

Initial appraisal of a European Commission Impact Assessment

Fourth Railway Package: European Commission proposals for a Regulation and a Directive on market – opening for domestic passenger transport services by rail

Impact Assessment (SWD (2013) 10, SWD (2013) 11 (summary)) for i) a Commission Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EC) No 1370/2007 concerning the opening of the market for domestic passenger transport services by rail (COM (2013) 28), and ii) a proposal for a Directive of the European Parliament and of the Council amending Directive 2012/34/EU of the European Parliament and of the Council of 21 November 2012 establishing a Single European Railway Area, as regards the opening of the market for domestic passenger transport services by rail and the governance of the railway infrastructure (COM (2013) 29).

- **Background**

This note seeks to provide an initial analysis of the strengths and weaknesses of the European Commission's Impact Assessment accompanying the above-mentioned proposals. The impact assessment in question covers the issue of *domestic market – opening* dealt with in the aforesaid proposals. The part of proposal COM (2013) 29 concerning *infrastructure governance* is discussed in a different impact assessment (SWD (2013) 12).

In its White Paper on transport policy of March 2011, the Commission declared its objective of creating a Single European Railway Area, implying an internal railway market without unnecessary barriers. The need for an integrated and open railway market has been voiced by both the Commission and the European Council.¹ Three legislative railway packages introduced in the last decade regulate the railway market at European level to 'open up national markets and make railways more competitive and interoperable at the EU level, while maintaining a high level of safety' (IA, p. 4). A recasting of the First Railway Package² has recently been adopted to simplify, consolidate and reinforce existing provisions on competition issues, regulatory oversight and financial architecture of the railway sector. A Fourth Railway Package is now put forward to 'realise the Single European Railway Area by removing the remaining

¹ Commission Communication on Action for Stability, Growth and Jobs of May 2012 (COM (2012) 299); Commission Communication on strengthening the governance of the single market (COM (2012) 259); European Council *conclusions* of January 2012.

² 2012/34/EU.

obstacles of technical, regulatory and economic nature and fostering thereby the performance and competitiveness of the railway sector' (IA, p. 4). The Fourth Railway Package includes six proposals covering three areas: interoperability³, the opening of the domestic rail passenger market⁴ and infrastructure governance⁵.

• Identification of the issue at stake

The IA clearly identifies the problem of the railway market at stake. The problem definition includes a detailed description of the existing regulatory framework and current market developments (IA, p. 8-16). While markets for freight services have already been opened to competition in 2007 and those for international rail passenger transport and cabotage services in 2010, domestic rail passenger transport remains largely closed to both foreign and national competition. 'In many Member States national incumbents are in either a monopolistic or dominant position' (IA, p. 12). The railway sector is subject to substantial public funding with €46bn of public subsidies for services and infrastructure in 2009. But 'in spite of significant public support, many railway undertakings have been making losses for several years in a row, which indicates either serious efficiency problems or systematic underfinancing' (IA, p. 22). Furthermore, the modal share of rail in transport compared to road and aviation is small and does not increase. 'Passengers perceive a mismatch between the expectations of potential travellers and the service provided by railway undertakings for the fare requested' (IA, p. 20) in terms of price, networks, reliable and frequent services, time of journeys and comfort of trains.

The main problems, their drivers and root causes are identified in a chart (IA, p. 25). The following root causes are named:

1. Non-competitive award of Public Service Contracts (PSCs), a lack of a control mechanism to limit the scope of the Public Service Obligations (PSOs) definition and too large PSCs lead to an absence of competition for PSCs. Two thirds of domestic rail services are covered by PSCs. Most local and regional rail services operated under PSOs are attributed by direct award.
2. Discrimination in access to ticketing systems and limited access to rolling stock lead to market distortions.
3. Legal monopolies (rail service contracts granted with an exclusive right without PSOs) and local establishment requirements lead to restricted access to national rail services.

These root causes are stated to trigger the two problem drivers of:

1. A lack of competitive pressures –
 - a. In the market: while routes with competition experienced traffic increase, price reductions and service innovations, 'competition is slow to expand and in some cases remains unsustainable in the long-term' and 'competition in the market is not always successful' (IA, p. 28).

