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**RAIL TRANSPORT**

**RAILWAY REFORM AND CHARGES FOR THE USE OF INFRASTRUCTURE  
CONCLUSIONS AND RECOMMENDATIONS**

*This document will be examined under item 3.3 "Rail Transport" of the draft agenda of the Moscow Council of Ministers.*

*Ministers are invited to adopt the Recommendations.*

**English - Or. English**

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## RAILWAY REFORM AND CHARGES FOR THE USE OF INFRASTRUCTURE

### Introduction

Ministers adopted Resolution 2002/1 on the Development of Railways at the Bucharest Council to promote the development of seamless rail services across Europe and to foster the development of competition in rail freight markets to improve the efficiency and quality of rail services. The Resolution supports the restructuring of railways driven by European Union Directives and focuses on three critical regulatory issues.

- An appropriate set of charges for the use of infrastructure is required to ensure non-discriminatory access to, and efficient use of, the network;
- Fair competition has to be supervised by independent, proactive regulatory bodies;
- The most effective approach to introducing competition depends on the market, thus:
  - charges for the use for infrastructure need to be structured differently according to market (freight, main line passenger, high speed rail, commuter services);
  - competition for markets, as opposed to competition on the tracks, is probably most effective for most passenger train operations and especially for regional and commuter passenger services, and it is important that the award of exclusive concessions for these services is made through competitive tenders;
  - in markets suited to competition between integrated track and train operators, such as in European Russia, serious consideration should be given to restructuring railways to achieve this kind of competition between evenly matched companies, as it imposes a lower burden on regulatory authorities than promoting competition from new market entrants, especially when the national train operator owns the national rail infrastructure or is part of a holding company that owns it.

Development of rational charges for the use of infrastructure is reviewed in report CEMT/CM(2005)18. Much progress has been made since adoption of the Resolution of 2002, but **the European dimension is missing** from the critical freight market. Ministers now need to focus on achieving a set of simple charges for freight that create similar incentives for the management and planning of train operations across national borders.

The way charges are determined is also crucial to the recurring issue all Ministers face: **how big a rail network and how many non-commercial passenger services should be supported by the public budget?** Undercharging trains threatens the long term financial sustainability of the network and deferring renewals can increase costs to crisis point in the long run. Undercharging subsidized passenger trains often results in over-charging freight, damaging its competitiveness with road haulage.

## Conclusions

Existing infrastructure charging regimes are not fully consistent with Minister's objectives:

- for promoting financially stable infrastructure providers;
- for providing effective price signals to users of rail infrastructure; or
- for promoting effective competition in the markets (especially international freight) where competition would be sustainable.

The divergence of current infrastructure charges is illustrated in figure 1, showing cost recovery rates, and figure 2, showing average charge levels. Some differences are to be expected. For example, the upper bound for cost recovery is a question for political decision at the national level. Also the mix of traffic (see figure 3) and traffic densities vary greatly between countries and this has a strong influence on costs.

