



**COUNCIL OF
THE EUROPEAN UNION**

Brussels, 4 February 2013

**Interinstitutional File:
2013/0029 (COD)**

**5985/13
ADD 7**

**TRANS 36
CODEC 216**

COVER NOTE

from: Secretary-General of the European Commission,
signed by Mr Jordi AYET PUIGARNAU, Director

date of receipt: 31 January 2013

to: Mr Uwe CORSEPIUS, Secretary-General of the Council of the European
Union

No Cion doc.: SWD(2013) 13 final

Subject: COMMISSION STAFF WORKING DOCUMENT
EXECUTIVE SUMMARY OF THE IMPACT ASSESSMENT
Accompanying the document
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

Delegations will find attached Commission document SWD(2013) 13 final.

Encl.: SWD(2013) 13 final



Brussels, 30.1.2013
SWD(2013) 13 final

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{COM(2013) 29 final}
{SWD(2013) 12 final}

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Lead DG: MOVE

1. PROBLEM DEFINITION

The Single European Railway Area as defined in the 2011 White Paper on transport policy aims to create an internal railway market where European railway undertakings (RU) can provide services without unnecessary technical and administrative barriers. Despite existing legislation, efficiency and competition problems still exist.

Rail infrastructure is the backbone and driver for the internal market but is also a natural monopoly due to its high costs. Given growing pressure on public finances, improved efficiencies are more crucial than ever to ensure optimal management and utilisation of the shared infrastructure by different RUs. To allow sustainable growth the barriers to entry in the rail sector need to be addressed.

Strengthening the single market by optimising the governance of infrastructure management, in particular by ensuring that the infrastructure manager (a) performs a consistent set of functions coordinates with its EU counterparts on cross-border issues and is responsive to the needs of rail undertakings ("efficiency challenge"); and (b) allows for effective non-discriminatory access to the infrastructure ("equal access challenge"), is a way in which to assist such sustainable growth.

Firstly, an efficiency challenge raises because the current governance does not provide sufficient incentives and means for infrastructure managers (IM) to respond to the needs of the transport services market and to contribute to the optimisation of the performance of the sector taken as a whole. While the Recast of the First Railway package has introduced the obligation to IM to consult users and foresees use of performance schemes and targets, these do not allow for a structured and continuous dialogue with users. In addition, the distribution of different infrastructure management function among different market players can lead to inconsistencies in the management of infrastructure and increase coordination costs. Finally, an important condition for completing the Single European Rail Area is to improve the functioning of cross-border cooperation of IMs.

Secondly, conflicts of interest in vertically integrated railway holdings naturally lead to protectionist practices of historical incumbents which impair competition in rail services for all other applicants and thus result in "equal access challenge". Experience over the last

decade has demonstrated that the implementation of current separation requirements did not completely prevent the conflicts of interest and discriminatory practices in respect of access to rail infrastructure and related services. In addition, the existing legal framework has proven to be insufficient to allow detection of and prevent cross-subsidisation from IMs to incumbents. Even reinforced regulators' powers under the Recast cannot prevent this, as the risk is inherent in the existing structure.

The problems described above and the measures to be proposed to address them will affect a large number of players in the rail market including national authorities, IMs, RUs and indirectly also passengers and users of rail freight services.

2. SUBSIDIARITY

Articles 58, 90 and 100 of the Treaty extend to railways the objectives of a genuine internal market in the context of an EU Common Transport Policy.

Actions by Member States alone cannot ensure the coherence of EU railway market and address the divergent interpretation of the legislation, as persistence of national rules and sub-optimal functioning of national institutions, acting as barriers to the internal market, is in fact at the centre of the problem. Action at EU level aims to ensure consistent implementation of the EU rail *acquis*, which should lead to the creation of the Single European Railway Area with no unnecessary administrative and technical barriers.

3. OBJECTIVES

General objective: Strengthen further the governance of railway infrastructure, thereby enhancing the competitiveness of rail sector vis-à-vis other modes and developing further the Single European Rail Area.