³ Addressed in the impact assessment SWD(2013) 8 covering the proposals COM (2013) 27, COM (2013) 30 and COM (2013) 31.

⁴ Addressed in the impact assessment SWD(2013) 10 covering the proposals COM (2013) 28 and COM (2013) 29.

⁵ Addressed in the impact assessment in question SWD (2013) 12 covering the proposal COM (2013) 29.

- b. For the market: 11 Member States use fully or partially competitive tendering and in 16 countries direct awards take place. 'Even if competitive tendering is de jure a requirement, effectiveness of tender depends notably on the number of bidders for each PSC' (IA, p. 29) while 'the number of bidders remains low in most Member States', so that 'despite the efforts and costs to organise tenders PSCs are actually awarded to the incumbent or its historical successors' (IA, p. 30).
2. Different market access rules in the Member States: 'In the absence of a common approach at EU level, a patchwork of national models has emerged, which, according to stakeholders, prevents the emergence of the Single European Railway Area' (IA, p. 31). This makes it difficult for railway undertakings (RUs) to develop consistent business strategies throughout the EU.

These problem drivers entail the two core problems of a low quality of services and low operational efficiency.

Member States are adopting different models to solve the existing problems. Competition in the railway sector can be either *for* the market, with several operators competing for the exclusive right of one route, or *in* the market, with several operators running in the same route ('open access'). The IA defines five clusters of Member States according to their adopted policies⁶:

1. The UK and Sweden are the only Member States with fully liberalised markets and competitive tendering of all PSCs.
2. Austria, Italy and Germany are considered largely liberalised markets, with more than 33% of the passenger-kilometres in open access or corresponding to competitively tendered PSCs and new entrants successfully competing *in* and *for* the market.
3. The Czech Republic, the Netherlands and Portugal have partially liberalised markets, with less than 33% of the passenger-kilometres in open access or corresponding to competitively tendered PSCs, but where new entrants account for an important market share.
4. Eight Member States (Bulgaria, Denmark, Estonia, Latvia, Lithuania, Poland, Romania and Slovakia) are classified as quasi-liberalised markets with 'open access', but direct awarding of PSCs in practice.
5. In nine Member States (Belgium, Finland, France, Greece, Hungary, Ireland, Luxembourg, Slovenia, and Spain), incumbents operate all commercial services and PSOs in non-liberalised markets.

The IA includes a 'benchmark exercise' showing the state of play in efficiency and quality in railway systems in the EU. The results show a growing divergence between the performance of railway systems in Member States. Despite the fact that 'there is no optimal efficiency applicable to all operators' (IA, p. 18), 'there are also overall important variations between assumingly comparable railway systems' and 'geographic concentration, population density and public funding play an important role' (IA, p. 21), the analysis draws a clear link between the market structures and performance, allowing an inference to the effects of different policies. The problem definition is thus very detailed, including an analysis and descriptions of the effects of different market structures of rail, but it mixes the identification of the issue at stake with the

⁶ Malta and Cyprus do not have a railway system and are therefore not included.

causal connections and lacks a clear structure. The text does not follow the same structure as the graph that maps the problem and its drivers.

• Objectives of the legislative proposal

All the proposals of the Fourth Railway Package have together the *overall objective* to 'improve the quality of rail passenger services and enhance their operational efficiency thereby improving the competitiveness and attractiveness of rail sector vis-à-vis other modes and developing further the Single European Railway Area' (IA, p. 43). In line with the 2011 White Paper on transport policy and the Europe 2020 Agenda for smart, sustainable and innovative growth, the proposal in question should contribute to a shift from airplane and road vehicles to rail and to the reduction of GHG emissions.

The two *specific* objectives of the two proposals in question are to intensify competitive pressure on domestic rail markets and to create more uniform business conditions. They are formulated correspondingly to the problem drivers to tackle the lack of competitive pressure and the different market access rules in the Member States. These specific objectives are to be attained by the *operational* objectives that can be attributed to the corresponding root causes presented above:

1. to facilitate cross-border entry into domestic rail passenger market;
2. to abolish legal monopolies;
3. to open the PSC market for competition;
4. to establish a common approach to control the definition of PSOs and to define public service contracts;
5. to facilitate the level playing field in access to ticketing.