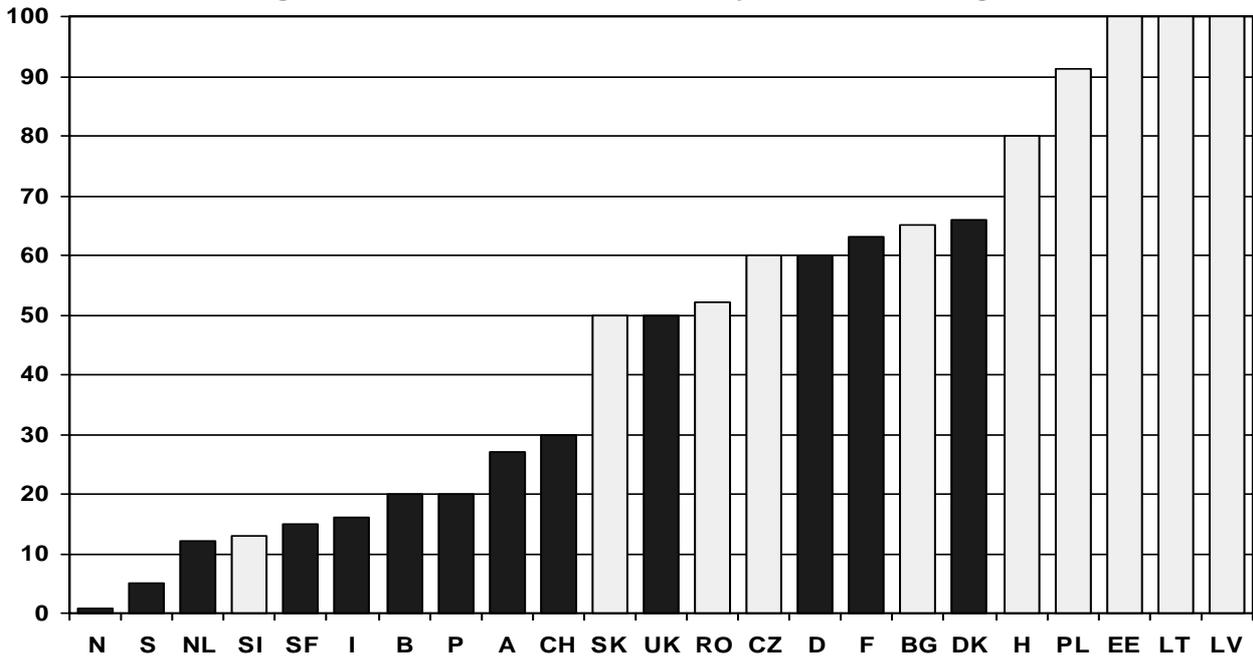
Some of the differences observed, however, create financial risks or undermine the competitiveness of rail services.

- Some countries charge at levels significantly below the rational lower bound represented by marginal costs, including renewals. It makes little sense to carry traffic that can not even pay the marginal costs it imposes on the network in terms of wear and tear and train planning<sup>1</sup>.
- Some charging systems result in freight trains covering some of the costs of passenger trains in order to push down the budget transfers required to pay for passenger service obligations. This is financially un-sustainable as it will destroy the competitiveness of rail freight.
- There are many instances of barriers to international services created by differences in the way countries along international corridors structure charges. Freight train charges that are structured to provide incentives to consolidate loads and run fewer, longer trains in one country, and structured to promote operating short, light trains in a neighbouring country complicate train path planning and increase the costs of international paths. This will suppress international rail traffic.

There has so far been a failure to co-operate internationally to correct these distortions, seriously undermining international rail markets. Harmonizing the structure of charges for freight trains would:

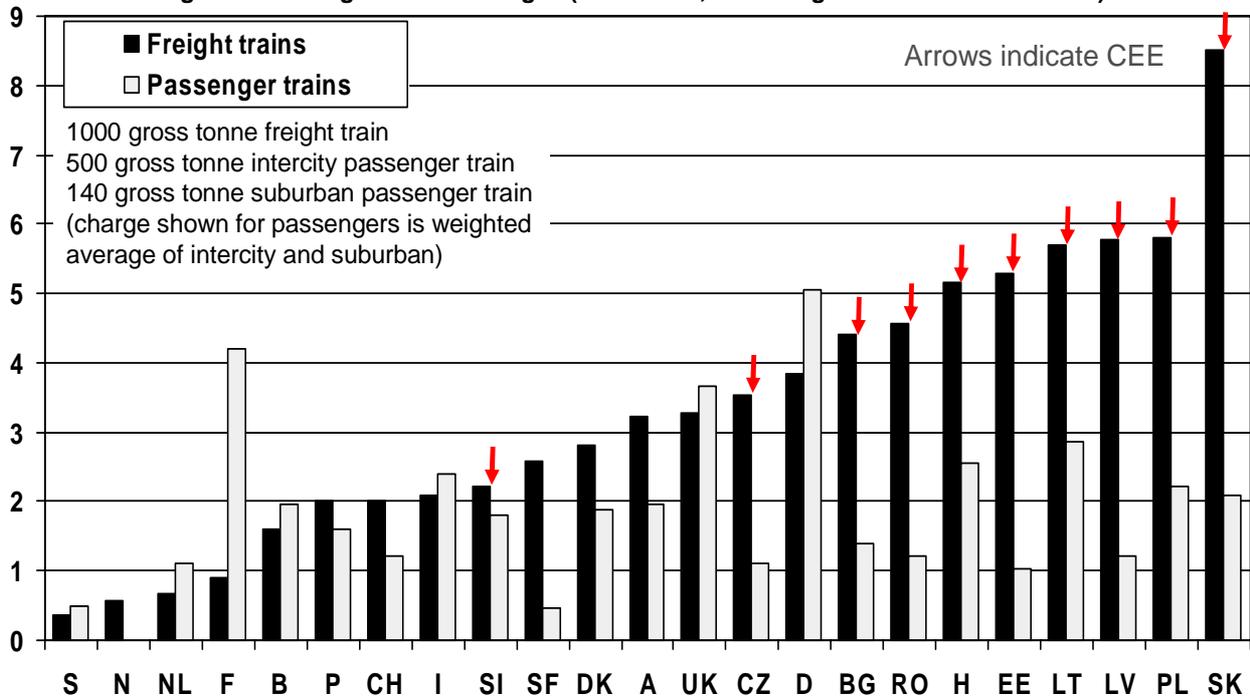
- reduce the cost of international services, improving competitiveness;
- facilitate the planning of international services; and
- enable railways to be more responsive in quoting prices to shippers.

