HOUSE OF LORDS

European Union Committee

4th Report of Session 2004-05

Liberalising Rail Freight Movement in the EU

Report with Evidence

Ordered to be printed 22 February 2005 and published 4 March 2005

Published by the Authority of the House of Lords

London : The Stationery Office Limited
£20.00

HL Paper 52

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ABSTRACT

Freight movement within Western Europe has been a growing market for many years. Despite a substantial decline in traditional rail freight markets, especially the movement of heavy goods such as coal and steel, the overall growth of freight markets has enabled the rail freight market to maintain its volume in recent years. But rail freight has lost market share to other modes and not least to road.

A competitive and efficient rail freight industry is important for the competitive position of industry and commerce. This coupled with the fact that rail freight is more environmentally friendly than road freight, has led the European Commission to believe that measures are required to stimulate further growth in the movement of freight by rail.

In 2001 the European Commission's First Railway Package was adopted. It sought to introduce open access for new international rail freight operators and to ensure accounting separation of rail infrastructure management and freight and passenger operations. The Second Railway Package, to be implemented in 2005, set up the European Rail Agency and brought forward the date of opening of the complete rail network for European freight services to 2006.The Third Railway Package has not yet been adopted. It seeks to introduce compulsory compensation to be paid to customers when rail freight operators do not meet stipulated quality standards. It also proposes an international rail drivers' licence.

This Report reviews the background to the Railway Packages, considers why they were introduced and offers a provisional analysis of their effect thus far. The quality of service offered to customers of rail freight movement in Europe falls seriously short of standards required in a competitive environment. Liberalisation of the United Kingdom freight market since 1994 has however resulted in better performance and a growing market share for rail freight.

We welcome the Commission's drive to improve the performance of the rail freight industry but some parts of the Third Railway Package cause us concern. We believe that it is wrong to impose an international rail driving licence on all train drivers and that the proposal for compulsory compensation to rail freight customers for poor quality service should permit an opt-out from this scheme.

The Channel Tunnel is the only direct rail link between the United Kingdom and mainland Europe. There are particular issues relating to the operation of the Channel Tunnel which are quite separate from the wider issues raised by the Rail Packages. These issues were not the specific focus of our inquiry but we examine some of them because witnesses frequently referred to them and because they pose major constraints on the ability of the United Kingdom to benefit from rail freight liberalisation.

Liberalising Rail Freight Movement in the EU

CHAPTER 1: WHAT THIS REPORT IS ABOUT

1. For many decades, European rail transport was dominated by nationally based vertically integrated state monopolies, which dealt with international traffic through cooperation rather than competition. It is the aim of the European Commission to liberalise the market, so that incumbents are encouraged to compete with each other, and new entrants attracted in. This is widely thought to be particularly important in seeking to raise the rail share of the market in European freight traffic.

2. To this end, the European Commission has introduced three packages of Directives. The First Railway Package, which became law in 2001, ought by now to have been implemented in all the European Union-15 Member States. The Second Railway Package was adopted by the European Union in 2002 but has not yet been implemented in Member States. The Commission has now produced a Third Railway Package of Directives which has not yet been adopted.

3. Against the legislative background, which is explained more fully in paragraphs 13-18, Sub-Committee B decided to undertake an inquiry into the implementation of the European Union policy of open access for European rail freight services. We were particularly keen to know to what extent there remained barriers to the development of competition in international rail freight, and if there were such barriers, what could be done to remove them.

4. A further element of European transport policy, put forward in the European Commission's 1998 White Paper on Fair Payment for Infrastructure Use and reiterated in its 2001 Transport Policy White Paper (Transport Policy for 2010 – Time to Decide) is the policy of charging each mode of transport according to the costs it imposes by use of the infrastructure, including the external costs of congestion, accidents and environmental damage. Appropriate charging for the use of infrastructure on all modes could be a very important complementary measure to liberalisation, in order to ensure that traffic allocates itself between modes of transport on the most efficient basis possible. However, we did not seek evidence on this issue and do not therefore seek in this report to reach conclusions on this aspect of European policy.

Acknowledgement

5. We are grateful to all witnesses for their evidence, in particular for evidence from continental companies and organisations many of whom travelled long distances to give oral evidence. We should like to thank our Specialist Adviser, Professor Chris Nash, for his help and advice throughout the inquiry and the drafting of this report.

Recommendation to the House

6. The Committee considers that the European Union's policy of open access for international rail freight services raises important issues to which the attention of the House should be drawn, and recommends this Report to the House **for information**.

CHAPTER 2: PAST TRENDS AND THE CURRENT POSITION OF RAIL FREIGHT IN THE EUROPEAN UNION

7. Rail freight has steadily lost its market share in the movement of freight in Western Europe over the last 30 years. Figure 1 shows that its market share has dropped from 20.1 per cent in 1970 to just 8.1 per cent in 2000 in the then 15 European Union Member States. In the new Member States the decline in market share has been more precipitous since the end of communism and the end of protection of the rail freight market.

8. However, freight movement as a whole is a growing market and whilst the rail freight industry has lost percentage share of the market, the actual volume of freight moved by rail has, as Figure 2, shows, stayed roughly constant within the EU-15 in recent years.

9. The Committee were concerned to discover that the rail freight industry had not grown substantially in the past thirty years since freight transport in the European Union has grown in that time and some of the barriers restricting European rail freight ought to have been removed.

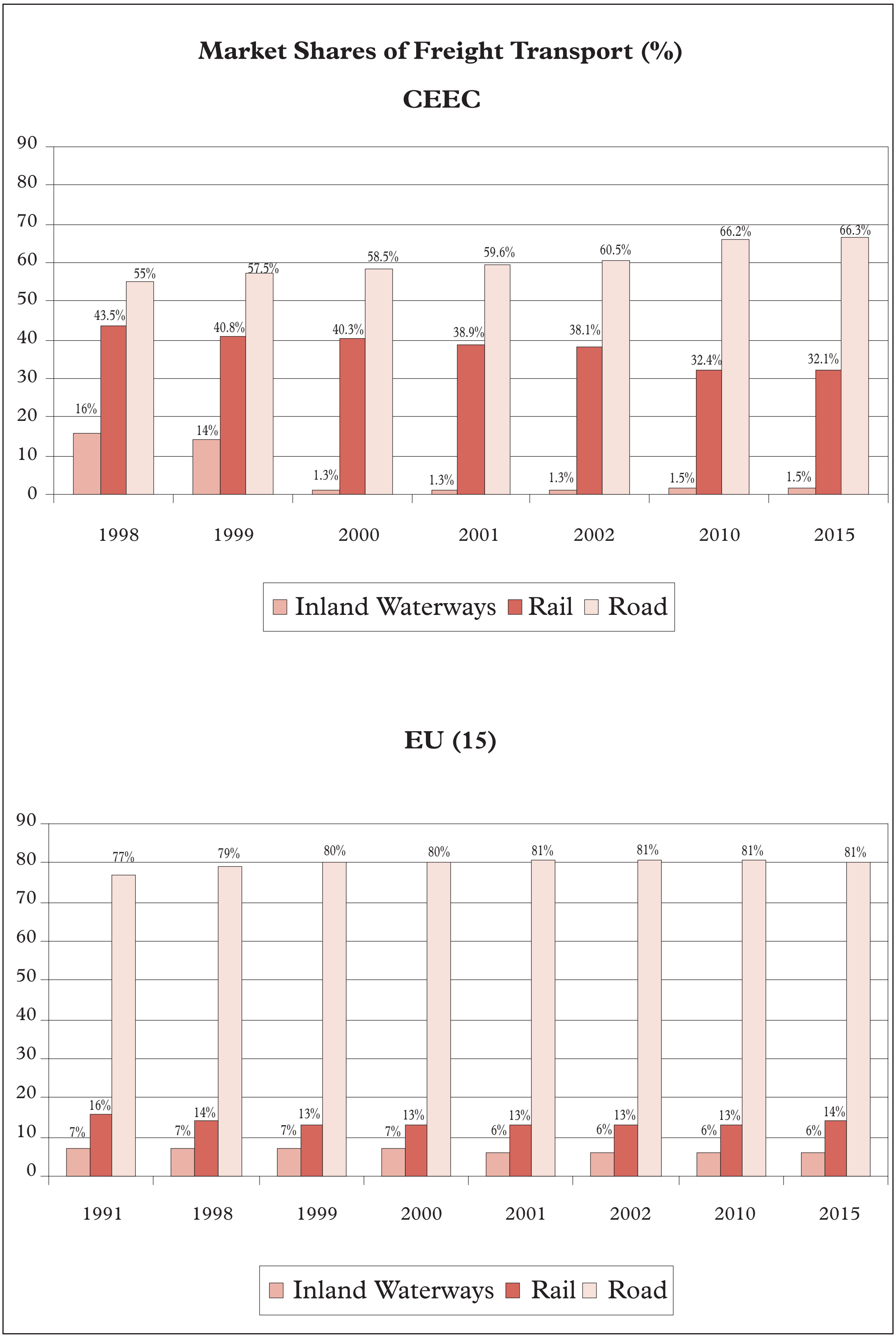
10. Rail has traditionally moved heavy, bulk items such as coal and steel. The great reduction in these markets within the European Union (illustrated for France, Germany and Great Britain in Figure 3) in the past 30 years has undoubtedly had a large negative effect on rail freight. The industry has however managed to achieve some growth in other markets, such as the transport of goods in containers and manufactured goods.

11. Rail is cheaper than road freight over long distances, as the written and oral evidence that we received, especially that from Transfesa, demonstrated. Transfesa estimates that rail freight costs approximately €0.45 per kilometre per container or swap-body whereas road freight costs between €0.65 and €0.80 per kilometre per container or swap-body[1] (Tr Supp. Wr evi). Admittedly this is based specifically on Spanish data, but we have no reason to suppose that the comparison is substantially different elsewhere in Europe.

12. Even though rail freight has lost some of its market share, the favourable economic climate of the late 1990s allowed rail freight in the European Union to grow in absolute terms but, as Figure 2 shows, it slipped back in 2001. Figure 4 also shows that rail freight has grown considerably since privatisation in Great Britain. Lord Berkeley (European Rail Freight Customers Platform) said that since privatisation rail freight volumes in Great Britain have gone up by 50 per cent (Q 70). The Department for Transport claimed that in Great Britain since privatisation, rail freight has increased by 42% in terms of freight moved (w.evi.para 2). Lord Berkeley was clear that competition between the four private rail freight companies now operating in the United Kingdom had helped this increased market share. He described open access in Great Britain as a success (Q72). We recognise that a mature industry and an independent regulator have added to this.

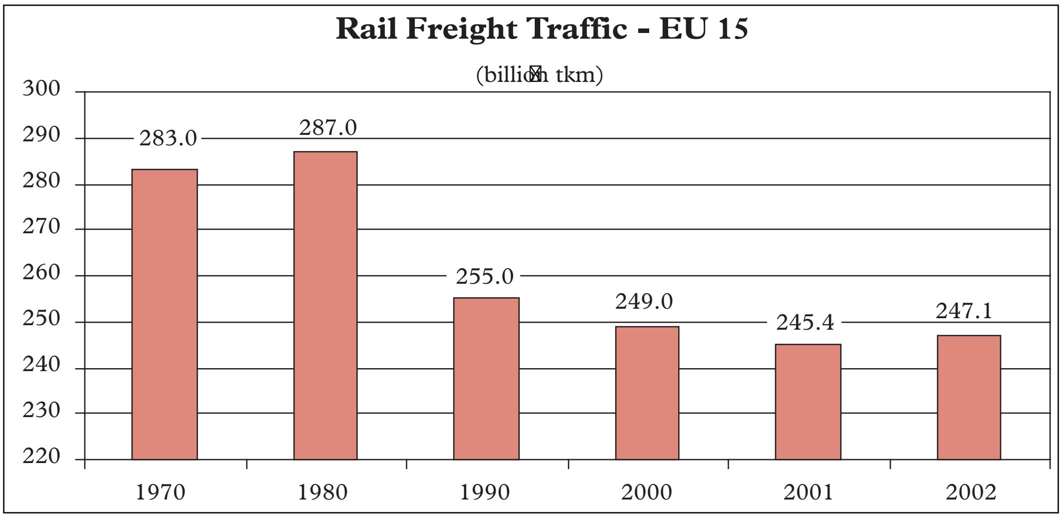
[1] An inter-modal loading unit

FIGURE 1



From *Current Developments in European Integration Financial Services*, *Transport Policy*, edited by Dirk Heremans *et al*, Leuven Law Series 18, Leuven University Press, 2004, p.164 reproduced by kind permission of Leuven University Press

FIGURE 2



From *Current Developments in European Integration Financial Services, Transport Policy*, edited by Dirk Heremans *et al*, Leuven Law Series 18, Leuven University Press, 2004, p.164 reproduced by kind permission of Leuven University Press

FIGURE 3

Rail Freight Traffic (m. tonnes) 1982-2002

	Germany		**France**		**UK**	
	Total	Of which coal, ore	Total	Of which coal, ore	Total	Of which coal
1982	228	100	130	31	146	91
1992	275	117	92	12	122	68
2002*	189	62	89	11	87	41

*1998 for France
Source: Eurostat for France, Germany
The commodity categories are coal and mineral fuels, iron ore and waste.
Germany includes the former DDR for 1992, 2002.
SRA for Great Britain. Data for iron ore and waste not available.

FIGURE 4

Rail freight traffic in Great Britain since 1990

Rail Freight Traffic b tonne km

	Great Britain
1990 – 1991	16.0
1995 - 1966	13.3
2000 - 2001	18.1
2001 - 2002	19.4
2002- 2003	18.7
2003 - 2004	18.9

Existing and proposed European legislation

13. We have already explained that the rail freight industry is not as successful as many would wish (see paragraphs 7 to 12). Against this background, the European Community has legislated and is introducing further legislation. In its 2001 White Paper it set itself the target of stabilising the rail share of the freight market, and cited the contribution rail could make to the relief of road congestion and environmental damage as reasons for seeking this reversal of trends. One key measure to achieve this was the introduction of infrastructure charging regimes in all modes which would fully reflect all costs of use of the infrastructure by the traffic in question, including congestion, accidents and environmental costs. Directive 2001/14 provides for such an approach for rail. However, the only measure proposed regarding road transport infrastructure charges since this White Paper, the Eurovignette proposals of 2003, did not permit the level of charges to reflect all these costs, and in any case agreement on the introduction of this measure has yet to be achieved.

14. As far as rail is concerned, the European Commission believes that part of the solution to the declining market share of rail freight lies in creating a liberalised single market within the European Union. The three Railway Packages contain an attempt to deal with the problems that have hindered the rail freight industry in the recent past so that the industry can improve its performance and increase its share of the freight market.

15. The key approach of the Commission to achieving this has been to open the rail freight market to competition. This process began with Directive 91/440, which created open access rights for certain international rail freight operators, but has greatly accelerated with the proposals contained in three Railway Packages in recent years.

16. The First Railway Package[2], which Member States were required to implement by the end of 2003, extended the European Union's policy of open access for international rail freight services. Due to fears that vertically integrated operators would use their control of the infrastructure to favour their own services, it also introduced various measures to try to ensure transparent and non-discriminatory charges and access conditions for use of the infrastructure. Specifically it required that:

- the body responsible for path allocation and the setting of charges must be independent of any transport operator;
- where infrastructure, passenger operations and freight operations are part of the same organisation, they must be in separate divisions with separate accounts;
- in each Member State there must be a regulator, to hear appeals and regulate access charges, who is independent of the infrastructure manager;

[2] The 1st RP comprises three Directives; Directive 2001/12/EC of the European Parliament and of the Council of 26 February 2001 amending Council Directive 91/440/EEC on the development of the Community's railways [2001] OJ L 075; Directive 2001/13/EC of the European Parliament and of the Council of 26 February 2001 amending Council Directive 95/18/EC on the licensing of railway undertakings [2001] OJ L 075; Directive 2001/14/EC of the European Parliament and of the Council of 26 February 2001 on the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure and safety certification [2001] OJ L 075

- any charges to train operating companies for access to infrastructure must be based on direct cost although non-discriminatory mark-ups are allowed in cases where a higher level of cost recovery is necessary; and
- all authorised international rail freight operators should have open access to the trans-European rail freight network[3] and, by 2008, open access to the whole network.