No specific targets have been set in the IA, with the argument that 'the initiative aims to act as a catalyst of more competitive rail passenger market, but its effectiveness heavily depends on specific approach taken at national level' (IA, p. 44).

• Range of the options considered

In the IA, DG MOVE presents policy options four areas of action concerning open access (A-options), competitive tendering of PSCs (B-options), ticketing (T-options) and rolling stock (RS-options):

Policy options A address the competition in the market for open access lines.

- A0 Baseline scenario: no open access rights to domestic market provided under EU law;
- **A1: Open access, limited when the viability of the PSC is compromised;**
- A2: Open access limited to routes that are commercially viable;
- A3: Open access limited to routes that are not covered by PSCs;
- A4: Unlimited open access.

After the pre-screening of policy options, options A0, A1 and A3 are retained for further analysis.

Policy options B concern the competition for the market, i.e., for PSCs and the supervision of the scope of PSCs.

- B0 Baseline scenario: authorities can choose between direct award and competitive tendering without common criteria for defining PSCs;
- **B1: Mandatory tendering with flexibility and defined minimum criteria and the scope of PSCs is controlled by a national regulatory body:**
 - De minimis threshold under which tendering procedures would not be mandatory of €5m and 150.000 train-km
 - De maximis threshold on the maximal size of clusters of train services of 10m train-km or 33% of the total national volume of rail passenger services
 - 10 years phasing-in of competitive tendering of PSCs until 2023⁷;
- B2: Mandatory tendering with flexibility and defined minimum criteria and the scope of PSCs is controlled by the Commission.

After the preliminary assessment of impacts, options B0 and B1 are retained for the main IA.

The main assessment of impacts considers the six possible combinations of retained A- and B- options as options for market opening:

- Option 0 (A0-B0): Baseline scenario;
- Option 1 (A1, B0): Broad open access and no competitive tendering of PSCs;
- Option 2 (A3, B0): Limited open access and no competitive tendering of PSCs;
- Option 3 (A0, B1): Only competitive tendering of PSCs;
- **Option 4 (A1, B1): Broad open access and competitive tendering of PSCs;**
- Option 5 (A3, B1): Limited open access and competitive tendering of PSCs.

The IA results in option 4 being the preferred option. Although the benchmark analysis in the problem definition stated that 'interestingly, non-liberalised markets score almost twice as much as quasi-liberalised markets' (IA, p. 21) for both quality and efficiency evolution, no options of less market opening are retained for the policy scenario analysis.

Policy options T are set as framework conditions for the A-B-policy options to tackle the discriminatory access to ticketing systems.

- T0 Baseline scenario: With the implementation of existing regulation, RUs and ticket vendors shall offer tickets, through tickets and reservations, voluntary service to other operators has do be non-discriminatory;
- **T1: Voluntary national integrated and non-discriminatory ticketing systems;**
- T2: Mandatory national integrated and non-discriminatory ticketing systems;
- T3: Integrated EU ticketing system, subject to non-discriminatory requirements.

After the pre-screening of policy options, options T0, T1 and T2 are retained for further analysis. **The IA concludes in choosing T1 as preferred option.**

⁷ The IA offers an analysis of several alternative thresholds for the possible sub-options, and explains the reasons for the selected ones, for example, depending on the size of countries and the number of rail km in different countries (IA, p. 52-53).

Policy options RS are defined as framework conditions for the A-B-policy options to enable open access to rolling stock.

- RS0 Baseline scenario: No EU requirements, implementation of State Aid Guidelines;
- RS1: Mandatory creation of rolling stock leasing companies;
- RS2: Mandatory ownership of rolling stock by competent authorities;
- **RS3: Mandatory selling or leasing of rolling stock by the previous PSC beneficiary;**
- **RS4: Obligation for the competent authority to take the financial risks, providing or procuring residual value guarantees on rolling stock;**
- RS5: Guidelines on best practices of rolling stock procurement for national measures.

