-owned businesses. It is envisaged the CSO payments delivered to both Sydney Trains and NSW Trains acts as a form of 'top-up funding' for TAHE, as it allows the rail operators meet its ongoing payments for use of TAHE's infrastructure assets. No CSO payments to TAHE are assumed under TAHE Pure as the top-up funding delivered to rail operators is expected to be sufficient to meet its payments to TAHE.

There is not a single definitive measure as to the level of CSO funding being assessed as limited or major Government intervention. Rather, this assessment is subjective and therefore careful structuring and consideration of the final funds flow under TAHE Real will be required to achieve the desired outcomes.

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Market producer

CSOs also play a part as to an entity's 'market producer' determination. The concept of a 'market producer' as defined by the ABS as follows:

- What proportion of total production costs are covered by total sales?
- What government interventions are in place to influence the supply of goods/services?
- Does the producer compete with other providers and/or is the consumer's choice of provider influenced by government interventions?

The rail operators' primary purpose is the day-to-day operations and delivery of rail services to the general public. In return, the operators will earn farebox revenue (i.e. user charges from rail passengers). The combination of farebox revenue and CSO payments, in turn, allow sufficient funds for the operators to meet its access fee expenses with TAHE. A high ratio of CSO payments to user charges can signify government intervention, depending on how the CSO is structured.

If the rail operators do not meet the market producer status, their PNFC status is at risk. If the rail operators are not PNFC, this, in turn, creates a risk to TAHE's PNFC status.

For-profit TAHE status

For-profit status of TAHE indicates that the government shareholder can reasonably expect a sufficient return, which supports treatment by the GGS of injections of equity into TAHE. It is a matter of judgement as to whether a reasonable expectation is present and what constitutes a sufficient return. There is also judgement when considering the period over which a return is expected. The nature of the business will influence these judgements.

The final determination of TAHE's profitability is subject to the final funds flow (flows themselves and quanta) between TfNSW, TAHE and the rail operators. Determining any final funds flow will be an iterative process due to the interdependencies across various entities.

Illustrative fiscal impact of TAHE Pure

The fiscal impacts discussed below focus on the impact at the GGS level. These impacts represent anticipated changes to the current Budget Forward Estimates as a result of implementing TAHE Pure and assume that any fiscal risks referred to previously have been mitigated.

The anticipated impacts on the GGS have been modelled based on the flow of funds illustrated in Figure 9 below and assumptions as directed by TfNSW which are set out in Appendix 1. The funds flow represents our initial and current understanding of the arrangements that will be in place once full implementation has occurred. There are limitations to the illustrative impacts:

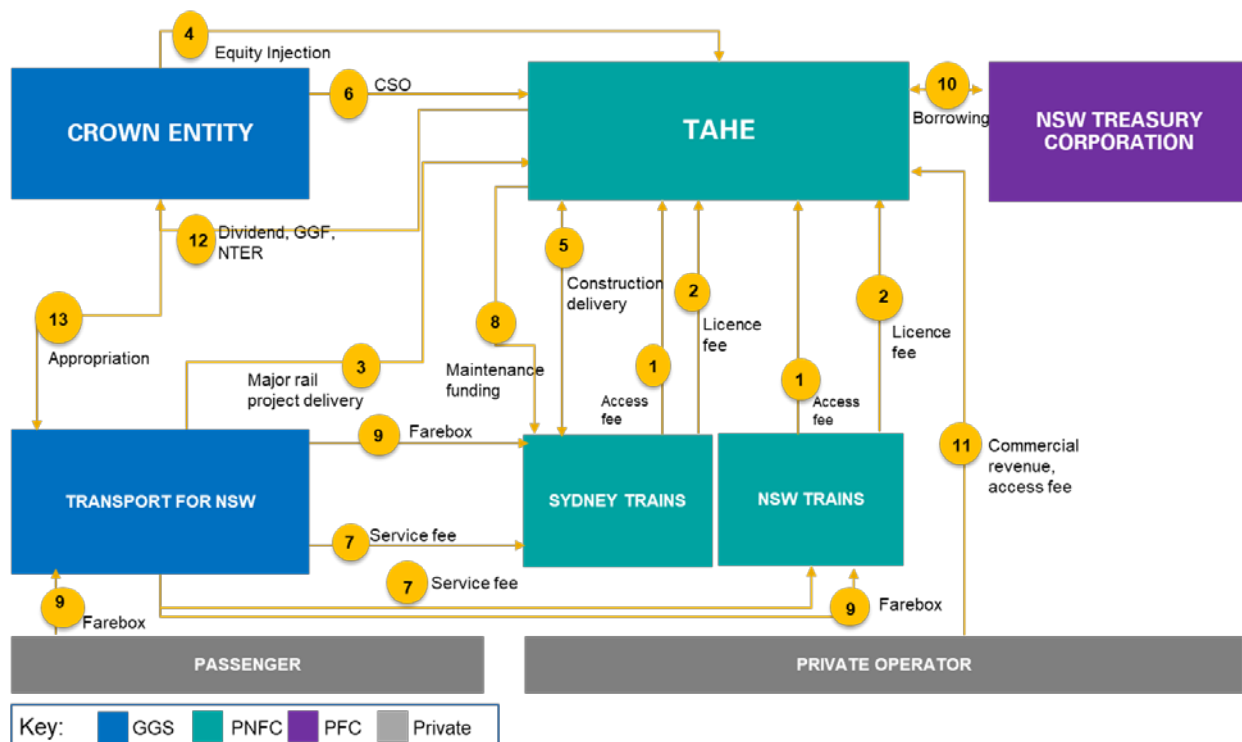
- Arrangements would be subject to review and based on government directions during the implementation period;
- Underlying flow and amount of these funds flows may alter; and
- Assumptions are expected to be iterated and refined during implementation.

In essence, if there are any changes to funds flows or amounts, then variation to the fiscal impacts outlined below would be expected. As such, impacts at this stage are illustrative. Where implementation is deferred, illustrative impacts can be assumed to also occur in later years.

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Funds flow

Figure 9: TAHE Pure funds flow



Assumptions regarding these fund flows are further explored in Appendix 1

Impacts

Summary: Notwithstanding an expectation of adverse impacts upon the State's budget result and GGS expenditure as a result of implementing TAHE Pure, should implementation not occur, a larger adverse impact on the Budget Result is expected.

The Model indicates implementation of TAHE Pure increases GGS expenditure once all funds flows are in place. The impact is in the order of \$2 billion per annum once fully implemented based on current assumptions in the financial model. This occurs mainly because the scenario contemplates a significant increase in the payment TfNSW is required to make the operators via the State budget process. This additional payment ensures the operators have sufficient funding to pay access fees to TAHE for access to rail network assets.

A Community Service Obligation (CSO) from Government would be required where access or license fees are not at the level TAHE would otherwise commercially undertake the provision of assets to operators. The impact of the CSO would have the same effect on GGS expenditure as additional payments by TfNSW to the operators.

The GGS Budget Result is also expected to be adversely impacted by the TAHE Pure scenario but not to the same extent as the impact on GGS expenditure. This reduced impact is due to the receipt of Dividends, National Tax Equivalent Regime (NTER) payments and Government Guarantee fee (GGF) payments from TAHE as revenue into the GGS.

Based on the current assumptions in the financial model, receipts will be in the order of \$800m annually, reducing the adverse impact on the budget result to around \$1.2bn annually. The extent of this reduction will vary based on the assumptions around any potential write-down of assets in TAHE (and the resultant reduction in depreciation expense), and the dividend payout ratio.

