Private investments into rail – what framework conditions?

Input paper

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Market opening – where do we stand?

Formally, the rail market is open to new entrants. Customers appreciate the freedom of choice offered by an open market. Competition improves the service level, stimulates innovation and investments, and increases efficiency – to the benefit of the market, the customers and society as a whole.

Yet the current regulatory structures allow dominant rail operators to strangle the new players such as private railway undertakings and even state-owned railway undertakings who wish to operate outside of their home country.

The impact? It hinders the access of new entrants into the market, diminishes the added value that new entrants bring, and even pushes them off the market. All with the effect of slowing down market opening and restoring the dominance of traditional rail companies.

Current regulatory conditions strangle new entrants

The more the market opens, the more new entrants encounter discrimination.

The source of this discrimination? Rail infrastructure managers and railway undertakings under one rail holding act as an unholy alliance with vast discrimination potential, often backed by a public administration which for historical and economical reasons is more bound to "its" railway than to newcomers.

A strong independent regulation is essential to resolve these issues, but it is not sufficient if the structure of the rail sector and the links between these bodies is unclear. A properly open rail market that attracts private investment needs both.

Experience shows: where there is discrimination potential, it will be exploited as soon as the game gets tough.

Market opening needs more than free access

Free access is only the very first step on the long way to market opening. Well performing markets require the full spectrum of adequate regulatory conditions:

Field	Main underlying question	Comment
Access regulation	Are new entrants welcomed and incentivized to access the rail market?	Free access to the rail market is formally granted, but is still insufficient in most parts of Europe at various degrees. De facto, new entrants still encounter big hurdles.
Utilisation regulation	Under what conditions can new entrants operate transport services?	It is of no use if there is access to the network, but that anticompetitive conditions prevail. Practice shows: to safeguard existing economic interests, imagination has no limits.
Network management	Which strategy for network management and development?	Infrastructure is the key tool for increasing efficiency and productivity of the rail system. Cost and service policies can favour the whole system – or they can clearly benefit one railway undertaking instead of another.
Regulators	How strong is the controller allowed to be?	Every market opening is only as good as its regulator.

Basic question:

Is Europe interested in attracting private investments into the rail market?

Examples from day-to-day business of rail new entrants

The following list highlights the current working conditions encountered by ERFA members in countries with insufficient separation between infrastructure manager and state railway undertaking. The regulatory conditions vary slightly from country to country, but the discriminatory purpose is generally the same.

The strategy is to hinder or delay market entrance and to force newcomers to give up.

Public administration – protects and favours its own railway undertaking

- Grants subsidies according to criteria which fit the incumbent, but de facto exclude new entrants
- Holds service contracts with the incumbent based on opaque cost calculations, enabling unfair market advantages and cross subsidies
- Places orders directly to the incumbent for passenger transport services, instead of launching tenders which would give a chance to new entrants
- Launches tenders, but keeps back relevant information
- Delays technical approvals (locomotives, wagons)
- Uses safety issues for market protection purposes.

State railway holding – uses its dominant position to maximise benefits for its daughters:

- Hides cost structures and enables capital flows within the Holding with the aim to indirectly subsidise single branches securing advantages vis-à-vis the competitors, and strengthening its position
- Diverts public funds in order to indirectly cover specific company interests
- Takes advantage of better access to investment funds and better conditions in bank credits
- Helps its daughters with cash injections or asset transfers (locomotives, wagons etc.)
- Strengthens the umbrella brand enabling cost-free benefits to its daughters

Infrastructure manager that is part of an integrated holding – works to the interest of the holding and not to the interest of the market and the modal shift policy:

- Refuses or offers unattractive train paths to new entrants (long running times, bad time slots etc.)
- Hinders or delays access to essential infrastructures such as terminals, marshalling yards and railway stations
- Hinders or delays access to service facilities such as workshops, filling stations, cleaning facilities etc.
- Hinders last mile traffic between terminal and main lines, by means of delays, bad service, artificially high prices etc.
- Practices delaying and stalling tactics in negotiations with new entrants, causing market disadvantages
- Increases access prices on routes used by new entrants, which hits newcomers harder than incumbents

- Grants unjustified track access discounts to incumbents
- Allows incumbents to change track slots without charges (e.g. unused track slot can be given back and exchanged against another, better one)
- Only pays low lump sums to new entrants regarding braking energy fed back into the system
- Keeps high energy prices causing multiple distortions: 1) high prices are subsidized for incumbents, but fully borne by new entrants; 2) infrastructure manager accumulates means to be re-invested in other branches of the holding
- Builds and upgrades lines and facilities which are in the interest of the incumbents, and neglects lines and facilities which are in the interest of new entrants
- Requests technical standards which are unaffordable for new entrants in terms of time and investments
- Refuses, delays or distorts the transmission of real time data for passenger information relating to newcomer trains
- Hinders new entrant's communication on railway stations (info-displays, info-desks, advertising) or requests excessive fees from the new entrant
- Informs newcomers later than the incumbent about track incidents

State railway undertaking – cargo and passenger sector:

- Artificially lowers the fares on lines which are also operated by new entrants (dumping)
- Benefits from privileged dialogue channels with infrastructure manager and public administration
- Hinders or delays bottleneck transport services such as shunting or last mile services
- Hinders or delays access to relevant councils and committees
- Hinders or delays access to linked transport systems with common ticketing
- Introduces rules which prevent or delay the allocation of ticket income to new entrants
- Hinders access to unused rolling stock
- Hinders access to service facilities to new entrants (argument: facility is 'full', although empty)

How to improve market conditions for new entrants

At a time of severe limits to public sector finance, private investors in the rail sector are essential for the development and improvement of the railway. Private investors can assess and cope with commercial risk; it is their business. What can put them off is the unquantifiable risks associated with competing with state owned enterprises which do not work to the same rules but, through historic and unchallenged custom and practice, can ensure that new investments fail.

Regulation is rarely strong enough to cope with discrimination. The creativity put in place by the dominant players is always faster than the typical “complaint & correction” process of regulation, even in member states where regulation actually is, and is seen to be, independent.

The most efficient way to guarantee a truly open market is to eliminate the need for discrimination at the root:

- The Infrastructure Manager should be empowered to offer optimum conditions to all railway undertakings without maintaining privileged relationship with sister-railway operators of the same holding.

- There must be full transparency of financial flows between different parts of a holding company model to ensure that all undertakings have equal opportunities.

The market pillar of the 4th Railway Package as supported by the EP TRAN Committee in November 2013 foresees efficient solutions to this regard.

- Institutional separation between infrastructure manager and railway undertaking as simplest and most transparent way

or

- Maintaining of the holding structure, but introduction of strict measures to ensure legal, financial and operational independence of the infrastructure manager („Chinese walls“).

ERFA supports the urgent adoption of that version of the market pillar of the 4th Railway Package, in order to safeguard investments into the rail system and promote the further development of the railways in the interest of the market, the environment and society as a whole. Unfortunately, the amendments voted on at First Reading in February 2014 neuter most of the market pillar, and are strongly opposed by ERFA as putting back the clock of private investment in the rail sector for many years.

With the predicted market growth, competition is a benefit for all players – incumbent, new entrant, foreign incumbent etc. - as it forces them to free their creative energy and to improve their services, in order to strengthen the rail system and to gain market share from other modes of transport.

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