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European Green Deal: What Implications for State Aid in the Rail Sector?

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Highlights

In its European Green Deal the European Commission sets the objective of achieving climate neutrality in Europe by 2050. To support the delivery of this objective in relation to transport, which accounts for a quarter of the EU's total greenhouse gas emissions, the Commission has declared 2021 as the European Year of Rail. A significant modal shift will be needed from less environmentally sound modes, such as road in particular, but also aviation, towards the greenest modes, namely rail and inland waterways, without compromising the connectivity of goods and persons, which is at the heart of the single market. This, in turn, will require measures to manage better, and to increase the capacity of railways and inland waterways, which the Commission has pledged to propose by 2021. COVID-19 has hit the transport sector particularly hard. There is a broad consensus that EU and national regulations should seize the opportunities afforded by the recovery plans to exit the crisis to promote the twin green and digital transformations.

The 19th Florence Rail Forum, co-organised by the Transport Area of the Florence School of Regulation together with the Commission's DG COMP and DG MOVE, examined the role of State aid in meeting the challenges of the Green Deal. Evaluations are currently underway of the relevant State aid guidelines including those pertaining to railways. Any revision will have to reflect the policy objectives of the Green Deal and ensure a level-playing field in the internal market. Investments will be paramount to boosting intermodal freight transport, in particular in transshipment terminals but also more generally in rail infrastructure (to ensure interoperable and sufficient capacity), and, possibly, in rolling stock or technology (e.g., automation for train composition). The Forum discussed the cases that justify State aid in order to support investment as well as operations, and moreover, the conditions under which State aid should be declared compatible to make intermodal freight transport attractive. The possibility and conditions to set up public service obligations for (structurally non-viable) rail freight routes was also discussed in view of ensuring sufficient capillarity and addressing the issue of the unprofitable last mile service. As regards passenger rail, the forum examined the demonstration of the necessity of public service contracts by public authorities.

State Aid in a Sustainable and Smart Railway Ecosystem

A comment by Juan Montero and Matthias Finger, Florence School of Regulation – Transport Area

The Community guidelines on State aid for railway undertakings need a review to be adapted to the European Green Deal's new policy goals. Railways can thrive if their competitive advantages are fully exploited, which requires bottlenecks and market failures to be reduced. The guidelines could provide more guidance on State aid for multimodality as well as for very-long-distance services. State aid for digitalisation could unleash the competitiveness of rail. New possibilities for Public Service Obligations could be explored.

The new objectives for a sustainable and smart transport system in the European Union require new coordination policies and a review of the State aid policy for the coordination of transport.

The Green Deal objectives call for bold policies to ensure a shift to rail both for freight transport and passenger mobility. Net climate neutrality in Europe by 2050 is the ambitious target set in the European Green Deal Communication. Transportation accounts for a quarter of the EU's total greenhouse gas emissions. Railways and inland waterways are the environmentally more sound transport modes and thus the shift to railways and inland waterways is the only form to reach the sustainability objectives.

The Community guidelines on State aid for railway undertakings need a review in order to be in line with the new policy goals, as State aid plays a fundamental role in the coordination of transport. The guidelines, adopted in 2008, already identified in railways a great potential for contributing to the development of sustainable transport in Europe. However, twelve years later, the necessary modal shift to rail has still not happened. A bold change in the transport coordination policies is necessary, and it has to be based on the exploitation of the competitive advantages of railways. State aid has an important role to play.

Firstly, the guidelines could provide more guidance on multimodality. Railways are the most competitive transport mode in dense routes, but they are hardly competitive for door-to-door services, as the first and last miles tend to have low density of usage, both for goods and passengers. We have learnt that modal shift will not be the result of railways completely substituting other transport modes. On the contrary, goods and passengers will shift to railways, as they are better integrated in the wider transport and mobility system. For railways to increase their modal share, goods and passengers need to use other transport modes for the first and last miles, so they can reach the high capacity routes served by railways. Together with more traditional public transport solutions, the new micro-mobility solutions are the perfect complement for railways both for urban and long-distance traveling. Goods also require simple and efficient transshipment from road to rail, as well as from vessels to railways in ports.

The guidelines could evolve from ruling State aid to railway undertakings, to rule State aid for multimodal land transport. Specific mechanisms are necessary to solve market failures related to railways' interconnection with other land transport modes. State aid can support the investment in multimodal terminals, both road-to-rail and inland waterways-to-rail terminals. Furthermore, the land transport system needs to be better connected to maritime routes by building specific terminals in maritime ports. Investment in infrastructure to facilitate the efficient transfer from railways to other public transport modes and new micro-mobility solutions would also be of interest. Operating aid to reduce the cost of the transshipment of goods and integrate railway services with other land transport modes in public service contracts, would also facilitate modal shift. Certainly, multimodality increases complexity not only in the operation of transport and mobility systems, but also in the analysis of State aid. This is why more directions in relation with multimodality in the guidelines would be helpful.

Secondly, the guidelines could provide more support for international services. Railways are competitive in very-long-distance routes. The longer the route, the more competitive railways are for the transport of goods. This is why railways enjoy larger modal shares in large countries such as Russia and the US. Even passengers are increasingly interested in using rail services as a substitute for flights, particularly if the trip takes place at night. The

EU's very long-distance services are necessarily cross-border services, and cross-border railways in the EU means interoperability challenges and poor coordination of access to tracks across national systems.

The guidelines could provide specific attention to cross-border services. Interoperability in general, and cross-border infrastructure bottlenecks in particular, are well-recognised challenges and they are already subject to specific EU funding programs. Furthermore, State aid for investment in cross-border rolling stock, and specific equipment for managing services across systems with different gauges would be helpful. Operating aid for cross-border services in the form of payment of track access charges could incentivise long-distance railway services, both for goods and passengers. Economic incentives for infrastructure managers in the form of subsidised track access payments could increase cross-border services' reliability.

Third, the guidelines could provide specific guidance for the use of digital technologies in land transportation. Digitalisation can play a fundamental role in the coordination of a system as fragmented as land transport in the European Union. Digital technology can facilitate the coordination of different transport modes, including micro-mobility services. It can also facilitate the coordination of national railway systems for cross-border services. Digitalisation can finally enhance the railway system's efficiency, for instance, increasing capacity in the congested segments of the railways' network.

Fourth, the guidelines could explore new possibilities for public service obligations. At the moment, no guidance is provided for freight public service obligations in freight transport, and these services are excluded from Regulation 1370/2007. Services in remote areas under harsh conditions for road transport or intermodal solutions for islands (maritime and railways) could benefit from some guidance.