17. The Second Railway Package[4] has been adopted but does not have to be fully implemented by Member States until 31 December 2005. It seeks to deal with the barriers to entry posed by safety regulation and lack of interoperability of rolling stock and also extends and accelerates the introduction of open access by requiring that:

- A new European Rail Agency should be set up to advise the Commission on the implementation of technical standards for interoperability and common safety requirements; and
- The date of complete opening of the rail network for international freight services should be brought forward to January 2006 and that open access for domestic freight should be introduced in 2007.

18. The Third Railway Package[5] which has not yet been adopted has three main objectives:

- to introduce open access for international rail passenger services;
- to further improve interoperability by introducing an international rail drivers' licence valid throughout the Union; and
- to give direct incentives for the improvement of rail service quality by introducing compulsory provisions in rail freight contracts for compensation to be paid to customers when stipulated quality standards are not met.

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[3] A network which includes almost all routes currently used by international freight trains

[4] The 2nd RP is comprised of three Directives: Directive 2004/49/EC of the European Parliament and of the Council of 29 April 2004 on safety on the Community's railways and amending Council Directive 95/18/EC on the licensing of railway undertakings and Directive 2001/14/EC on the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure and safety certification [2004] OJ L 164; Directive 2004/50/EC of the European Parliament and of the Council of 29 April 2004 amending Council Directive 96/48/EC on the interoperability of the trans-European high-speed rail system and Directive 2001/16/EC of the European Parliament and of the Council on the interoperability of the trans-European conventional rail system [2004] OJ L 164; Directive 2004/51/EC of the European Parliament and of the Council of 29 April 2004 amending Council Directive 91/440/EEC on the development of the Community's railways [2004] OJ L 164.

[5] This includes COM(2004) 139, COM (2004) 140, COM(2004) 142 and COM(2004) 144

CHAPTER 3: CURRENT POSITION OF EUROPEAN RAIL FREIGHT

19. The evidence that we received demonstrated that there were a number of major problems for the European rail freight industry. In this chapter we:

- explain what these problems are;
- outline the evidence we received about each; and
- explain how the Railway Packages have sought to address each problem.

Continued Domination by Large, Publicly-owned Operators

20. Large publicly owned operators continue to dominate the European rail freight market, not least because they are in many cases still vertically integrated and so the company which owns the infrastructure also has a rail freight operating arm. The First Railway Package demands that if these functions are part of the same organisation they must, at least, have separate accounts. Member States have satisfied this requirement in different ways.

21. In 1994 the United Kingdom placed the infrastructure in a separate organisation, Railtrack. The operation and the infrastructure management were privatised and access to the rail freight market was opened completely. In the United Kingdom there are now four competing rail freight operators – English Welsh and Scottish Railway (EWS), Freightliner, Direct Rail Services and GB Railfreight.

22. In 1997 operations and infrastructure in France were put into separate organisations but both remained in government ownership and, so far, there is no other operator on the national rail network.

23. In Germany infrastructure and operations are separate divisions of the same company, DBAG. But, as Mr Meyer of the European Rail Freight Association told us, "they talk about Chinese Walls between the infrastructure side and the operating side, but often our members asked for a slot and the next day the client informed the private company that the state-owned company had already tendered for this transport" (Q 198). The efforts made by the European Commission in the First Railway Package to ensure fair and open access to the rail freight network by splitting the operation and infrastructure arms of the organisations do not appear to be producing the required results.

24. **Further consideration should be given to requiring Member States to put rail infrastructure and freight operations into separate companies.**

25. Even where infrastructure and operations are split, the size and financial position of the dominant rail freight operator is often such as to discourage competition. This makes entry into the market by small, privately-owned firms even more difficult.

Quality of Service

26. Rail freight has to compete directly with the road freight industry and, in some cases, with the water-borne or air freight industries. If rail freight is to offer a viable alternative to the other modes of freight transport it has to be

similarly reliable, economically comparable and deliver a quality of service which is at least satisfactory.

27. The evidence that we received from Ford, the motor car company, led us to believe that the reliability and flexibility of the rail freight industry did not meet customer demands. We heard that from July to September 2004, 39 per cent of the trains from Dagenham to Valencia carrying freight for Ford were more than four hours late and, of these, a considerable number were over 24 hours late and some were 48 hours late. The UIRR (International Union of combined Road-Rail transport companies) has recently produced figures for delays on its members' trains for 2001 and 2003 (see Figure 5). Although these figures show an overall improvement, they demonstrate that the punctuality of freight trains within the European Union still falls seriously short of standards required by commercial customers in a competitive environment. Road freight, on the other hand, showed a 92 per cent record for arrival within 15 minutes of the estimated arrival time (Q 4).

FIGURE 5
Delays to the freight trains of members of International Union of Combined Road-Rail Transport Companies (UIRR)

	2001	2003
Total trains run by UIRR members	21,324	27,247
On time	43%	57%
Late	57%	43%
3 hours late	32%	24%
24 hours late	7%	5%

28. The lack of reliability of rail freight often results in customers being forced to use other modes of freight transport, such as road and air (Q 6). Many customers, despite being attracted by the use of rail to transport freight because they perceive it as being more environmentally friendly, easier to track en route (Q 4) and cheaper than road freight (Q 53), have turned away from or at least started to lose confidence in the rail freight industry.

29. With the growth of distribution systems based on "just-in-time" principles, it has become increasingly important that any commercial business must be confident that their goods are going to reach their destination on time if they are to continue to use rail. The evidence from Ford and UIRR appears to demonstrate that the rail freight industry is often not able to engender this confidence and this is one of the major factors in its loss of market share in recent years. However, it should be noted that, according to the Strategic Rail Authority, 95 per cent of domestic United Kingdom traffic does run on time.

30. The First Railway Package sought to address this problem through the introduction of open access for new operators in the expectation that this would encourage competition and therefore lead to a better level of service to customers. The Second Railway Package sought to further this through facilitating greater interoperability and extending open access to the rail

network. The Third Railway Package attempts to deal with the problem head-on through its proposals for compulsory compensation to be paid to rail freight customers when specific quality standards are not met.

31. Much of the evidence that we heard would suggest however that compulsory compensation is unlikely to solve the problem of lack of confidence in the industry. As Mr Hall of the Community of European Railways (CER) put it, "the reality is the customer does not want compensation, he wants a quality service" (Q 178).

32. Mr Hall of CER was also concerned that imposing compensation performance regimes for operating companies risked sending a message at odds with that being given by the other Directives. In his view the First and Second Railway Packages made it clear that the rail freight industry should be an open and competitive market where the direct result of inefficiency would be a loss of custom and market share to competitors. The Third Railway Package on the other hand, would seek to impose compulsory compensation regimes which, in his view, seemed to indicate that competition was not a sufficient incentive to ensure that the operators delivered an efficient service (Q 178). This measure was also criticised in the written evidence from the Department of Transport (wr evi para 28) and from EWS (Q 4) who argued that it might – by adding unnecessarily to the costs of rail operators – actually hamper the growth of rail freight.

33. On the other hand, we heard evidence on the part of customers of rail freight that unreliability of services is a source of real concern. Data provided to us on late arrival of rail freight trains reinforce the view that this is not a marginal matter. Train operators oppose the introduction of a compulsory compensation regime but rail freight customers may well favour it and could be given the option. If the proposed Regulation COM(2004) 144 were to permit an opt-out from compulsory compensation for poor quality of service should a customer prefer to pay less for a rail freight service but receive no compensation in the event of problems, then this would meet some of the criticism noted above while giving the choice to the customer. A Regulation setting out the basis for compensation payments and an opt-out clause would require careful drafting and may require further consultation to ensure that the needs of customers, as well as operators, are met. Whilst recognising the difficulties involved, we come down in favour of the customer having the option of compensation. **We therefore recommend that the proposed Regulation should permit an opt-out from a compulsory compensation regime and that the United Kingdom Government should support this recommendation.**

Continuing Barriers to Open Access

34. The Commission's policy of opening access to the rail freight industry, which the three Railway Packages are aiming to achieve, was intended to give customers a choice of rail freight operator. However, we heard that there were still significant barriers in place which prevented this open access.

(a) Safety certificates and operating licences

35. A freight train operator who wishes to enter the international market must obtain an operating licence and safety certificate from the national authority of each Member State in which they wish to operate.

36. New rail freight operators are subject to repeated approval processes when entering the market, requiring the provision of evidence which is not then mutually recognised between Member States. Written evidence was submitted to us by the Commission stating that there was little indication of formal liaison between national certification bodies during the certification of international operators. Deutsche Bahn held the view that there should be "one set of European rules for rail safety, uniformly applied in all the Member States and leading to full mutual recognition of safety certificates" (DB w.evi). The Commission believed that the safety certification process should be in two parts, "one part is a European general safety certificate and a second part will always be needed at national level because you have to check whether the security structure . . . and the rolling stock fits for that particular line" (Q 93).

37. We were concerned to learn from UNICE (Union des Industries de la Communauté européene) that the safety requirements may "appear to apply disproportionately to potential new entrants to the market, thus reinforcing the dominance of the incumbent operator." An example of which we were told was that of the class 66 diesel locomotive. Both Mr Goundry (Freightliner) and Mr Smith (EWS) praised the Class 66 General Motors locomotives (Q 116 and Q 236) for their reliability, and they are in use in much of Europe. However, when new entrants wished to use this locomotive in France, it was not permitted.

38. The Commission pointed out that Member States are frequently very slow in issuing safety certificates. However, the Railway Safety Directive[6], part of the Second Railway Package which was adopted in April 2004, obliges Member States to grant safety certificates within 4 months of any successful application (Q 293). This Directive seeks to provide for a transparent, harmonised and non-discriminatory process of issuing the safety certification but, as it does not have to be implemented by Member States until 2006, we are unable at this point to pass judgement on its success or otherwise.

(b) Access charges

39. Furthermore, the structure and level of access charges to infrastructure are not transparent across all Member States and some charging regimes implicitly favour incumbent operators by the imposition of fixed charges or by significant volume rebates. We heard that RFF still operated a two-part tariff system which gave a significant advantage to the incumbent operator SNCF (Q 294). The EU Directive on rail access charges[7] does not explicitly disallow two-part tariffs but Article 8 (3) requires that equivalent traffic within the same market segment should face comparable charges. Mr Hilbrecht told us that he thought it would be very difficult to make a two-part tariff system compatible with Article 8 (3). Mr Falchi from European Rail Infrastructure Managers (EIM) told us that differential access tariffs could be defended if they were based proportionally on the number of paths

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6 Directive 2004/49/EC of the European Parliament and of the Council of 29 April 2004 on safety on the Community's railways and amending Council Directive 95/18/EC on the licensing of railway undertakings and Directive 2001/14/EC on the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure and safety certification (Railway Safety Directive) [2004] OJ L 220/16

7 Directive 2001/14/EC of the European Parliament and of the Council of 26 February 2001 on the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure and safety certification [2001] OJ L 75/29

being bought, "in any business you can have a price for a big buyer and a price for a small one." (Q 145).

40. Such charging structures can create affordability problems for new, privately financed companies competing with major, publicly-owned railway service providers that benefit from public funding support. This problem of charging structures was one of the central problems which the First Railway Package sought to address.

Physical barriers to interoperability

41. The rail network across the European Union is not physically interoperable. Mr Gurmin of Ford told us that harmonisation of the standards used in the international rail freight industry was a key goal if companies such as his were to continue to use rail rather than other modes to transport their freight (Q 12). The physical barriers to interoperability include differences in the loading gauge[8], axle-weight and train speed.

42. We understand that the loading gauge in the United Kingdom is a particular problem since it is more constrained than that elsewhere in the European Union. Ford told us that they could transport two Focus C-MAX cars on a double-deck car transporter throughout other Member States but that once the cars reached the United Kingdom, they had to be transferred to a single-deck flat wagon. This doubled the cost of transporting the cars within the United Kingdom and often caused delays because of lack of availability of wagons (Q 12).

43. Mr Smith from EWS explained that work was being done on rail freight lines from Felixstowe and Southampton to allow the movement of nine foot six inch high deep-sea boxes. He thought it essential that this work was also carried out on other lines in the future to allow these containers, which are becoming the standard international size, to be moved throughout Great Britain to major freight centres (Q 117 and Q 120). Both the Channel Tunnel itself and the new high speed route to London are of larger gauge than is normal in Great Britain, so this problem does not apply to them.

44. Crossing international borders remains a significant problem for rail freight operators as often the driver and locomotives have to be changed at that point. Transfesa pointed out that there is a similar problem within France as the railway is managed on a regional basis and therefore freight crossing France has to change locomotives four times and six different drivers will be used! (Q 45) Changeovers often cause major delays and an urgent solution to this problem is required. One solution would be to permit train drivers to drive trains for longer distances but we heard that this was being resisted by the French trade unions (Q 45).

45. On international routes the problems of differences in rules and technology, as well as language, are more acute. As CER points out, these problems cannot be solved by the railway companies on their own and the European Rail Agency, set up under the Second Railway Package, is tasked with "bringing together rail expertise and Member State representation to tackle the political and financial challenges presented by such widespread system change." (CER written evidence)

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[8] The size of locomotive, truck or swap body which can be transported on a particular rail route. The gauge of a railway is determined by such factors as the height and width of bridge arches and the width of platforms.

Competition from Road Freight and Water-Borne Freight

46. Rail freight has to compete with the other freight modes such as road, water and air. Road freight, in particular, provides a flexible and high quality service and carries much long distance traffic which in principle is suitable for rail.

47. The Commission's policy of opening-up access to the rail freight market has sought to ensure that rail infrastructure and operations are separate, and that each rail freight operator pays appropriate charges for use of the infrastructure. By contrast, the European Union has been unable to agree on an appropriate way of charging Heavy Goods Vehicles (HGVs) their full social, environmental and economic costs (Q309). Although a draft Directive on this was introduced in 2003, it fell short of fully taking external costs into account in charging, and in any case agreement on this has still not been reached.

48. **Implementation throughout Europe of a charging system reflecting the full costs of road freight transport is urgently needed to ensure that rail is able to compete with road on equal terms.**

Competition from Passenger Trains for Access to the Network

49. Across the rail network as a whole, the number of trains, both passenger and freight, is constrained by the capacity of the tracks and other rail infrastructure. In the absence of a network of dedicated rail freight lines, decisions have to be taken about which should be given priority. We heard that in the vast majority of cases passenger trains were given priority over freight trains perhaps because, as Lord Berkeley suggested, "passenger trains carry people who have votes" (Q 89). Passenger trains generally run at a higher average speed than freight trains and thus we do not believe that freight trains should automatically have priority over passenger trains. However the evidence that we heard led us to conclude that the bias towards giving passenger trains priority sometimes prevents the rail freight industry from delivering an efficient service. Although the first railway package requires infrastructure managers to publish clear criteria for the allocation of paths, and to consider the needs of international freight trains in this process, the evidence we received suggests that they are still given too little priority.

50. **We accordingly urge the rail network managers of the European Union Member States to give greater priority to international freight in the allocation of paths over the network.**

Risk of Over-Regulation

51. We share the concerns expressed by a number of our witnesses that some elements of the Third Railway Package might impose burdens on the rail freight industry whose costs exceed any benefits they might bring. As EWS put it, "sometimes the European Commission may go too far and create legislation that it believes will be helpful but which would increase cost (Q 99). Of particular concern in this regard to some witnesses are compulsory performance regimes for operators (we deal with this at paragraphs 30-33). Nearly all witnesses expressed concern about the international train drivers' licence.

52. But we are also mindful of the position of the customers of rail freight. Reliability of service is one of the most important elements of service for the customer. If they do not get a more reliable rail freight service, they will go to other modes and that is what has happened to much of freight movement.