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Illustrative outputs

The outputs below illustrate the expected impact of TAHE Pure on GGS expenditure and the GGS Budget Result to 2026-27. The outputs are based on a series of assumptions including a transition pathway to a TAHE 'end state' (noting that this is not yet fully defined) where all funds flow and arrangements are fully implemented. It has been assumed that the full implementation of TAHE Pure would likely take only two years, which may not eventuate. In the interim, all existing funds flows are likely to remain.

Table 10: TAHE Pure illustrative outputs

\$m	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Increase in GGS expenditure	-	-	1,800	1,800	2,000	2,100	2,100
Impact on the budget result							
Favourable/(unfavourable)	-	-	(1,200)	(1,200)	(1,200)	(1,300)	(1,300)

Key modelling assumptions

The illustrative fiscal impacts above are based on outputs of the financial model. The financial model is premised on significant assumptions, some of which are outlined below. If these assumptions do not hold, significant variation in financial outcomes would be expected. Further work is required to confirm and validate these assumptions. Some of the key assumptions include:

- The value of TAHE rail assets will be written down based on a discounted cash flow valuation methodology. It is currently assumed a 50% write-down will occur across all assets held;
- TAHE will enter into a fee for service agreement with TfNSW for the delivery of capital projects (funds flow consistent with current arrangements and accounting treatment);
- TAHE will receive access fees from operators for access to rail assets, or a Community Service obligation from the government where access or license fees are not at the level TAHE would otherwise commercially undertake the provision of assets to operators. It is currently assumed access fees are set at levels which allow TAHE to provide a return to the GGS;
- Access arrangements between TAHE and the operators do not give rise to leases under AASB16 or service concessions under AASB 1059;
- Farebox revenue will continue to be recognised as revenue by the operators;
- TAHE will source borrowings through the NSW Treasury to achieve a target gearing ratio over time; and
- TAHE will be subject to the NSW Treasury Commercial Policy Framework and be required to pay a dividend, NTER and Government Guarantee fee.

Further detail, including additional steps to confirm and validate these assumptions, are disclosed in Appendix 1.

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'TAHE Real'

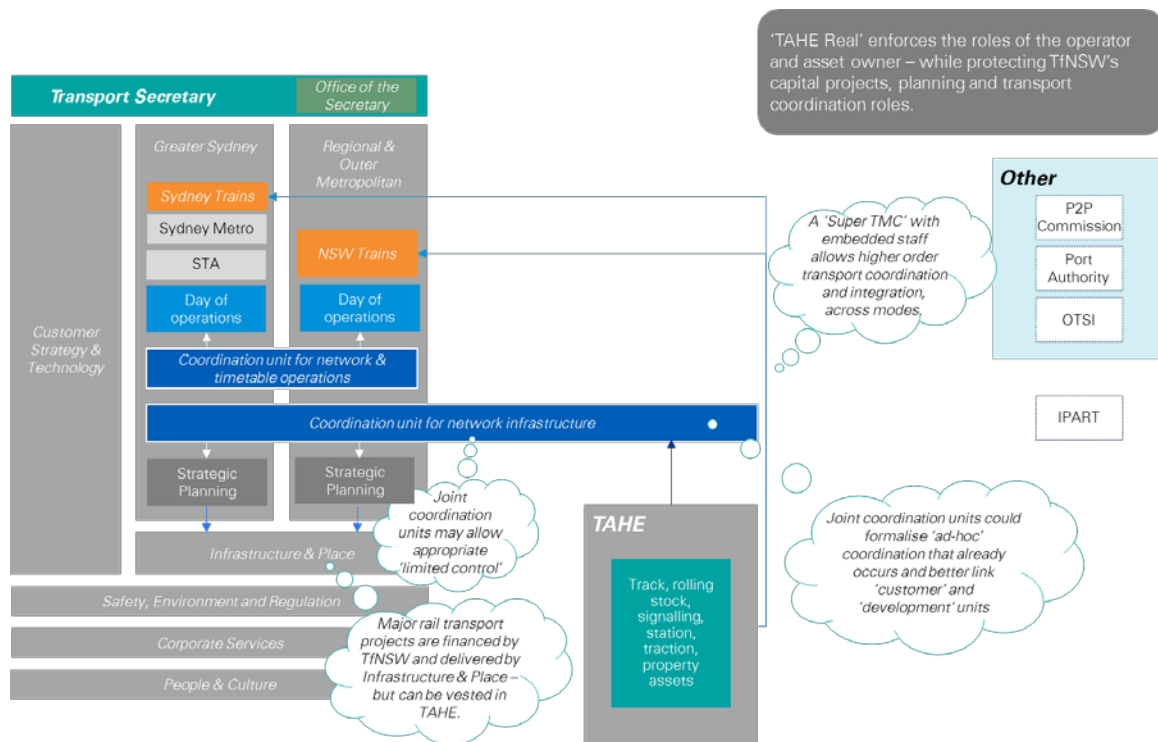


'TAHE Real'

'TAHE Real' seeks to bring coordination between TAHE and the rest of the Transport cluster through two coordination units relating to infrastructure investment decision making and network operations – two of the major issues raised during consultations. TAHE Real seeks to retain as much of the tenor of Evolving Transport as possible, but recognising the splitting away of rail asset ownership from the Transport cluster.


Accordingly, TAHE Real seeks to mitigate the identified challenges through the creation of two functional alignments – termed as 'coordination units' spanning both operations and capital funding.

Figure 10: TAHE Real



Functional description

Figure 11: Functional description of entities

'TAHE Real'	 Transport for NSW	
<ul style="list-style-type: none"> • Governed by a fiduciary board and legislation; • Owns all 'RailCorp' assets (e.g. trains, tracks, stations and land etc.); • Controls access and pricing for rail operators; • Controls the capital funding of rail projects; • Embedded on the coordination unit for network infrastructure; and • Controls land and may control property development. 	<ul style="list-style-type: none"> • Coordinates transport operations, via a new 'super TMC' unit; • Coordinates project prioritisation across modes via a new coordination unit for network infrastructure; • Determines the standard working timetable for rail operators, and all other services; • Determines and funds major rail projects, later vested in TAHE Real; • Long-term planning; and • Sets customer fares (no change). 	<ul style="list-style-type: none"> • Operate rail services, stations etc.; • Embedded in the coordination unit for networks & timetables; • Undertakes minor maintenance activities on behalf of and funded by TAHE; • Collects passenger fares (no change); and • Pay TAHE access charges.

Change one: Coordination Unit - Networks & Timetables

The introduction of an integrated, functional network and timetable coordination function with TfNSW is contemplated to redress the potential fragmentation of operational accountabilities posed by 'TAHE Pure'. This operational coordination unit is envisaged along the lines of a 'Super TMC'; comprising rail and other modes. This would allow a high degree of coordination between and across modes for operational aspects.

It is important that this can be constructed as 'transport coordination' rather than 'rail asset control' by TfNSW. Subject to further analysis and definition, this could conceivably allow:

- TfNSW to specify the standard working timetable for rail – allowing coordination between modes;
- Allow TfNSW to adopt different timetables in response to network operational needs, e.g. special events; and
- A single, integrated operational response centre to provide overall transport coordination, across modes.

