

POSITION PAPER

Structural Models for Europe's National Rail Sectors

21 December 2011

COMMUNITY OF EUROPEAN RAILWAY AND INFRASTRUCTURE COMPANIES - COMMUNAUTÉ EUROPÉENNE DU RAIL ET DES COMPAGNIES D'INFRASTRUCTURE - GEMEINSCHAFT DER EUROPÄISCHEN BAHNEN UND INFRASTRUKTURGESELLSCHAFTEN



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Summary position statement

CER welcomes the intention of the European Commission to “ensure non-discriminatory access to rail infrastructure” in such a way as to “ensure the development of competition, continued investment and efficiency in the cost of service provision” ⁽¹⁾. The time has come for a rational analysis of what structural forms foster the Union's emerging Single Railway Area.

CER fully supports the principles of free and fair competition which can only be fully realized under the condition of non-discriminatory access to infrastructure. However CER notes the fact that both vertically-integrated and vertically-separated sectors are found among both the best-performing and worst-performing national rail sectors in terms of traffic performance and in terms of cost-efficiency. CER therefore does not believe in a single one-size-fits-all model for all Member States.

It is CER's conclusion that vertically-integrated systems should incorporate efficient mechanisms that effectively protect the rights of non-incumbent operators, while vertically-separated systems should allow for a better alignment of incentives between the operators and the infrastructure manager in order to raise efficiency. CER considers that each Member State should be empowered to: reconsider its existing rail sector model; have sufficient flexibility to pursue reforms within a given model; and switch between models, if national conditions so require. CER emphasizes that new legislation on unbundling should only be proposed if it proves necessary for the development of the European railway market after a thorough analysis.

CER recommends the development of at least two optional models that ensure non-discriminatory access without necessarily resorting to full separation. It should then be up to each individual Member State to opt for a given model, while conforming to a common set of principles concerning non-discriminatory access, the development of competition, whole-system efficiency, good governance, and strong and independent regulatory control.

¹ This was the wording chosen by the Commission in the 2011 Transport White Paper, see COM(2011) 144 final, page 18.

CER considers that *efficient* non-discriminatory access can be ensured according to three main models. The first model is full vertical separation in combination with mechanisms to re-align incentives between operations and infrastructure. A second model consists in having an integrated system where control over the critical parameters that govern access to infrastructure is ceded to independent bodies (separation of essential functions). A third model, also in the context of an integrated system, is to provide for efficient monitoring and consultation within the infrastructure manager's handling of essential functions.

CER therefore calls for a new way of thinking concerning structural models for the rail sector, with a particular focus on how virtuous economic incentives and good governance can be supported, whilst avoiding obligations or prohibitions concerning non-essential functions or processes.

I. INTRODUCTION

The Commission wishes to assess the need for and contents of potential new legislation that would impose structural reform, or possibly several distinct options (or models) for structural reform, on the rail sectors of Member States. It is understood that this exercise shall consider only the question of separation between infrastructure managers and railway undertakings, i.e. the question of unbundling of infrastructure from operations.

It is assumed that the underlying goals of the Commission are to improve the functioning of competition within the rail sector, with particular reference to the goal of non-discriminatory access to infrastructure for all railway undertakings, while prioritising the options that best support investment and efficiency in the cost of service provision.

Following a series of consultations with its members, CER formulates a set of principles underpinning its view of how the Commission should best approach this important issue (Section II). The principles underpinning CER's position are then presented (Section III). Concrete recommendations are then outlined for three structural models which CER believes should be allowed to develop (Section IV).

II. RECOMMENDATIONS CONCERNING THE COMMISSION'S APPROACH

Pursuant to the 2011 Transport White Paper, CER considers that the Commission is bound by the objectives of “*competition, continued investment and efficiency in the cost of service provision*” for proposals it would make on structural reform of the rail sector.

Furthermore CER considers that the focus should not only be on the cost-efficiency of service provision, but on the whole-system efficiency of the rail sector, therefore including the efficiency of infrastructure management.