After the preliminary assessment of impacts, options RS0, RS3 and RS4 are retained for the main IA. **As the IA does not show a clear advantage of RS3 or RS4, both policy options are retained for the analysis of the final preferred policy scenario.**

• Scope of the Impact Assessment

The IA concerns 25 Member States⁸. An elaborate baseline scenario is developed considering the existing railway packages, i.e. the possibility of competitive tendering, no open access and rolling stock requirements in EU law and no obligation of access to ticketing systems. It further factors in growth in the demand for rail services, increasing market shares of new open access operators in some Member States and growing variance of efficiency ratios. The analysis of impacts of this option of no policy change at EU level on competitive pressure and market distortions (in terms of access to ticketing and rolling stock) results in the conclusion that 'competition in railways will continue to evolve at the fringe and the Single European Railway Area will remain incomplete' (IA, p. 41) under this scenario. The IA is preceded by a pre-screening in order to reduce the complexity of the 17 policy options and their 54 possible combinations. This preliminary assessment is based on stakeholder views, effectiveness in terms of policy objectives, efficiency, overall feasibility, subsidiarity and proportionality. Discard of options was in most cases based on subsidiarity concerns. As a result, twelve policy options (A-B-options 0-5 T0, T1, T2, RS0, RS3, RS4), including four baseline scenarios, have been retained for the main assessment of impacts. For policy option B1, an additional preliminary assessment was issued for the sub-options.

The comparison of options is an elaborate and detailed qualitative analysis based on the three dimensions of the scope of impacts, lessons learned from Member States and exogenous and endogenous risks. Clear scenarios of the scope of options are developed and illustrated with numerous examples from Member States and charts.

First, the retained A- and B-options are assessed in six combinations of possible market opening options. The direct impacts on competition levels, transport demand, industry revenues and costs, public funding, investment in rail, administration costs for operators, administrative costs for public authorities, multinational rail activities and small and medium enterprises in rail are assessed as economic impacts. Short notes on indirect economic impacts cover the aspects of innovation, macro-economic growth, regional impacts, relations with third countries and SMEs outside rail, but the results are not included in the comparative table of economic impacts. The category of 'social impacts' includes the assessment of direct impacts on passenger fares, service quality in terms of frequency, destination choice and punctuality,

⁸ Malta and Cyprus do not have railways.

employment in RUs, employment in rail-related sectors, working conditions and rail safety. Two comments on social inclusion and noise are included as indirect social impacts. Environmental aspects are briefly mentioned.

Secondly, the T- and RS-options are considered as framework conditions for the A-B-policy options. Economic impacts for the T-options, i.e., on competition, industry revenues and costs, transport demand, multinational rail activities, administrative costs for public authorities and innovation, are shortly assessed in terms of scope of the potential impacts as well as social impacts on passenger fares and service quality. RS-options are assessed in terms of competition, public funding, multinational rail activities, property rights, industry revenues and costs and innovation in the economic dimension and safety as social dimension. Comparative tables with a description of results for each of the AB-, T- and RS-options in all categories are attached to the respective analysis. The options scoring best over all categories are selected as preferred policy choices.

The categories of assessment are adapted for each set of options to its specific dimensions of impacts as described above. However, the use of different categories reduces the comparability and consistence of the IA. Experiences from Member States include numerous in-depth and accurate examples and a vast array of risks is considered, but the assessment of scope lacks the listing of concrete costs and savings or benefits. DG MOVE admits deficiencies in the assessment of impacts that cannot provide an adequate foundation for the choice of options: 'There is a certain degree of uncertainty in the assessment of impacts of some options, as some evidence for instance is fairly recent (competition in the market in open access services) and sometimes ambiguous (evidence is provided only by specific stakeholders). In this context, the choice to move forward with the aforementioned combination remains a political choice' (IA, p. 100).

