CER
The Voice of European Railways

## Position Paper

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# Revision of Railway State Aid Guidelines

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## 1. Introduction

The Community of European Railway and Infrastructure Companies (CER) would like to share its members' views in regard to the content of the updated text of the "Community guidelines on State aid for railway undertakings" (hereinafter "Railway Guidelines", "Guidelines"), which is currently being developed by DG Competition, and would like to thank the Commission for taking the points outlined in this position paper into account.

In its Communication on "The European Green Deal"[1], the Commission noted that "*as a matter of priority, a substantial part of the 75% of inland freight carried today by road should shift onto rail and inland waterways*". Similarly, in its Communication on a "Sustainable and Smart Mobility Strategy – putting European transport on track for the future"[2], the Commission noted the need for "*decisive action to shift more activity towards more sustainable transport modes* (notably […] shifting a substantial amount of freight onto rail", indicating that transport by rail should double by 2050. In line with these policy objectives, the updated text of the Railway Guidelines should provide strong incentives for modal shift to rail and thus should make it easier for Member States to support rail transport. The following paragraphs outline CER's vision in regard to which stipulations of the updated text of the Guidelines would be most appropriate to reach these objectives.

## 2. General remarks

In our view, it is important to note in which political, social, and economic context the current revision of the Railway Guidelines is taking place, and to take these circumstances into account during the drafting process.

Rail fulfils a critical socio-economic function of providing sustainable, energy efficient, socially-inclusive, and environmentally friendly transportation. In order for the EU to reach its climate neutrality goal in 2050, the modal shift from more polluting transport modes to rail has to be urgently accelerated, which should be reflected in the European Commission's approach to State aid.

At the same time, railway is one of the sectors that suffered the highest losses as a result of the COVID-19 crisis. In two years of the pandemic (March 2020-March 2022) the railway sector has accumulated more than 54 billion EUR of revenue losses in EU27, which have been only partially compensated. Thus, the updated text of the Guidelines could provide a specific basis for compensation of the COVID19-related losses of the railway companies, reflecting the specificities of the railway sector.

Besides, it should also be noted that due to the recent significant rise of energy prices, the overall costs of rail transport increased accordingly. Therefore, we would also suggest to the Commission to consider that the updated text of the Guidelines could provide guidance to Member States on what kind of support could be provided to railway undertakings to mitigate the effects of the increase of traction electricity costs.

[1] COM (2019) 640 final of 11.12.2019. Available at: https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal_en.
[2] COM (2020) 789 final of 9.12.2020. Available at: https://transport.ec.europa.eu/transport-themes/mobilitystrategy_en.

Apart from that, railway undertakings will inevitably suffer additional losses in terms of traffic and revenues due to the on-going conflict in Ukraine, which will have a negative impact on the development of EU-Asia rail transport and the international rail transport in general.

## 3. Presumption of compatibility of interoperability aid and aid for reducing external costs with intensities of up to 100% of the eligible costs

The current text of the Railway Guidelines provides that the necessity and proportionality of the aid for reducing external costs or the interoperability aid will be presumed if such aids do not exceed 50% of the eligible costs; while for such types of aid with aid intensities above 50% threshold the Member States must demonstrate the need and proportionality of the measures in question. This requirement imposes an unnecessary burden of proof upon Member States, having the effect of unnecessarily limiting their interventions to the set limit. For example, out of fifteen decisions issued by DG Competition in 2019-2022 that approved aid schemes for reducing external costs after analysing the aid intensities based on the stipulations of the Railway Guidelines, in every single case the respective Member State has notified the scheme with maximum aid intensities defined at or below 50% of the eligible costs.[3] Presumption of compatibility of the aid for reducing external costs and the interoperability aid up to 100% of the eligible costs would relieve the Member States from the administrative burden of proving the need and proportionality of such aids and, therefore, would promote higher amounts of support to be granted to railways, supporting the EU modal shift objectives.