Change two: Coordination unit for network infrastructure

The coordination unit for network infrastructure is contemplated as a mechanism to manage the potential for misalignment between TfNSW, the rail operator and TAHE capital investment priorities.

A key desire of Evolving Transport is the aim to provide an integrated view on optimising capital and operational expenditure and prioritising this expenditure appropriately; principally by being able to allocate available funding on a rational basis. For the first time, TfNSW under Evolving Transport

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has the opportunity to make these decisions considering all modes, all customer needs, all community needs – and Transport’s long-term capital priorities contemporaneously.

The coordination unit for network infrastructure would continue to draw upon the planning functionalities and delivery functionalities of Greater Sydney, Regional & Outer Metropolitan and Infrastructure & Place. To provide TAHE and the operators with a sufficient level of control over their assets and operations, the coordination unit would embed staff from TAHE and the operators with TfNSW to maximise opportunities to collaborate in real-time on strategy, planning, option development, business case development, configuration, operationalisation and the like – not only on rail matters – but also concerning matters that involve other modes and services. This embedding is critical – not only to avoid past instances of policy siloing and the inability to transfer accountability to different divisions – but to develop a new culture of planning to create seamless journeys for customers and to consider the whole of life implications of creating and managing long life rail assets.

In many respects, coordinated network development itself would simply formalise arrangements on the heavy rail network, for example, Sydney Trains staff embed within TfNSW for the development and delivery of certain *More Trains More Services* initiatives and actively coordinate specifications and requirements on many other rail-related initiatives with TfNSW.

Under this model, governance arrangements between the different entities will be important in managing their potentially conflicting objectives. Potential arrangements that may need to be considered include:

- Ensuring that future investment decisions are well aligned with agreed existing as well as future iterations of medium-term rail and transport strategies;
- Monitoring this alignment through an independent investment and configuration assurance process overseen by TfNSW, and INSW for high-risk high-value projects; and
- Implementing working group and executive-level committees, with membership drawn from all relevant entities, to check that major proposed investments are capable of aligning with the requirements of each entity.



Under any TAHE model, a significant degree of protection and oversight over TAHE is afforded via the various mechanisms of the “SOC Toolkit” that underpins the establishment of TAHE as a SOC. Such key mechanisms include:

- The ability for the portfolio minister to give a direction to the board of TAHE (which is facilitated by the TAHE enabling legislation);
- The ability of the shareholders to give a direction to the board of TAHE (which is facilitated by the SOC Act, and governed by NSW Treasury); and
- The agreement of a TAHE Statement of Corporate Intent – agreed between the SOC and the shareholders on an annual basis, following Treasury’s Commercial Policy Framework.









TAHE Real: Objective assessment

Table 11: TAHE Real vs agreed objectives

Key: *Green* = likely to meet the objective, *Orange* = requires further investigation, *Red* = unlikely to meet the objective






Organisational	Rating
Support TfNSW’s ‘Evolving Transport’ long-term operating model	
Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds	

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Facilitate the integration of networks, services and project planning, across modes with a customer focus	
Allow future reform to rail service delivery models	
Account for the TAHE Board's duties and corporate objectives	
Operational	Rating
Maintain and enhance safe network operations	
Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators	
Fiscal	Rating
Meet accounting standard requirements, by 1 July 2020	
Sustain the accounting treatment, over time	
Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSW)	

'TAHE Real': Organisational objectives

Table 12: TAHE Real vs agreed organisational objectives

Organisational	Rating
Support TfNSW's 'Evolving Transport' long-term operating model	
Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds	
Facilitate the integration of networks, services and project planning, across modes with a customer focus	
Allow future reform to rail service delivery models	
Account for the TAHE Board's duties and corporate objectives	

Does 'TAHE Real': Support TfNSW's 'Evolving Transport' long-term operating model?

Maybe – subject to future developments.

The two coordination units are a functional response to the structural challenge posed by TAHE Pure's impacts on operating and capital prioritisation and coordination. These units will apply business rules to define clearly the line of control, in addition, the coordination unit will enable better dialogue

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and coordination of strategy, allowing TfNSW to achieve overall transport outcomes through effective and thorough coordination. In the event of any conflict, the aforementioned 'SOC toolkit' mechanisms do provide a significant degree of protection and oversight.

In practice, this will rely on the careful, detailed design of business rules (consistent with the operating licences etc.) to govern each actor within each coordination unit, but also navigate the accounting and fiscal parameters and can withstand scrutiny over time.

Does 'TAHE Real': Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds?

Maybe – subject to future developments.

The coordination unit for network infrastructure ensures TfNSW and TAHE can regularly collaborate and align on transport planning activity to meet customer outcomes through asset delivery.

Does 'TAHE Real': Facilitate the integration of networks, services and project planning, across modes with a customer focus?

Maybe – subject to future developments.

Under TAHE Real, responsibility for the standard working timetable moves from TAHE to TfNSW. This addresses the issue of coordination across modes and providers; and is likely to also allow TfNSW to determine a large degree of its rail service operating costs, which are simplistically factor of services operated.

The TAHE Real scenario would see major projects controlled by TfNSW under current arrangements; with the asset vested in TAHE on completion.

The potential for divergent priorities between the TAHE, the rail operators, and the general government sector / TfNSW is contemplated as being managed through business rules and the 'SOC toolkit', to resolve any divergent corporate and public interest objectives.

Does 'TAHE Real': Allow future reform to rail service delivery models?

Yes.

TAHE Real requires either public PNFC customers and / or private rail operators, meaning that service franchising could occur within the TAHE Real scenario.

Does 'TAHE Real': Account for the TAHE Board's duties and corporate objectives?


Maybe – subject to future developments.

An ability to acquit a sensible allocation of responsibilities between the two proposed public sector corporations will largely influence the governance reach of TAHE's directors.

While almost any business rules may be contemplated to retire these risks, these will need to navigate the accounting and fiscal parameters and withstand scrutiny over time. This is a current issue, given the contemplation of new operating licenses to enable the 1 July 2020 'switch on'.

Operational objectives

Table 13: TAHE Real vs agreed objectives

Operational	Rating
Maintain and enhance safe network operations	

Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators



Does 'TAHE Real': Maintain and enhance safe network operations?

Maybe – subject to future developments.

As discussed in the objectives above, TAHE Real seeks to use functional integration and clear business rules to resolve risks to safe network operations.

Does 'TAHE Real': Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators?

Maybe – subject to future developments.

As discussed in the objectives above, TAHE Real seeks to use functional integration and clear business rules to resolve risks to safe network operations.

The introduction of the coordination units reduces siloing, allowing for greater coordination of activities between entities on the day to day operations, and investment in the rail network.

This unit structure may be modelled as a Transport Management Centre or a Cargo Coordination Movement Centre. The Cargo Movement Coordination Centre (CMCC) was established in 2014 and works with road carriers, rail operators, stevedores and related supply chain stakeholders to maximise the use of existing network capacity and continuously improve the efficiency of cargo movement through Port Botany, Port Kembla and regional NSW.

In this model, the joint coordination unit provides a function that coordinates strategic and day-to-day activities – but this role needs to be defined and tested to navigate the accounting and fiscal control parameters.

It is conceivable that these functional arrangements would formalise much of what currently occurs and opportunities to improve the existing interfaces across multi-modal transport.

Fiscal

TAHE Real Scenario will provide similar fiscal and financial outcomes to the TAHE Pure scoring against objectives:

Table 14: TAHE Real vs agreed objectives

Fiscal	Rating
Meet accounting standard requirements, by 1 July 2020	
Sustain the accounting treatment, over time	
Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSW)	

Does 'TAHE Real': Meet accounting standard requirements, by 1 July 2020?