Finally, as State aid becomes more relevant under the Green Deal, and the analysis is more complex as it includes more transport modes and more players, the guidelines would benefit from simplification. Models for the notification of straightforward schemes, and even block exemptions, could be an example. The review of some confusing thresholds could be another. In parallel, more guidance in the application of Regulation 1370/2007 in the definition of public service obligations, the coexistence of competition and public service obligations in some segments and the definition of compensation schemes would be welcomed. In this regard, the resilience of public service obligations against risk becomes an even more relevant issue, as COVID-19 has demonstrated.

Shift to rail will not become a reality just reiterating the same policies that have failed over the last decade. The bottlenecks and market failures are well-known at this stage, as well as the competitive advantages of rail over other transport modes. State aid can be used to eliminate the obstacles that hinder the full exploitation of railways' competitive advantages.

Main Takeaways from the Discussions

By Teodora Serafimova, Florence School of Regulation – Transport Area

The 19th Florence Rail Forum took place against the backdrop of the ongoing evaluation of the Community guidelines on State aid for railway undertakings. Since their adoption in 2008, a number of important regulatory developments have taken place in the rail sector, which in turn, call for a revision of the guidelines. Following the latest round of legislative revisions in 2016, the domestic passenger rail market was opened up to competition, and this is set to become a reality in December 2020 with the introduction of the new railway timetables. Furthermore, competitive tendering has become the norm for the award of public service contracts for passenger rail services, with a transition period envisaged until the end of 2023. Evolutions have also taken place on the technical side, where the EU Railways Agency has gained new powers with regard to certificates and authorisations when it comes to placing vehicles on the market, and has been entrusted with conducting the European Rail Traffic Management System (ERTMS).

State aid has clearly been at the forefront of the response to the COVID-19 pandemic, with additional possibilities for Member States to grant support to hard hit sectors of the economy, such as transport. The Commission has notably announced its Recovery and Resilience Facility, whereby the European Green Deal objectives and the promotion of clean modes of transport, such as rail, are set to play a pivotal role in Member States' national recovery and resilience plans. In view of this, the 19th Florence Rail Forum sought to examine the regulatory framework for State aid beyond the COVID-19 pandemic, thus taking into account the longer-term perspective and EU objectives.

For transport, which accounts for a quarter of the bloc's total greenhouse gas (GHG) emissions, the European Green Deal places a particular emphasis on CO_2 emissions reduction, modal shift, multi-modality and automation. The benefits of rail transport are widely known: rail is the cleanest and safest mode of transport. Railways use already existing infrastructure, they can carry large amounts of goods and ample room remains for the further expansion of this transport mode. Accelerating the modal shift calls for a major boost in rail freight. This will, in turn, necessitate an increase in capacity, a strengthening of cross-border cooperation and coordination of infrastructure managers (IMs), improved management of the rail network, a better alignment of the Rail Freight Corridors (RFCs) concept with the Trans-European Transport Network (TEN-T) concept, and the strengthening of the network of multimodal terminals, which are currently marked by scarcity of transshipment infrastructure. In legislative terms, the Commission will revise the Combined Transport Directive. On the side of rail passenger transport there is an intention to present an Action Plan for cross-border rail transport in 2021, which will focus on facilitating multimodal ticketing and payment systems, and will thus have a strong digital dimension.

Different types of State aid can be observed today. Significant support is being directed at railway infrastructure, which, however, is not considered as 'aid' per se, given that it is a natural monopoly, and thus open to all under regulated access. One main category is 'investment aid' to infrastructures that are commercially operated, such as for example service facilities, maintenance workshops, and intermodal terminals. A second major category is aid for the 'coordination of transport', which has, in fact, been the most successful chapter of the current railway guidelines. Member States are allowed to compensate railway undertakings (RUs) in order to help cover infrastructure charges, which other transport modes, such as road, do not have to pay. Another type of aid is 'aid for interoperability'. Typically this type of aid targets investments to roll out ERTMS, to tackle noise pollution from brakes or to improve safety. Whereas there is a presumption of proportionality if the aid covers less than 50% of the investment costs, where needed, a Member State could cover up to a 100% of the costs incurred. Furthermore, State aid can be granted for the reductions in external costs. It is well known that rail has lower externalities as compared to other transport modes, in terms of pollution and congestion amongst others, and Member States can compensate rail for part of these external cost reductions. Finally, there are public service contracts, which account for two thirds of the passenger market today. With the opening up of the market to competition, we are now seeing a co-existence of open access operators and public service operators,

which, in turn, calls for the careful scoping of public service contracts.

The granting of State aid should contribute to set policy objectives, including sustainability and CO_2 emission reductions, multimodality, as well as smart mobility in relation to the introduction of digital tools, which boost the resilience of the transport system. Of course priority should continue to be given to competition and the completion to the Single European Railway Area (SERA), where interoperability still generates additional costs. Increasing the modal share of rail will thus require significant investments and ongoing public support to compensate for some of rail's operating cost-disadvantage compared to other modes, at least until a critical size is reached. The basic principles surrounding the granting of State aid should be respected, in relation to non-discrimination, full transparency, and a solid justification of State aid. It is important that all public support, be it in the context of public service contracts, investment aid or operating aid, is directed where it can make a difference (i.e., where there is a market failure or a shortfall of private investment) and is limited to the minimum necessary. The sections below synthesise the main takeaways from the 19th Florence Rail Forum, pertaining to the different types of State aid for both freight and passenger rail.

Rail Freight Transport: State Aid and Investment

While in theory the railway market has been open to competition for some time, in reality, important barriers remain especially in relation to cross-border rail services. Unlike passenger rail, which is rather national in nature, rail freight transport is mostly international. In fact, the international dimension of rail traffic for freight stands at 52% as compared to 7% for passengers[1]. Despite some positive trends, namely a growing demand for heavier trains and for the transport of goods by rail, the share of rail freight has stagnated at 18%. The lack of harmonisation and standardisation has been a clear barrier for rail freight. Whilst there have been many EU projects and initiatives aimed at promoting interoperability, the process has been slow. What is more, the overarching absence of a 'European mindset' in the regulation of railways continues to be responsible for the poor coordination among Member States.

The aim of State aid should be to lower access barriers or upgrade production. In reality, therefore a complete disconnect between infrastructure investments and operating aid is not apparent. The revised State aid guidelines for rail should be based on a number of specific objectives, namely capacity, inter-modality, interoperability and quality of the railway system. These are the key elements that will need to be promoted to foster rail freight. When it comes to capacity, for example, there is a clear agreement on the need for longer trains, the need to implement ERTMS, and the need to complete the TEN-T network.