Figure 1. Percent of Total Cost Covered by Infrastructure Charges



Cost recovery = Revenues from charges as a proportion of total expenditure on the network on operations, maintenance, renewals, interest and depreciation; Light shading indicates central and eastern European countries. Marginal costs can be expected to lie at roughly 15 to 20% of the cost figures reported.

Figure 2. Average Access Charges (€/ train-km, excluding cost of electric traction)



Baltic freight trains are much larger than elsewhere. Baltic access charges are not directly comparable with those in other countries and have been adjusted here. In Estonia, for example, a typical 3145 tonne train is charged €11 per train-km. Data displayed for all countries for which reliable figures have been collected.

## Recommendations

Ministers need to cooperate to promote the development of more coherent charges for the use of infrastructure. For international rail freight services this is an urgent priority. Ministers will need to provide guidance to their national infrastructure managers and consult with rail regulatory agencies to facilitate this.

Independent<sup>2</sup> economic rail regulatory authorities can play an important role in ensuring many of the specific recommendations that follow are implemented, and could play a useful role in all Member countries.

### **1. *Harmonise charges for international freight trains***

The structure of charges for freight trains should be harmonised, especially along key international corridors. Charges should be set on the basis of marginal costs, with simple mark-ups where required. There could be merit in adopting similar charges for domestic freight as well in many countries.

These charges need not be uniform in level but must be consistent in structure and should be based on a set of simple factors of use, at least outside of capacity bottlenecks and peak hours. Charges per gross tonne-km should be employed to reflect maintenance and renewal costs for track<sup>3</sup>. Where freight capacity is not constrained, such a single factor, simple charge may be sufficient. Where capacity for freight is constrained (and the marginal costs of freight traffic are significant) charges per train-km may also be useful.

It should be accepted, however, that where rail freight is the dominant use of the network and its market position is strong (as in the Baltic States for example) an alternative approach based on full costs is appropriate.

### **2. *Structure charges for passenger and freight trains to balance competition and financial objectives***

National access charge regimes should be related to the complexity and intensity of the use of the rail network. Countries with intensive traffic and a multiplicity of users could best construct their access regime from a mix of approaches:

- Full cost based charges (with costs recovered as a two part tariff) for suburban and non-competing intercity passenger operators running on exclusive rights of way.