Specific objectives:

Efficient management challenge:

1. Improve the IM ability to manage efficiently the infrastructure in favour of users

Equal access challenge:

2. Eliminate conflict of interest and distortions of competition in infrastructure access

Operational objectives:

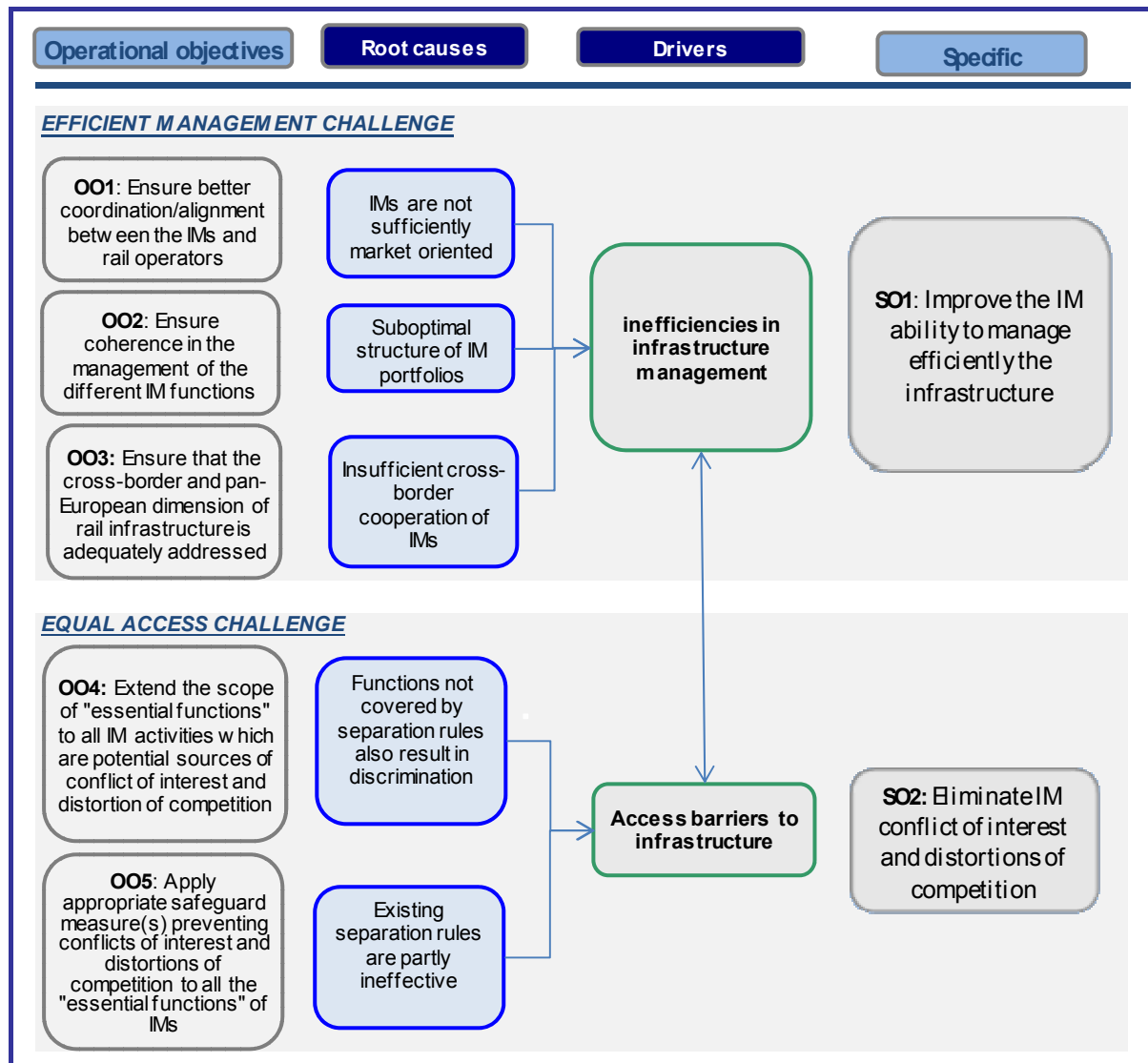
Efficient management challenge:

1. Ensure better coordination/alignment between the IMs and rail operators
2. Ensure coherence in the management of the different IM functions
3. Ensure that the cross-border and pan-European dimension of rail infrastructure is adequately addressed

Equal access challenge:

1. Extend the scope of "essential functions" to all IM activities which are potential sources of conflicts of interest and distortions of competition
2. Apply appropriate safeguard measure(s) preventing conflicts of interest and distortions of competition to all the "essential functions" of IMs

Figure 1 – Mapping between Problems drivers, root causes and objectives



4. POLICY OPTIONS

To address the two main challenges of efficiency and equal access in order to find an optimal governance structure five groups of options were screened, each proposing measures to remedy the different problem elements, such as market co-ordination, consistency of function, cross-border interfaces, conflicts of interest and equal access. For each group two to four options were developed in addition to baseline options. The combination of all these options could create theoretically 576 scenarios. To reduce complexity, for each set of measures, pre-screening was based on stakeholder views, compliance with subsidiarity/proportionality principles, effectiveness in terms of policy objectives and overall feasibility. The table below

shows the 11 options that have been retained including 5 baseline scenarios of the 19 options assessed.