Because of its high fixed costs, rail continues to be at a competitive disadvantage when compared to road and inland waterways. Given the proportional relation between the intermodal market share and the corresponding trucking price, subsidies could have a positive effect for modal shift. Taking a closer look at the experience of Belgium, 94% of goods transport is carried out on trucks, and there remains significant spare capacity on the rail network. In line with the EU ambitions of doubling the volume of rail freight, Belgium aims at increasing its share of rail freight to about 16% by 2030. While the European Green Deal stresses the role of rail above 300 kilometers, the experience of Belgium shows that there is significant potential for modal shift also below 300 kilometers. This, in turn, suggests that State aid will thus have an important role to play also for these shorter distances. The gap between a truck company and a rail company offering a service above 300 kilometers is about 40% in cost, due to the lower daily frequency of trains among others. An increase in the daily frequency of trains, it was argued, can help to reduce the stock-related costs, thus potentially creating a positive gap for railways. The gap would, however, need to be reduced to 30% to incentivise companies to shift to rail. Stakeholders also underlined that the picture could further change if the expected increase in costs for road transport, due to exacerbated congestion for instance, are taken into account.

Investment aid to date has rightly focused on terminals: on increasing the capacity and density of the network of terminals, and on improving their connections to sea and land ports.

1. Figures for 2018 for EU-27.

Investment aid will also be needed for intermodal transport with regards to container loading equipment (e.g., forklifts), special loading equipment for placing cargo into intermodal loading units, and the intermodal-specific assets (e.g., cranable semi-trailers). Only 5% of trailers today are cranable, which calls for standardisation to provide purchasing assistance, alternatively to cover the cost of additional transshipment equipment to make road compatible with rail.

Intermodal transport is the engine of rail freight development, which fosters growth and competition within the rail freight sector. Unlike the share of rail freight which has stagnated, intermodal freight transport has grown by almost 50% over the past decade. The supply chains today are based on truck load quantities meaning that the intermodal loading unit is tailored to the truck load, which enables the efficient transshipment of cargo between the different modes of transport, placing combined transport in the horizontal perspective of logistics. While in the long run, intermodal transport should be viable without subsidies, the new realities brought about by the pandemic, and the persisting absence of a level-playing field and fair pricing between the transport modes, call for State aid to be considered for the sector. Intermodal operations can be enhanced through digital databases for wagons, for loading units, and for infrastructure. Standardisation, paperless consignment notes, digital identifiers, standard codes and interfaces between the stakeholders can help to improve the communication and cooperation between actors. Digitalisation of oversight authorities, tracking and tracing, quality control, and estimated time of arrival (ETA) will all be needed going forward. Despite their obvious benefits, digital platforms should be regulated with caution given that they can lead to market distortions and the excessive concentration of market power in the hands of a few platforms.

One interesting example has been the port of Antwerp, as Europe's second largest port, whose main driver of growth over the past 20 years has been maritime container transport. In order to accommodate this growth, it is estimated that over €1 billion equivalent of public and private investments will need to be channeled into new terminals and additional capacity. This includes investments into new rail infrastructure, as well as the building and re-building of terminals, which alone will cost over €300 million. However, this growth will need to be almost exclusively accommodated by barges and rail. With this in mind, the transport of containers by rail will need to be facilitated from the point of view of the rail operator, the terminal as well as the shipper. One way of achieving this would be to include legal or contractual provisions in the concession agreements between the terminal operators and the shipping lines, obliging them to prioritise rail or barge transport. However, this approach is controversial given that it can distort the market and should thus be seen as a 'last resort'.

The disproportionately high last-mile costs of rail constitute a major bottleneck in any rail development. In fact, studies suggest that ca. 15% of total rail costs are due to these last-mile operations within ports. The inland transport of maritime containers are predominantly over shorter distance transport (e.g., within Belgium, southern part of the Netherlands, France and part of Germany). Here, the promotion of single wagon transport also deserves explicit mentioning in the revised guidelines, in view of its importance in promoting a shift to rail freight transport, but also given its economic viability problems. Having said that, it is not only the rail operations that are very costly, but also the maintaining and operating of rail infrastructure that pose a major financial burden. Financing schemes, thus, need to take these issues into account by focusing on the cost reduction of rail operations within ports while supporting infrastructure development, as a means to support rail transport development as a whole.

State aid schemes for rail in ports need to take into account the different rail infrastructure management models in place in the different European ports today. In Antwerp, for instance, the rail infrastructure is an integral part of the national network, owned by Infrabel. From a financial point of view, this enables a better balance between costs and income. Conversely, ports which own their own rail infrastructure, tend to struggle to raise sufficient funds to maintain and operate infrastructure, let alone finance new investments. Raising rail access fees in ports is not an option given that it may risk rendering rail uneconomical. Having said that, ports owning their own rail infrastructure offers advantages in the form of greater freedom in organising rail operations in function of the port. Often there appears to be no commercial relationship between a maritime terminal

and the railway undertakings. Legal frameworks, especially those governing the rail sector, should take into account the specificities of the port environment. Rail is a highly regulated sector and this can come into conflict with the requirements of ports, which by nature, have to be flexible and rapidly adapt to an ever-changing environment. As mentioned above, digitalisation and the development of port digital platforms that facilitate the exchange of information between all stakeholders will be key to integrating planning processes and boosting the attractiveness of rail. Given the significant upfront investments, from both EU and national sources, that will be needed for the implementation of digital-automatic coupling in rail freight and the use of digital platforms, the inclusion of an explicit chapter on digitalisation and automatisation within the scope of the new guidelines would be beneficial.

Importantly, the sector also needs further investments and aid for the purchase of new rolling stock and for the improvement of service facilities, in particular those that are publicly accessible. The purchase, retrofitting and scrapping of rolling stock would benefit from a close alignment with the taxonomy, which is currently under development, in order to facilitate the uptake of zero tailpipe emission trains (e.g., hydrogen, bi-mode trains and hybrid systems) in line with the Green Deal objectives.

Rail Freight Transport: Operating Aid

The existing guidelines allow the granting of State aid for interoperability (e.g., ERTMS, noise reduction, and digitalisation). While the guidelines have a presumption of proportionality and necessity at 50%, specifically for this type of interoperability investments, going beyond this presumed threshold is possible as long as the need is justified. In fact, up to a 100% of these costs can already be covered under the existing guidelines today. The idea behind ERTMS is to enable more trains to run, thus increasing the overall infrastructure capacity of the system, improving the reliability of services, safety and interoperability. This translates into system-wide benefits, which are wider than those accruing to the individual operator making the investment. In light of this, the incentive for the operator may not be sufficient, pointing to the existence of a market failure and the need for State aid. Enhanced flexibility and more explicit wording on the intensity thresholds and eligible costs for the coordination of transport will, however, be needed. Alternatively, block exemptions for certain cases could be considered, removing the notification requirement as long as the rules are being respected, while enhancing legal certainty, reducing bureaucracy and accelerating the process.