Yes – based on completion of current work.

The application of the new revenue standard does not alter between TAHE Pure and TAHE Real.

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Does 'TAHE Real': Sustain the accounting treatment, over time?

Maybe – subject to future developments.

Post 1 July 2020, as a result of the additional organisational and operational coordination mechanisms provided under TAHE Real, TAHE will transition to a model where there is greater coordination of network operations and development between TfNSW and the PNFC entities.

This aims to allow TfNSW having the required level of visibility and harmonisation of the NSW transport network (i.e. multi modes). It is important that whatever activities TfNSW will be involved with under TAHE Real, that these activities do not contravene the aforementioned PNFC criteria of limited Government intervention by a GGS entity.

Also, continuing to navigate the 'control' requirements under all relevant accounting standards (including those applicable in 2020-21 for the first time) will be necessary to balance maximum oversight and co-ordination capabilities for TfNSW without encroaching into 'control' accounting parameters that would yield divergence from the State's fiscal strategy.

As highlighted in the Next Steps, we believe any risks can be managed and a balance between operational requirements and fiscal objectives be achieved.

Does 'TAHE Real': Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSWT)?

Maybe – subject to future developments.

Matters discussed in TAHE Pure have application to TAHE Real. Where TAHE Real diverges from Pure also raises further consideration. TAHE Real provides TfNSW continued oversight and co-ordination abilities concerning the provision of transportation services. As such, there is the potential for risk to TAHE's PNFC classification. This risk can be mitigated via careful structuring of TfNSW rights are not carefully structured to ensure that TfNSW is not being seen to control TAHE. As highlighted in the Next Steps, we believe this risk can be managed and a balance between operational requirements and fiscal objectives be achieved.

All other risks (remaining PNFC classification matters and accounting treatments) noted under TAHE Pure are identical and remain relevant to the TAHE Real option.

Illustrative fiscal impact of TAHE Real

The illustrative fiscal impacts of TAHE Real are expected to be identical to TAHE Pure. As previously discussed, these impacts were modelled based on the flow of funds illustrated in Figure 9 and assumptions as directed by TfNSW which are set out in Appendix 1.

Table 15: TAHE Real illustrative outputs

\$m	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Increase in GGS expenditure	-	-	1,800	1,800	2,000	2,100	2,100
Impact on the budget result							
Favourable/(unfavourable)	-	-	(1,200)	(1,200)	(1,200)	(1,300)	(1,300)

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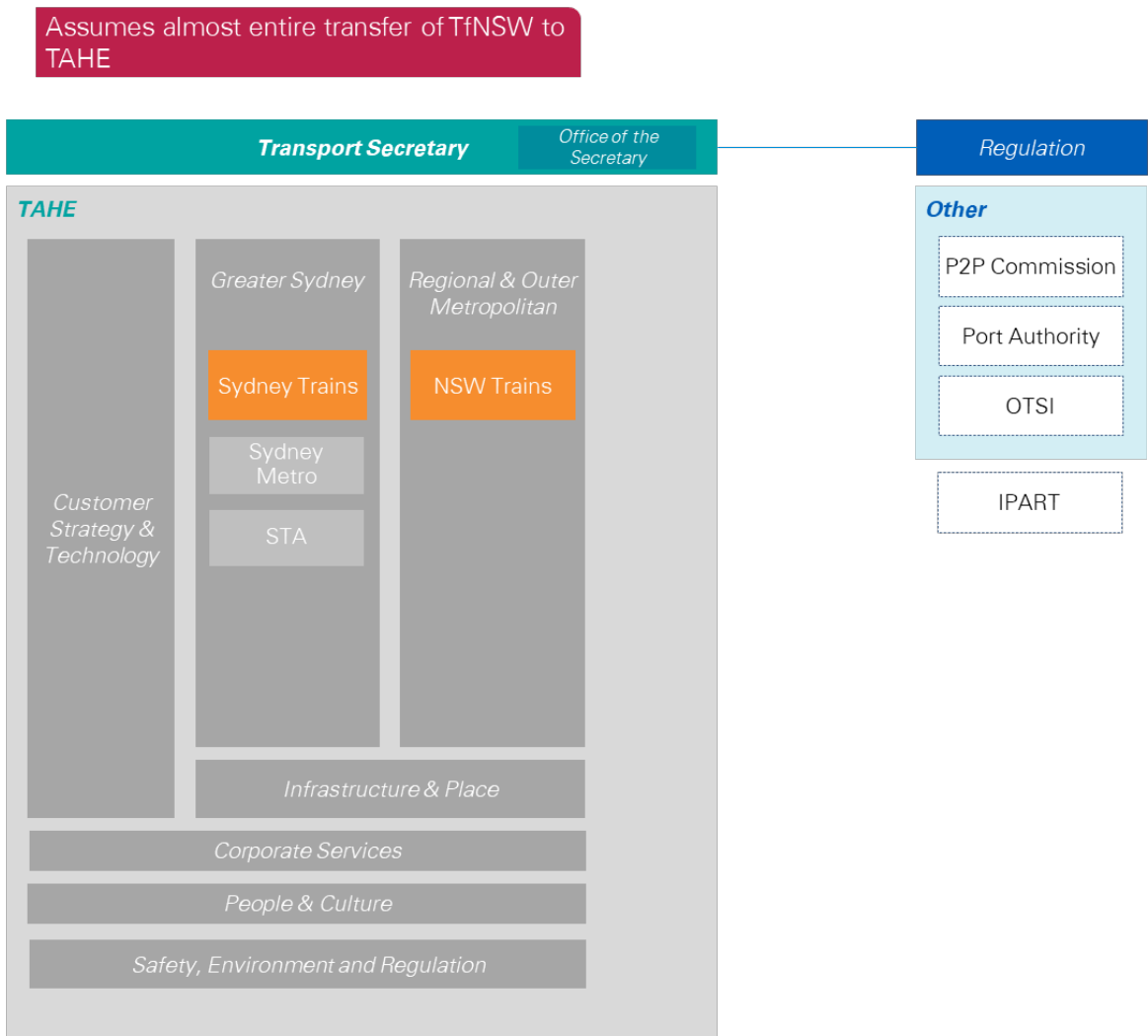
'TAHE for
NSW'



Description of 'TAHE for NSW'





'TAHE for NSW' is a functional representation of a holistic approach to the corporatisation of transport services and infrastructure. It is designed to broaden the disciplines sought by Treasury through TAHE; while providing a permanent resolution of the planning, operational and financial separations and interfaces introduced by recreating independent statutory agencies that are modally specific.