International train drivers' licence

53. The Third Railway Package seeks to address some of the interoperability problems by introducing an International Rail Drivers' Licence which would remove the necessity of changing drivers at an international border. Whilst we recognise the advantages of such a licence, we have reservations about that Directive as currently drafted as it appears that all rail freight drivers, even those who only drive domestic freight trains, will have to have an international licence.

54. The Minister reassured us that the United Kingdom Government were keen to ensure that the benefits of the Third Railway Package would outweigh the financial costs and that they would use this cost versus benefit test as a guiding point in negotiations on the Third Railway Package. He shared our concern that the international driving licence, in particular, would have costs which far exceeded its benefits (Q 350). **We urge the United Kingdom Government to continue to resist the requirement of a full international rail drivers' licence for all train drivers.**

CHAPTER 4: PROBLEMS WITH THE CHANNEL TUNNEL

55. Any international rail freight to or from Great Britain has to go through the Channel Tunnel. We were therefore particularly interested to find out how the Channel Tunnel was operating.

56. At the time of the opening of the Channel Tunnel in 1994, the volume of rail freight through it was forecast to be between 6 and 8 million tonnes per annum, rising to over 10 million tonnes a few years later (Berkeley supp w.evi). In fact, freight traffic through the tunnel has only ever reached 3 million tonnes per annum.

57. Of the 88.9 million tonnes of freight moved using rail within Great Britain during 2003-04, only some 2 million tonnes was freight moving to or from the Channel Tunnel. The amount of rail freight moving through the Channel Tunnel is, according to Mr Graham Smith of EWS, "about 3 per cent of the cross-Channel market" (Q 103). We heard from other sources that the rail freight which used the Tunnel was only about 3 per cent of addressable or potential traffic (Q315).

58. The physical capacity of the Tunnel and the lines leading to it is obviously a constraint on the amount of traffic that can go through it. We were nonetheless disappointed to learn from Network Rail that of the 35 paths in each direction available for freight trains between the Channel Tunnel and London, only twelve were in use at that time (Q 390). We understand that in January 2005 5-6 freight trains in each direction were using the Channel Tunnel per day. There is therefore capacity available for a large increase in international rail freight through the Tunnel.

59. We were disappointed to learn that the Channel Tunnel was operating way below its capacity. Our witnesses suggested a number of reasons for this which we examine in the following paragraphs.

Channel Tunnel access charges

60. EWS, in partnership with SNCF in France, is the only company which provides international rail freight services through the Channel Tunnel (through its subsidiary EWS International). The Freightliner Group, a rail freight operator in Great Britain, told us that access charges for the Channel Tunnel were, for any operator other than EWS, "way outside anything you would regard as being reasonable" (Q 230).

61. When the Channel Tunnel was opened in 1994, the national rail companies of France, Great Britain and Belgium contracted to buy half of its capacity at guaranteed prices. When British Rail was privatised, EWS took over its share of the international freight business through the Channel Tunnel, but charges for the United Kingdom portion of this are still paid by the residuary British Railways Board and not by EWS. These charges have three elements:

- variable tolls relating to the volume and type of traffic conveyed;
- a contribution to Eurotunnel's operating costs; and
- a top-up fee known as the Minimum Usage Charge (MUC) which guarantees Eurotunnel a certain level of income even if traffic levels through the Tunnel achieved by Eurostar and the freight operators are below a certain level (DfT written evidence).

62. In the case of freight services, these three elements amount to a total of roughly £26 million per annum and last until 30 November 2006, after which the MUC element falls away leaving an annual charge of around £17 million should traffic remain at current levels. In order to facilitate the privatisation of its unprofitable international services, the British Railways Board had initially agreed to pay these charges until 30 April 2005 with the result that EWS had access to the Channel Tunnel free of charge for this period (DfT written evidence). EWS told us that with current traffic levels through the Channel Tunnel they would not be able to bear the additional £26 million in Tunnel charges (Q 131) after this date. We heard from the Minister, however, that he had asked the Strategic Rail Authority (SRA) to negotiate a fixed term extension to the current funding arrangements for EWS's Channel Tunnel Freight usage charges through to 30 November 2006 (Q 331).

63. The Minister acknowledged that this extension would simply prolong the current regime but it would provide a breathing space whilst greater liberalisation was sought (Q331). During this period, one operator, EWS, will effectively pay no access charges, whilst any competitor would have to pay the high tariff published by Eurotunnel for open access operators. We heard evidence that the published rates involve charges for rail freight which are roughly twice those typically paid to the equivalent freight through the Tunnel by road. Of course, the situation would be somewhat different if Eurotunnel itself were to become an international rail freight operator, since it would be paying the charges to another part of the same organisation; we heard from Mr Hilbrecht of the European Commission that Eurotunnel has a subsidiary company which now has the necessary operators licence and safety certificate and an allocation of paths to run through France (Q 287).

Safety requirements

64. The high access charges to the Channel Tunnel for new entrants were by no means the only problem we heard about. There are stringent safety requirements which any locomotive running through the Channel Tunnel must meet; only 2 fleets of locomotives currently meet these – Eurotunnel's own locomotives and the Class 92 which are operated by EWS. Mr Goundry of Freightliner hinted that these safety requirements might be slightly too stringent because, "there is an emotional response to being under the sea in a tunnel" and pointed out that the safety requirements on very long rail tunnels through mountains in the Alps were not as demanding (Q 236). **We recommend that regular consideration should be given to the licensing of additional models of locomotive for use in the Tunnel.**

65. **Given the complex contractual position surrounding the Channel Tunnel, the issue of compliance with the First Railway Package in respect of the Channel Tunnel is itself a complex one, but one which the British and French governments need to address if international rail freight services between the United Kingdom and continental Europe are to meet the needs of British industry and commerce.**

66. **A way needs to be found urgently of securing competitive access charges to the Channel Tunnel so that the rail freight industry as a whole can compete on equal terms with the freight ferry industry across the Channel.**

CHAPTER 5: PROBLEMS AND SOLUTIONS AT EUROPEAN LEVEL

European Union action

67. Despite the problems and difficulties surrounding the rail freight industry at the present time, there is potential for the industry to grow if the necessary steps are taken at European and Member State level. In this chapter we outline what action we believe the European Union should take.

68. **The Commission must first and foremost ensure that the First Railway Package is fully implemented across the EU-15. The 10 new Member States may need longer to implement the legislation but the Commission should work with them to ensure compliance as soon as possible.**

69. The First Railway Package, which aims to introduce open access to the infrastructure and fair, transparent and non-discriminatory rules for the allocation of paths, has already made some progress towards solving some of the problems faced by the rail freight industry. Mr Hilbrecht from the European Commission put it to us that, "there are small flowers starting to come out." (Q 306). We were pleased to note particular signs of progress in a number of areas which we now consider.

70. It is encouraging that in some parts of Europe real competition does exist between rail freight companies. We were told that competing operators exist in many countries, including Germany, Denmark, Sweden, the Netherlands and Italy. By contrast there is no competition at all to date in France and Spain.

71. The freight corridor through the Alps is one of the most important in Europe and competition between rail companies is developing here. The pattern typically is for the main operator in one country to form a subsidiary in another through which to operate European services. For instance, Swiss Rail Cargo Germany (a joint venture between the Swiss operator SBB Cargo and the German private railway company HGK) operates trains between Switzerland and the Netherlands in direct competition with the German operators, including Railion. SBB Cargo also competes with the Italian operators including Trenitalia, through its Italian branch, Swiss Rail Cargo Italy. Railon Deutschland, through its association with BLS Cargo, now operates freight trains through Switzerland in direct competition with SBB Cargo. For their part, Trenitalia Cargo have entered the German rail freight market through a stake in the German private operator TX Logistics (CER written evidence).

72. These are encouraging ventures and we hope that they will be replicated across Europe so that real competition and choice for the customer becomes an integral part of the rail freight industry. The full implementation of the First Railway Package in spirit and in the letter should help to further this welcome competition.

73. Many of our witnesses told us that getting rail freight through France was very difficult. The significance of this problem is greater because France's geographical position means that international rail freight to and from Great Britain and the Iberian Peninsula travels through France. We were therefore encouraged by Mr Hilbrecht's confirmation that Europorte 2, a subsidiary of

Eurotunnel, had received a licence and a safety certificate to operate in France. A subsidiary of Connex was awaiting a safety certificate, having already obtained an operating licence and Rail4Chem, a German Company, was exploring the possibility of operating in France (Q 287).

74. The French two-part tariff system was also said to be a particular barrier to open access and fair competition within France. Mr Hilbrecht was happy "to say that we have achieved agreement with France . . . . They agree that it (the two-part tariff system) should be changed" (Q 283). Unfortunately the French government claim that because of the public service contracts with regions they cannot do so before 1 January 2006. **This two-part tariff system needs to be abolished. We hope that the Commission will ensure that the French government abolish it as soon as possible.**

75. The last problem that we identified is the least tangible, but is nevertheless an important challenge facing the rail freight industry. The evidence we received led us to believe that the rail industry in general, and in particular the rail infrastructure managers, have inadequate incentives to win new traffic. We recognise that, for political reasons, rail passengers are given priority over the movement of rail freight. This appears to have resulted in an institutional framework within the rail industry in which there is little incentive to increase and improve rail freight. Whatever the cause of this lack of commercialism and competitive performance, it has to be overcome if the rail freight industry is to revive and achieve its potential.

76. We were pleased to note however that an alliance of European rail freight operators, known as European Bulls, had been formed in January 2005 to enable freight customers to use rail for their European long-haul transport requirements. The organisation aims to guarantee high quality over the whole route and to achieve a significant increase in rail's share of international transport services in the next few years.

77. We were similarly pleased to learn about Rail Net Europe which is a group of infrastructure managers from 23 European Union Member States with a head office in Vienna. They work together to provide every rail freight operator with a one-stop shop to plan, organise and troubleshoot any rail freight path they want to use. The operator can use any member in any country (Q 409). In Great Britain this group is still in its embryonic stages but it has worked well in other Member States. The Group aims to provide a champion for rail freight operators so that they do not have to negotiate with a myriad of infrastructure managers but simply interact with one person who will deal with all the issues that might arise. This Group therefore seemed to us to be a good example of the industry seeking to be more customer focused.

78. **We applaud these initiatives and hope that the Commission and the United Kingdom Government will do all that they can to help them to succeed.**

79. However, despite these encouraging signs, implementation of the First Railway Package is still patchy. A number of Member States, including the United Kingdom, have not fully implemented the Directives. The European Court of Justice has taken negative decisions against the United Kingdom, Germany, Greece and Luxembourg. The Commission has prepared infringement procedures against Spain and Belgium, and has entered into dialogue with countries such as France where they have seen problems or

have concerns. **The Commission must maintain pressure on Member States to ensure they implement this package.**

80. The continued existence of vertically-integrated rail freight companies which have both infrastructure and operation arms is a potential barrier to fair competition. As we have already explained, some of our witnesses believed that the two functions were imperfectly separated in some companies. On the face of it, the simplest solution would be to pass European Union legislation which would force the complete separation of these two functions. Mr Hilbrecht said however it had proved impossible to achieve agreement in the European Council to complete separation, although he would like to see this (Q 300).

81. We have already indicated that we believe that the issue of complete separation of infrastructure from operations should be re-examined. In its absence, **we accept that the requirement that rail freight operators should be at arms length from the infrastructure managers and that their funding should be transparent may be the best alternative. But we believe it is important that track access should be regulated and appeals concerning the conduct of the infrastructure manager should be heard by an independent regulator.**

82. The current legislation requires that the regulator be independent of the infrastructure manager. The regulator can still be a part of the Ministry which is also responsible for the finances of both the infrastructure manager and the incumbent operator, as is the case in France.

83. Whilst we understand that some Member States are unwilling to set up an independent rail regulator because, with the current situation and lack of competition, they would have little to do, we perceived this as a chicken and egg situation. An independent rail freight regulator can only operate in a fully competitive market but for a fully competitive market to develop, there must be fair and open access to the infrastructure. Only an independent regulator can ensure this. The half-way house adopted by some Member States where the regulator is a department within the transport ministry (Q 287) is not acceptable in the long-term, given that the same ministry is frequently responsible for the state owned infrastructure manager and main freight operator.

84. **We believe therefore that the relevant legislation should be amended to make clear that each Member State requires an independent rail freight regulator, independent from the government, with appropriate powers and resources and tasked with ensuring fair and open assess to the rail freight market.**

CHAPTER 6: ACTION FOR THE UNITED KINGDOM GOVERNMENT

85. **The Government of the United Kingdom's first priority must be to implement fully the First Railway Package as soon as possible**. It is impossible for the Government to press others to comply with this legislation until they transpose it fully themselves.

86. We found it difficult to ascertain exactly why the United Kingdom had not yet implemented fully the First Railway package. Mr Hilbrecht from the European Commission told us that, "in the United Kingdom the basic work has been done. There are probably some questions with regard to the infrastructure charging but nothing should be so important as to cause such a delay. Honestly, I do not know why there is a delay in the United Kingdom." (Q 284).

87. Even when directly questioned, the Minister did not give us a clear picture of the problems which the United Kingdom was having in implementing the First Railway Package. He said that, "part of the delay was the transmogrification from Railtrack to Network Rail and all that that ensued in terms of definitions and everything else." (Q 319). He was unable to give a date or an estimated date for the full transposition. Mr Bolt, in his oral evidence, suggested that – although Britain was ahead of the rest of Europe in implementing many of the measures required by the first railway package – access to terminals, regulation of the Channel Tunnel Rail Link and some safety issues may need further action before the United Kingdom is fully compliant.

88. We regard it as urgent that the United Kingdom complies fully with the First Railway Package. We were therefore pleased to be reassured subsequently by the Minister that the Government regards compliance as a priority and expects to transpose the package by the end of 2005 (DfT suppl written evidence).

89. The Channel Tunnel is the United Kingdom's only direct rail link with the European mainland. The Minister told us that the subsidies to EWS would continue until 30 November 2006. EWS had told us that they would not be able to continue to operate freight services through the Tunnel if the subsidies ended. We recognise that this extension of the subsidies is necessary because it provides a breathing space but, as the Minister acknowledged, the extension simply continues to provide more favourable prices for the incumbent operator rather than opening up the market to fair and open competition.

90. It is essential that the period between now and 30 November 2006 is used to ensure that when the subsidies end the necessary changes have been effected to allow the market to open up. We understand that open access at competitive prices through the Channel Tunnel can only be achieved by co-operation between the United Kingdom Government and the French government in the Inter-Governmental Commission. **We urge the Government to work with the French government to ensure fair and open access through the Channel Tunnel.**

91. Despite the evidence that we have received, the Committee is unclear whether the usage agreements between the railways and Eurotuneel take precedence over or are subsidiary to the European Union Directives. The

United Kingdom Government and the European Commission must clarify this.

92. We have already discussed the problems with the British loading gauge and we agree with the CER that this problem cannot be solved by the railway companies on their own (see para.29). We acknowledge that valuable improvements have been made in recent years but there remains much to do. Movement of goods by rail remains an important element in ensuring that British industry and commerce is internationally competitive. For some business and industries the movement of freight by rail remains extremely important. **The Government must continue to work with the rail freight industry to identify those rail routes that still require an upgraded loading gauge.**

CHAPTER 7: RECOMMENDATIONS

93. In this Chapter we draw together and summarise the recommendations that we have made in this Report.

94. The Commission must first and foremost ensure that the First Railway Package is fully implemented across the EU-15. The 10 new Member States may need longer to implement the legislation but the Commission should work with them to ensure compliance as soon as possible (para 68).

95. The Commission must maintain pressure on Member States to ensure they implement this package (para 79).

96. Further consideration should be given to requiring Member States to put rail infrastructure and freight operations into separate companies (para 24).

97. We accept that the requirement that rail freight operators should be at arms length from the infrastructure managers and that their funding should be completely transparent may be the best alternative to complete separation. But we believe it is important that track access should be regulated and appeals concerning the conduct of the infrastructure manager should be heard by an independent regulator (para 81).