Incentives schemes and positive discrimination for rail access charges can play a key role, be it for the reduction of noise, environmental pollution or ERTMS rollout. In the case of Italy, for example, the Ferrobonus scheme was implemented to correct the imbalances between rail and road in terms of external costs. Similarly, in the Netherlands, track access charges were reduced for 5 years to compensate for non-paid external costs in road transport with the objective of accelerating modal shift. Another example of useful State aid could be in the form of a temporary compensation to address the productivity gap regarding trains with a length under 740 meters. Significant capacity wins can be achieved with 740-meter trains. If a 740 meters path were needed but not available, compensation could serve to motivate infrastructure managers to ensure that this gap is covered as soon as possible. Specific support could be envisaged for the upgrade of the network.

Following the introduction of a new Italian law in 2016, port authorities are now to be considered 'port networks', which in practical terms, has resulted from the merging among some port authorities (e.g., the ports of Trieste and Monfalcone are now a 'port system' in the inland and the shore). This law has helped to improve the conditions for the efficiency of the port's railway activities. As one of Europe's best performing ports, Trieste has since 2015 doubled its number of trains. 60% of its network is dedicated to semi-trailers, and the other 40% to containers. In the course of the next five years, the Port expects to increase its number of railway stations from the current 1.5 to 3. Roughly €200 million worth investments have been channeled into the port jointly by the Italian government, the Italian infrastructure manager RFI and the EU.

A key takeaway from the experience of the Port of Trieste has been the need to make optimal use of existing infrastructure within the territory and to support intermodal services that rely on existing infrastructure. Every part of the system is connected to the railway system,

and no development can be undertaken by the port unless the nodes of the logistic platform are connected by rail. As of 2020, the Port of Trieste has started taking over the ownership and management of the port of Monfalcone as well as of the railway infrastructure in the port. Together they have created a unique authority composed of ports, railways, free zones (Frieste), maritime, and industry, all of which are connected by railways. The Port of Trieste strives to be the last mile operator for the entire system. A framework agreement was reached with RFI regarding the capacity allocation of the port railway services. The local management of an integrated port system is key. As underlined in the previous section on investment aid, State aid should also be considered for the shorter distance connections, which are closely linked to sustainability issues in ports and represent a particular cost for rail freight. This complexity of the ecosystem will probably require State aid schemes to adopt a more dynamic approach in terms of providing the right incentives for the entire logistics chain and not only for the recipient of the aid.

Advancing the European Green Deal agenda will also require support, in the form of State aid or Public Service Obligations (PSOs), with regard to market segments that are not profitable today. PSOs could be defined for routes that are less dense and less profitable on the basis of specific operators or specific activities within the ports. While PSOs could facilitate modal shift in the hinterland of the port or in the rolling motorway to cross the Alps for example, caution should be exercised to avoid making them the principle for rail freight given that many alternatives exist today to increase the economic viability of rail freight in a non-discriminatory manner. Approaching the single wagon load issue, for instance, calls for a set of different measures to be considered in parallel, as no silver bullet exists for this market segment. Single wagon loads feed all other transport modes along the way, and should thus not be considered as a single product. PSOs would be difficult to implement for single wagon load, which is more irregular (i.e., does not follow a set timetable), so perhaps a waiver of track access charges for first and last miles could offer a more appropriate solution. Therefore, prior to considering State aid and PSOs for market segments that are loss-making today, Member States should consider, as a preliminary measure, reducing to zero the costs of the use of infrastructure.

In view of the fact that access charges are often low for rail freight, infrastructure managers lack strong incentives to prioritise freight over passengers. Therefore, instead of reducing access charges, a more market-oriented approach could be considered, whereby railway undertakings or even shippers are granted State aid to pay for access charges, so as to ensure a real incentive for infrastructure managers to boost traffic. There is, in fact, a similar approach already in place in Switzerland, where the track access charges remain constant, and instead other kinds of subsidies and support are granted to operators and railway undertakings. While this means that the infrastructure manager receives the track access charges that are previously defined, such an approach may be administratively more complicated as compared to the direct lowering of track access charges. The principle that infrastructure managers have an incentive to treat freight traffic in an equal way (e.g., priority rules for path allocation) to passenger traffic should certainly be considered. Last but not least, the debate on the subsidisation of railways should go hand-in-hand with the phase-out of subsidies to polluting modes of transport, if a level playing field is to be achieved.

Passenger Rail

Only about 7% of the total European rail passenger market is currently cross-border in nature; most of rail passenger transport is domestic and roughly two thirds of it is accounted for by PSOs in the EU27. With the opening up to competition of the domestic rail passenger market, the need to ensure a level playing field between public service contracts and open access services becomes paramount. A progressive shift towards competitive tendering will have to happen, as the direct award of contracts will only be possible until the end of 2023. In parallel, a paradigm shift will have to take place in the market, as has been observed in the aviation and maritime sectors, where competition is the rule, and public service contracts the exception.

After almost 11 years of application of Regulation (EC) No 1370/2007 (the 'PSO Regulation'), significant jurisprudence has been issued, and important changes will be introduced with the Fourth Railway Package. The Commission's DG MOVE has launched a study at the end of 2020 to assess the implementation of the PSO

Regulation. The study will produce an overview of the current status of the Regulation's transposition in the Member States, and assess the provisions' effectiveness in contributing towards the achievement of the Regulation's objectives (i.e., to ensure that high quality public services are being provided at the least cost to society). Subsequently, DG MOVE will be reviewing the interpretive guidelines to the PSO Regulation. The 19th Florence Rail Forum was, thus, welcomed as a valuable first stakeholder input into this evaluation on the functioning of the PSO Regulation.

Public Service Contracts and Open Access Rail Services

With the opening of the market to competition, the commercial offer will increasingly be viewed as the starting point, on the basis of which market failure can be identified. Some participants argued that the burden of proof should be placed on the Member States, who would have to justify that State aid is necessary and proportional.

A typical situation is one where PSOs cover an entire franchise area and offer services at an affordable charge and at uniform conditions of supply. It is thus assumed that essential mobility needs covered by PSOs are homogeneous. In the reference model, the travel patterns of the daily or weekly commuter are behind this way of planning services and all the supply is organised around the needs of this category of customers. Some stakeholders pointed out that while in ideal situations, the data used in defining the scope of PSOs is derived from the number of tickets sold and proceeds, in most cases it appears that the scope is defined based on historical records, rather than based on an objective assessment of real demand needs. Some participants thus cautioned that competent authorities rely on static information on demand, which does not capture potential demand, and which, in turn, may be diverted by other modes. In view of this, the need for a shift away from the historical approach to PSOs resonated among some participants. This new approach is to be founded on a solid understanding of demand and a definition of PSOs, which integrates alternative transport modes, multi-modality and micro-mobility.