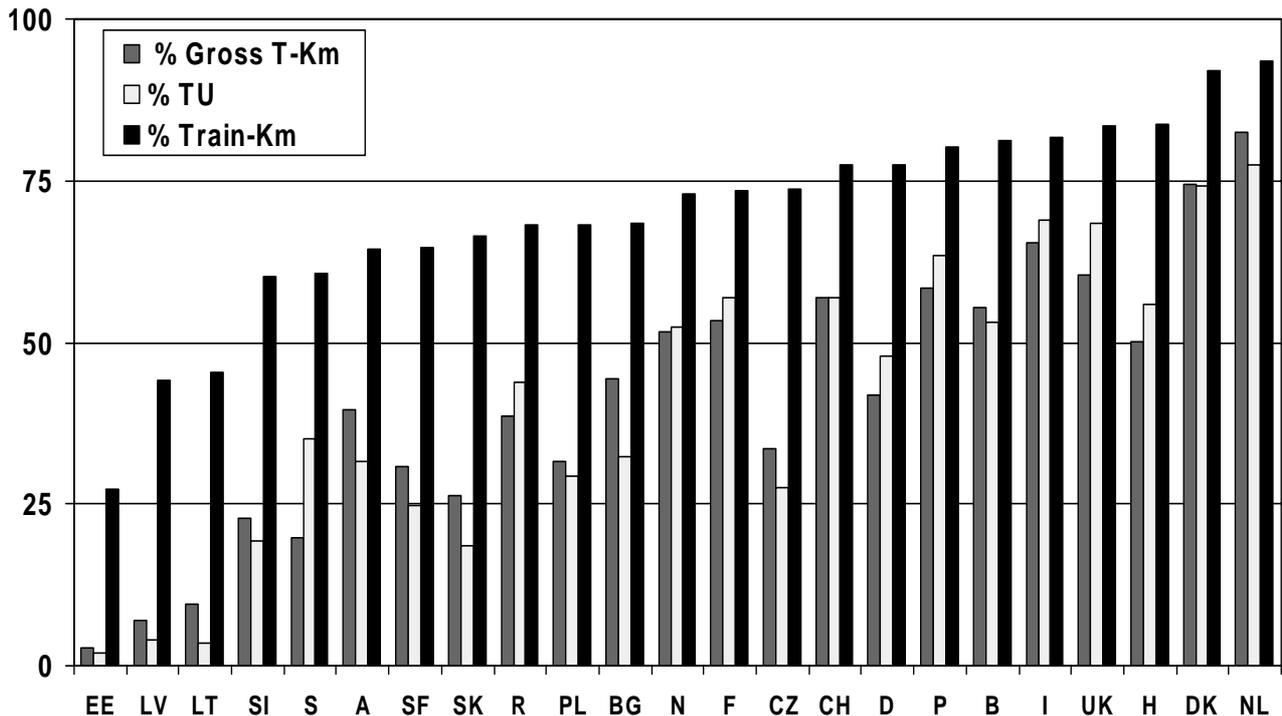
It makes sense to recover full costs from these services where they are the dominant user of the system, generating most of the costs, which is almost always the case around major cities, and generally the case across the whole network in many member countries. Where passenger trains are a marginal user on freight dominated systems it may be appropriate to charge them only marginal costs.

In the case of passenger services supported from public budgets under public service obligations, charging these trains the full costs they impose on the network makes the costs entailed more transparent for the public authorities that decide on the level of services that should be provided. This should help reconcile the demands for services from one part of government (for example transport local authorities) with the resources available from public budgets for rail infrastructure.

- Simple marginal cost based charges, plus a mark-up where necessary, for situations where intercity passenger trains will compete on the same tracks. Fixed charges need to be avoided as they almost always present a barrier to small operators seeking to enter the market.

Such a mixed approach, with simple marginal costs charges for freight, with a mark up where required for higher cost recovery, will permit the best balance among competition and financial stability objectives to be achieved.

Figure 3. Traffic Mix (Percent Passenger Traffic)



Note: TU=P-Km + T-Km

### **3. *Provide for renewals***

Infrastructure managers should at least collect marginal costs, including accelerated renewals, from all trains. Variable, traffic-driven renewal costs, that is the increased present value of costs that result from having to undertake renewals sooner than if a train had not been run on the track, are not always charged for at present. As noted above, it makes little sense to carry traffic that cannot pay at least these costs. For rail freight to remain competitive with alternative modes it is important to achieving recovery of these infrastructure renewal costs also in other modes of transport.

### **4. *Respect financial commitments***

Transport policy determines the size of the gap between the revenues generated from access charges and the full cost of maintaining and renewing the infrastructure network. The key factors are specification of the services to be delivered under public service contracts and setting the framework for infrastructure charges. Filling the gap from public funds is essential for financial sustainability, with long term implications for the quality and safety of the network and the cost of maintaining it. Short term pressures inevitably lead finance ministries and parliaments to seek cuts in spending from time to time that are inconsistent with existing policy. The chief risk is delays to renewals that cause the condition of the network to deteriorate and a backlog of expenditure to accumulate. Regulatory agencies with powers to set charges, and that are independent of government (at least in the short term), can play an important role in ensuring agreed funding is provided fully and reliably from State contributions. This represents the enforcement of agreements rather than an open cheque for the railways and can be complemented with duties to assess the efficiency of the rail infrastructure manager. Table 1 summarises the current regulatory arrangements in Member countries

### **5. *Use public service contracts with competitive tendering***

Long term public service contracts are another important guarantee of financial sustainability. They should always be used for passenger services that are not fully commercially viable but are required of train operators by the State. These contracts should fund train operators to cover at least the avoidable costs of the services concerned, including infrastructure charges. As competition on the tracks is difficult and sometimes impossible to create for these services, competition for the market is to be preferred, through competitive tendering for exclusive public service contracts.