Regarding the aid for reducing external costs, it should be noted that currently the external costs are not being correctly allocated to the modes of transport in accordance with their level of pollution. As stated by the Commission in its "Handbook on the external costs of transport" (2019), the average external costs of passenger rail transport are 2.8 times lower than for road (without congestion), and 3 times lower than for aviation. For freight transport, the average external costs for road freight transport are 2.6 times higher than for rail (including congestion - 3.2 times higher). Member States should be incentivised to compensate this imbalance in full. Therefore, the compatibility of the aid for reducing external costs with aid intensities of up to 100% of the avoided externalities should be presumed, and this would encourage Member States to provide such level of funding. Only the aid schemes covering up to 100% of the difference in external costs would create a level playing field between different modes of transport, as well as they would adequately support the necessary shift to rail, in accordance with the above-mentioned ambitious targets set out in the Communication on a "Sustainable and Smart Mobility Strategy".

In regard to the interoperability aid, the need for higher aid intensities has been recognised in the established Commission's decision-making practice. In several cases[4] the Commission has approved the interoperability aids related to ETCS/ERTMS with aid intensities of 85%-100% of eligible costs. In these decisions the Commission concluded that such aid intensities should be regarded as necessary and proportionate due to the exceptionally high investment costs necessary to deploy ETCS/ERTMS. Besides, it could be noted that the funding of the ETCS/ERTMS benefits the society as a whole, and in a

[3] See the following decisions on State aid: SA.100486, SA.62208, SA.62018, SA.59448, SA.60383, SA.58046, SA.55507, SA.55025, SA.54990, SA.51559, SA.51714, SA.62800, SA.57886, SA.53615, SA.55912.
[4] See in particular the following decisions on State aid: SA.100432 approving aid with intensity of up to 100% of the eligible costs, SA.44621 approving aid with intensity of up to 85% of eligible costs, SA.55451 approving aid with intensity of up to 90% of eligible costs, SA.58908.

much lesser extent the rail transport services operators as such. Presumption of compatibility of the interoperability aid with aid intensities of up to 100% of the eligible costs would allow Member States to provide adequate public funding for deployment of ETCS/ERTMS easier and faster, by eliminating the redundant step of demonstrating the need and proportionality of higher aid intensity in every single case.

## 4. At least twice higher threshold for presumption of compatibility of aid for rail infrastructure use and aid for reducing external costs in relation to total cost of rail transport

In the present text of the Railway Guidelines the threshold for presumption of compatibility of the aid for rail infrastructure use and the aid for reducing external costs is set at 30% of the total cost of rail transport. We believe that this threshold needs to be raised to at least 60%. In regard to the aid for reducing external costs, the threshold of 30% of the total cost of rail transport doesn't allow for sufficient compensation of external costs savings achieved by the RUs, and, hence, doesn't encourage further external costs savings in transport sector, and, therefore, such threshold limits the possible benefits to society.

Besides, the aid that amounts to only 30% of the total cost of rail transport is insufficient to compensate for the imminent extensive cost burden that the rail freight sector faces. Rail transport is characterised by extremely high fixed costs, which account for over 80% of its total costs. This means that the traffic volumes that are necessary to break-even are far greater for rail transport (than for road transport). Yet, rail transport has much lower externalities: rail represented only 0,4% of the $CO_2$ emissions from all transport modes in the EU27, while road transport accounts for 71,7% of the $CO_2$ emissions from all transport modes in the EU27[5].

In accordance with the current text of the Guidelines, for aids for rail infrastructure use and aids for reducing external costs with intensities above 30% of the total cost of rail transport the Member States must demonstrate the need and proportionality of such measures. This requirement creates a very high administrative burden for the Member States and likely results in Member States strictly limiting the amounts of funding to this set threshold. For example, out of fifteen decisions issued by DG Competition in 2019-2022 that approved aid for reducing external costs after analysing the aid intensities based on the stipulations of the Railway Guidelines[6], only in two cases, which both related to the same aid scheme[7], have the respective Member States notified the scheme with higher aid intensities than the set threshold (namely, intensity of 40-50% of the total cost of transport).