Proponents of a new approach underlined the need for a scope specification of PSOs, which is carried out on a more quantitative basis, and preceded by an assessment of the potential demand and behaviour based on survey and predictive views of big data. This, they argued, would be key to capturing the evolving travel patterns related to ongoing social and economic change, and not least the changes induced by COVID-19. A demand assessment for future services would, furthermore, need to take into account the EU's long-term climate targets so as to define targets accordingly and to ensure that the traffic and offer are developed in line with these goals. It would be up to the competent authority to demonstrate a correct analysis of the parameters of public service and that the contract was awarded to the right size of the territory.

In addition to demand, affordability constitutes another important aspect. Going forward, the differentiation of charges based on segments and categories of passengers may need to be considered, as well as the linkage of affordability to more specific social and economic objectives. While this has been left to the discretion of policy makers, a more objective assessment of certain objectives, such as those related to social and territorial cohesion, may be relevant to consider. Such an approach, based on a set of reliable indicators, could help to identify specific areas needing PSOs, instead of setting PSOs for an entire region.

Another common policy objective is inclusiveness, which can be tackled with appropriate tools, such as preferential rates or exemptions for low-income passengers for example. PSOs, for instance, have been a necessary solution, where social inclusion and fairness have had to be ensured, such as in cases of sub-urban and regional services, where thousands of people commute daily for essential services. However, the definition of a specific discounting charge for a commuter is not a straightforward exercise, which may be complicated further where passengers commute once or twice a week: an occurrence which may become increasingly prominent in future, with the diffusion of home working. Another question that needs to be tackled relates to the extension of the affordability criteria to multimodal travels. This, in turn, should go hand-in-hand with the effective enforcement of passenger rights regulations and protection.

When dealing with areas of weak demand, the role of alternative modes of transport (e.g., on-demand mobility) in satisfying these social needs should be taken into account. One way of providing for a more effective

rail supply after having defined the demand needs in a PSO contract, could be through the introduction of an obligation for a competent authority to assess the intermodal and intramodal substitutes, taking into account their impact on the environment. In other words, competent authorities should impose PSOs only when alternative substitutes do not exist and only when PSOs are the most convenient tool to satisfy essential needs, at comparable supply conditions. An objective methodology will also be needed on this side of the economic equilibrium test. The PSO Regulation does not deal with other competing non-rail modes of transport.

Traditionally the most common way of financing PSOs has been cross-financing. Alternative solutions could be to apply a fee to spin off some of the more profitable routes, while avoiding cherry picking effects, or to apply a fee also on the more profitable routes whose revenues could be earmarked to PSO services. In addition, there are two alternatives to financial compensation or assignment of exclusive rights: direct compensation to customers and horizontal PSOs, the latter being a concept borrowed from the EU Regulation 3577/92 on maritime cabotage. These two alternatives would need to be complemented by customer rights regulation and protection, or by quality minimum requirements including social standards.

Currently, there is a focus on the domestic and commuter trains, though international trains should also be prioritised through, for instance, the lowering of operating costs. In the case of the Malmö-Berlin service, spending as much as 25-30% of the total costs on using the tracks acts as an important barrier to increasing trains on the track. Similarly, the operation of night trains without subsidies for the most part remains challenging, especially in cross-border contexts. There are, however, some examples (e.g., Snälltåget in Sweden), which have demonstrated that night trains can operate commercially, without subsidies under a PSO. In both Sweden and Czechia, where competition has existed for some time, higher demand, more passengers, and lower prices have been observed, including in the night train segments. In view of this, open access alternatives should be promoted, and where a public procurement alternative through a PSO is still needed, competitive tendering should be followed. Any State support to night trains should be provided on a fair and non-discriminatory basis, enabling equal access to rolling stock, and reduced track access fees. Short-sighted 'painkillers', in the form of cartels and unfair State aid, can block market development, reduce the number of players and increase costs. Price and demand play an important role in sustaining international night train services. In view of this, public intervention, which gives tariff support to night train operators could benefit passengers, through the imposition of general rules. The setting of maximum prices for operators on the market could help to create a more stable framework for night train service operators and foster demand.

With the exception of Czechia, currently there are no commercial night train services that run on a daily basis and the services are primarily offered in high demand season with depreciated rolling stock, because there is no private investment in night train rolling stock. Whereas this may not necessarily be a barrier for holidaymakers, it is unlikely that business travelers will make a consistent switch to night train services until there is a 24/7 offer. Opportunities will need to be secured for private actors to enter the market and a long-term availability of rolling stock will need to be ensured. With this in mind, the Commission will be conducting a study on the barriers to the development of night trains. In particular, the study will assess technical barriers, the availability of rolling stock, path and capacity allocation, charges, as well as PSOs. The Commission study also intends to look into the critical question of 'hybrid PSOs'. In other words, exploring the possibility of a night train service, whereby a subsidised segment is merged with a segment under a commercial regime.

A PSO may be appropriate in cases where a dedicated time needs to be bridged until there is possibility for open access solutions. PSOs may, for instance, be needed where the intention is to expand on secondary lines. The risks linked to the overlap between commercial and PSO services are clearly illustrated in the case of Austria. It may be difficult to demonstrate market failure on the one hand, and abuse of a dominant market position, on the other. This overlap of commercial and public services risks hampering competition and giving a competitive advantage to incumbent players. A clear differentiation between commercial and public services or alternatively, a clear control on the level of positive network effects will be needed. Support should be granted to all transport operators and companies based on special compensation rules system in order to ensure an integrated network. Data sharing obligations should be mandatory for PSO

operators, and, in particular in the case of long-distance services, where data is not shared, there should be a reduction in the compensation. Not the least, differences in signalling systems, languages, working rules and other national regulations continue to pose a challenge for the operation of cross-border trains, and should thus be overcome.

Compensation Parameters

All compensations related to PSO contracts are to be established in advance and calculated in line with parameters set out in the PSO Regulation. Article 4 establishes the rules to be followed in order to prevent overcompensation. In case of direct award, no compensation payment may exceed the amount required to cover the net financial effect. The competent authority should take into account the revenue kept by the public transport operator with reasonable profit. The Commission's interpretative guidelines on the Regulation clarify that the level of reasonable profit should be in line with normal parameter conditions and that it should not exceed what is necessary to reflect the level of risk. When benchmarks do not exist, the Commission argues that the reasonable profit should be defined based on the profit margin required by a typical railway undertaking. A uniform regulatory framework for the definition of the network effects would be key. Some mechanisms need to be put in place that guarantee the economic equilibrium of the PSO over the years, in particular in the case of unforeseen circumstances.