Problem element	Respective category of options	Policy options considered	Retained
Insufficient market orientation of IMs	C options: Coordination between IM and RUs	Option C0: Baseline – improvements as foreseen by the Recast	✓
		Option C1: RUs participation to IMs' board	
		Option C2: IMs-RUs coordination bodies	✓
		Option C3: Alignment through new financial incentives	
IM functions managed in an inconsistent manner	F options: Consistent management of key functions	Option F0: Baseline – the content of existing essential functions is clarified by the ECJ	✓
		Option F1: New coordination mechanism between the various entities in charge of IM functions	
		Option F2: Unified IMs (all IM functions under IM responsibilities)	✓
Cross-border cooperation between IM not sufficient	CB options: Cross-border IM management	Option CB0: Baseline - implementation of existing EU law (the Recast, regulation of rail freight corridors, etc.)	✓
		Option CB1: Establishment of an EU network of IMs	✓
		Option CB2: Creation of an EU structure integrating national IMs	
Equal access needs to be assured to all key functions	SF options: Functions subject to the separation requirements	SF0: Baseline – separation requirements applying only to path allocation and track access charging	✓
		Option SF1: Current essential functions+ traffic management separated	
		Option SF2: Current essential functions +traffic management + maintenance separated	
		Option SF3: All IM functions separated	✓
Conflicts of interests in the management of IM functions management	S options: Way of separation of IMs from RUs	Option S0: Baseline - existing separation requirements for the essential functions as interpreted in the forthcoming ECJ ruling	✓
		Option S1: Additional competences for regulatory bodies	
		Option S2: Clarify in EU law the concrete implications of existing separation obligations	✓
		Option S3: Institutional separation	✓
		Option S4: Compliance officer in integrated structures	

After screening, only the following scenarios and options have been retained:

Category of options	Baseline Scenario	Scenario 1	Scenario 2	Scenario 3
Coordination between IM and RUs	Option C0: Improvements as foreseen by the Recast	Option C2: Coordination bodies	Option C2: Coordination bodies	Option C2: Coordination bodies
Consistent management of key functions	Option F0: existing essential functions are clarified by the ECJ, but scope remains limited	Option F2: Unified IMs	Option F2: Unified IMs	Option F2: Unified IMs
Cross-border IM management	Option SC0: implementation of existing EU law - the Recast, regulation of rail freight corridors.	Option CB1: establishment of an EU network of IMs	Option CB1: establishment of an EU network of IMs	Option CB1: establishment of an EU network of IMs
Functions subject to the separation requirements	Option SF0: Only path allocation and track access charging separated	Option SF3: All IM functions separated	Option SF3: All IM functions separated	Option SF3: All IM functions separated
Way of separation	Option S0: Existing separation requirements	Option S0: Existing separation requirements	Option S2: Clarify in EU law the concrete implications of existing separation obligations	Option S3: Institutional separation

5. ASSESSMENT OF IMPACTS

Assessment was carried out on the main economic impacts of the scenarios, derived from their impact on the railway sector. The report focuses on direct impacts on the railway sector in terms of enforcement costs, transaction costs, regulatory costs, the costs of discriminatory practises, that of the cross-subsidisation, but also the impacts of separation on the efficiency of infrastructure usage (including assessment of misalignment costs). Assessment of induced impacts of the initiative, such as level of competition, level of activity, investments, service quality, safety and SME impacts is also presented. It also considers the wider indirect impacts on the European transport system and economy. The analysis is mostly derived from qualitative assessment of the policy options supported by quantitative elements where possible.

Furthermore assesment on environmental impacts included climate change, pollution and noise, and social impacts such as impacts on employment levels, safety and working conditions including wages were considered.