### **6. *Ensure adequate public information on rail costs and accounts***

Getting adequate data into the public domain is pre-requisite to full implementation of these recommendations. Data is currently insufficient to say with certainty which infrastructure managers charge below marginal costs or just how serious the practice, traditional in Eastern Europe, of covering passenger costs from freight charges is.

Ministers should require line of business accounts and a complete record of government support to be reported annually to public authorities by infrastructure managers and train operators, in a consistent format. Reports from infrastructure

managers should include a discussion of any changes in the condition of the infrastructure from the previous year, and a statement of the degree to which income from users plus government support meets or falls short of the cost of maintaining the infrastructure including any required renewals. This should be included in the annual Network Statement that infrastructure managers are already required to produce in the European Union.

**Table 1. Industry Structure and Regulatory Arrangements**

Country	Industry structure	Overseen by independent rail regulator	Overseen by independent general competition authority	Overseen by Ministry of Transport
Austria	I	Yes	Yes	
Belgium	I			Yes
Bulgaria	S			Yes
Czech Republic	S			Yes
Denmark	S	Yes	Yes	
Estonia	I freight	Yes		
Finland	S		Yes	Yes
France	S			Yes
Germany	I	Yes	Yes	
Greece	I		Yes	Yes
Hungary	I	Yes		
Ireland	I		Yes	
Italy	I		Yes	Yes
Latvia	I	Yes	Yes	
Lithuania	I	Yes		Yes
Luxembourg	I			Yes
Netherlands	S		Yes	
Norway	S			Yes
Poland	I	Yes		
Portugal	S	Yes	Yes	
Romania	I	Yes		
Russia	I		Yes	
Slovakia	S			
Slovenia	S	Yes		Yes
Spain	S			Yes
Sweden	S	Yes	Yes	Yes
Switzerland	I	Yes	Yes	Yes
United Kingdom	S	Yes	Yes	

S, vertical separation, where the infrastructure manager (or affiliated company) is not allowed to operate services on that infrastructure;

I, vertical integration, where the infrastructure manager is allowed to operate services on that infrastructure, holding company structures are included in this category.

There is ample precedent in regulatory experience, for example in the USA and Canada, for requiring that railways report their annual results in a common format that permits analysis of individual railway performance and facilitates comparisons among railways. The burden this imposes on railways is negligible as they should already be collecting this information for proper management of their assets.

Europe's railways also need a common understanding of how to define and measure marginal private and external costs for use of rail infrastructure. Joint efforts are needed for a common approach and a consistent database. This has direct policy relevance and is not simply a research question.

### **Follow-up**

The work on which these conclusions and recommendations is based has been discussed extensively with the Task Force on Rail Track Access Charges of the European Union. It will be important to ensure all ECMT Member countries clearly understand the EU policy developments that result from the deliberations of this group, in order to be in a position to adopt appropriate measures of their own and bring maximum benefits to European rail markets.

In continued coordination with the European Commission, ECMT should bring the results of research into the measurement and definition of rail costs into the policy making arena to provide the basis for developing more precise guidelines for establishing efficient infrastructure charges.

ECMT should provide guidelines on the public reporting of rail costs and accounts and the condition of infrastructure necessary as the basis for full implementation of the recommendations made here.

Deputies will report to Ministers on progress towards implementing the recommendations, and in particular harmonization of the structure of infrastructure charges for international freight trains.

Ministers are invited to:

- Adopt the six recommendations set out in this report;
- Approve the follow-up foreseen.

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1 Unless this is explicitly to correct for distortions on other modes and in that case the better course of action is to remove those distortions.

2 Independent of government as well as train operators and infrastructure managers.

3 Or per wagon-km, which is simpler but less accurately reflects gross weight.