Besides, the desired increase of the threshold for presumption of aid compatibility to up to 100% of eligible costs, which is described in the previous paragraph, should go hand in hand with the increase of the threshold for presumption of aid compatibility in relation to the total cost of rail transport. If the threshold for presumption of aid compatibility in relation to the total cost of rail transport is not increased to at least 60%, the mere increase

[5] Commission Staff Working Document Accompanying the document report from the Commission to the European Parliament and the Council Seventh monitoring report on the development of the rail market under Article 15(4) of Directive 2012/34/EU of the European Parliament and of the Council, SWD/2021/1 final, p. 17: https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52021SC0001&from=EN

[6] See the following decisions on State aid: SA.100486, SA.62208, SA.62018, SA.59448, SA.60383, SA.58046, SA.55507, SA.55025, SA.54990, SA.51559, SA.51714, SA.62800, SA.57886, SA.53615, SA.55912

[7] SA.51559, SA.51714.

of the threshold for presumption of aid compatibility to up to 100% of eligible costs would be ineffective and would only have a very limited effect.

Against this background, we believe that the current threshold for presumption of aid compatibility in relation to the total cost of rail transport should be at least doubled, i.e. increased to at least 60% of the total cost of rail transport.

## 5. Simplifications: cutting red tape

In order to support rail transport as the greenest land transport mode, it should be made easier for Member States to provide funding for railways. In particular, it should be avoided that the Member States are required time and time again to provide substantiated lengthy analyses in regard to the points that have already been sufficiently proven on a number of occasions.

For example, eligibility of aid schemes providing support for rail should not be conditioned on showing reduction of external costs by a certain percentage compared to a road only alternative. Estimation of the reduction of external costs by using rail by a certain percentage compared to road is already widely reported by the various Commission's studies and reports. There is sufficient data demonstrating that railway transport has significantly lower external cost than the road transport. All studies confirm that the external cost gap between road and rail transport is persistent. Therefore, the obligation to prove this fact in the context of a specific aid scheme constitutes unnecessary administrative hurdle, which at the least delays the moment when the funding is actually made available for the undertaking.

The same can be said about the aid eligibility criteria requiring a proof that the rail transport services are not fully competitive vis-à-vis alternative road transport services. It is a well-established fact that the railway undertakings in the freight sector are struggling with competitive disadvantages due to higher costs compared to road transport. There is enough data already confirming that road transport has lower operational costs (but higher external costs), and hence can offer lower prices and delivery terms to the clients, giving it a competition distortive advantage compared to railway transport. Demanding proof of lacking competitiveness on the side of rail transport leads to unnecessary administrative burden. In our view, the ongoing revision of the Guidelines should encourage and therefore make it as easy as possible for Member States to provide the necessary funding for railways. Hence, such redundant compatibility conditions for aid should not be upheld in the updated text of the Guidelines.

## 6. Specific guidance on State aid to rail service facilities

In our view, the revised text of the Railway Guidelines should also include specific provisions in regard to State aid to service facilities. Presently, the funding of service facilities is not addressed in a clear and transparent way by the EU rules.

We believe that State aid for rail service facilities should be allowed up to 100% of the funding gap, ideally with presumption of compatibility of such aids with aid intensities of up to 100% of the eligible costs. Such approach would be in line with the established decision-making practice of the Commission. In a number of decisions, the Commission has approved aid schemes that finance construction or upgrade of rail service facilities with aid intensities of up to 75%-100% of the eligible costs.[8] In these cases the Commission found such high aid intensities necessary and proportionate due to the fact that, while such projects require high investments, there is a risk that the required construction/upgrade of respective service facilities would not take place with lower aid intensities, due to the lack of willingness to invest on the part of private investors.