CER notes that comparisons with other network industries (e.g. electricity, natural gas, water supply, telecommunications, postal services) are of limited validity when analysing the case of rail. This is notably due to a significant difference in the intensity of downstream competition: rail competes directly with a very dynamic (indeed dominant) road sector; the intensity of downstream competition in electricity or water supply is negligible in comparison.

Any structural reform that is imposed on a Member State's rail sector must be such as to increase the efficiency and the competitiveness of that rail sector.

CER asks that the Commission: evaluates the net benefit of any structural reform that would be imposed on a Member State, and proposes only those reforms, if any, that would credibly lead to a net benefit to society in that Member State, and documents in detail its reasons for selecting each specific option.

The consequences of implementing specific options for structural reform must take into consideration national specificities and respect the principle of subsidiarity. This should include, but should not be limited to, a case study for the three Baltic States whose networks and main transport activity are related to third countries.

If the Commission cannot identify reforms that meet these sets of criteria then the Commission should refrain from proposing new legislation on this topic.

It is also to be noted that the body of empirical economic studies made to-date on the question of vertical separation in the rail sector do not lead to clear conclusions as to whether, and subject to what assumptions, vertical separation may lead to a positive or negative net benefit.

Sound overall principles should form the basis of any new legislation on unbundling. Lists of explicit prohibitions or obligations on points of detail should be avoided wherever possible.

III. PRINCIPLES AND DEFINITIONS UNDERSCORING CER'S POSITION

Non-discriminatory access

CER fully supports the principle of non-discriminatory access to infrastructure - it is a vital component of a liberalised and efficient rail sector.

Non-discriminatory decisions should be guaranteed within the following key processes: capacity allocation; path allocation; mid-term and long-term traffic planning; timetabling; infrastructure charging; and access to essential rail-related services.

The process leading to strategic investment decisions must be transparent and must involve a fair representation of the railway undertakings.

Distinction between key processes and essential functions

In line with CER's position on the Commission's recast proposal, CER considers that the *essential functions* of infrastructure management are path allocation and the setting of charges (but not their collection).

Separation

CER notes that existing legislation already contains provisions on organisational, functional and accounting separation between infrastructure management and transport activities.

CER endorses the view that the rail sector is more efficient when there is a better alignment of processes and incentives between the infrastructure manager and the operators.

CER notes that efficient alignment may in principle be secured using a variety of organisational and governance structures.

CER notes the diversity of existing models in the Union and the difficulty in establishing a single narrowly-defined model that would suit every case.

Any new legislation should therefore allow for national specificities. This may be achieved, either by putting forward several distinct yet flexible models for Member States to choose from, or by adopting only a limited number of common criteria.

The question of separation cannot be analysed in isolation, neither from the questions of governance and financing of infrastructure managers, nor from the issues of market opening and competition. The Commission must look at these sets of questions simultaneously.

Governance of infrastructure managers

The general principles below are relevant whether or not further steps towards separation are taken as compared to the status quo.

The governance and financing of infrastructure managers need to be regulated by EU law, based on the principles of economic efficiency and fair inter-modal competition.

Rail infrastructure managers are natural monopolies that should be closely regulated in terms of their economic decisions so as to protect the interests of all operators and users.

Such regulation should provide the right incentives for infrastructure managers to improve their internal efficiency and support growth in rail's modal share - without unduly limiting their commercial freedom and their ability to act on the market.

Rail infrastructure managers are comparatively far away from the market for rail services. There is therefore a need for feedback mechanisms to give input to the decisions of infrastructure managers on the basis of the experience of railway undertakings.

In particular with unbundled systems, it is recommended to have a coordinating process, co-managed by the infrastructure manager and a fair representation of the applicants, in order to promote whole-system efficiency, punctuality, safety, and service quality.

IV. STRUCTURAL MODELS

Vertically-integrated systems should incorporate efficient mechanisms that effectively protect the rights of non-incumbent operators. Conversely, vertically-separated systems should allow for a better alignment of incentives between the operators and the infrastructure manager in order to raise efficiency. Last but not least, CER considers that each Member State should be empowered to: reconsider its existing rail sector model; have sufficient flexibility to pursue reforms within a given model; and switch between models, if national conditions so require.