Figure 12: TAHE for NSW structure



Functional description

Figure 13: Functional description of entities

'TAHE for NSW'	 	 
<ul style="list-style-type: none"> TfNSW is corporatised, governed by a fiduciary board and legislation; Owns all transport cluster assets; Controls the standard working timetable for all transport operators; Controls access and pricing for all modes; Controls all capital projects; Controls all land and property development; and Controls and allocates capital funding 	<ul style="list-style-type: none"> General government retains regulatory, assurance, safety and other core government functions. 	<ul style="list-style-type: none"> Within TAHE for NSW




Assessing TAHE for NSW against the agreed objectives

Table 16: TAHE for NSW vs agreed objectives

Key: *Green* = likely to meet the objective, *Orange* = requires further investigation, *Red* = unlikely to meet the objective






Organisational	Rating
Support TfNSW's 'Evolving Transport' long-term operating model	●
Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds	●
Facilitate the integration of networks, services and project planning, across modes with a customer focus	●
Allow future reform to rail service delivery models	●
Account for the TAHE Board's duties and corporate objectives	●
Operational	Rating
Maintain and enhance safe network operations	●
Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators	●
Fiscal	Rating

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Meet accounting standard requirements, by 1 July 2020	
Sustain the accounting treatment, over time	
Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSWT)	

Organisational

Table 17: TAHE for NSW vs agreed objectives

Organisational	Rating
Support TfNSW's 'Evolving Transport' long-term operating model	
Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds	
Facilitate the integration of networks, services and project planning, across modes with a customer focus	
Allow future reform to rail service delivery models	
Account for the TAHE Board's duties and corporate objectives	

Does 'TAHE for NSW': Support TfNSW's 'Evolving Transport' long-term operating model?

Yes.

Evolving Transport seeks to shift the focus from individual transport modes to Greater Sydney and Regional and Outer Metropolitan customer needs. TAHE for NSW ensures the future transport needs are met by guaranteeing one organisation has accountability for the voice of the customer, future transport planning and asset ownership/investment decision making. This will embed multi-modal thinking within an organisation, rather than risk reverting to the old Transport operating model which focused on individual transport modes.

Does 'TAHE for NSW': Support a long-term model that improves the management of assets, commerciality, and transparency of the use of public funds?

Yes.

The TAHE for NSW model will allow for better management of assets since all the assets (e.g. road, rail, bus, light rail and ferries) will fall under the umbrella of one organisation which will allow better transparency of the use of public funds.

Mainly, this 'all-in asset base' model into the SOC asset base, may allow the commercialisation of the transport assets.

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Does 'TAHE for NSW': Facilitate the integration of networks, services and project planning, across modes with a customer focus?

Yes.

Day of operations may be affected through the implementation of this option noting the relationship between the entities will shift to an asset owner vs. operator arrangement. However, this can be rectified through the implementation of key governance forums and protocols to ensure alignment of day of operations activities.

Implementation of TAHE for NSW mitigates the risk of duplication and misalignment present within TAHE Pure and TAHE Real. This is achieved by consolidating accountability for:

- Ensuring the digital network is fit for purpose and has the capacity to support future technologies within one organisation; and
- Safety management and mitigation of safety risks within one organisation.

TAHE for NSW could result in a more accurate integration of technology systems across individual modes of transport, therefore, improving connection points and integration between services. TAHE for NSW seeks to maximise the delivery of customer outcomes and the long term effectiveness of the customer strategy.

Does 'TAHE for NSW': Allow future reform to rail service delivery models?

Yes.

The TAHE for NSW model may allow for future rail service delivery model reforms, such as the potential for franchising.

Franchising, along with many other reform types, will require definitive boundaries to be set and understood to be an attractive proposition.



Does 'TAHE for NSW': Account for the TAHE Board's duties and corporate objectives?

Yes.

The TAHE for NSW Pure model may allow TAHE Board to carry out their duties and corporate objectives. The main reason is that safety management and the mitigation of safety risks fall within the one organisation, allowing the Board to have accountability over network safety.

Operational objectives

Table 18: TAHE for NSW operational impacts

Operational	Rating
Maintain and enhance safe network operations	
Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators	

Does 'TAHE for NSW': Maintain and enhance safe network operations?

Yes.

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Does 'TAHE for NSW': Create clear, logical operational accountabilities between TAHE, TfNSW and rail service operators?

Yes.

Fiscal

The 'TAHE for NSW' option contemplates an 'all-in asset base' model. Therefore, the 'TAHE for NSW' option can be seen as the existing asset base that would have resided within TAHE (either 'TAHE Pure' or 'TAHE Real'), plus the addition of other modes (inclusion of roads) into the SOC's asset base.

Table 19: TAHE for NSW vs agreed objectives

Fiscal	Rating
Meet accounting standard requirements, by 1 July 2020	
Sustain the accounting treatment, over time	
Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSW)T)	

Does 'TAHE for NSW': Meet accounting standard requirements, by 1 July 2020?

NA – a single entity means there is no need to consider which entity records farebox.

Does 'TAHE for NSW': Sustain the accounting treatment, over time?

Maybe – subject to significant further work and preliminary indications are not positive.

In the absence of a sophisticated financial model, and current uncertainty as to the financial funds flows and profitability means there is limited ability to understand whether ongoing equity investments would be possible.

It is important to note that sustaining the accounting treatment relies upon continuing to implement TAHE as envisaged under the current legislation. The current legislation does not contemplate implementation of an option such as TAHE for NSW (i.e. establishment of essentially a different SOC and abolition of existing agencies).

This means TAHE for NSW is a substantial departure from the established contemplation of TAHE. As well as presenting very complex legal, structural, policy and practical implementation challenges, the departure presents a significant risk to sustaining the accounting treatment over time.

We also note the increased risk in respect of the next fiscal objective; increased PNFC risk (i.e. the risk raised in the next objective) adds to risks to sustaining the accounting treatment over time.

Does 'TAHE for NSW': Maintain PNFC classification from the ABS (for-profit TAHE, NFP for ST and NSW)?

Maybe - subject to significant further work and preliminary indications are not positive.

The introduction of roads presents an additional and new risk to TAHE's PNFC classification, as a substantial portion of roads' revenues is derived from taxation revenues (through the motor vehicle registration).

Notwithstanding policy deliberations around road *user charges*, under GFS, such charges are classified as taxes and cannot count toward TAHE for NSW's PNFC determination. GFS is based on an international economic framework that applies concepts that do not always align with policy perspectives.

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On the basis that this option consolidates TAHE as well as Sydney Trains and TfNSW functions, this objective equates to maintaining for-profit PNFC status for TAHE only. Separate classifications for other entities do not occur.

In addition to the PNFC risk outlined above arising from the inclusion of roads, based on the departure from the established contemplation for TAHE, the ABS's transitional status applied to TAHE could be at risk.

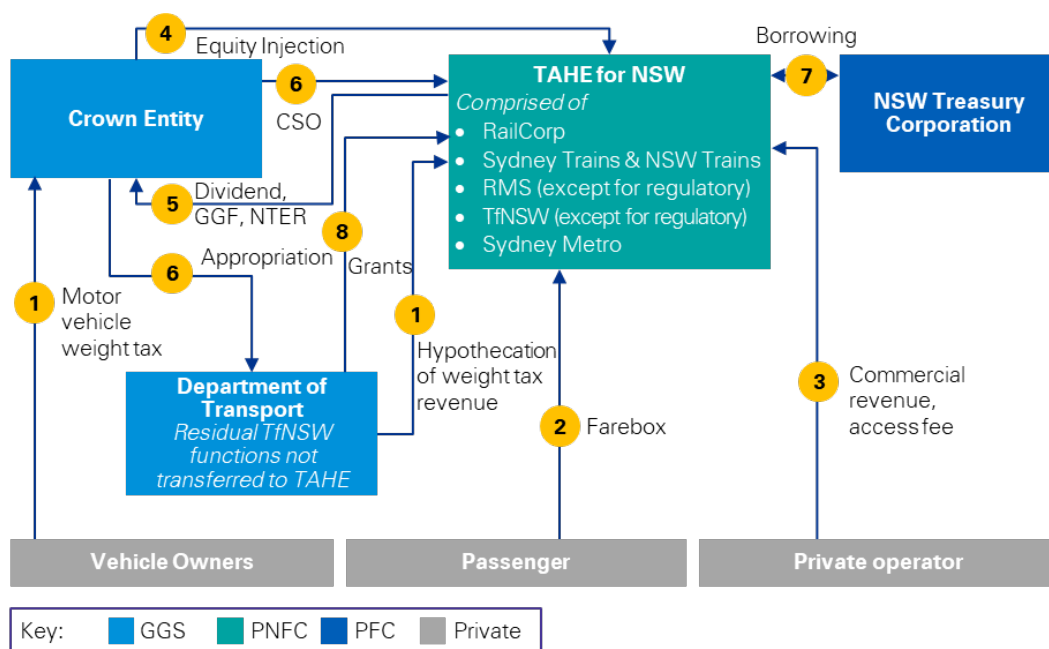
GFS classification has regard to an entity's functions. As such, the inclusion of various current TfNSW functions could provide further evidence to suggest TAHE for NSW should be classified as a GGS entity. Further work would be required to determine the appropriate perimeter of transferred functions.