98. We believe that the relevant legislation should be amended to make it clear that each Member State requires an independent rail freight regulator, independent from the government, with appropriate powers and resources and tasked with ensuring fair and open assess to the rail freight market (para 84).

99. The French two-part tariff system needs to be abolished. We hope that the Commission will ensure that the French government abolish it as soon as possible (para 74).

100. Implementation throughout Europe of a charging system reflecting the full costs of road freight transport is urgently needed to ensure that rail is able to compete with road on equal terms (para 48).

101. We urge the rail network managers of the European Union Member States to give greater priority to international freight in the allocation of paths over the network (para 50).

102. The Government of the United Kingdom's first priority in relation to rail freight must be to implement fully the First Railway Package as soon as possible (para 85).

103. The Government must continue to work with the rail freight industry to identify those rail routes that still require an upgraded loading gauge (para 92).

104. We urge the United Kingdom Government to continue to resist requirement of a full international rail drivers' licence for all train drivers (para 54).

105. We recommend that Regulation COM (2004) 144 should permit an opt-out from a compulsory compensation regime and that the United Kingdom Government should support this recommendation (para 33).

106. We urge the Government to work with the French government to ensure fair and open access through the Channel Tunnel (para 90).

107. Given the complex contractual position surrounding the Channel Tunnel, the issue of compliance with the First Railway Package in respect of the Channel Tunnel is itself a complex one, but one which the British and French governments need to address if international rail freight services between the United Kingdom and continental Europe are to meet the needs of British industry and commerce (para 65).

108. A way needs to be found urgently of securing competitive access charges to the Channel Tunnel so that the rail freight industry as a whole can compete on equal terms with the freight ferry industry across the Channel (para 66).

109. We applaud the Rail Net Europe initiative and the European Bull alliance. We hope that the Commission and the United Kingdom Government will do all that they can to help them to succeed (para 78).

APPENDIX 1: SUB-COMMITTEE B (INTERNAL MARKET)

The Members of the Sub-Committee were:

Baroness Cohen of Pimlico
Baroness Eccles of Moulton
Lord Fearn
Lord Geddes
Lord Haskel
Lord Shutt of Greetland
Lord St John of Bletso
Lord Swinfen
Lord Walpole
Lord Woolmer of Leeds (Chairman)

Professor Christopher A Nash was appointed as Specialist Adviser for the inquiry

Declaration of Interest:

Baroness Cohen of Pimlico

Non-executive Director, Defence Logistics Organisation (Ministry of Defence)

Husband – Main Board Director of Balfour Beatty plc (responsible for Balfour Beatty Rail/ Balfour Beatty Power systems which build track and signalling)

APPENDIX 2: CALL FOR EVIDENCE

Sub-Committee B (Internal Market) of the House of Lords Select Committee on the European Union is undertaking an inquiry into the implementation of the European Union policy of open access for international rail freight services, as implemented in Directive 2001/12. The inquiry will wish to consider the effect of the First and Second Railway[9] Packages of measures in this respect.

The specific questions on which the investigation will concentrate are:

1. What are the current barriers to entry in the international rail freight market?
2. To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?
3. Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?
4. Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?
5. What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?

9 The "First Railway Package" comprised: (COM(2000) 571, COM(2000) 572 and COM(2000) 575. The "Second Railway Package" included (COM)(2002) 18, COM(2002) 21, COM(2002) 22, (COM)2002 23, COM(2002) 24 and COM(2002) 25.

APPENDIX 3: LIST OF WITNESSES

The following witnesses gave evidence. Those marked * gave oral evidence.

Central Railway
* Community of European Railway and Infrastructure Companies (CER)

Deutsche Bahn AG
* English Welsh & Scottish Railway (EWS)

Environmental Freight Services Ltd
* European Commission,

Directorate-General for Energy and Transport and Directorate for Competition
* European Rail Freight Association
* European Rail Freight Customers Platform
* European Rail Infrastructure Managers (EIM)

Eurotunnel
* Ford Motor Company
* Freightliner Group

GB Railfreight Ltd

Kelvin Hopkins MP, The Rail Freight Group

Kohn & Nagel Management AG
* Network Rail
* Office of Rail Regulation

Rail Freight Group

Réseau ferré de France

Swiss federal railways SBB
* Department for Transport and the Strategic Rail Authority
* Transportes Ferroviarios Especiales, S.A. (Transfesa), Madrid

Union of Industrial and Employers Confederations of Europe (UNICE)

Minutes of Evidence

TAKEN BEFORE THE SELECT COMMITTEE ON THE EUROPEAN UNION
(SUB-COMMITTEE B)

MONDAY 11 OCTOBER 2004

Present		
Present	Cohen of Pimlico, B	St John of Bletso, L
	Eccles of Moulton, B	Shutt of Greetland, L
	Fearn, L	Swinfen, L
	Geddes, L	Walpole, L
	Haskel, L	Woolmer of Leeds, L (Chairman)

Memorandum by Ford Motor Company

(Note: this submission does not include the views of Ford Motor Company's other subsidiaries operating manufacturing facilities or whose products are manufactured in Europe, namely Jaguar Cars Ltd., Land Rover, Aston Martin Lagonda, Volvo Cars and Mazda Motor Corporation.)

1. *What are the current barriers to entry in the international rail freight market?*

Prior to offering our opinions on this subject we would like to provide an overview of our current operations in Europe and our current use of rail services to provide transportation of components and finished vehicles.

Ford Motor Company has major vehicle assembly or component manufacturing operations in Southampton (UK), Dagenham (UK), Bridgend (UK), Halewood (UK), Genk (Belgium), Saarlouis (Germany), Cologne (Germany), Valencia (Spain) and Kocaeli (Turkey).

Concerning major flows of components by rail we have contracts for rail deliveries from:

Valencia (Spain) to Dagenham (UK)

Valencia (Spain) to Cologne (Germany)

Genk (Belgium) to Cologne (Germany)

Cologne (Germany) to Kocaeli (Turkey)

Concerning flows of finished vehicles by rail we have contracts for rail deliveries from:

Dagenham/Southampton to Liverpool

Dagenham/Southampton to Glasgow

Cologne, Saarlouis, Genk, Valencia assembly plants to distribution compounds in France, Germany, Spain, Italy, Netherlands, Austria and Denmark.

In determining the appropriate transportation mode for delivery of components or vehicles the deciding factors are straightforward ie lowest cost provided that appropriate standards of performance and quality are available. We will then lean in favour of an environmentally friendly mode when these three criteria are met For many routes we have a potential choice between rail and road and in some cases also inland waterways or sea freight. Rail tends to be a favoured overland mode where the distances are relatively long and the loads of sufficient volume or concentration to create economies of scale.

Ford Motor Company has contracts with various rail service providers and or rail operators,. examples being: EWS (UK); Freightliner (UK); Transfesa (Spain); STVA (France/UK); ATG (Germany); Railmax (Belgium). These companies in turn have contracts with either or both the rail traction provider and/or a rail infrastructure provider. Our major concern with the current set-up is that whilst Ford Motor Company contracts with the service provider (or in some instances our primary carrier does so), the issues we have with cost, performance, and to a lesser extent quality, are mostly with the traction and infrastructure providers.

To deal with the specific points of performance, cost and quality:

(a) Performance

As a general observation our biggest concern with rail freight is inconsistency of performance. Over the years we have learned to live with some of these inconsistencies and have developed contingency plans eg emergency freight via fast truck or aeroplane to avoid stoppages in our plants. When rail operates to agreed performance, it confers many advantages, especially that in many instances rail continues to operate on weekend and public holidays when roads in much of continental Europe are closed to commercial transportation. We also have the advantage that rail may not be subject to the delays incurred on road through adverse weather conditions and traffic congestion.

However our experience of the reality of rail transportation is that performance inconsistencies are so great and have placed our production at risk so often that we are now very reluctant to commit more business to rail and also actively reviewing other modes for current routeings. Our biggest concerns at present are rail shipments moving through France and reliant on SNCF as infrastructure and traction provider. Reasons for delays tend to be spread around operational failures (eg lack of drivers), a weak industrial relations environment (eg prone to strikes including targeted strikes by organisations unconnected with the transport industry) and less commonly technical failures (eg signalling faults). As a specific example 15 per cent of trains running on the Spain to UK route have been more that 24 hours late so far this year. This is an unacceptable level of performance from logistics service providers expecting to serve modern manufacturing industry.

(b) Cost

Of the cost that Ford as an end customer pays our "Tier 1" service provider, circa 80 per cent goes to the "Tier 2" traction and infrastructure provider. Our experience is that these "Tier 2" organisations (predominately state monopolies) do not operate with a modern "cost-down" mentality and do not recognise or perceive a need to offset their own cost increases through improved productivity. They are therefore inclined to expect annual Consumer Price Index level rate increases to cover their pay awards and other cost increases. On many occasions we have also experienced a significant lack of transparency in that price increases by the traction/infrastructure provider are not explained or evidenced in any way to either the service provider or the end customer. As a comparison when dealing with more competitive transportation modes eg road, we will typically negotiate prices with carriers for a one to three year period either with fixed rates or commitments to annual productivity and/or cost-down targets.

(c) Quality

The differences in quality of service provided by road and rail would not be by itself great enough to discourage Ford Motor Company from placing more business on rail. For component shipments there is no significant difference in quality between road and rail transportation. For vehicle shipments quality is a greater risk compared to direct road transportation. This tends to be associated with a variety of factors eg vandalism and theft risk when trains are not moving, risk when vehicles are being loaded and unloaded, heavy shunting operations and in some cases track ballast causing minor damage.

In general all of the above lead to an environment that does not encourage us as a potential rail user to increase or even maintain our rail freight business. We also need to mention at this point the lack of investment by rail service providers in appropriate rolling stock to support finished vehicle transportation by rail. Generally the specialised rail wagons used to transport finished vehicles are decades old, reaching or have already reached the natural end of their working life but are not being replaced by the service providers. We see this very simply as understandable risk avoidance by the service providers who are reluctant to invest substantial sums in such wagons when there is a likelihood that their customers will give up on rail transportation due to the concerns outlined above.

As a customer of rail services we would be delighted to experience an active competitive market place of rail service providers able to offer attractive costs, performance and quality. We suspect that the biggest barrier for potential entrants to the market for rail transportation services is quite simply that they do not believe that they can maintain a consistent business ie retain their customer base based on the performance of the current traction and infrastructure providers.

2. *To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?*

In this context as a customer of rail freight services we would not describe ourselves as experts in the EU Directives that have created the current rail freight environment. As end customers, so far as we are aware, most national authorities have at least formally indicated their compliance with Directives to create the so-called "Trans European Rail Freight Network". The issue is whether in reality the day-to-day operation of this network is adequate to meet customers' needs and then secondly once this has been resolved, what next steps are required to greater use of rail. As covered in our response to Question 1, the day-to-day operation of the network especially in France is inadequate to maintain customer confidence in this business. Some suggestions for next steps are covered in the response to Question 4.

3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

The end result required is a re-orientation away from that of a weak process driven state monopolies to that of a customer driven business. It would appear that the intent of the legislation through introducing more competition is to achieve this. Appropriate follow-up by appropriate EU and national authorities to ensure compliance may be as simple as monitoring new entries to the rail freight business and also maintaining performance metrics on conformance to agreed service levels for the main freight routes.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

The following is a list of actions that we would anticipate supporting greater competitiveness within the rail freight industry and between rail and road transportation, some of which may already be covered under the EU "Second Railway Package".

Rail traction providers: we would like to see far greater freedom for independent operators to conduct competitive business throughout a genuine European network—including one locomotive used for a complete pathway thus avoiding frontier changeovers.

Locomotive Crew: similar to above: we wish to see complete flexibility of locomotive crew, assuming of course compliance with appropriate safety standards.

Different line voltage: eventually should be standardised but initially remove barriers on introduction of modem locomotives able to operate a "through service" in various systems.

Length of trains: different train lengths are mandated by each infrastructure provider (may also vary by route)—should be commonised (to the longest standard ie 700m).

Loading gauge: we would like to see this standardised ie principal routes in the UK to be able to accommodate the larger continental gauge.

Track gauge: we would like to see this standardised ie principal freight routes in Spain (and Portugal) to operate on the standard EU gauge.

Imposed Price Increases by Infrastructure Providers: we would support directives or legislation to avoid exploitation of quasi-monopolistic status of infrastructure providers.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

Loading Gauge

We would favour the development of strategic freight corridors able to accept the largest EU loading gauge as a way of improving the price competitiveness of rail freight.

High Speed Freight Wagons/Vehicle Transporters

A consequence of the increased congestion experienced in the UK rail network is insufficient allocation of train paths for slower freight trains, especially during busy commuter periods. This increases costs because wagon turnaround times (utilisation) are reduced. A solution is to develop freight wagons with higher running speed capabilities, which because of their greater complexity are expensive. Therefore Government grant provision for new investment in high-speed freight wagons should be considered.

Train Length

The strategic freight corridors as mentioned above should not have restrictions on train length. Maximising the train length potential on all major freight routes would be a cost effective way to enhance the competitiveness of rail freight.

Development of Rail Terminals

Continue and extend Government grant support for the development of rail and multi-modal freight terminals.

Ford Motor Company

17 August 2004

Examination of Witnesses

Witnesses: Mr Bill Gurmin, Director Material Planning & Logistics, and Mr Howell James, Manager Material Planning and Logistics, Ford of Europe[1], Ford Motor Company Limited, examined.

Q1 ***Chairman:*** Good afternoon, Mr Gurmin and your colleague, Mr James. I am sorry that we are starting late; I apologise for that. We are aiming to conclude around 5.15, so I am sorry that we have lost three minutes of this session. Thank you very much for your written evidence. It was, as I expected, to the point, very focused and extremely helpful. We will obviously during our questions wish to develop one or two of the points that you have raised there with us. Is there anything you would like to say before we fire our own questions at you?
Mr Gurmin: I would just like to thank the Committee for the invitation on my own behalf and on Howell's behalf and on behalf of this company. We are delighted to be here to give evidence and we think this issue is very important for Ford Motor Company logistics. We will do whatever we can to support the Committee.
Chairman: Thank you very much indeed. At the start of your paper you did helpfully set out a background and thank you for that.

Q2 ***Lord Walpole:*** You have some idea of what we are going to ask you but I think the first three questions you have already answered extremely well in your written evidence. So, could we start with the first three questions and ask you, is there anything else that you wish to add in the light of anything more recent?
Mr Gurmin: As regards the organisational arrangements within Ford, we are a large company, as you know, producing motor vehicles. We have 10 major manufacturing sites throughout Europe, three of which are in the UK: Dagenham, Southampton and Bridgend. The evidence I give today will be on Ford Blue Oval and will not concern Land Rover, Jaguar, Volvo nor indeed Mazda. We have a large manufacturing presence in Europe. Our manufacturing locations are spread far from St Petersburg in the north right down to Valencia in the south. We have rail and road at all of those facilities with the exception of St Petersburg where we have a rail spur but currently it is not tied into the European network. We have river or sea at most of those facilities for totally multi-modal facilities (different transport modes). With the specifics of the Channel Tunnel and the question you asked about the Channel Tunnel, we were in fact the first commercial organisation to contract to the Channel Tunnel and we have been using it from the start. We will continue to use the Channel Tunnel and we are committed to it. Our major service provider through the Channel Tunnel on our routes down to Valencia—and we have a daily route from Dagenham to Valencia and back again—is Transfesa and they subcontract to Renfe, SNCF, Eurotunnel and EWS. We currently move about 33 per cent of our vehicles by rail and around 8 per cent of our inbound material by rail. So, rail is clearly a major part of our logistics network and we are committed to improving that service.

Q3 ***Lord Geddes:*** You made a most interesting comment at the beginning that you were not going to talk about Land Rover, Jaguar, Mazda and . . . . .
Mr James: Volvo.