## 7. Clearer and more flexible provisions on funding for the purchase and renewal of rolling stock

The current provisions of the Railway Guidelines on aid for purchasing or renewal of rolling stock lack clarity, in particular in regard to their scope. In our view, going forward this ambiguity should be corrected, and the updated text of the Railway Guidelines should explicitly cover the aid for purchase, renewal and retrofitting of freight rolling stock as well. While freight rolling stock is generally available, measured against high costs and low profitability in the rail freight transport sector it remains to be too expensive. This results in the railway undertakings focusing only on the most profitable services and leaving a substantial part of transport demand to road. Funding schemes for purchase and renewal of freight rolling stock would help mitigating this market failure. Besides, while in our view it could be justified to subsidise the purchase of rolling stock by leasing companies, it would be important to have it alongside the possibility to provide such aid to railway undertakings directly. In the rail freight sector, the demand for affordable rolling stock is best served if the railway undertakings can choose between purchasing and leasing rolling stock, so it should be possible for Member States to support each of both models. For example, leasing of the rolling stock addresses potential transitory necessities for rolling stock by railway companies, e.g. for ETCS or DAC (Digital automated coupling) refurbishments and downtimes of owned rolling stock due to refurbishments.

Railway undertakings also still face difficulties in having access to passenger rolling stock, despite the possibilities provided by Regulation 1370/2007/EC. In particular, it could be highlighted that, there is a need of state funding for the long distance passenger transport equipment, i.e. new or existing rolling stock for international cross-border services with multisystem technology. The supplier market in regard to such rolling stock is very limited and the Member States' standards vary greatly all-over Europe. The latter leads to high investments when providing cross-border services, which hinders railway undertakings from providing such services. Therefore, it is important that the updated text of the Railway Guidelines outlines a straightforward and clear framework for the Members States on how to design compatible support schemes to finance purchase or lease of passenger rolling stock.

## 8. Block exemption for aid for coordination of transport and PSO compensation for rail freight

CER would like to express its full support to the initiative launched by the Commission to block exempt aid for coordination of transport and compensation of public services in the freight sector as reflected in the Proposal for a Council Regulation on the application of Articles 93, 107 and 108 of the TFEU to certain categories of State aid in the rail, inland

[8] See in particular the following decisions on State aid: SA.64546 approving aid with intensity of 99.6% of the eligible costs, SA.64434 approving aid with intensity of approximately 74% of the costs, SA.52716 approving aid with intensity of 83.89% of the eligible costs, SA.46341 approving aid with intensity of 80% of the eligible costs.

waterway and multimodal transport sector (COM(2022) 327 final), which has been published on 6 July 2022[9].

Exempting aid for coordination of transport would reduce administrative burden for the Member States and make it easier for them to provide support for the rail sector. This would promote further modal shift from road to rail. The Commission has gained significant experience in relation to aid for the coordination of transport covered by Section 6.3 of the Railway Guidelines. And from the Commission's experience, aid for the coordination of transport is instrumental to modal shift and does not give rise to any significant distortions of competition. Such exemption would also allow for the Commission to focus on cases with the biggest impact on the internal market.

As mentioned in the Explanatory Memorandum to the Proposal, while Article 9(1) of Regulation No 1370/2007 provides for the exemption from prior notification of PSO compensation for rail passenger services, a similar block exemption for PSO compensation does not presently exist for freight transport even if the EC already defined the outlines in its decision-making practice[10]. CER fully agrees that this omission should be corrected and thanks the Commission for the referenced Proposal.

As furthermore correctly stated in the Explanatory Memorandum to the Proposal, "*public service obligations may be an appropriate instrument to promote services in areas and segments where otherwise freight transport would occur by road only*". In our view, until the level playing field is fully achieved, there should be a clear legislative framework in place outlining how to establish public service obligations in rail freight transport and to provide respective compensation, for instance to support single wagon rail freight transport or combined transport. Therefore, we believe that to ensure full transparency and predictability, the updated text of the Railway Guidelines should contain a clear guidance for the Member States on how to design the PSO compensation for rail freight services in accordance with the State aid rules.

## 9. Specific rescue and restructuring rules for railways

We believe that specific rules on rescue and restructuring of railway undertakings in difficulty should be included into the updated text of the Railway Guidelines in order to cater for the specificity of the rail sector, such as, in particular, the long-term investments as well as the competition with the more polluting transport modes that don't internalize their negative externalities.

The horizontal Rescue and Restructuring Guidelines[11] ("R&R Guidelines") are difficult to be applied to railway undertakings and require some special derogations. Due to the distinctive features of the rail transport, such as long lead times, significant investments, high fixed-costs and inflexible labour market, the restructuring of railway undertakings in difficulty should be determined according to sector-specific criteria.

