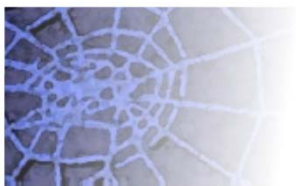


Competition and Third Party Access in European Railroads

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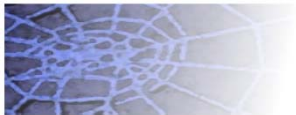
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The gradual process of market opening for train services on the EU level

- The liberalization process started in 1991 with Council Directive 91/440/EC for the specific market niches of international groupings.
- Meanwhile, rail operators are permitted to run all types of rail freight transport services within and between EU countries, international rail freight transport services (since 2008) and national rail freight transport (since 2012). Markets for international passenger services were opened in 2007, although the right for cabotage was not granted.
- The opening of national passenger rail markets has been proposed in an ongoing revision called the 4th railway package. Thus, the long-lasting process of market opening on the EU railway markets abolishing all legal entry barriers is converging into its final round.



Mandatory third party access

- The basic philosophy of third party access policies (antitrust policies and regulations) is that the owner of an infrastructure is obliged to provide non-discriminatory access to competitors on the (downstream) service markets.
- The term (mandatory) third party access only makes sense in the context of vertically integrated industries; in the context of infrastructure providers not active in the complementary service markets the term (mandatory) open access seems more adequate.



Third party access regulation

- In the context of the Fourth Railway Package proposed by the European Commission on January 1, 2013 a proposal for amending Directive 2012/34/EU has been provided aiming to strengthen ex ante third party access regulation. In particular, an integrated railroad company must not have control over the decision making of the infrastructure manager.
- Nevertheless, an integrated undertaking is still allowed and ownership unbundling not enforced, so that third party access regulation rather than open access regulation may continue.



The danger of over-regulation

- According to the proposed Article 7c amending Directive 2012/34/EU the Commission would gain the competency to decide whether providers of train services belonging to vertically integrated railway companies are allowed to become active (on a home market or a foreign market).
- Even the fulfillment of access regulations in the proposed Articles 7a and 7b would not necessarily guarantee the right to enter the markets for train services. The problem of enforcement of third party access regulation is thereby mixed with ad hoc evaluations of the Commission whether a level playing field on the relevant markets of train services can be observed.
- Such a regulation would be completely anti-competitive and not compatible with the disaggregated approach of regulatory economics. It would be a combination of two failures: misunderstanding the many faces of competition on the markets for network services and mistrust of the proper application of the instruments of third party access regulations.



The essential facilities doctrine

- The concept of third party access continues pursuing to balance the trade off between property rights and competition on the track.
- The essential facilities doctrine has its origins in US antitrust law. In accordance with this doctrine, a facility can only be regarded as essential if the following two conditions are fulfilled: (1) market entry to the complementary market is not actually possible without access to this facility, and (2) providers in the complementary market cannot, using reasonable effort, duplicate the facility; substitutes do not exist either.
- Case-by-case identification of essential facilities by court judgments does not guarantee a consistent localization of market power in liberalized network industries. The proper design of ex ante regulation requires generalizing the concept of the essential facilities doctrine to a class of facilities characterized by network-specific market power.



Limiting regulation to monopolistic bottlenecks

Network area	with sunk costs	without sunk costs
Natural monopoly (bundling advantages)	(1) monopolistic bottlenecks	(2) potential competition (contestable networks)
no natural monopoly (bundling advantages exhausted)	(3) competition among active providers	(4) competition among active providers



Railway infrastructure as a monopolistic bottleneck facility

Network area	Natural monopoly	sunk costs
Railway traffic	no	no
Railway infrastructure	yes	yes



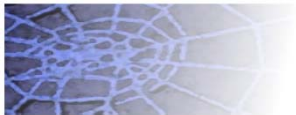
Implications for third party access regulation

- It is important to differentiate between network services and network infrastructure. Service markets should not be regulated, irrespective of whether they are old or new ones or whether players have high market shares or not.
- In order to allow active and potential competition on service markets non-discriminatory access to railway infrastructures is necessary. To the extent that a monopolistic bottleneck is observable, ex ante regulation should be in place; otherwise the evolution of service markets will be hampered.
- Incentive regulation must be restricted to monopolistic bottleneck components; cost based regulation should be avoided.



Cabotage and third party access (1)

- Since market opening will not be finished until train companies in Europe do have free entry to the markets for domestic passenger train services throughout Europe, the issue of cabotage remains topical.
- Thus, cabotage is no longer per se forbidden. However, such a market entry and in particular cabotage must not conflict with public service contracts (Article 11(1)). The question arises whether there is an unsolvable conflict between cabotage and the provision of public services.



Cabotage and third party access (2)

- In order to strengthen competition on the international and national long distance markets for train services it is necessary to allow all forms of competition on the track and simultaneously raise an entry tax in order to compensate the holder of the exclusive right for providing subsidized train services.
- Subsequently the stated conflict between competition on the track and competitive tendering with exclusive rights to provide subsidized train services would disappear.