Q4 ***Lord Geddes:*** Why not? In your opinion, are the problems that they face roughly similar to yours?
Mr Gurmin: I am the Director of Material Planning and Logistics for Ford Blue Oval[2]. I have opposite numbers in Jaguar, Volvo and Mazda. The data and the evidence I have collected are from our own sources. I know that they have similar issues. However, they are on a smaller scale than Ford of Europe. We produce 1.7 million vehicles a year and clearly, to do that, we have to move an awful lot of freight. If I can move on to question two which is about the competition and the flow of traffic, if we take the first point which is competition between modes, we always have the ability to move from rail to road and, on some occasions, into sea or indeed river freight. We move a number of vehicles from Cologne using the Rhine and we are happy with that from a freight point of view. So, we always have that competition available to us. Competition between rail providers exists but is very much more limited than that that we have with our road providers and we would like to see a great deal more competition in that field. The service providers predominantly

[1] Ford of Europe encompasses all of Ford's European activities, including those of Ford Motor Company Ltd (UK).

[2] The term "Ford Blue Oval" is used to distinguish the Ford brand from other brands (Jaguar, Land Rover, Volvo, etc) under the Ford Motor Company umbrella.

have to use the national rail companies and indeed many of them are subsidiaries of the national rail companies. As such, I would say that we do not have the competition that we would want in that field by some considerable margin. We would like to see at least three providers tendering for business. At times, we are tied into one or two. Very rarely do we have three organisations that can tender for the business. If you compare that to road, I always have three and many times I have as many as 10 tendering for the business. As to the main advantages and disadvantages of rail, let me cover the advantages first. We believe that it is cost effective, particularly over distances of more than 350 kilometres and we believe that at that point rail, providing that we have a full train—and I will come back to that in a moment—is the mode that we would prefer. That said, there are significant issues that affect that. The fact that we need a full train means that when we put freight on to an individual carriage and try and feed it through the national network, it just gets lost. We do not have traceability and it takes prohibitively long periods to get to the destination. So, we have decided that we need a full train. To that end, we have many full trains running in different directions throughout Europe. We believe the trains are easy to track inasmuch as we know where they are. If they are stuck, it is very difficult to get material from the train on to another mode of transport and, in that sense, it becomes an inhibitor. We are able to move the material at weekends and over holidays by rail and that is very important for us. We have a plant in Russia in St Petersburg and their calendar is not the same as our calendar; they work over our Christmas, so they will work through and have the Orthodox Christmas in the New Year. Also, we have a joint venture in Turkey in a company called Ford Otosan[3] who produce Transits and they of course have a Moslem calendar and, again, work through Christmas and Easter and times like that. So, rail is quite an advantage providing I can get the service that I need. Finally, we believe that it is more environmentally friendly than road transport and, as such, we would like to increase the amount of business that we do on rail. If we look at the disadvantages, there is one big disadvantage with rail and that is reliability. We cannot rely on the train being at the destination on time. If I may illustrate that. When I contract a truck driver or a truck company to deliver material to our plants, we need that material within a certain time period or we stop production. I can get a truck company to deliver on time on a 15 minute plus or minus time window and 92 per cent of the time those people are there. I did an analysis over the last three months, July to September, of the train service from Dagenham into Valencia. Thirty-nine per cent of the trains were late and, when I say late, they were more than four hours late, many of them were 24 hours late and some of them were 48 hours late. The major issue here is going through France. France is a very difficult area to move trains through. We have all sorts of issues there. In this time period, we had some technical issues that accounted for 14 per cent of the problems. This was heavy rain and flooding on the track. There were catenary problems with the power lines, we had some technical issues there, and we had a tunnel fire and a loco breakdown. Acts of God and weather were 10 per cent—this was mainly the flooding that I referred to earlier. Then we had strikes seven per cent of the time. As I speak, we are under threat of strike from Renfe, a Spanish company. Indeed, we had three of our trains cancelled due to strike action. The Spanish union of rail workers are protesting against the privatisation. We are going to have a one-day strike this week and probably further strikes coming. When that happens, I have to find road transport to fill in for the train or our suppliers do. Last week, we had to charter four aeroplanes to keep our plant in Valencia going otherwise we would have lost production and there is enormous cost involved in that. We had to move over 50 trucks into that supply chain. This is getting so common that we are getting good at it! However, it is something that we should not have to think about. I carry one day's additional inventory for everything going into Spain from the UK. Anything into Spain through France dependent on rail I must carry one day. It is not just the inventory carrying costs, it is the energy to move the material in and out of the warehouse. We have to build a warehouse; we have to keep that running; we have to put people in to run that warehouse. It is an enormous amount of cost that, quite frankly, is waste. So, in answer to your question, that is the way we see the situation on the first three questions.

Chairman: That is exceptionally helpful.

Q5 ***Baroness Cohen of Pimlico:*** We are enormously indebted to a customer talking to us because one can get a good deal of pious thought out of everybody else but a customer at the sharp end tells us what actually happens. Did I get it right that, despite all of this, 80 per cent of your goods and I do not mean your finished vehicles, the sub-assemblies and the other bits and pieces, are going by rail?

Mr James: Eight per cent travels by rail.

Mr Gurmin: Where we do have a full train right from Dagenham into Valencia, the vast majority of our freight goes on that train. We are currently running a train from Germany to Istanbul for our Turkish operation and I would think that probably 80 per cent of the inbound freight traffic is by train.

[3] Ford Otosan is a joint venture between Ford Motor Company and our Turkish partner, the Koc Group.

We have a route from Germany to Valencia daily. What I would like to do is expand rail to other areas of our business, other suppliers, smaller deconsolidation areas where I do not have the volume for a full train and that is the kicker. If I could put a full train on and I could track it, I could move more into rail. However, the reliability of individual wagons is certainly nothing we could live with in our organisation.

Q6 ***Baroness Cohen of Pimlico:*** The point I am after is which way is all this going? You would like to expand. It is the psychiatrist's question: what do you actually think is happening?
Mr Gurmin: Let me take that in two parts, if I may. We have just started the operation into Turkey and the rail has been an absolute boon for us in that, to run that supply train with trucks, the capacity of trucks that I would need is astronomical: it is in excess of 500 trucks moving up and down Europe moving that material. However, I still have a reliability issue and, just two weeks ago, our trains were stopped because there were rail works in Hungary and we were not notified. The trains came up to the rail works and they sat there. We had to back them out and we lost two days on our route which meant that we again had to put trucks on the road. We also had to move material by aircraft and all of the disruption that caused. I had to move my orders back in the factory because I have critical parts that I cannot actually get to the plant. I had to move orders forward and pull others back and that affects the customer. The customer does not get the vehicle on time which affects our business very much. So, potentially, it has great advantages but I do not think the industry has leverage in the advantages they have.

Q7 ***Chairman:*** Describe the route from Germany to Turkey; which countries does it go through? Germany, Austria . . .?
Mr James: Hungary, Romania, Bulgaria—six countries in total.

Q8 ***Lord Swinfen:*** And Greece?
Mr James: No. Romania, Bulgaria, Turkish border into Istanbul.

Q9 ***Chairman:*** Romania and Bulgaria are not in the Union. Does your company and the companies that you use to move these goods around face the same problems in each of these six countries or do they vary?
Mr Gurmin: It does vary. However, we have not had the same level of problems that we have going through France, for instance. The Hungarian issue was the first time that we have had a major issue. Bear in mind that we have been running this route starting about six months ago, so our experience is somewhat limited whereas we have been running routes into Valencia for many, many years.

Q10 ***Chairman:*** So, you face more difficulties going from the UK, through France to Spain after a six-year operation than you do from Germany to Turkey . . .
Mr Gurmin: Yes, going through six countries at the moment.

Q11 ***Lord Swinfen:*** Why?
Mr Gurmin: There are a number of areas of concern that we have. It is not exclusively France, let me say, but France tends to be the area of most concern. Lack of drivers is a problem. Lack of locomotives. Strikes are endemic and they can be by third parties not even rail workers—it can be farm workers or truck drivers. They can stick a truck across a track and we are finished. There is a whole miscellany of issues but they tend to be in the area of France. We do have, as I say, right now problems in Spain. They had a three-day strike last week. However, until recently, it was not a big problem in Spain.

Q12 ***Lord St John of Bletso:*** In fact, we have covered largely what I wanted to raise with you today, both in your written evidence and what you have told us today about reliability and inconsistency of railway performance, and you have singled out France and the SNCF. You mentioned that 8 per cent of your inbound freight is transported by rail and you also said that you would like to increase your rail freight business; the clear implication in your evidence is that you intend to maintain, if not even reduce, rail freight. My question is, what would need to happen to reverse the trend in the short and medium term?
Mr Gurmin: There are three things that I think are key to the longevity of the relationship. First of all, reliability is a given. As I explained, when I use a truck, I can get that truck to the facility in the time window of plus or minus 15 minutes and, by the way, I am not satisfied with 92 per cent turning up on time, I want closer to 98 per cent. That is what we are working towards. I have to get that reliability in my supply chain. Secondly, I would like to see harmonisation of the standard used in the industry. We have differences in rolling stock, voltage being used, pitch of the axles, we have gauge difference and height, a whole miscellany of the things that I think need to be standardised to the best in class level, not standardised to the lower level which would not help the industry at all. For example, in Britain, I cannot get two Focus C-MAX on a double-deck car transporter because the gauge allowable prohibits me from doing that. I can do it right through Europe but, in Britain, I have to go

with a C-MAX single deck on a flat-backed wagon. This makes it twice as expensive to transport and also, importantly, the availability of flat-backed wagons is not sufficient for the business that I have. So, I would like to see harmonisation and optimisation of many of those things. Axle weights need to be harmonised; I can take a higher axle weight on the continent that I can in Britain. Then, train lengths need to be harmonised. There are many things that we need to optimise in the industry in order that we, as the customer, are satisfied. Finally and very importantly for me, cost transparency. We do not get cost transparency from the national rail companies. What we get is, "Here is an increase. Now, go away and pay us", to the point where they will walk away if we do not pay. We have sat down with our service provider and said, "Let us look at ways to offset the cost. Maybe we are doing things that are costing more money. Let us work together." We have a process called TVM[4] where we go through the cost base up. We expect people to make a profit, do not misunderstand me, but we expect to get transparency of cost and we cannot do that with the industry. Those are the things that I think are vital for the trend to change. Where we have no alternative, clearly we will continue to use rail and we are committed to rail. We have invested heavily in rail and many, many of our operations have spent a lot of money putting in the facilities required for rail.

Q13 ***Lord Geddes:*** How is your shopping list going to be achieved?
Mr Gurmin: I am hoping this Committee is going to help! We are also meeting with the Minister of Transport in France and also in Germany regularly where our biggest issues have been. Germany at the moment is not a problem. It was a considerable problem last year when the Rhine water level went down to 1.5 metres and all of the freight had to come off the Rhine on to rail and I could not get a train to move vehicles to our customers. So, I think the whole industry needs to work together to try and change it but I think it needs a dose of reality to some of the national providers that they are in the commercial world and people will find alternatives if the service is not provided. I hope that the service will be provided.
Mr James: May I just explain the reason why we could not get vehicles when the Rhine was at lower levels: it was that the rail company decided, of their own volition, to prioritise freight from other customers and again that is a typical action that we are seeing, this kind of almost whimsical nature in which the companies deal with our business.

[4] Team-based Value Management.

Q14 ***Chairman:*** If I am right, essentially you have three parts of a system: you have the companies you use to move things around, you have the rail companies, who may or may not be the same thing, and you have the rail track businesses.
Mr Gurmin: That is right.

Q15 ***Chairman:*** So, you face a fairly complicated picture since the people you deal with are actually one or two removed from where the real problems are. Do I have that right?
Mr Gurmin: Yes, you have.

Q16 ***Chairman:*** You said to the Committee that you would like them all, the industry, to realise the problem, get together and do something about it. Who were you talking about? Which part of the system? Have you any evidence at all across Europe and in this country that they, whoever "they" are, are taking the problem seriously?
Mr Gurmin: When I refer to "they", I am essentially talking about the service provided to our service providers, the national rail companies, the people who own traction and the rail network. I am sure that they are trying to improve. However, the evidence does not lead me to believe that we are making sufficient progress that would lead us to have a first-class rail service across Europe that can move freight in the timeframe that my industry needs and I would be looking for all parties to support improvement. We are trying, for our part, to work with the senior people in these organisations to motivate them to make the changes but they are faced with some difficulties, of which I am not an expert I have to say, and much of the evidence I am giving you is from my side of the table and I have to say from where I am standing right now that we are significantly concerned. However, we have no imminent plans to do anything drastically different from where we are today but we are always considering what the alternatives are for our company.

Q17 ***Chairman:*** In your evidence, you did actually say to us that the environment does not encourage you as a potential rail user to increase or even maintain the freight business.
Mr Gurmin: We did and that is in fact what we said. First of all, we would not increase our liability because right now at times it is an absolute liability and we would obviously look at areas where, if we were to continue to get service of this nature, we would have to consider our options. Just take last week where I had five trains planned to go into Dagenham from Valencia and from Dagenham to Valencia, so 10 trains in all, and I had to cancel six.

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Q18 ***Chairman:*** Why?
Mr Gurmin: Because of the strike in Spain, the Renfe strike. I had to then move all of that material by road whether I wanted to or not. As I said, I also had to charter planes to keep the plants running. If that sort of service were to continue, clearly no manufacturer could live with that sort of service level. I am faced with a one-day strike this week and next week the threat of a strike and so on. At this time, it is Renfe and I had the same problem with French rail. It is almost easier to tell you when we do not have a problem in France with industrial action than when we do.

Q19 ***Lord Swinfen:*** Assuming for the moment that you have no problem such as strikes or flooding, are your trains fitted into the normal rolling programme or programme of trains running through the various countries at regular times with no problems, or do you just have to take pot luck?
Mr Gurmin: No. We have what we call slots. We have a regular timetable when a train would leave and arrival times and we take that out for a five or six day period.

Q20 ***Lord Swinfen:*** But you cannot book it for a year in advance?
Mr Gurmin: We tend to book it in advance and we would lock that in. If one train becomes blocked in some part of France or in some other part of Europe we have to wait. In Germany we have the same issue with regard to timing. At that point the train sits. That train has to get there and get back before I can fill it again, so clearly when you get a delay that delays the whole pipeline.

Q21 ***Baroness Eccles of Moulton:*** You have already answered part of the question which was about inter-operability and you talked about harmonisation of the infrastructure. Can you see a big benefit to be derived from the through operations for locomotives and drivers, which is probably an easier solution than rebuilding bridges and changing access specifications?
Mr Gurmin: Yes, I can see a definite advantage because we are often delayed because a driver is not available, and what we would like to see is the same organisation taking the material from start to finish and not a hand-off. We have at least a hand-off at every international border but at times we have got it regionally. Then you have a regional problem and we get caught in a region, so that would definitely help and we would very much encourage that. The flexibility that would give me would be improved, and although I accept that we are going to have a four-hour time window, I would like the train to arrive at a given hour. That is what we would be working towards but right now I am looking at four hours. If it arrives three and a half hours late we consider it on time.

Q22 ***Baroness Eccles of Moulton:*** What do you think about introducing a policy so that the quality conditions were met and there would be heavy fines imposed if they were not?
Mr Gurmin: We do have with some of our providers (not rail providers) monetary compensation. First of all, it is extremely difficult to get. It is very difficult to prove who is absolutely responsible. The compensation never even starts to cover our costs because I may have to lay off a factory with 6,000 people in it because I have not got the material. That is what happens when the material does not get there, our organisation has to send up to 6,000 people home. When we build vehicles, with all the costs involved, it pales into insignificance in terms of compensation. However, if it drives the right behaviour and improves the service that would be very welcome.

Q23 ***Baroness Eccles of Moulton:*** Do you think that if it became a directive, and therefore became law, it would sharpen up the way the service operates?
Mr Gurmin: I think it would motivate them very much.

Q24 ***Chairman:*** You said in answer to Baroness Eccles that there were problems even regionally in handovers. In which countries do you have regional problems?
Mr Gurmin: We have had problems in France on a regional basis.