Illustrative fiscal impact of TAHE for NSW

The fiscal impacts on the GGS have been modelled based on the flow of funds illustrated in Figure 14 below and assumptions as directed by TfNSW which are set out in Appendix 1. As with other options, if these funds flow or assumptions are altered, then variation to the fiscal impacts outlined below would be expected. The flow of funds assumes the majority of Transport delivery and assets are transferred to TAHE and assume that the PNFC and Accounting classification risks referred to above have been mitigated.

Funds flow

Figure 14: TAHE for NSW funds flow



Illustrative outputs

Implementation of the TAHE for NSW option is expected to result in an increase in GGS expenditure over time. GGS revenue is also transferred to fund some of these expenses. These revenues include the transfer of the motor vehicle weight tax, transfer of metro farebox revenue and other user charges currently received concerning activities associated with the former RMS.

The analysis does not consider increases in GGS expenditure that would be expected to implement such a wide-ranging reform and change.

The GGS Budget Result is impacted to a lesser extent than GGS expenditure due to the receipt of Dividends, NTER and GGF. Based on current assumptions in the financial model the adverse impact to the Budget Result is in the order of \$0.5bn annually. This occurs because the reduction in depreciation and other expenses previously included in the GGS is offset by the increase in funding

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required to provide TAHE with enough revenue to cover its expenses and depreciation when the assets are held in a for-profit entity.

The extent of the impact on the GGS Budget Result will depend on the extent of the write-down which may occur in all the transport assets being held by TAHE. Larger write-downs of assets will result in lower depreciation values. Lower depreciation reduces the extent of GGS grants or CSOs required TAHE to fund its expenses. These write-downs may vary across the different transport modes.

Assuming a 50% write-down of all assets and the resulting reduction in depreciation expense, the impact on the budget result would be in the order of \$0.5bn annually.

Illustrative outputs

The outputs in Table 20 below illustrate the expected impact of TAHE for NSW on GGS expenditure and the GGS Budget Result to 2026-27. The outputs are based on a series of assumptions including a transition pathway to the end state. For illustrative purposes, a two-year transition has been assumed but this would likely take several years to fully implement. In the interim, all existing funds flows are likely to remain.

Table 20: TAHE for NSW illustrative outputs

\$m	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27
Increase in GGS expenditure	-	-	(1,700)	(500)	200	800	1,200
Reduction in budget result	-	-	(700)	(600)	(500)	(600)	(700)

Key modelling assumptions

The illustrative fiscal impacts above are based on outputs of the financial model. The financial model is premised on significant assumptions which are outlined below. If these assumptions do not hold, significant variation in financial outcomes would be expected. Further work is required to confirm and validate these assumptions. Some of the key assumptions include:

- The valuation of TAHE transport assets will be written down based on a discounted cash flow valuation methodology with a corresponding reduction in ongoing depreciation. A broad assumption has been made across all asset classes (50%) but this will likely need to be considered on a network by network basis.
- All of TfNSW/RMS functions except for regulatory and policy will be transferred to TAHE. These residual functions will be held in the Department of Transport.
- RMS assets and associated depreciation are no longer in the GGS
- Motor vehicle weight tax revenue be received by TAHE through the Department of Transport
- All farebox revenue is received by TAHE.

Further detail on these assumptions, including additional requirements, is disclosed in Appendix 1.

Scenario analysis

In particular, the impact on GGS expenditure and the Budget Result are highly sensitive to the asset valuation assumption. Table 21 below highlights this sensitivity and shows the effect on GGS expenditure and the Budget Result under different valuation assumptions across the asset base. The smaller the proportion of the write down the larger the adverse impact on GGS expenditure and the budget result

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Table 21: TAHE for NSW Scenario analysis

\$m	2026-27	2026-27	2026-27
	25% write down	50% write down	75% write down
Increase in GGS expenditure	2,500	1,200	-
Reduction in budget result	(2,000)	(700)	600

A detailed valuation would be necessary for each class of transport asset which would result in different valuation proportions across the asset base.



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Next steps for TAHE



Next steps to operationalise TAHE

TAHE's legal and administrative stand up from 1 July 2020 closely replicates arrangements on 30 June, reflecting the complexity of changing accountabilities in the heavily regulated rail sector – and the practicalities of establishing a new corporation.

TAHE's initial stand up period is only transitional – meaning that the detailed definition and analysis of the corporation's long-term operating model is of signal importance.

Noting the limitations outlined in the Executive Summary of this report and the form and effect of Cabinet's decision in May 2020 – the next phase of work is focused heavily on the detailed development of operational and financial models and formal safety assurance – alongside an ongoing focus on fiscal needs.

Key activities

Cabinet has requested the TfNSW lead a collaborative process with TAHE and NSW Treasury to allow Cabinet to consider TAHE's long-term operating model in October 2020. Noting the limitations to this work, a number of activities are needed to respond to Cabinet's request, including:

- **Safety opinion:** With the constrained timeframe involved in providing the initial high-level advice in this report, the critically important issue of safety has not received the focus required. In developing the detailed models in the next phase of TAHE development, safety considerations will be paramount. Once the models are developed, an expert safety opinion will be sought, and any necessary sign-offs will be obtained prior to any model being recommended.
- **In-depth operational design:** We will work with TfNSW to design and refine clear, real-world operating models for each identified option.

We will define the functional specification of each TAHE option – what each option controls, owns, decides and operates – and design the business rules needed to meet the operational and organisational objectives determined by the Cabinet.

- **Detail organisational design:** TfNSW is mid-way through the most fundamental change to transport operations and governance in NSW's history; through 'Evolving Transport'.

Evolving Transport fundamentally seeks to place the 'customer at the centre' of TfNSW's strategy – moving away from mode-specific agencies for road and rail services – in favour of geographic, cross-modal functional alignments. Without careful consideration and customisation, TAHE would have consequences on the Cabinet's agreed cluster-wide structural and service reforms.

With the functional and operational structure and resourcing of TAHE resolved – and initial 'business rules' developed under each option, we will define the resource profile (e.g. resourcing need and the implications of each model on budget, investment, and the existing entities such as TfNSW) and implications of each option and their alignment with 'Evolving Transport'.

- **Robust financial modelling and impacts:** the next phase of work will provide a more sophisticated financial model which will allow the capability to understand the impacts on various PNFC and GGS entities – and the likely fiscal impacts.