Assessment of direct impacts

Impacts compared to the Baseline	Scenario 1 (only efficiency measures)	Scenario 2 (efficiency and enforcement of separation)	Scenario 3 (efficiency and institutional separation)
Enforcement costs (one off)	0/-	-- Potential scale of costs €0.17 billion	- Potential scale of cost €0.24 billion -
	Limited costs related to establishment of coordination bodies in many MSs and unifying IM functions in some MS.	Related to the costs of internal reorganisation necessary to put in place "Chinese walls". Impacts the MSs having integrated or holding structures.	~0.9% of yearly operating costs. Impacts the MSs having integrated or holding structures.
Transaction costs	+	- Potential cost range €0.05 bn and €0.16 bn per annum	-- Potential cost range €0.05 bn and €0.16 bn per annum
	Some improvement due to better coordination. Impacts to all MSs.	At least 0.15% of operating costs. Impacts the MSs having integrated or holding structures.	~0.3% of operating costs. Impacts the MSs having integrated or holding structures.
Regulatory costs	0	0	+
	It is not expected the costs of regulatory enforcement under Scenario 1 to be materially lower than those arising in the Baseline.	It is not expected the costs of regulatory enforcement under Scenario 2 to be materially lower than those arising in the Baseline.	Regulatory costs per train-kilometre could decline by up to 75% as a result of institutional separation. Impacts the MSs having integrated or holding structures.
Other costs and benefits, linked to:			
Discrimination	0	0/+	++
	No impact	The scope of oversight of regulatory bodies is extended, but remains mostly reactive thus only partly evading discrimination related opportunity costs.	Full institutional separation would eliminate opportunity and motivation for discrimination.
Cross-subsidisation	0	0/+	++
	No impact	Transparency issues and cross-subsidisation risks remain inherent in integrated and holding structures even if account separation requirements are in place.	Full institutional separation would provide necessary transparency and eliminate opportunity for cross-subsidisation.
Efficiency	+	+	++
	Increasing competitive pressure and specialisation of the market players will have an additional positive effect on their productivity and efficiency. At the same time, as further explained under Annex V, there are risks of loss of synergies and economies of scope which can appear in cases of separation between IMs and a dominant RU. However, this is inherent in order to ensure a level playing field for all operators. These risks will be mitigated by the enhanced coordination between IMs and infrastructure users as well as full implementation of the financial incentives foreseen by the Recast (modulation of charges, incentive scheme and performance regime). Such measures will ensure adequate alignment of strategies and investments leading essentially to long term efficiency gains.		

Assessment of induced and indirect impacts

Impacts compared to Baseline	Option 1	Option 2	Option 3
Economic impacts			
- Impact on railway business			
Level of competition	+	++	+++
Level of activity of railway operators	+	++	+++
Level of investment	+	++	++
Level of service quality and punctuality	0/+	+	++
Level of rail safety	0	0	0
Impact on SMEs	0	+	++
- Impact on the transport sector			
Modal shift	0/+	+	+
Efficiency of the transport system (congestion and travel times)	+	+	++
European economy	+	+	+
Impact on the European economy	+	+	+
Environmental impacts			
Climate change	0/+	+	+
Pollution	0/+	+	+
Rail noise	0/+	0/+	0/+
Social impacts			
Employment and working conditions in the railway sector	+	+	++
Transport safety	0/+	0/+	0/+

6. COMPARISON OF OPTIONS

Taking into account all impacts, scenario 3 is considered to be the most beneficial where an IM users' coordination body is created, functions are unified, an EU network of IMs is created and all IM functions are subject to institutional separation requirements.

In addition this scenario best meets the general, specific and operational objectives, improves conditions for competition and efficiency in the railway system. It facilitates economic growth, enhances capacity utilisation and infrastructure performance, and reduces obstacles and barriers to entry through the elimination of conflicts of interest. It also ensures financial transparency and reduces the cost of regulation with limited enforcement costs.

The overall results of the comparison of scenarios are set out in the table below.

	Effectiveness		Operational IM efficiency	Efficiency			Coherence		Motivation
	SO1: Improve the IM ability to manage the infrastructure	SO2: Eliminate distortion of competition in infrastructure access		Enforcement costs	Regulatory costs	Transaction costs	Employment and working conditions	Environmental sustainability	
	0	0	0	0	0	0	0	0	Scenario 0
Scenario 1	++	+/0	+	0/-	0	+	+	0/+	Scenario 1 is expected to already have a substantial positive impact on IM efficiency. However, in terms of reduction of conflicts of interest, it will have only a limited impact resulting from the extension of the existing independence requirement to all IM functions. While existing transaction costs are impacted in a positive but limited manner by better alignment between IM and RUs, regulatory costs and enforcement costs increased moderately as efficiency measures imply a limited administrative burden. Social and environmental impacts are moderate but positive.
Scenario 2	++	++	++	--	0	-	+	+	Scenario 2 will have the same positive impact than Scenario 1 on the IM ability to manage the infrastructure. However its operational efficiency will improve further with increasing competitive pressure on RUs. Scenario 2 removes conflicts of interest in infrastructure access but does not ensure optimal financial transparency and the absence of distortion of competition. Transaction costs increase with the number of new entrants and traffic growth. Both enforcement and regulatory costs are higher due respectively to the implementation of "Chinese walls" and the absence of financial transparency. Social and environmental impacts are moderate but positive.
Scenario 3	++	+++	++	-	+	--	++	+	Scenario 3 improves further the IM ability to manage the infrastructure thanks to the specialisation benefits on institutional separation. With full financial transparency, it eliminates completely risks of distortion of competition at a relatively low enforcement and regulatory cost. Transaction costs increase further despite the mitigating effect of better alignment between IMs and RUs. Traffic growth and efficiency generate the highest positive social and environmental impacts.