PSOs have to be based on financial analysis and rigorous key performance indicators (KPIs), rather than on a request or a speculative bid. As outlined earlier, some participants cautioned that the scope of PSOs is often based on historical records, as opposed to an assessment of real needs and demand. The compensation by the public authorities should strive to maintain and develop a public good, which in the given case is the railway network. In light of this, it was underlined that the compensation of PSOs should not only cover the operating costs, but also the depreciation of the rolling stock and the costs of access to infrastructure, related to long-term investment programmes.

Non-discriminatory access to rolling stock is key to enable competition. Rolling stock is a critical asset for railway operators, and public investment needs to be carefully targeted to safeguard a level playing field. The PSO Regulation foresees several ways to make rolling stock available. The competent authority may acquire the rolling stock and make it available to select public transport operators. Alternatively, the competent authority may provide a guarantee for the financing of the rolling stock and it may commit to taking over the rolling stock once the contract ends. Lastly, it can decide to cooperate with other competent authorities to create a larger pool of rolling stock. There is no 'one-solution-that-fits-all' and each competent authority is to make their own decision on the most suitable model. For instance, it was argued that allowing the operator to own the rolling stock has several advantages, in particular a greater incentive for the railway undertaking to use and manage rolling stock efficiently. The clear efficiency gains by train operators who own fleet and rolling stock are illustrated in the Austrian case, where the ownership of a large fleet allows the railway undertaking to shift its rolling stock from one region to another in response to demand changes or rolling stock restrictions. Furthermore, ownership of the rolling stock by the railway undertaking, can enhance the level of transparency in the contractual relations between the railway undertaking and the awarding entity.

Notwithstanding those advantages, ownership of rolling stock by the railway undertaking may undermine competent authorities' objectives of ensuring non-discriminatory access to rolling stock while securing maximum participation in public tendering procedures. This is because some new entrants may be unable to take the financial risk upfront to invest in new rolling stock. Therefore, sometimes the only alternative is for the competent authority to invest in the rolling stock. The fact that the economic lifetime of rolling stock is much longer than the duration of a PSO contract is another aspect to be taken into account. Here, it was noted that leasing companies have a role to play in guaranteeing equal access to all participants in the competition.

The discussion also touched upon the potential value of a second hand market for regional rolling stock. If interoperable, rolling stock can be passed on from one operator to another in case one goes out of business. Here issues pertaining to the interoperability of different technical systems across countries have been a barrier. In other words, the prevalence of different track gauges, different energy supply systems, and different signalling

systems makes it virtually impossible to move trains freely around Europe, thus complicating further the prospects of a second hand market for rolling stock. Pre-conditioning the interoperability of rolling stock that is bought for a PSO may act to increase the investment costs significantly.

The French case study of Centre-Val de Loire Region has offered some interesting considerations for the discussion on increasing the legal certainty on the calculation of PSO compensation. SNCF Voyageurs is still the sole train company operating in France through a PSO, although since December 2019 it is no longer a monopoly. Some regions have started a competitive tendering process even if the contracts are not yet awarded. All PSO contracts in France are based on the same model, and since public funding is involved, all information is made publicly available. Every PSO contract has two types of costs: first, the costs that are directly incurred by SNCF Voyageurs, which are set at the beginning of the contract through a bargaining process between the public transport authority and SNCF. Then, there is an index that increases during the lifespan of the contract. Secondly, there are external costs (i.e., mostly rail infrastructure charges and taxes), which are passed on to the public transport authority to cover.

The public transport authorities have to ensure there is no overcompensation to SNCF. In the Provence-Alpes-Côte d'Azur Region in the South of France, in 2007 and 2018, SNCF Voyageurs and the public transport authority were unable to agree on the total cost of the PSO (i.e., the lump sum cost). The public transport authority therefore set a unilateral prescription based on a consultant's assessment, who estimated the actual cost of SNCF to be lower than what they had requested. The case was brought to court by SNCF, which did not agree to the assessment. The judge ruled that the contract of Provence-Alpes-Côte d'Azur was not legal and thus could not be used to settle the compensation of a PSO, because the charges in that contract constituted a lump sum with an indexation. Following an independent expert's assessment, the right amount of compensation to be given to SNCF was calculated, and a new contract between the public transport authority and SNCF was drawn.

This judgment is interesting in that it opens up the question as to whether all contracts between public transport authorities and railway undertakings in France are to be deemed illegal given that they are based on the same lump sum. Drawing on this, in the case of a monopoly or direct award, an independent third body should be entrusted with the definition of the right level of compensation to avoid overcompensation. This is already the case in Austria, for instance, where directly awarded PSO contracts are subject to strict overcompensation rules and an overcompensation test is carried out by an independent authority. The establishment of an overarching EU legal framework in regards to compensation will be key in putting in place a harmonised approach to limiting overcompensation. Going forward, authorities need to build up technical expertise and exchange experiences in defining parameters for compensation.

Conclusion

The revision of the State aid guidelines for rail is a welcome opportunity to shift towards a more modern and flexible State aid framework, which safeguards that funding is targeted, proportional, well-dimensioned and non-discriminatory, while helping to advance the EU's long-term objectives, notably those linked to the European Green Deal. In view of this, the Commission's DG MOVE and DG COMP are planning studies to ensure that the future guidelines are anchored in solid facts.

While 60% of passenger kilometers today are still based on PSOs, there is overwhelming agreement that a shift away from the current model is needed towards one that is based on more open access competition. Enhanced guidance and objectivity, based on rigorous KPIs, will be needed in the definition of the scope of PSOs. While the long-term perspective was prioritised during the 19th Florence Rail Forum, COVID-19 has certainly helped to expose that the PSO model in many countries is under immense strain, and should thus be re-considered following the crisis. Similarly, the need to reconsider the balance and distribution of risks in PSO contracts is not only a short term issue, but also an issue for the future.

Although the State aid guidelines to date only apply to aid granted to railway undertakings, it appears sensible to enlarge the scope of the State aid guidelines to include the entire logistical chain, including road transport companies, which would need to make significant upfront investments into containers. In view of this, the guidelines may be more appropriately labelled under the broader term of 'land transport'. There is a need to shift away from the silo-approach to regulation, towards a more holistic approach.

With regard to rail freight, whereas the discussions were structured around two sessions, it became clear that the distinction between investment aid and operating aid is blurred in reality. CAPEX investments into digital platforms and rail traffic management should receive particular support given their importance in fostering modal shift. To avoid the risk of crowding out private investment, State aid should be horizontal (i.e., open access), non-discriminatory (CAPEX and OPEX), and conditioned on objective criteria. In the case of operating aid, the revamping of loss-making services (e.g., single wagon loads, last mile but also start-ups) was highlighted, which in turn will necessitate new business models.