Q25 ***Lord Geddes:*** Just for the record, you did say that one truck driver could take a truck from Dagenham to Valencia without any changes?
Mr Gurmin: He can and does but he has to stop in line with the legislation.

Q26 ***Lord Geddes:*** He has regulation hours but it is the same person?
Mr Gurmin: All over Europe I have truck drivers routinely going down to Turkey. Daily they go down to Turkey right through all of those countries without a problem. Anywhere in Europe I can take a truck without a problem.

Q27 ***Lord Haskel:*** Has this led you to think that you should employ your own train drivers or staff on the trains?
Mr Gurmin: I am sure if you asked our service providers they would love to do that; they would be delighted to do it, and we would support that. As a matter of interest we do have loco drivers in our organisation but they obviously just stay local to our facilities. Logistics are not our core business.

Making motor cars is our core business and that is why we go and give this contract to service providers who are the experts in the field and who spend a lot more time on these matters than we can.

Q28 ***Lord Haskel:*** Finally, coming to the point about Great Britain, maybe you could tell us what you perceive to be the most important problems regarding increasing rail freight to and from Great Britain. You have told us some of the problems with low loaders here. Is there anything the British Government could do to help you overcome these problems?
Mr Gurmin: We would like to see some freight corridors that would accommodate the extra height I have referred to. We would like to look at the speed of the trains and try and harmonise that more in keeping with the speed we can move at on the continent. We would like to look at axle weights. Right now it is capped at 1,200 tonnes. We believe that should be higher. To give you an example, when I run a train to Valencia out of Britain, in terms of the axle weight, it is at maximum. However, instead of having 44 wagons (maximum length) it generally has 38, so I could get six more wagons on a train and that would help. We want better knowledge of the planned rail maintenance work so that we can accommodate it better. That is probably a minor point. The preceding three points are the most important for us from a cost point of view.

Q29 ***Lord Haskel:*** What about the Channel Tunnel?
Mr Gurmin: As I said, we were the first commercial organisation to use the Channel Tunnel and we have used it extensively. We have had some significant issues with the Channel Tunnel, particularly when it was being invaded by illegal immigrants. We had many days when I could not tell whether I could get a train through or not, and certainly for two weeks I did not get any freight trains through there and that was a major issue for us. We run ships three times a day from our facility in Dagenham to Flushing in Holland where we move an awful lot of our freight. If the rail tunnel was more competitive we would look at moving some of that through it, but at the moment it is not competitive with our ships.
Baroness Cohen of Pimlico: It is perhaps rather a hard thing to ask you, Mr Gurmin, but I have a great need to know this. If we could get some of these local problems sorted out how much more of your business would go that way? I do not necessarily need an answer now. I just wondered if there was any broad brush answer to that because it is quite a key piece of information: how great is the prize for which you are playing? At the moment we see the rail freight business going slightly backwards because it is all so difficult and this is not an impression you can change for us. Not only what would it take to move it forward, which I think you have answered, but how much of your business could actually go that way? I see that not all of it can. You have made the point that you cannot have vehicles standing around, and I see that not all of your business could move by rail but how much more by any number you care to produce—percentage, value, whatever—could move by rail? I would like a number for what value does move anyway and what order of percentage increase there might be. We would be happy to take this in writing, I am sure.

Q30 ***Chairman:*** If you are not prepared for an answer out of the blue you must write to us, but if you have an answer please give it to us now.
Mr Gurmin: We spend on rail €310 million a year and that represents 8 per cent of our inbound material and 33 per cent of our vehicle delivery. We would like to put more vehicles on rail. We run regularly from Cologne into Italy and the problem I have is that I cannot get the capacity I need to move any more down to Italy and I end up moving the vehicles north to a Channel port and then taking them by ship all the way down to Italy. All of that would go immediately if I had more capacity. For a breakthrough—and that is what we would be looking for and everybody should be looking for—you have to get into mixed trains. If I go with a single train, wherever I go I have to have sufficient material or vehicles to fill a whole train. If I had the reliability of mixed trains then we would move into a paradigm shift where we could make a significant difference but the service is so poor that it would take a considerable change in that service and traffic to allow me to do that.
Lord Swinfen: Would you like to go back to the system in the war where freight had priority over passenger trains?

Q31 ***Chairman:*** I do not think that will be in any party manifesto.
Mr Gurmin: We would like to.
Chairman: Do not even follow that because I promise you no major party would put that into a manifesto. We have not touched on that, and I hope we will with the next witnesses, this whole problem of passengers versus movement of freight. It is a serious issue, but we have not got the time.

Q32 ***Lord Fearn:*** It seems a gloomy picture all round. Do you perceive with the greater degree of liberalisation for the rail freight market in some countries there are benefits? So far what can you cite

as good customer practice and are they pleased or not?
Mr Gurmin: I am delighted to say that the best service we get is from the UK and within the UK. We do get a lot fewer problems within the UK. We are moving the material short distances but we tend to have good service from EWS in the UK. Then I would say Deutsche Bahn is probably the next best service we get and then you fall into Renfe and SNCF. That tends to be how we would see it as a customer. If you are saying to me, "Can you give me some data on that?", I would need to take that away. What comes across my desk are the failures, "This train is not going to happen and, by the way, can you spend €30,000 for an air freight?", which is what you have to do every time you move a bunch of material by plane.

Q33 ***Lord Fearn:*** In the majority are the customers not pleased with your service even though it is not your fault?
Mr Gurmin: I have to say that we stop our factories a lot less for parts than we have ever done and we work hard on that, but we have to spend an awful lot of money on premium freight to prevent us stopping factories. We do stop a factory from time to time because of freight issues but we try to put in contingency plans. As I said earlier, because of the issues we have previously had we have got some pretty robust contingency plans now but even with the best contingency plans, when you have, as we did last week, the threat of a truck strike in Spain and a rail strike coming together, we are probably going to have a stoppage. On the whole I would say that our customers are pleased. The production management in our plant, where these trains are due in, are very critical when they are late and very demanding, and on a couple of occasions they have to come to me and said, "For goodness' sake get this moved across to road", and when I explain why we would not do that it is an understandable reaction when you have got a whole factory stopped for parts.

Q34 ***Lord Fearn:*** You said that truck drivers sometimes go all the way through whereas freight train drivers did not.
Mr Gurmin: No, sorry. If I said that it is not correct. Truck drivers go all the way through. Train drivers change at each national border.

Q35 ***Lord Fearn:*** Where do they get their safety training from? In the various countries?
Mr Gurmin: Yes, I believe that is the case but it is no more difficult driving a train than driving a truck and we manage to drive a truck through all our borders without an issue.
Chairman: Unfortunately this train has to stop. Can I thank you genuinely and warmly for your evidence today. You have been extremely helpful. As for your written evidence, it was forthright and to the point and we are in your debt. Thank you.

Memorandum by Transportes Ferroviarios Especiales S.A. (Transfesa)

1. *What are the current barriers to entry in the international rail freight market?*

The main problem of transporting goods by rail in Europe is the lack of reliability of trains arriving for loading and unloading, instrumental in the progressive loss of its market share (an average of 7 per cent across the 15 EU member countries in 2003). Public enterprises give preference to passenger transport which, when delayed or lacking traction, leads to goods trains being stopped or engines transferred to passenger transport, causing the goods train to lose its next connection and time slots in the subsequent zone, thus accumulating delays throughout its route.

The main barrier to the entry of other traction companies is the failure to apply Community Directives in some of the countries with the largest rail networks, mainly in south-west Europe. Today, it is in some cases impossible, and in others extremely difficult, for public or private operating companies to provide traction for international goods traffic using their own locomotives from origin to destination, passing through different countries.

Other barriers are:

The difficulty of obtaining an Operator's Licence in some countries.

The even greater difficulty of obtaining the Safety Certificate, the conditions which must be met by the operator in some countries possibly becoming a political and arbitrary barrier, making rail liberalisation more difficult and slower.

Unfair competition by the public operators with a dominant position, and the difficulty of demonstrating this in accounts which include international and national goods and passenger transport.

The lack of analytical accounting to establish the costs of track for goods and those generated by passenger transport, making it impossible for managers to calculate with the required precision the profits or losses generated to it by each of the markets, passengers and goods, (the International Union of Private Wagons (UIP) has made a study of the costs of a track for goods, called COFRAIL).

The lack of independence of the referee, in some countries reporting to the Ministry of Transport and not to the body regulating competition.

Failure to completely separate the track manager and the public manager providing the transport, in some countries with an extensive rail network, such as France and Germany.

The lack of a supranational track manager so that, as things stand, operators are forced to deal with too many track managers, whose conditions and demands vary.

The technical demands which must be met by goods trains in order to run on the same lines as passenger trains are imposed by the latter, so that operators must compose trains no more than 800 metres long, not exceeding 20 metric tons per axle (22.5 metric tons on certain routes), running at set speeds between 100 and 120 km per hour. All limitations which make the transport more costly and not competitive with other modes.

Safety demands on rail deserve special mention as they are too high for the slower goods trains as they are established according to passenger requirements. This extra cost has to be absorbed by the latter service (safety requirements on rail are far superior than roads where 50,000 people die in accidents every year in the EU of 15 countries).

2. *To what extent are these barriers a result of a failure fully to implement exisiting EU Directives in all Member States?*

Rail's recovery will only be possible if the public enterprises are faced with healthy competition, forcing an essential change to their managerial strategy. At that point, goods transport will no longer be discriminated against and the service can become reliable.

Goods transport within the current technical and operational conditions is profitable in most cases, while passenger transport is not. A liberalised market will give priority to profitable transport, thus respecting the slots and traction of goods trains, even though they are slower, longer, and heavier to move.

Current barriers are a consequence of the failure to apply the Community Directives in all countries. For the provision of international traffic traction, all countries must adapt their domestic legislation to the Directives.

3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

The failure to liberalise a major sector like rail transport prevents improvements to competitiveness in European industry and reductions in external costs, caused by the current modal distribution. Failure to transfer Community Directives to member countries' legislation should be penalised in the same way as failure to comply with budgetary discipline. In creating obstacles to liberalisation, they are causing loss to the whole of European industry, and so must be heavily fined. This is not the time to merely reprimand rail, and heavy fines can be used to cover part of these external costs created by the present situation (in the EU of 15 member countries, external costs represent more than 700 billion euros, 8 per cent of the Zone's GDP).

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

The current legislation developed by the European Commission with the Rail Directives and the Railway Packages is enough to transform European rail, attain reliability in goods services and reach a market share for this category of transport which must not be less than 20 per cent.

In the Third Railway Package, the periods established for the liberalisation of internal goods and passenger transport must be reduced, if still possible. Rail's current market shares are 6 per cent in passengers and 7 per cent in goods. This means that in passengers, if dedicated high-speed line and city commuter services are excluded, the market share in the rest of the services does not amount to 2 per cent, making rail a marginal form of transport, with nothing to lose if the deadlines established for liberalisation are shortened, but which may succeed in saving itself.

This Third Package should give the European Rail Agency more power, and the responsibility to begin to manage some continental rail trunks which are important to goods transport.

It is important to force the elimination of subsidies to the public operators as soon as possible and ensure that only those authorised in the Directives are applied. In this way, the public companies would quickly begin to convert to efficient and profitable enterprises. There would be an end to the unfair competition, which today makes it so difficult for private operators to appear in countries where national legislation has been adapted to the European provisions.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

It must back United Kingdom operators so that they are able, as soon as possible, to run in neighbouring countries with their own locomotives. Rail is more competitive at distances over 300 km, and in most cases they have to get to France to exceed those distances. It must participate in the formulation of financial claims for damages caused to UK companies not able to haul trains with their own engines in neighbouring countries due to the failure of that country to apply the Directives, once the term for mandatory compliance has begun.

Support must be given to the creation of a rail network preferentially or exclusively for goods transport, to avoid the difficulty of managing lightweight and increasingly fast passenger trains with heavy, long and slow goods trains. Goods can be transported on track and with security and signalling systems which are far cheaper than those for passengers, so that separation would produce quality and profitability for goods service, making this line profitable on reaching the volume sought to secure that average share of at least 20 per cent in the Europe of the fifteen.

TRANSFESA

Transfesa is one of Europe's largest rail operators with 61 years of experience in moving goods by rail throughout European countries, hiring the traction from the different public operators. The headquarters are in Madrid, Spain. The company owns a fleet of 7,845 wagons with interchangeable axles that provide the capability of shipping international consignments throughout the different rail gauges and of which 1,000 comply with British rail gauge transit specifications. Transfesa also owns and operates a fleet of 243 general cargo trucks, 98 car carrier trucks, 2,115 swapbodies, manages multi-modal terminal operations at various locations in Europe and operates two axle changing stations for rail traffic operating between Spain and France. All services are monitored by a state of the art IT system that allows on-line consignment tracking.

This evidence is submitted on a corporate basis.

Emilio Fernández Fernández
Chairman and Executive Director

30 August 2004

Examination of Witnesses

Witnesses: MR EMILIO FERNÁNDEZ FERNÁNDEZ, Chairman and Managing Director, Transportes Ferroviarios Especiales, S.A. (Transfesa) Madrid, and MR OSCAR VERDÚ, Manager of Transfesa Benelux S.P.R.L., Brussels, examined.

Q36 ***Chairman:*** Good afternoon, Mr Fernández and Mr Verdú. Can I on behalf of the Sub-Committee give you a very warm welcome. We are extremely grateful to you for travelling to meet us today. We are also grateful to you for your written evidence. As with the previous witnesses, it was to the point and extremely helpful. We aim to close this session by six o'clock. As always, our time with you is too short. Is there anything you would like to say by way of introduction before we get into the questions?

Mr Fernández: My Lord Chairman, thank you very much for inviting us to come and have this opportunity to help you and to try to clarify what the problem is with the railways regarding freight transport in this continent. I hope my English is good enough for you to understand what I have to say. Perhaps you know something about our company. We have been working with rail for 61 years. Today 75 per cent of our business is done by rail. We own our wagons and have subsidiaries in the main European countries. We have 1,400 people dedicated to logistics and transport, so we believe that we have great experience regarding rail. We have an annual turnover of €300 million and we transport about 305,000 consignments every year and, as I have said, 75 per cent of that is by rail. 40 per cent of our business is done in dedicated block trains with timetables paid for in advance.

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Q37 ***Lord Geddes:*** Mr Fernández, I was delighted that both you and Mr Verdú were sitting listening to the previous evidence because you have already, I hope, got a flavour of the sorts of questions we have. May I start with a very simple one. What sort of companies use your services and who do you use to carry out whatever it is you are asked to do?
Mr Fernández: More than 80 per cent of the business is done for the automobile makers. Half of that business is components and half is fully assembled automobiles. We have focused on the automobile sector, not because it is our business strategy, but because we are working on rail; to work on rail you have to make things easy and the automobile sector is able to provide both regular and large amounts of load, therefore, for railway companies it is easier to provide the traction.

Q38 ***Lord Geddes:*** Do you have long-term contracts?
Mr Fernández: Not really. For components we sometimes manage to sign contracts for up to three years. For assembled cars we do not have any contract. We have to go into the market and compete with road and ships, customers do not have any obligation nor contract. We have to buy the traction from the traction companies, we buy the use of the track and the traction, to move our wagons and provide the service to our customers.

Q39 ***Lord Geddes:*** You have no contract at all?
Mr Fernández: Not at all.

Q40 ***Lord Geddes:*** It is all on what I call a day-to-basis or a week-to-week basis?
Mr Fernández: In components we do not because we work with the car makers for a long time to study their service before we start the transport. We had to decide the value for this and we had to invest quite a lot of money to provide the service. Usually in this business you have to invest one euro per euro of turnover because the rotation of wagons is not high. In these cases we sometimes manage to sign contracts for three years. In the rest of the business we can lose the customer from one day to the other and, in fact, when there is no service we lose the customers and our wagons are laid off doing nothing. In such cases we lose all the turnover and the customers go to an alternative mode of transport.