Subsequently to the main assessment of impacts, two policy scenarios are analysed for the combined preferred options. Scenario 1 focuses on cost savings assuming that authorities aim to maximise the financial savings from compulsory competitive tendering, with no reinvestment in capacity or quality. Scenario 2 takes reinvestment by authorities into account that are assumed to reinvest 50% of the potential savings of competitive tendering in capacity and/or quality. Sensitivity tests for several categories of assumptions are included. An additional analysis by clusters based on the different baseline situation of Member States is provided, grouping the countries by the level of market liberalisation and the separation between the infrastructure manager and rail operators. In addition, the IA considers the combined impacts of the initiatives of the Fourth Railway Package and states significant synergies of the proposals. Institutional separation of the RUs and the infrastructure managers⁹ is concluded to be 'an important precursor to the delivery of the full benefits of market opening' (IA, p. 107) and 'further boost will be given by quicker time and cost to market for rail undertakings, as proposed by the revised scope of the European Railway Agency' (IA, p. 108).

⁹ Dealt with in the proposal for a Directive of the European Parliament and of the Council amending Directive 2012/34/EU of the European Parliament and of the Council of 21 November 2012 establishing a single European railway area, as regards the opening of the market for domestic passenger transport services by rail and the governance of the railway infrastructure (COM (2013) 29).

- **Subsidiarity implications**

The IA includes a section on subsidiarity that thoroughly explains the necessity of EU action (IA, p. 41-43). The legal basis of the proposal is the EU Common Transport Policy (Articles 56, 58, 90 and 100 TFEU), as well as provisions on services of general economic interest (Article 14 and 106(2) TFEU). The necessity and the European added value of the proposals are checked and confirmed by the Commission. For the proposal COM (2013) 28 on the competitive tendering of PSCs and rolling stock, five reasoned opinions have been issued, from the national parliaments of Austria, Lithuania, Luxembourg, Sweden, and the Netherlands. For proposal COM (2013) 29 concerning the options on open access and ticketing, national parliaments from four Member States have issued reasoned opinions: Lithuania, Luxembourg, Sweden, and the Netherlands.

- **Budgetary or public finance implications**

Apart from national subsidies for the rail sector and budgetary implications for national authorities considered in the assessment of impacts, no further financial impacts are mentioned in the IA. The Commission does not refer to implications for the EU budget.

- **SME test**

No specific SME test has been included in the IA. Nevertheless, the impact on small and medium enterprises in rail is considered in the assessment of direct economic impacts (IA, p. 72) for the A-B-options. DG MOVE assumes that 'overall, the initiative is not likely to have major impact on rail SMEs' (IA, p. 72).

- **Competitiveness test**

As the IA defines the lack of competitive pressure in the rail sector as problem driver and intensifying the competitive pressure on domestic rail markets is named as specific objective of the two proposals in question, the assessment of impacts shows a clear focus on the aspect of competitiveness. Consequences for competitiveness are considered as part of the assessment of economic impacts for each set of options.

- **Stakeholder consultation**

The IA identifies stakeholders to be railway undertakings, passengers, railway manufacturing industry, workers of railway undertakings and national and regional public authorities. Due to the technical nature of the issue, the wide range of different interests in the sector and doubts concerning the representativeness, DG MOVE did not launch an open consultation. A supporting study including targeted consultations was conducted by an external expert (Steer Davies Gleave 2012). The consultations consisted of questionnaires for stakeholders from railway undertakings, infrastructure managers, public transport ministries, safety authorities, ministries, representative bodies and social partners that resulted in a 40% response rate and face-to-face interviews in ten Member States. Commission services met the representatives of interest groups of the railway sector. According to the Commission, 'all relevant parties have been given the possibility to participate in the consultation' (IA, p. 6).

Results from the consultations are continuously referred to throughout the whole IA. They were taken into account in the pre-screening and in most categories of the main impact assessment. In the targeted consultation, a majority of stakeholders agreed to the problems and problem drivers identified in the IA: 'According to stakeholders, existing railway undertakings are not sufficiently responding to market trends and curbing their operational inefficiencies due to a large extent to a lack of competitive pressures and to the existence of an increasingly complex patchwork of national approaches to liberalisation of domestic passenger rail markets which prevent the emergence of a genuine internal market for passenger rail services' (IA, p. 24). Most stakeholders and EU citizens supported the opening of the national and regional rail system to competition. Workers representations voiced concerns about worse working conditions and more strikes following a market opening and argued for greater State funding of the rail sector and its infrastructure to reach the objectives and for the inclusion of social criteria in the awards of contracts. These options proposed by stakeholders have not been considered or discarded with a justification in the IA. The concern of stakeholders that competition has to take place on the level of wages as the sector has very high fix costs is not addressed.