7. SUMMARY OF THE RESULTS OF THE 4TH RAIL PACKAGE INITIATIVES

The ultimate goal of separation is to create a more competitive and efficient rail sector and thus encourage a better service offer, while improving the use of public funds fed via subsidises into railways. The table below summarises the financial benefits for:

1. the separation initiative only (column 1)
2. the domestic passenger market opening only for two scenarios:

Market Opening Scenario 1 - Focus on savings (column 2) - In this scenario it is assumed that competent authorities would focus on cost savings, taking all the reductions in PSC tender costs as cash savings and not reinvesting any of these in higher rail quality or capacity.

Market Opening Scenario 2 - Reinvestment (column 3)- In this scenario it is assumed that competent authorities would not focus on cost savings but would instead implicitly “reinvest” half the potential reductions in PSC tender costs by specifying higher quality or capacity in PSCs. In terms of monetary impacts this implies reduction in NPV, while the benefits appear in terms of increase in passenger km-s.

3. combined impacts of both initiatives separating two different outcome scenarios:

Combined Impacts Scenario 1 – Focus on savings (column 4)

Combined Impacts Scenario 2 – Focus on reinvestment (column 5)

Combined core financial estimates of impacts of market opening and infrastructure governance policies					
All changes are illustrative estimates NPVs (bil €) to 2035, discounted at 4% to 2019	Separation Scenario 3	Market opening: Scenario 1 - Savings	Market opening: Scenario 2 - Reinvestment	Combined impacts: Scenario 1 - Savings	Combined impacts: Scenario 2 - Reinvestment
	1	2	3	4	5
Transaction costs (mean estimate)	-1.37	-0.42	-0.42	-1.77	-1.77
Domestic service benefits*	5.86	29.85	21.46	43.07	33.71
International service benefits	1.07			1.05	0.89
Freight benefits	1.00			1.00	1.00
Total NPV	6.56	29.44	21.04	43.35	33.83

The institutional separation envisaged under Scenario 3 is an important precursor to the delivery of the full benefits of market opening, as already implemented for rail freight market and international passenger rail market. The two initiatives together result in important synergies as demonstrated in the table below.

Combined outcome range impacts of market opening and infrastructure governance policies			
All changes are illustrative estimates in euro per annum	Financial benefits (NPV, € bn)	Increase in passenger km (bn)	Increase in new entry market share (%)
Scenario 1 – Focus on saving			
Vertical separation alone	6.56	0.8	0.5
Market Opening alone	29.44	2.0	3.8
Combination of market opening and vertical separation	43.35	3.8	6.4
Scenario 2 – Reinvestment			
Vertical separation alone	4.42	1.1	0.5
Market Opening alone	21.04	8.4	3.7
Combination of market opening and vertical separation	33.83	16.4	6.2

The first scenario focuses only on financial benefits (consisting mostly of public savings) while the second reinvestment scenario would allow provision of 16.4 billion additional passenger-km (6% increase of passenger-km on top of the baseline developments) and would enable an 6% increase in market share of new entrants to 25%.

8. MONITORING AND EVALUATION

The Commission will monitor and evaluate the implementation of the specific objectives of this legislation and its impacts through a set of indicators on an ongoing basis. In order not to increase the burden on bodies responsible for providing data, these indicators are aligned with those provided to the Commission as part of existing EU law through the enhanced Rail Market Monitoring Scheme (RMMS), regulatory bodies and the European Railway Agency.

Indicators will include infrastructure utilisation rates, traffic volumes, the number of new entrants, market share of new entrants and complaints to regulators.

Much of this information is already available from the existing RMMS which involves all relevant stakeholders and the Recast foresees enhancements to cover infrastructure charging, capacity allocation, investments in railway infrastructure, pricing, quality of services, public service contracts, licensing and the degree of market opening, harmonisation between Member States and employment and the related social conditions.