Q41 ***Lord Geddes:*** As I understand it you have your own wagons. Do you have your own locomotives and drivers?
Mr Fernández: No.

Q42 ***Lord Geddes:*** Who do you use?
Mr Fernández: We use the state companies, the state railroads. Here in the UK we use EWS. In France we use SNCF, in Germany we use Railion, in Spain we use Renfe and in Italy we use the Italian railway.

Q43 ***Lord Geddes:*** It may be an obvious question, but would you like to see competition?
Mr Fernández: Absolutely. We are absolutely sure that unless competition arises rail will be dead in a few years because, as you know, already the market share of rail in Europe does not reach 7 per cent. In Spain it is lower than 4 per cent. It is a big problem.

Q44 ***Lord Swinfen:*** When your trains cross international borders we have already heard that drivers have to change. Do you have to change the locomotives as well?
Mr Fernández: Every day we have 20 regular trains from origin to destination, full trains. We pay for them whether we fill them or not. These trains, when they cross France, become 120 trains. Trains change drivers and locomotives at every border but also do so inside their countries. To cross France a train has to change driver six times and the locomotive four times in the region's limits.

Q45 ***Chairman:*** Why do they have to change?
Mr Fernández: It is the way the railway is managed because in France the authority is in the hands of the managers of individual regions. They have their own means of traction and drivers which take the engine to the next province, they do not go further. In fact, we know that SNCF has been trying to change the system to make drivers and locomotives run longer, 300 kilometres instead of 200 or 250. They have not yet managed to succeed. The trade unions want to stay with this system. Apparently they live very well in little villages and to drive longer they have to move to big cities. This is why they have reliability problems. If a train arrives late at the next destination it loses the path and, because they give preference to passengers, if we lose the path, to find another path for our trains may take three, four or even up to 24 hours. This is why we arrive late on too many occasions.

Q46 ***Chairman:*** So do you have a contract with your wagons? You have a contract with each of these state monopolies to move these wagons through a country?
Mr Fernández: Yes.

Q47 ***Chairman:*** So if they do not achieve the contracted time is there a penalty clause in these contracts?

Mr Fernández: No, there is no such clause. Some years there were big strikes for a long period of time. For instance, in the case of Ford, it is a company that, as you have heard, has been dedicated to rail for many years. Because of the lack of reliability in the last two years they asked to transfer the mode of some of their shipments, to give them the service by any means, so if there is no rail service we have got to transport the freight by road or by air and we have to pay the difference. When there are strikes, we have to do that. We have to make a complete service offer to Ford by any means of transport to guarantee the quality; if more than 20 per cent of the service is done by road, because rail is not doing it, we start to lose money. In cases where SNCF have strikes for a long period they provide some compensation, but the compensation is very small, it is far less than the money that we, and the customer, lost. They do not compensate the losses at all. This is a small compensation; that is it.

Q48 ***Baroness Cohen of Pimlico:*** I have a quite specific question about competition. As I understand your evidence you have a kind of internal competition because if the railway stops you can put it on a truck; in fact, you are responsible for putting Ford's goods on trucks or into aeroplanes, but you have no choice at all about rail modes. Do you have to use the national rail service.
Mr Fernández: Yes. I think liberalisation has developed a little bit in the north of Europe but in France there was absolutely nothing; in Spain nothing. In Italy there are some private traction companies. In fact, two of them I believe are already working but the competition is still not very strong. Most of our business is between the Iberian Peninsula and the rest of Europe, where competition is non-existent.

Q49 ***Chairman:*** Non-existent in France and Germany, are you saying?
Mr Fernández: In France and Spain, in Germany and the north countries there is some competition.

Q50 ***Baroness Cohen of Pimlico:*** I was particularly interested in your view expressed in the evidence that the rail freight market was shrinking because it seems to me that you would know. Do you have many competitors? Are there many other people also contracting with the likes of Ford?
Mr Fernández: Yes, there are companies like Transfesa in Europe, but most of the private companies in Europe are renting wagons. They are not selling the service. They are renting the wagons to big customers and the customers deal with the public operators.

Q51 ***Baroness Cohen of Pimlico:*** So you are probably one of the very few what we call soup-to-nuts providers?
Mr Fernández: Yes.

Q52 ***Baroness Cohen of Pimlico:*** Has your own business shrunk or do you see this as solely the market?
Mr Fernández: We are growing 2, 3 per cent every year, very little, and we are growing on road. As I said before, now 25 per cent of our business is on road because rail is going down and it has been going down since 2000. In 2000, unfortunately, SNCF started to give the highest speed service from Paris to Marseilles, they thought that with a dedicated line for the high speed service the existing lines would be free for freight, but the result was to the contrary. It made congestion in the local lines in that area, and now to cross the south of France is a very difficult task. Even now if you go and ask SNCF to give you a path for a new train you might not get it. It is completely congested because of the high speed service and the commuter trains that are going from the local areas to the high speed stations.
Baroness Cohen of Pimlico: Yes; I think we have got something like that with the airport trains. They have also resulted in local congestion.

Q53 ***Lord Walpole:*** I was going to ask you what you see as the main advantages and disadvantages of the use of rail but it seems to me that you do not see any enormous advantages unless things go better. Is that right?
Mr Fernández: Yes, that is right, but I think the railway provides more advantages to transport goods than the road. I think the railway is cheaper than road, and also the railway allows you to send trailers long distances without sending the drivers. Today in Europe drivers still drive 3,000 kilometres, 2,500 kilometres. This is very expensive and is not good for the drivers. The quality of life of these people is poor. Drivers should drive 200 or 300 kilometres and they should sleep in their own bed almost every day. They can do that if they combine with rail. Rail is cheaper and also rail produces much less external costs than road. It is about €88 per tonne per thousand kilometres, while rail is producing only €19. This continent could save a lot of money in external costs by using rail. I think that rail has a big advantage there.

Q54 ***Lord Walpole:*** Presumably you think as we do that the price of oil will go up considerably?
Mr Fernández: Absolutely. It is already creating a lot of problems for road companies. Many road companies in this continent are losing money because the costs are going up and productivity is going down due to congestion. They cannot do as many

kilometres as they used to do. As you know, a road company, to be profitable, has to run at least 170,000 kilometres a year by lorry and sometimes this is difficult because of congestion. I believe that there are some areas in Germany where a lorry needs six hours to go 200 kilometres because of congestion, so this is creating problems in the profit and loss account of the road companies.

Q55 ***Chairman:*** But despite that road movement is increasing slightly and rail is decreasing?
Mr Fernández: Absolutely, because road is very competitive. When there is a very competitive market you have to discover new ways to do things to be profitable. Short sea shipping has already 42 per cent market share and is big enough for this continent, bearing in mind the kilometres of the sea shore, the ports and so on, so if rail is not giving reliability, industry has to go by road. There is no other alternative.

Q56 ***Baroness Eccles of Moulton:*** In your introduction you said that the automotive industry was attractive to you because you could make up full trains. Mr Gurmin, towards the end of his evidence, said that one of Ford's aspirations would be to be able to run more mixed trains and I wondered whether you had the same view, that being able to have mixed trains, as opposed to having to go for one use, would be helpful to you?
Mr Fernández: As I said, the problem of rail is reliability. If rail achieved reliability it would overcome the problems of serving different customers and types of freight on the same train. There are no problems to implement that. But in some countries you still cannot mix freight in trains because the tariff of the train is different depending on the freight you are carrying on it. We are still negotiating with SNCF to put cars and components on the same train but they refuse to allow us to do so because of the price policy. It is a completely artificial situation that is provoking a loss of productivity for rail. We are forced to work only with customers when they handle big volumes, to be able to fill a train. If they do not have that big volume, if they do not have the equivalent of at least 30 or 35 lorries, it is not possible to set up a service and they go by road, so for this reason we are losing a lot of opportunities for rail.

Q57 ***Baroness Eccles of Moulton:*** But the constraint is artificial rather than practical?
Mr Fernández: Absolutely artificial. There is no technical or economic reason for it.

Q58 ***Baroness Cohen of Pimlico:*** It sounds to me as if you are the person we need, in the sense that you must have in your company records or in your heads, very clear comparative costs on sending, say, a tonne of material by road, rail or air. We would find that very useful, if it were not a matter of commercial confidence, because it would get into our heads what the prize is if we carried more on to rail. Would it be possible for that to be provided outside this meeting?
Mr Fernández: Yes, I can do so. I would just like to say that one thing is the price and the other is the cost. The price is given by the road. The road is the leader, so anyone trying to compete with the road has to match the price of the road, so our prices to customers are always lower. Because the quality is lower, so the price is lower. When the price is higher because the cost of the railway is higher, we cannot do the business as we do not cover the cost. I can give you the cost of the road; that is no problem. I can also give you the cost of the rail, but no rail in this continent will agree with me about the cost because not even they know the cost. Until last week I was Chairman of the European Association of Private Owners and we made a study of the cost of the track, only the track. It is just a calculation to understand and know the cost of the track, because the track for freight is cheaper than the track for passengers; but we have not got any response yet, so the only study to date in this continent about the cost of the track for freight was done by private wagon owners. I can give you this information.

Q59 ***Lord St John of Bletso:*** Mr Fernández, we have covered a lot of ground today and, of course, one of the key issues has been the lack of reliability and of consistency. You mentioned that 75 per cent of your business is with rail freight; you gave a veiled threat that in the transportation of goods rail freight accounts for just 7 per cent and could possibly even collapse from that level. We have gone through issues in your evidence, such as loading and unloading; you mentioned the problems of state enterprises where passenger travelling takes precedence over goods freight, and the lack of competition and lack of transparency. One of the issues which I found very interesting in the evidence from Ford was the need for harmonisation and standards of performance. It was quite clear that there needs to be more harmonisation in order for us to see greater liberalisation of the freight market. How realistic is it for these problems to be resolved? Quite clearly, with the point that Lord Walpole made of escalating oil prices, who knows how much higher they are going to go? Personally, I think they are going to go down from these levels but even so this is a massive subject. The issue really is, what is the longevity, what is the sustainability of the rail freight market going forward unless these issues that have been raised today can be overcome?
Mr Fernández: In our organisation we are talking about interoperability. Many people have been working on making the European railway

interoperable, so any engine can go from one country to the other. This has to be done to implement liberalisation but I see that the people of the European Commission have been working hard on this issue and today this is not the problem. Transfesa in the eighties was sending to this country 250,000 tonnes of oranges and the railway was not interoperable, but the quality of the service was good. So the quality of the service has deteriorated because railways have focused on passengers and they were determined to compete with aeroplanes and buses. They have increased the speed of the rails. As soon as they increased the speed of the rails for passengers, they reduced the capacity of the line and the one thing that has been suffering from that is freight. Our trains moving components in this continent have to run at a speed of 120 kilometres per hour. To make two axle wagons able to run at 120 kilometres per hour is very expensive. It costs 40 per cent more than normal wagons and we spend 30 per cent more in maintenance on this, for nothing because we do not have any profit for that speed, we do not improve the service for customers. It is just because we have to live with the passengers. Unless we are able to go at a high speed we will not be able to have the path quality we are receiving. We will receive even worse quality. Interoperability is necessary to implement liberalisation but before that we believe that there should be political decisions. Somebody should decide to stop discriminating against freight in favour of passengers because, unless this is done, the benefit of liberalisation will not arrive in time to change this situation. As you know, liberalisation started in March last year. Very little has happened since then, and full liberalisation will not be reached until 2010. We believe that freight will not be able to support this situation for so many years. The problem is path allocation preference.

Q60 ***Lord Shutt of Greetland:*** We do have delays, Mr Fernández. I have had a delay today because of a late running train and therefore I have not had the benefit of hearing everything you have had to say. Following on what you have just said, I understand the preference for the passenger that has been referred to, but it seems to me, that from about seven o'clock in the evening till six in the morning there are not that many passengers moving around. There are some but there are very restricted services for 10 or 11 hours in the day. It was always thought that freight moved in the night—we used to have mail trains at one time. What is the position at night? Are you still having bother with the French and the Germans even with getting trains through during the night?
Mr Fernández: This was the case when the railways were moving internal traffic in their own countries and when the railways were running 400 kilometres or 500 kilometres. Now we are talking about our trains running an average of 2,000 kilometres, so if you leave at night in Spain you are in France in the morning and in Germany in the afternoon, so it is really difficult. We try to run at night but it is really difficult to organise freight trains at night everywhere. We have to go from Dagenham to Valencia, as was said before, in 48 hours, so in some countries we have to run during the day.

Q61 ***Lord Swinfen:*** Mr Fernández, you have already indicated that the greater degree of liberalisation of the rail freight market in some countries gives a better service to the customers. Would you like to expand on this and give us some examples?
Mr Fernández: One example is the United Kingdom. This country used to have a very small market share, even as small as Spain, 10 years ago, and now I believe the market share in this country has gone up to 10 per cent which is quite good. I believe that this was achievable, despite the size of the country, because you have to bear in mind that most of the industry is localised in the south of the country, so the average distance in this country is still small for rail. Therefore, even though rail has managed to reach that market share, imagine what could happen if EWS, for instance, was able to run its own trains and its own engines down to Milan or to Valencia. Again, rail is competitive over 300 or, even better, 500 kilometres. The main problem for the operators in this country is that they arrive in France and they have to leave the train in the hands of the French railways. Germany is also doing well. DB is giving a good service, much better than Renfe or SNCF, and is competing with other operators like Rail4Chem[5]. Rail4Chem is a profitable company and has been able to achieve a reasonable market share in the last three or four years. I think when liberalisation starts, public railways will start to be managed in a different way.

Q62 ***Lord Swinfen:*** We have been talking mainly so far of western Europe. What is the position with the newer nations coming into the EU?
Mr Fernández: These countries are still keeping up quite good market share. They came from 90 per cent 10 years ago. They still have 30 or 40 per cent. Of course the road has been winning market share in these countries but the aim of the Commission is to try to develop the railway there in order not to continue losing market share. Again, it depends on the liberalisation of these countries as well, if other operators are able to get into these countries railway will keep its strong position. Otherwise I believe the same might happen as in western Europe.

[5] German private traction company.

Q63 *Baroness Eccles of Moulton:* It is really a question of harmonisation and whether you can see that improvements to the interoperability to the international traffic would be benefited by that. You have talked about the benefits of not having these rather ridiculous-sounding restrictions on drivers but what about harmonising their length and axle weight—the harmonisation of the infrastructure?

Mr Fernández : It would be of great advantage to rail. To implement liberalisation for the rail network in Europe would be unwise. In fact, I think the European Rail Agency will do a good job in this field and should assume some responsibility for managing corridors that go from one country to another because this is the other problem. Even with liberalisation most of the operators will have to deal with different track operators, such as Network Rail in this country, DB Net in Germany, RFF in France and so on; having to deal with so many net managers is also a problem. There should be some kind of a European body able to manage the net on a continuing basis in order to be more efficient. The net should be harmonised with the same electric tension, the same length of trains, the same signalling system and so on. It should be managed in a unified way and not on a local basis, and the ERA[6] could do that.

Q64 *Baroness Eccles of Moulton:* In the Third Railway Package there is a Directive about maintaining standards and signing up to them through the contracts and then imposing penalties if they are not met. Do you think it can really be left to the market, and to competition as it arrives, to deal with that, or do you think there needs to be some compulsion?

Mr Fernández: We are in favour of this compulsory compensation scheme. I should distinguish two stages. In the short run we are in favour because anything that is done to improve the quality is very welcome but we also have to realise that compensation only will not solve the problem because the problem today lies in the way a railway is managed. I could say that some railways do not have an interest in freight. They have an accounting system under which they believe they lose money with freight. At the same time, they believe they earn money with passengers. They manage the passengers on dedicated lines because they have preference, according to their figures, so they earn money and they achieve a perfect service. On freight they lose money and they are blamed for everything, so they are not interested in freight. This is what should be changed. If a compensation scheme stimulates change, fair enough, but in the short run I do not think that only penalisation will solve the problem. In the long run, without a doubt, the compensation scheme should also be applied because even with a fully liberalised railway, the main railroads are going to have a predominant position and they can favour some against others. With a compensation scheme at least we should have some kind of guarantee that treatment is going to be the same for everybody.