The horizontal R&R Guidelines do not sufficiently take into account that the rail transport market is in some parts still characterized by market failures, which need to be addressed differently. Applying the R&R Guidelines to the railway undertakings could even result in

[9] Available at: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13153-Greener-land-transport-simplified-state-aid-rules-New-Land-Transport-Enabling-Regulation-_en.

[10] See in particular the following decision on PSO with regard to freight transport by rail: SA 32.179 and SA 32.953, §79.

[11] Communication from the Commission — Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty; available at: https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A52014XC0731%2801%29.

the discontinuation of vital transport services. Namely, the R&R Guidelines contain the condition to withdraw from loss-making activities, which, applied to a railway undertaking, could result in a termination of certain services which are not cost-covering due to particularly higher cost burden compared to road transport (e.g. Single Wagon load services).

Besides, the significant own contribution of at least 50% of the restructuring costs from the own resources of the aid beneficiary imposed in the R&R Guidelines also constitutes a bad fit for the railway undertakings, as it does not take into account the financial challenges of the rail transport market with its particularly high cost burden. To appropriately reflect the specificities of the sector, the minimum required contribution of a railway undertaking in question should be limited to the maximum of 10% of the total restructuring costs.

Furthermore, such conditions for restructuring outlined in the horizontal R&R Guidelines as the "one time, last time principle" and the necessary structural measures (divestments of assets and reduction of business activities) are poorly-matched for the railway sector. The "one time, last time principle" doesn't account for the fact that some railway undertakings struggle with a legacy of unfinished restructuring, along with a backlog of important system innovations. Further opportunities to restructure and/or innovate may be justified to ensure the long-term viability of the railway undertakings, as well as to make them better prepared to compete on the market on their own. Moreover, demanding structural measures in a restructuring scenario in the transport market could easily jeopardize the outcome of the restructuring. In contrast to other sectors, the successful train operations depend on the networks, which require a minimum scope of assets and business activities.

## 10. Provisions on governing the financial flows within vertically integrated companies already exist

The public consultation on the revision of the Railway Guidelines that was open from 22 December 2021 until 16 March 2022[12] contained, among others, a section on the financial transactions concerning railway undertakings. In particular, the questionnaire inquired whether there are any difficulties in application of the Commission Notice on the notion of State aid[13] to the vertically integrated railway companies, as well as whether there are any risks of cross-subsidisation between commercial and non-commercial activities of such companies.

The sector recognizes the possible benefits of providing further guidelines to the Member States on which of the two sets of rules should be applicable in each case, - the general legislation on transparency of financial relations between the Member States and public undertakings or the rail sector-specific financial transparency requirements. As the current version of the Guidelines were published before the adoption of the Directive 2012/34 establishing a Single European Railway Area, the Guidelines would benefit from alignment with the provisions on independence of railway undertakings set out in Articles 4-6 Directive 2012/34/EU, including a proper separation of accounts. It should, however, be noted that the Commission Guidelines are of a non-binding nature and therefore the updated text of the Guidelines may not establish any new legal obligations in addition to

[12] Official consultation page can be consulted at: https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/13154-Rail-transport-revision-of-State-aid-guidelines/public-consultation_en.
[13] Commission Notice on the notion of State aid as referred to in Article 107(1) of the Treaty on the Functioning of the European Union, available at https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A52016XC0719%2805%29.

the existing comprehensive set of rules on transparency of financial flows already provided for by the EU law. Directive 2012/34/EU and Regulation 1370/2007 already pursue the absence of any cross-subsidisation between the commercial activities of the railway undertakings and those subject to public service obligations. This is especially the case with regard to the existing transparency obligations of Directive 2016/2370 for vertically integrated companies. The risk of cross-subsidisation between commercial and non-commercial activities of vertically integrated railway companies might exist in the situation when Member States do not correctly transpose and/or apply the existing comprehensive set of rules. Therefore, the strict compliance with the formal and accounting separation obligations imposed by the existing regulation is a key.