Achieving the EU's objectives relating to modal shift will require the entry of new operators and market developments. The debate on State aid and PSOs needs to be placed in this context of creating a level playing field, both within rail (i.e., the same conditions for all rail competitors) as well as between rail and other modes of transport (e.g., road and aviation).

The revised State aid guidelines need to be future-proof, in terms of taking into account and promoting technological developments linked to CO_2 reduction, digitalisation, multi-modality and access to data and platforms. Data will clearly have a pivotal role to play, in terms of assessing the need for a PSO, better identifying the types of PSOs (e.g., metropolitan, cross-border, long-distance PSOs), assessing the amount of compensation in a more objective manner, and not the least, harmonising the criteria for assessing PSOs across public transport authorities. As we have seen, significant differences persist between Member States and data can help to overcome this fragmentation. The need for recipients of PSO contracts to share data with public transport authorities and regulatory authorities was a key takeaway from the debate.

Sea Ports, Rail Transport and State Aid: Some Reflections on the Way Forward

A comment by Koen Cuypers, Port of Antwerp

There has been a lot of discussion, even controversy, on the effectiveness and admissibility of State aid, especially when this aid touches private infrastructure and operations. However, State aid can play an important role in fulfilling policy targets, especially in the field of the development of sustainable transport solutions. To reach this aim, State aid policies should be very clearly focussed at removing the problems hampering this development and also taking into account the different circumstances, under which the policy has to function. This calls for a much more flexible approach and the realisation that a "one-size fits all" regulation for State aid policy is probably not the right way forward.

As my contribution to this discussion, I am putting forward four statements on the role and position of State aid in the context of rail development in ports.

1. Disproportionately High Last Mile Costs of Rail Services Constitute a Major Bottleneck for any Rail Development.

The real problems with rail operations are situated inside the ports themselves. Some studies indicate that on average 15% of the rail transport costs are due to the last mile operations in ports. These last-mile costs are sometimes prohibitive, especially for shorter distance transport.

And it is not only the rail operations which are very costly, but also the maintenance and operation of the rail infrastructure inside the ports comes at a significant cost and generates only limited income directly for the rail infrastructure manager. And in the Port of Antwerp alone, there are 600 kilometres of public rail tracks.

Financing schemes have to take into account these issues and should focus on cost reduction for rail operations in ports, while at the same time supporting infrastructure development, as a means to promote the development of rail transport as a whole.

2. There Are Different Rail Infrastructure Management and Financing Schemes for Ports in Place in Europe, Each With Their Own Advantages and Disadvantages.

In Antwerp, the rail infrastructure is an integral part of the national network and is owned and operated by the Belgian rail infrastructure manager Infrabel. The advantage, from a financial point of view, is that being part of the national network creates a better balance between costs and income. In comparison, ports who own their rail infrastructure are often struggling to raise enough money to maintain and operate their network, let alone financing investments. You just cannot raise your port rail access fees high enough to cover your costs because you will risk making rail transport uneconomical. Just look back at the first statement.

However, owning your own rail infrastructure as a port creates also a lot of advantages because you have a lot more freedom to organise the rail operations in function of your port and at the same time optimising the last mile rail operations.

Thus, when discussing financing schemes for rail infrastructure in ports, one has to be aware that there are different port rail infrastructure management models in place all over Europe.

3. Maritime Port Terminals Have Their Own Commercial Logic.

In most cases there is no commercial relationship or contract between a maritime terminal and a railway undertaking, only operational agreements. The terminal operator just receives the order to load a container or another type of cargo on a certain train, truck or barge from the shipping line or shipper and the cost of the operation is paid by the latter. This cost is often included in an "all in" price, the so-called Terminal Handling Charge, which makes no distinction between trucks, trains or barges.

Therefore, if we look at the whole discussion on State aid for rail terminals in ports, this is not just an issue of potential market distortion within the rail sector as a whole, between one railway undertaking compared to another railway undertaking, but just a way of supporting the rail sector in comparison to truck transport.

4. Legal Frameworks, for Instance for State Aid, Should Take Into Account the Specifics of a Port Environment Especially Those Governing the Rail Sector.

Rail transport is a highly regulated sector, rightly or wrongly so. But we see that this is often conflicting with the needs and requirements of ports who have to be, by nature, very flexible and quickly adapting themselves to an ever changing environment. Maybe it is a bit black and white, but maritime terminal operators sometimes complain that the rules surrounding rail transport are dictating the way their terminal has to function and not the other way around. Which, I have to say, is not beneficial for the attractiveness of the rail sector as a whole.

I would like to emphasise here that there are still many possibilities for improving the rail system, not by introducing new and even stricter laws or regulations, but by cleverly adapting the legal framework and procedures. This also applies to State aid rules.

State Aid in Rail Passenger Transport: What Can We Learn From the Italian Experience?

A comment by Germano Guglielmi, Ferrovie dello Stato Italiane

The European Union (EU) and national regulations should seize the opportunities offered by the recovery plans to exit the COVID-19 crisis and, even more, to promote the twin green and digital transformations that are at the heart of the European Green Deal. However, the possibilities offered by these new recovery instruments – that are actually still under discussion at the EU level and then will need some time for their implementation at the national level – should not put away those already existing tools that could serve the purpose. Looking at the wider context that goes beyond the contingency, the evaluation and revision of State aid guidelines could effectively contribute and support the Green Deal, for example by providing the Member States with the necessary flexibility to support actions whose contribution to the transition to climate neutrality by 2050 is more evident. At the same time, State aid guidelines should not allow the alteration of the level playing field and jeopardise the stability of the internal market.

Focusing on the transport sector, evaluations are currently underway of the relevant State aid guidelines including those about railways. The challenge of allowing flexibility while maintaining objective criteria applicable all over Europe is not an easy one. When it comes to rail passenger transport, key questions revolve around the possibility for public authorities to award public service contracts and the demonstration of their necessity.

In Europe, Regulation 1370/2007 lays down the conditions under which competent authorities compensate public service obligations (PSO) or grant exclusive rights in return for the discharge of PSO. The Regulation states that all compensation connected with a public service contract shall establish in advance, in an objective and transparent manner, both the parameters based on which the compensation payment - if any - is to be calculated, and the nature and extent of any exclusive rights granted, in a way that prevents overcompensation. According to Commission interpretative guidelines and Commission Communication on services of general economic interest, the determination of the reasonable profit margin should be in line with normal market conditions (or with the profit margin required by a typical well-run undertaking active in the same sector) and not exceed what is necessary to reflect the level of risk of the service provided.