This means that the development of a detailed and robust financial model, including a DCF, is a foundation stone of our approach. This model will allow TfNSW and NSW Treasury to have confidence in articulating the financial impacts of each option.

- **Extended stakeholder consultation:** All the above steps will be undertaken in conjunction with extended stakeholder engagement across every step of the process to inform and uncover any potential problems or opportunities ahead of Cabinet in October.

Appendix



Appendix 1 – Financial model assumptions

TAHE Real/Pure

Quantum

The quantum of values included in the financial model is based on the PRIME forward estimates unless otherwise noted below.

Funds flow and other assumptions

The table below summarises the key fund flow and other assumptions underpinning the modelling for TAHE Real.

Item	Assumption / Treatment	Further work to be performed	Ref ¹
Timing of transition to end state	2 years for illustrative purposes Assumed that existing funds flow would continue in the interim	Determine likely timing of any transition period including a detailed transition plan. Confirm that based on sufficient progress towards the TAHE Real end state that existing funds flow such as capitalisation of equity injection can continue to occur.	
Access / License fees	Access fee paid by operators to TAHE for access to assets. Calculated based on the profit required for TAHE to deliver the required rate of return, split between Sydney Trains and NSW Trains There is no difference between access fees and license fees Access fees are assumed not to give rise to lease arrangements under AASB16 or service concession arrangements under AAB1059	Confirm whether different arrangements are required for different asset classes (e.g. below/above rail, regulated/non-regulated assets) Confirm whether arrangements are not considered leases or service concession arrangements under AASB 16 and AASB 1059 respectively Determine likely quantum of access fees	1,2
Major rail project delivery	Major rail projects continue to be delivered by TfNSW and paid for by TAHE. TfNSW will recognise revenue and corresponding expense consistent with the current treatment Ongoing write-off is assumed to be not necessary as the initial write down and DCF valuation considers further cash flows including future capex	Confirm whether ongoing major project delivery capex needs to be written down by TAHE during the year of delivery	3
Equity injection	The Crown continues to recognise equity injections where required, however, TAHE may have excess cash as a result of access fees and potentially increased borrowings	Determine how excess cash which is built within TAHE is distributed back to the Crown (capital return) or used for future capital works	4

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Item	Assumption / Treatment	Further work to be performed	Ref ¹
Asset write off	<p>Assumed that a for-profit will value its assets under a DCF methodology; and write-down would likely occur as cash flows from access fees and CSOs will be less than its book value (DRC)</p> <p>A 50% write off value and the corresponding reduction in depreciation has been assumed for all rail assets</p>	<p>Confirm the size of write down and the corresponding reduction in depreciation</p> <p>Confirm the extent of the write-down which will be taken to the Asset Revaluation Reserve against existing reversive balances and the extent taken through the profit and loss</p> <p>Confirm whether an on-going write off of capex is required or whether the initial write-down of the network assets is sufficient</p>	
Construction delivery	TAHE continues to pay Sydney Trains for the delivery of minor and MPM Capex. Sydney Trains recognises revenue and corresponding expenses	Confirm whether ongoing minor capex needs to be written down by TAHE during the year of delivery or is considered as part of the initial DCF valuation	5
CSO	CSO currently not required as the access fee is sufficient to provide TAHE with a return	Determine appropriate CSO based on the quantum of access fee determined	6
Service fee	The service fee payment is equal to the operator access fee to TAHE and is required to ensure rail operators to have sufficient cash to pay access fees	n/a	7
Maintenance funding	TAHE pays Sydney Trains for maintenance of the rail network	n/a	8
Farebox	Per the current state, farebox revenue is recognised as revenue in the operators	n/a	9
Borrowings	TAHE will achieve a target gearing rate of 40% at the end state	Confirm optimal gearing ratio	10
Dividend	Assumed that TAHE will pay a dividend to the GGS to achieve a 3% rate of return on total equity	Confirm that the required rate of return is sufficient and whether the return of capital can be considered	12
Government guarantee fee (GGF)	Assumed that TAHE will be subject to the commercial policy framework and pay a government guarantee fee on borrowings based on a target credit rating (assumed to be 2% based on high level analysis of Sydney Water's 2018-19 financial statements)	Determine standalone credit rating for TAHE and the resultant GGF	12

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Item	Assumption / Treatment	Further work to be performed	Ref ¹
NTER	Assumed that TAHE will be subject to the commercial policy framework and will pay Tax Equivalents of 30% on profit	n/a	12
Appropriations	Additional appropriations are required for TfNSW to provide funding to operators to pay their access fee to TAHE	n/a	13
Return on investment	Assumed that a return on investment of 3% is required	Confirm whether a 3% return on total equity is sufficient.	
Additional TAHE cost	Assumed that TAHE will incur additional costs as a standalone entity. Assume additional \$100m per annum	Determine detailed organisational structure of TAHE and other entity enabling operating costs	

1 TAHE Real funds flow diagram reference number

TAHE for NSW

Quantum

The quantum of values included in the financial model is based on the PRIME forward estimates unless otherwise noted below.

Funds flow and other assumptions

The table below summarises the key fund flow and other assumptions underpinning the modelling for TAHE for NSW.

Item	Assumption / Treatment	Further work to be performed	Ref ¹
Timing of transition to end state	2 years for illustrative purposes Assumed that existing funds flow would continue in the interim	Determine likely timing of any transition period	
Asset write off	Assumed that a for-profit entity will value its assets under a DCF methodology, and a write-down would likely occur as cash flows from access fees and CSOs will be less than its book value (DRC) A 50% write off value and the corresponding reduction in depreciation has been assumed for all transport assets	Confirm the size of write down and the corresponding reduction in depreciation. It is likely that different transport asset classes may have different proportions of write-downs Confirm whether an on-going write off of capex is required or whether the initial write-down of the network assets is sufficient	
Regulatory and policy functions not transferred	It is assumed that regulatory and policy functions are not transferred to TAHE from TfNSW. This is because under GFS principles Government regulatory and policy functions are required to be in the budget	Confirm the size of the regulatory and policy functions which TfNSW which cannot be transferred to TAHE Confirm whether any other functions currently in TfNSW is not suitable for transfer into TAHE	

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Item	Assumption / Treatment	Further work to be performed	Ref ¹
	sector. (assumed to \$0.5bn annually)		
Motor vehicle weight tax	It is assumed that TAHE is hypothecated funding related to the Motor Vehicle Weight Tax	Confirm if/how this can be treated as revenue in a PNFC or if a mechanism is required for TAHE to directly receive these payments as user charges	1
Dividend	Assumed that TAHE will pay a dividend to the GGS to achieve a 3% rate of return on total equity	n/a	5
Government guarantee fee	Assumed that TAHE will be subject to the commercial policy framework and pay a government guarantee fee on borrowings (assumed to be 2%)	Determine the standalone credit rating for TAHE and understanding what the guarantee fee would be	5
NTER	Assumed that TAHE will be subject to the commercial policy framework and will pay Tax Equivalents of 30% on profit	n/a	5
Farebox	All farebox revenue is recognised by TAHE	Confirm accounting treatment is appropriate	2
Cost of implementation	The cost of implementation such as wide-ranging initiative has not been included in the analysis	Additional work to estimate the activities and costs involved for a major reform such as this.	