If it proves to be necessary for the development of the European railway market after a thorough analysis, CER recommends the development of reform options that ensure non-discriminatory access without necessarily resorting to full separation. Member States should then opt for a given model, while conforming to a common set of principles concerning non-discriminatory access, the development of competition, whole-system efficiency, good governance, and strong and independent regulatory control.

CER considers that non-discriminatory access can be ensured according to three main models. One model is full vertical separation. A second model consists in ceding control over the critical parameters that govern access to infrastructure to independent bodies (full separation of essential functions). A third model is to provide for efficient compliance monitoring within the infrastructure manager, in particular concerning essential functions.

If new legislation on unbundling is proposed, CER calls upon the Commission to allow Member States to develop structural models for their rail sectors notably in line with these three structural models, with a particular focus on how virtuous economic incentives and good governance can be supported, while avoiding obligations or prohibitions concerning non-essential functions or processes.

Common provisions: valid for all structural models

A voice for all railway undertakings on strategic decisions of the infrastructure manager

1. The infrastructure manager should have a Railway Infrastructure Committee (RIC).
2. The RIC should deliberate on matters of strategic importance for the network management and development in particular those concerning the investment plan and the contractual agreement as defined in Articles 8 and 30 of Directive 201x/xx/EC (recast of the First Railway Package).
3. The responsibility of the RIC shall exclude the day-to-day activities of the infrastructure manager. The RIC shall respect the managerial freedom of the infrastructure manager.
4. The RIC may issue an opinion on any proposal by the infrastructure manager according to point 2 above and also issue own-initiative opinions. The Infrastructure Manager shall respond to these opinions.
5. The RIC should be composed of representatives of the infrastructure manager and of the stakeholders of the infrastructure manager, in particular of representatives of railway undertakings. The composition of the RIC should include a fair representation of all railway undertakings.

Managerial freedom of RUs and IMs

Managerial freedom

6. In line with the Treaties, Member States should ensure that railway companies face no restrictions in how they may manage their assets and processes.

Model 1: Separated Infrastructure Manager

Member states may choose to fully separate the infrastructure manager from any operator.

Where this is applied, Member States should allow closer partnerships between railway undertakings and the infrastructure manager, on a non-discriminatory basis, in order to encourage whole-system efficiency.

Joint ventures for whole-system efficiency

7. In order to create positive incentives for coordination between operators and the infrastructure manager, Member States should allow infrastructure managers to offer, on a non-discriminatory basis, subject to criteria of commercial and legal feasibility, the possibility for applicants to take part in joint ventures, or other forms of collaboration, with the infrastructure manager in order to achieve cost-reductions for the sector as well as for taxpayers.

Model 2: Separated essential Functions

Member states may choose to retain or adopt a rail system where - subject to the full respect of the limits defined by competition and antitrust law - a single body may own the infrastructure manager and railway undertakings and provide for non-discriminatory access, either by ceding the control of the essential functions of the infrastructure manager to independent bodies, or by opting for Model 3.

Full separation of essential functions

8. The bodies responsible for the essential functions should be owned, managed, and financed either by the Member State, or by a fair representation of the entire rail sector. The bodies responsible for the essential functions may merge into a single body.

9. The essential functions are path allocation and the setting of charges.

Model 3: Monitoring of the essential functions

Member states may choose to retain or adopt a rail system where - subject to the full respect of the limits defined by competition and antitrust law - a single body may own the infrastructure manager and railway undertakings and provide for non-discriminatory access, either by introducing efficient mechanisms for compliance monitoring of the handling of the essential functions, or by opting for Model 2.

Compliance officer

10. The infrastructure manager should have a compliance officer. The RIC may issue an opinion on the appointment of the compliance officer. The Infrastructure Manager shall respond to this opinion.

The compliance officer would have the general responsibility of monitoring and reporting on regulatory compliance and of liaising with the regulatory body. The infrastructure manager and the RIC shall provide the compliance officer with the information that is needed for his tasks.

Compliance reporting

11. The compliance officer shall report on the measures taken to ensure non-discriminatory access with respect to the essential functions to the regulatory body on an annual basis.