Against this background, in Italy, the Transport Regulation Authority hugely redefined the regulatory framework on local public passenger transport services by rail and by road, and it went much further into depth than the Regulation to enhance transparency and to improve the efficiency and cost-effectiveness of the services. In particular, the Authority set forth rules and criteria governing the award procedures and the calculation of PSO compensation. Both in the case of contracts awarded by public procurement and in the case of contracts awarded on a concession basis, the Authority stated that the Awarding Entity should draw up a simulated Economic-Financial Plan (EFP), broken down for all the years of the contract period. What is interesting about the EFP is that it is not only a scheme to determining the tender price or the public service contract compensation, but it is also a tool to monitor the management of the award. The Authority also calculates and makes available to the Awarding Entities the procedures concerning the calculation of the reasonable profit margin for both directly awarded public service contracts and contracts awarded by tendering procedure. This procedure makes Italy quite a unique case study.

Indeed, aiming at the achievement of the Green Deal, of which the completion of a Single European Railway Area can be considered one of the building blocks, we should get rid of greatly different and diverging national regulatory frameworks. Yet in Italy, the Transport Regulation Authority defined a very detailed framework, much more articulated than any other EU country. Did Italy go towards an over-regulated system or is it the right way that should be followed at the EU level, for instance including similar schemes in new Guidelines or new Regulation?

If the Italian model is correct, there could be some lessons to learn when designing the new EU regulatory framework, bearing in mind it should both aim at providing flexibility and preserving the level playing field. On the one hand, a reporting scheme could be defined at EU level to determine further the criteria provided for by Annex of Regulation 1370/2007, and these criteria

should apply to contracts awarded both directly and via a tender procedure. In particular, an equal and uniform legal and regulatory framework concerning the calculation of the return on capital defined at European level would eliminate the differences existing among the Member States and thereby ensure a level playing field. On the other hand, one may concede that some aspects of the Italian experience are unsatisfactory. For instance, the Authority requires the public service operator to perform a gradual improvement in the effectiveness and efficiency of the services. Nevertheless, especially in railway transport, it should be borne in mind that some costs cannot be reduced and unforeseeable circumstances cannot be easily addressed. Therefore, additional mechanisms at the EU level could be established from the outset in order to flexibly guarantee the economic and financial equilibrium of public service contracts over the years.

How To Increase Legal Certainty Regarding the Calculation of PSO Compensation in Case of Direct Award?

A comment by Patricia Perennes, Centre-Val de Loire Region

Introduction

According to recital 27 of Regulation 1370/2007 (hereafter 'the PSO regulation'): *'The compensation granted by competent authorities to cover the costs incurred in discharging public service obligations should be calculated in a way that prevents overcompensation. Where a competent authority plans to award a public service contract without putting it out to competitive tender, it should also respect detailed rules ensuring that the amount of compensation is appropriate (…)'*

The question that naturally derives from this statement is: how can Public Transport Authorities (PTA) make sure that they are not overcompensating the operator in charge of rail service provision?

In case of competitive awarding, one can consider that - if the market is functioning well - market forces ensure that the selected operator is not overcompensated. Indeed, an operator that asks for a high margin would be more costly and would therefore not be selected in a competitive process.

The situation is more complex with directly awarded contracts. Which tools are available to a PTA to prevent overcompensation? A recent ruling of a local administrative judge in France gives some food for thought regarding this issue.

French Context

First, let us briefly recall the French context regarding rail PSO attribution. Since December 2019, the incumbent's legal monopoly is over.[1] However, till December 2023, the PTA (the Régions) can directly attribute a rail PSO contract to SNCF.

Up to now SNCF is still the only operator running regional trains in France (for PSO) even if some Régions have started competitive processes to tender part of their regional rail services (Provence-Alpes Côte d'Azur, Hauts-de-France, Grand Est, etc.).

All French rail contracts have the same structure.[2] The costs paid by the PTA are divided in two categories:

- C1: costs directly incurred by SNCF (for train driving, train maintenance, overheads costs, etc.). These costs are set at the beginning of the contract and indexed during its lifespan.
- C2: external costs (rail infrastructures charges, taxes, etc.). The PTA pays these costs *ad valorem*, i.e., the exact amount without any remuneration for the operator.

In addition, there is an annual sales revenue objective agreed upon by SNCF and the PTA ('OR') and a rule regarding risk sharing for revenue and ridership (for example a 50/50 split in case this objective is not reached).

Put simplistically (if the sales revenue objective is exactly reached and without considering other penalty mechanisms), the compensation is therefore equal to C1+C2-OR.

Based on this brief summary, one can understand that the overcompensation risk arises from setting an inaccurate C1 (too high or with an evolution that does not reflect SNCF's cost evolution).

Ruling n°1705056, Tribunal Administratif de Marseille, 15 October 2019, SNCF vs Provence-Alpes-Côte d'Azur

The Région Provence-Alpes-Côte d'Azur (PACA) and SNCF signed a ten years contract in 2007. In 2016, PACA did not agree to pay the C1 costs indexed accordingly to the contract. According to PACA, this amount was too high regarding the costs actually incurred by SNCF.

Therefore, the PTA decided, and voted, 'unilateral prescription' deciding unilaterally, based on analysis realised by a consultant (hired by the Région), how much

1. The incumbent operator in France was called SNCF from 1937 to 2014. In 2014 it became SNCF Mobilités and in 2020 SNCF Voyageurs. SNCF Réseau is the infrastructure manager. For the sake of simplicity, the incumbent train operating company will be referred to as SNCF.

2. See for example Auvergne-Rhône-Alpes contract, p.96-105 https://www.auvergnerhonealpes.fr/actualite/237/23-la-convention-ter-de-voilee.htm

money is required for rail PSO in 2016. SNCF brought the case into court.

The judge conclusions were the following (Author's translation):

- 'One cannot say that the contract provisions apply by the PSO regulation'
- 'C1 Charges are a lump-sum. Therefore, the PTA cannot make sure compensation is adequate'.
- 'SNCF have a monopoly for rail PSO contracts. Therefore, the compensation given to SNCF should be substantiated. If not, this compensation can be recharacterised as an illegal state aid'.

Food for Thought

If they are upheld by higher courts, these conclusions may be groundbreaking. They may imply that all the French rail PSO contract are illegal.

These conclusions are also interesting outside of a French context, on a European level. They question the role that can be played by negotiation between an operator and a PTA when this PTA chooses direct awarding.

To our understanding of the judge's interpretation of the PSO regulation reaching an agreement through negotiation between both parties of the contract is not enough to protect against overcompensation. Should we conclude that the compensation needs to be set by an independent third party (the rail regulator? another independent expert?) to abide by the PSO regulation? It would be valuable to have the view of the European Commission on this French case law.

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