1 TAHE for NSW funds flow diagram reference number

Appendix 2 – State's fiscal context and objectives

NSW Government's fiscal strategy

NSW public sector finances are managed in line with the Government's fiscal strategy. The fiscal strategy is underpinned by the *Fiscal Responsibility Act 2012* (FRA), the objective of which is to maintain the State's triple-A credit rating.

The Government delivers on the fiscal strategy through budget surpluses and managing expenditure growth. A negative impact on the State's budget result and/or increases in general government expenses will not support the fiscal strategy.

The FRA includes a fiscal target that annual growth in general government expenses is less than the long-term average general government revenue growth. The long-term average general government revenue growth is currently prescribed at 5.6 percent. Increases in general government expenses add to the risk that the State will breach the requirements of the FRA.

State budget framework

The State's Budget reflects the revenues and expenses of the General Government Sector (GGS) entities. The GGS is comprised of those agencies that are funded in the main by taxation (directly or indirectly). These agencies provide public services, carry out policy or perform regulatory functions.

Government-owned businesses and trading enterprises are not within the GGS and instead are referred to as the Public Non-Financial Sector (PNFC). These agencies operate within a broadly commercial orientation where user charges represent a significant proportion of revenue.

Classification of agencies as GGS or PNFC occurs using Government Finance Statistics (GFS) criteria as published by the Australian Bureau of Statistics (ABS). These criteria are explored in more detail later in this report.

PNFCs may be for-profit or not-for-profit, depending upon their objectives and governance structures. State-Owned Corporations (SOCs) in NSW are for-profit PNFCs.

Appendix 3 – Safety case studies

Case study one: Waterfall Rail Crash (NSW) 2003

Overview

The Waterfall rail crash occurred on the morning of 31 January 2003. The crash involved the derailment of a four-car Outer Suburban Tangara on a bend of the South Coast Line soon after departing Waterfall Station en route to Port Kembla. The crash led to the death of six passengers and the driver.¹ A further 42 people had injuries of varying severity.

Notwithstanding the failings within SRA, the inability of the rail sector to be able to provide a whole of system view on safety meant that no assurance could be provided on whether the operating practices, culture, assets and infrastructure were safe.

The image illustrates the Tangara train and the scale of the crash. Three cars were derailed with the fourth driving car sustaining significant damage. All four cars were subsequently written off.

A Special Commission of Inquiry into the Waterfall Rail Accident was undertaken during 2003-04 to determine the cause of the accident and propose changes to prevent similar crashes in the future.



Contributing Factors

The following sections are based on the Ministry of Transport's *Rail Safety Investigation (2003)*.

Factors on the day

- **Speed** – The train was estimated to be travelling at 117km/h around the bend while the speed limit was 60km/h, causing the train to derail. No system was in place to stop trains from overspeeding.
- **Deadman system (DMS)** – The DMS was designed to apply emergency braking in the event of a driver becoming incapacitated or leaving the controls (i.e. when weight is relieved from the DMS). The investigation found the driver had a medical condition that led to him becoming incapacitated and the DMS was inadvertently deactivated due to his weight, approximately 118kg. It was recognised that the deadman's brake was not properly designed, and that despite there being known issues with the brake (of the brake, and the drivers cabin), no action was taken to rectify.
- **Door release:** No internal or external door release mechanism was available to enable to escape of passengers or to allow rescuers access into the carriage.

Organisational factors

- **Organisational restructure** – Before 1995, the State Rail Authority (SRA) was a vertically integrated statutory authority with four divisions. Following the National Competition Policy Agreement, the SRA was restructured and it lost the authority to regulate the safety of other operators on its track.
- **Poor safety culture** - The SRA had known for more than 14 years that the DMS could be inadvertently deactivated by the drivers' weight and/or deliberately be deactivated by wedging objects against it.

¹ Ministry of Transport 2003, *Rail Safety Investigation*.

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There was a poor safety culture within the SRA with little motivation to report hazards. The management of on-time running also resulted in some drivers compromising safety to avoid delaying trains.

- **Training** - The guard had not been trained to identify when a train was out of control, and was unable to make the decisions required to address the situation. The management within SRA discouraged some guards from challenging the decisions of drivers, even on matters of safety.

Changes implemented

The Special Commission of Inquiry into the Waterfall Rail Accident detailed 127 recommendations. The NSW Government now publishes an annual report outlining the changes that have been implemented.² Key changes include, but are not limited to:

- Task linked vigilance resulting in emergency braking being activated if the driver does acknowledge a buzzer after train controls have been changed (e.g. speed).
- Automatic train protection system that communicates with rail signals, trains and trackside infrastructure (currently underway).
- Internal emergency door releases to make it easier for passengers to exit and emergency services to access the carriage.

Case study two: Hatfield Rail Crash (UK) 2000

Overview

The Hatfield rail crash occurred in the early afternoon of 17 October 2000. The Great North Eastern Railway (GNER) InterCity 225 train from London King's Cross to Leeds was travelling at around 185km/h when it derailed near Hatfield. Of the 170 people on board, four died and over 70 were injured.

The train travelled for a further 900m after the derailment. The driving car and second car remained upright, while the following cars came to rest on their side – as seen to the right.

The maintenance contractor and manager were both fined for their involvement in the crash.

Contributing Factors

The following factors are based on the Office of Rail Regulation's *Final Report by the Independent Investment Board (2006)*.

Factors on the day

- **Rail maintenance** – The derailment was the result of the fracture and fragmentation of the left-hand rail as the train travelled along it. Poor maintenance led to the presence of multiple and pre-existing fatigue cracks in the rail. The train speed and other rail infrastructure were not considered to have contributed to the crash.

Organisational factors

- **Industry structure** – British Rail, the owner and operator of rail infrastructure in the United Kingdom (UK), was privatised in 1997. Following the privatisation, a private company, Railtrack, was responsible for managing safety and overseeing maintenance carried out by private contractors.
- **Maintenance contractor** - Balfour Beatty Rail Maintenance Ltd (BBRML) was responsible for maintenance on the length of track where the crash occurred. BBRML employees often failed to complete tasks in accordance with their responsibility and comply with industry standards. Some employees did not have adequate training and BBRML's safety systems did not enable effective inspections.



² Office of the national Safety Regulator 2020, *Waterfall Rail Accident*.

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- **Maintenance manager** – Railtrack had a history of poor rail management, including a derailment in 1997 which resulted in several recommendations that could have prevented the Hatfield rail crash – none of which was acted upon. Key organisational factors included:
- **Contractor management** - Railtrack were aware of BBRML's poor maintenance performance in the lead up to the derailment but did not take the measures required to improve standards.
- **Culture** – The Railtrack culture was performance-driven which focused on minimising train delays rather than safety. Railtrack employees were also unable to instigate action when they raised issues regarding rail maintenance. There were also cases of compliance certificates being signed, despite the rail not meeting the required standards.
- **Data management** – There was no system in place to view the number and type of safety defects present on the network. The infrastructure quality audits were also poorly delivered or incomplete.

Changes implemented

In the months following the rail crash, speed restrictions were implemented and significant rail maintenance reviews were undertaken.³ Railtrack went into administration as it was unable to meet the high repair and maintenance costs on its infrastructure.

The government not-for-profit company, Network Rail, purchased Railtrack in 2002.⁴ This brought rail safety and the delivery of maintenance back into government control while operations remained privately owned.

³ BBC News 2005, *How Hatfield Changed the Railways*.

⁴ The Guardian 2002, *Railtrack*.



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