- **Quality of data, research and analysis**

DG MOVE admits that quantification of the impacts of market opening is very challenging and 'results [of an attempt to quantify impacts on investments, profits and public savings] were rather illustrative estimates with up to 50% uncertainty range' (IA, p. 58), because Member States have different baseline situations, experience of market liberalisation is limited and exogenous factors affecting the passenger rail demand are uncertain. But the qualitative analysis shows deficiencies, too. While the results of stakeholder consultations and experiences from Member States are continuously referred to, the argumentation of the IA lacks a foundation of scientific evidence. Assumed impacts of the different options are well illustrated and described, but the reasoning as to why these impacts occur as a result of a specific policy does not appear to be based on facts, academic literature or existing evidence. Especially the assumed reduction in costs of RUs as a result of market opening is not science-based or further explained in detail. Hence, DG MOVE has to admit that 'there is a certain degree of uncertainty in the assessment of impacts of some options, as some evidence for instance is fairly recent (competition in the market in open access services) and sometimes ambiguous (evidence is provided only by specific stakeholders)' and that therefore 'the choice to move forward with the aforementioned combination remains a political choice' (IA, p. 100). Moreover, some of the charts presented in the IA are illegible.

- **Commission Impact Assessment Board**

The Impact Assessment Board (IAB) issued a first opinion on 9 November 2012 asking for resubmission of the IA. A second opinion was given on 30 November 2012 requesting to resubmit the IA again. The IAB subsequently published a third opinion on the second resubmission on 10 January 2013. As recommended by the IAB, DG MOVE improved the IA, better addressing subsidiarity concerns, describing the impacts on employment, referring to the robustness of the calculations, explaining the consultation method, referring to stakeholder opinions and including the European added value. However, the IAB's demands for clearer arguments and factual evidence for the lack of competition in domestic rail markets as problem driver, for more comprehensive alternative policy scenarios, for assessment of impacts on subsidiarity concerning urban and suburban networks, for alternative options for the

competition for PSCs and for the use of available studies on market liberalisation were not fully met in the final document. Furthermore, the IA's section on the Impact Assessment Board does not include a description of the issues addressed by the IAB and of the points improved in answer to the board's criticism, even though this was called for by the IAB in its last opinion.

- **Coherence between the Commission's legislative proposal and IA**

In terms of open access and ticketing, the amending Directive 2012/34/EU (COM (2013) 29) seems to be coherent with the results from the IA, i.e., the preferred options A1 of open access with the possibility to limit access when the viability of the PSC is compromised and T1 of voluntary national integrated ticketing systems, subject to non-discriminatory requirements. Concerning the PSCs and the rolling stock, the proposal amending Regulation (EC) No 1370/2007 (COM (2013) 28) appears to be complying with the conclusions of the IA: the provisions on the PSCs are in line with option B1 of mandatory tendering with flexibility and the thresholds defined in the sub-options. As the impact assessment did not result in a clear advantage of any one option on rolling stock, the proposal leaves it up to Member States to decide for either RS3, meaning mandatory selling or leasing of rolling stock by the previous PSC beneficiary, or RS4, with an obligation for the competent authority to take the financial risks, providing or procuring residual value guarantees on rolling stock.

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This note, prepared by the Impact Assessment Unit for the European Parliament's Committee on Transport and Tourism (TRAN), analyses whether the principal criteria laid down in the Commission's own Impact Assessment Guidelines, as well as additional factors identified by the Parliament in its Impact Assessment Handbook, appear to be met by the IA. It does not attempt to deal with the substance of the proposal. It is drafted for informational and background purposes to assist the relevant parliamentary committee(s) and Members more widely in their work. This document is also available on the internet at:

<http://www.europarl.europa.eu/activities/committees/studies.html>

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Manuscript completed in May 2013
Brussels © European Union, 2013.

ISBN 978-92-823-4434-7
DOI 10.2861/23291
CAT BA-01-13-011-EN-N