Q65 *Chairman:* Given that passenger traffic is substantial on rail networks and no government is going to set its face against passenger traffic—indeed in France they have dedicated passenger lines as you say—one of your suggestions in your written evidence was that there should be more dedicated freight lines. I will ask you what in this country might be called the nuclear question, and that is, if it is such a good idea why is the market place not funding freight lines? In other words, if it is profitable, if it is simply not good accounting systems, why is the market place not funding dedicated freight lines?

Mr Fernández: First of all I would like to explain that state rail companies are efficient. They produce quality when they are working on dedicated lines. They do it at high speed; they do it for the commuters. This is why we are asking for dedicated lines because freight is completely different, for technical and economic reasons, from passengers. Passengers receive good quality because they run on dedicated lines, so freight should be successful if it is run on dedicated lines. Then we have to bear in mind that market share in passengers in this continent is 6 per cent. If we take out the passengers that are running on high speed trains and commuters, the rest of the passenger rail has only around 2 per cent market share, so it is not important. We really believe that the only business able to support the 180,000 kilometres of railway lines in this continent is freight. Spain, for instance, has initiated a strategy for transport by building a high speed net. From my point of view it is madness. It requires a large amount of money. The government is spending money investing in high speed lines to everywhere where there is no economic volume to support these lines so, at the same time, the government will be obliged to subsidise these high speed lines for ever. Passengers have other more economic and efficient ways to get around, by aeroplane or by bus. Freight unfortunately has not. This is something that decision makers in this continent have to realise in order to stop freight discrimination[7].

[6] European Rail Agency.

[7] Transfesa is participating in a consortium of European companies to develop the New Opera project, involving the setting up of 15,000km of a railway net solely dedicated to freight. The project was given the highest mark among the 11 presented to receive finance for the study under the 6th Framework Programme.

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Q66 ***Lord Geddes:*** Before I come to the last question I wanted to pick up an answer you gave to Baroness Eccles previously on interoperability. You were talking of an entity, a European body, to (my words, not yours) drive through common factors in axle weights or power or bridge heights or whatever it may be. How do you see that? Do you think private industry can do that? Would that have to come from Brussels? Would it be a political thing? What is your vision of that?
Mr Fernández: I was talking about the European Rail Agency. The role of the European Rail Agency is going to be to supervise and to orientate for technical reasons and nothing more. What I would say is that, perhaps, the European Rail Agency should assume responsibility for the management of certain corridors that are important for the movement of freight. This is my idea.

Q67 ***Lord Geddes:*** The question I was going to ask is the parochial one as to what your opinion is regarding the British rail freight system. How adequate or inadequate is it in your opinion and what should the Government (whatever Government it might be) be doing to make it better?
Mr Fernández: I believe that what has been done in this country is the envy of its neighbours. I think you have gone far because you have already liberalised and privatised the railway and I suppose this is the reason why the business of freight transport by rail in this country has improved. The only thing that you should do now is to try to help the private rail operators go to the neighbouring countries with their own locomotives. Otherwise this country is too small to make rail freight transport competitive and profitable. I think this country is doing a good job on this issue but to improve even further you should invest a little money to improve rail productivity. For example, wagons are too small in this country and some investment to increase the gauge in some corridors would improve the productivity. This has been done already in the line from the Channel Tunnel to London. Now European gauge wagons can come up to London, this could also be done up to Birmingham or even up to Liverpool, perhaps in one or two corridors to allow wagons with a bigger gauge to get there[8].

[8] Other decisions that would facilitate the management of the line both for freight and passengers would be the enlargement of rail sidings. Rail sidings of several kilometres would allow passenger trains to overtake freight trains without the latter having to stop completely: this would also allow much longer trains (only 750 metres long at present), therefore there would be an increase of productivity leading to a quicker return of the investment.

Q68 ***Chairman:*** Can I ask you what was not meant to be the last question but will be? How will the three railway Packages of EU legislation help to solve these problems? Do you believe yourself that there is a political will in key Member States to take the necessary steps to implement these Packages in the kind of time-scale you have been talking about, bearing in mind that the implication, as you have eloquently said, is highlighting a conflict between passenger and freight movement. Will there be a political will to tackle it and achieve real liberalisation?
Mr Fernández: I think the job that has been done by the Commission was good enough. I think that all the Packages and Directives are enough to implement liberalisation in this continent, but unfortunately local governments have done very little to implement them. This is the main problem. I think local governments should realise that they have to implement these Directives and these Packages as soon as possible. Again, I believe that now we are a little bit late because even if we speed up the implementation of the Directives and the Packages and if we speed up liberalisation, the effect of this liberalisation, to change the minds of the public companies in this continent, will take too long so there should be political decisions. For instance, if I am in one path with one engine and I am on time, and the passenger is late, my engine should not be taken from our freight train to the passenger train. At least we should achieve respect for the train timetables. For instance, this will be a big advantage because most of the delays to freight are caused by restrictions because a passenger train is late, so the freight train waits until the passenger train goes by and then loses the next connection and the next path. Let the freight trains run in their own paths at their own time at least. Otherwise, if we have to wait for liberalisation I am not very optimistic.
Chairman: On that note of realism I fear we must come to an end for this session. Can I thank you and your colleague very warmly indeed. You have come quite a way to see us. It is greatly appreciated and you have been very helpful to us. Thank you very much indeed.

Supplementary written evidence from Transportes Ferroviarios Especiales S.A. (Transfesa)

Costs for Freight Transportation

In the following paper we try to show that rail can be substantially more efficient than road under certain conditions, specially when efficiently managed. We are going to offer figures, some of them official and some of them based on our best estimates, for container/swap-body transportation by road and rail. Due to significant differences in cost-factors and prices between European countries, detailed figures will only be given for Spain and will not take into account the latest changes in petrol prices and its impact on transport costs.

Road Freight Transport

There are no official prices for these services, and due to the fierce competition between companies it is one of their best kept secrets. Nevertheless, price for clients is around 0.8 Euros per km for transporting a container or a swap-body.

In terms of costs, we have to make a distinction: costs over km charged or costs over total km.

- In order to compare with prices and calculate margins and profitability, costs should be calculated over km charged, and these vary significantly depending on truck productivity. Considering a hypothesis of 10 per cent empty returns, costs per charged km are 0.89 Euros if the truck does 100,000 km per year, and 0.73 Euros if the truck does 140,000 km per year. Break-even point is around 115,000 km per year.
- When we want to compare efficiency with other modes of transport, of which we don't know efficiency ratios, we should compare costs over total km. In this case, and with the same hypothesis, costs per total km are 0.80 Euros if the truck does 100,000 km per year, and 0.65 Euros if the truck does 140,000 km per year.

The following table summarises the data.

	Truck + semi-trailer (T)		*40*	*Truck + Semi-trailer (T)*		*40*
Hypothesis	*km pa*		*100,000*	*km pa*		*140,000*
	Per cent empty returns		*10 per cent*	*Per cent empty returns*		*10 per cent*
	Per cent	*Euros*	*Euros/km*	*Per cent*	*Euros*	*Euros/km*
Revenues per total km		72.000	0.72		100.800	0.72
Revenues per km charged		72.000	0.80		100.800	0.80
Direct costs		**79.772**	**0.80**		**91.476**	**0.65**
Fixed costs		50.511	0.51		50.511	0.36
Depreciation	8.7	9.099	0.09	9.9	9.099	0.06
Vehicle financing	0.9	978	0.01	1.1	978	0.01
Personnel costs	33.4	23.433	0.23	25.6	23.433	0.17
Insurance	6.8	5.751	0.06	6.3	5.751	0.04
Fiscal costs	1.1	760	0.01	0.8	760	0.01
Travel expenses	15.0	10.489	0.10	11.5	10.489	0.07
Variable costs		29.261	0.29		40.965	0.29
Fuel	25.5	21.445	0.21	32.8	30.023	0.21
Tyres	4.1	4.311	0.04	6.6	6.035	0.04
Maintenance	1.9	1.675	0.02	2.6	2.345	0.02
Repairs	2.6	1.830	0.02	2.8	2.562	0.02
Cost per total km—container or swap-body			0.80			0.65
Cost per km charged—container or swap-body			0.89			0.73

We enclose as a reference a comparison done by F&L (European Freight & Logistics Leaders Forum) in 1999, where road freight cost is analysed for different countries.

Cost price of freight trucking in Europe—4th quarter 1999 in Euros per km (40 tonne truck + semi-trailer—100,000 km pa)

	Standing cost		*Running cost*			*Total*			
Country	*Taxes & Insurance*	*Depreciation*	*Fuel*	*Tyres*	*Maintenance*	*Vehicle costs*	*Driver costs*	*Overhead costs*	*Total (Euros/km)*
Austria	0.12	0.18	0.21	0.04	0.08	0.63	0.41	0.17	1.21
Belgium/Luxembourg	0.08	0.19	0.21	0.04	0.10	0.62	0.40	0.17	1.19
Denmark	0.18	0.19	0.24	0.03	0.10	0.74	0.38	0.19	1.31
Finland	0.06	0.14	0.23	0.03	0.08	0.54	0.32	0.14	1.00
France	0.07	0.15	0.23	0.03	0.08	0.56	0.35	0.16	1.07
Germany	0.08	0.17	0.24	0.03	0.08	0.60	0.43	0.17	1.20
Greece	0.02	0.12	0.19	0.05	0.07	0.45	0.15	0.10	0.70
Ireland	0.13	0.13	0.22	0.05	0.11	0.64	0.30	0.16	1.10
Italy	0.15	0.16	0.25	0.04	0.08	0.68	0.32	0.17	1.17
Netherlands	0.04	0.16	0.23	0.04	0.09	0.56	0.39	0.16	1.11
Portugal	0.03	0.13	0.16	0.03	0.04	0.39	0.15	0.09	0.63
Spain	0.03	0.14	0.19	0.03	0.06	0.46	0.23	0.11	0.79
Sweden	0.06	0.16	0.25	0.05	0.12	0.64	0.35	0.17	1.16
United Kingdom	0.10	0.15	0.37	0.05	0.11	0.78	0.34	0.20	1.32
EU Average	0.10	0.16	0.23	0.04	0.09	0.59	0.32	0.15	1.07

Sources: Trade Associations and Local Hauliers.

Rail Freight Transport

In terms of prices we have taken RENFE official figures, where we can observe rail is cheaper than road for distances longer than 350 km (approx).

RENFE official prices

	Madrid-Valladolid	*Valencia-Barcelona*	*Madrid-Barcelona*
Approximate distance km	180	350	650
Price per container/swap-body Euros	220	250	390
Price per container/swap-body per km Euros/km	1.22	0.71	0.60

Regarding the costs, RENFE offers a figure for 2003 of 11.65 Euros per train and per km. When converted to costs per container/swap-body, taking average characteristics for trains which means 26 wagons, this amounts to 0.45 Euros per km per container/swap-body.

Train hypothesis

RENFE Train—kilometres	*000*	*24.876*
Length of average train	m	450
Average number of containers/swap-bodies	#	26

RENFE freight unit costs (before corporate cost distribution and extraordinary results)

		Total 2003	*Euros/Train/km*
Personnel	000 Euros	143.173	5.76
Energy and Materials	000 Euros	5.530	0.22
Transferred traction energy	000 Euros	33.211	1.34
External services	000 Euros	18.014	0.72
Transferred internal services	000 Euros	52.975	2.13
Depreciation	000 Euros	33.628	1.35
Financial costs	000 Euros	2.533	0.10
Other costs	000 Euros	836	0.03
Total costs	000 Euros	289.900	11.65
Train cost per km	Euros/train/km		11.65
Container/swap-body cost per km	Euros/km		0.45

If no other considerations are taken, such as service reliability, apparently rail is much more efficient than road: 0.45 vs 0.65–0.80 Euros per km per container/swap-body. Although the difference is big enough, this should be considered carefully, because there is no information about empty returns.

Besides RENFE figures we can analyse what should be the situation for a new rail freight operator. Our best estimates result in a total cost of 0.27 Euros per km per container/swap-body.

New operator best estimates		*Euros/Train/km*
Traction costs		5.54
Nine year locomotive renting	*1.67*	
Energy	*1.16*	
Maintenance	*0.78*	
Personnel costs	*0.83*	
SG&A costs (10% over revenues)	*0.55*	
Margin (10% over revenues)	*0.55*	
Infrastructure costs		1.50
Total costs		7.04

Train cost per km	*Euros/train/km*	*7.04*
Container/swap-body cost per km	*Euros/km*	*0.27*

In this case, difference with road is in a range of 0.38–0.53 Euros per km per container/swap-body (when compared to road costs of 0.65–0.80 Euros per km). Most of the time, this margin is enough to cover wagon costs, handling and manipulation, and movements by road at origin/destination.

Other Modes of Freight Transport

Although it is not comparable, because you only use an airplane when you have no other alternative (at least regarding goods moved by rail and road), we enclose two real examples we had:

— For an already programmed flight

Dagenham—Almusafes		
Londres—Valencia		
Length	2,000 km	
Weight	3.03 Tm	
Price	6,500 Euros (approx from 8,050 USD)	
Price per km	Euros/km	3.25

— For a charter flight (small plane)

Neath—Almusafes		
Londres—Valencia		
Length	2,000 km	
Weight	1.86 Tm	
Price	23,000 Euros	
Price per km	Euros/km	11.5

Sea transportation usually is complementary with rail and road and not comparable in terms of costs. In any case, we show you below some of the quotes we have got for some traffic—only sea freight and related costs included.

		Kiel—Germany St Petersburg—Russia	*Thamesport—UK St Petersburg—Russia*	*Valencia—Spain St Petersburg—Russia*
Approx Length	km	2,500	5,000	10,000
Price per container/swap-body	Euros	855	1,175	2,550
Price per container/swap-body per km	Euros/km	0.342	0.235	0.255

But sometimes, if the distance is not very big, eg Kiel-St Petersburg, rail can be cheaper if there is an efficient service between origin and destination: 0.27 Euros per km by rail vs 0.34 Euros per km by sea.

November 2004

MONDAY 18 OCTOBER 2004

Present		
Present	Fearn, L	Shutt of Greetland, L
	Geddes, L	Swinfen, L
	Haskel, L	Walpole, L
	St John of Bletso, L	Woolmer of Leeds, L (Chairman)

Memorandum by European Rail Freight Customers Platform

Introduction

The European Rail Freight Customers Platform (ERFCP) is the representative body of rail freight customers in Europe. Both directly and indirectly through other industry bodies, it represents probably about 90 per cent of the customers of rail freight. ERFCP was set up to provide a voice for the customer in the world of rail freight previously dominated by the suppliers, mainly the national railway bodies of Member States.

ERFCP's objective is to achieve the realisation of a reliable, cost-effective and efficient European rail system for transport of freight, able to meet the requirements of customers.

ERFCP works with European institutions, including the European Commission, the European Parliament and other bodies, including Member States' representatives, to seek to achieve these objectives.

Background

Demand for efficient freight movement continues to increase at a high rate. The EU Transport White Paper (2001) suggests that demand for freight in the EU will increase by nearly 40 per cent between 1998 and 2010, but a more recent report for the Union International des Chemins de Fer (UIC)[1] suggests that combined transport will increased by 135 per cent between 2002 and 2015. Combined transport is, of course, only part of the potential rail traffic, but it includes most non-bulk traffic to and from deep sea ports and much of the future international rail freight potential. This figure compares well with forecasts from other bodies which suggest that the year on year growth of container imports of 7 per cent per annum is likely to continue.

Thus, for customers to get their goods moved around Europe efficiently and effectively, reliable and cost effective rail freight services, in increasing volumes, are clearly essential, not least as road congestion gets even worse than it is today.

Until recently, services provided to customers by the national railways was often poor and unreliable with frequent strikes in some countries and, with a few exceptions, customers generally found that they had no alternative suppliers by rail. Furthermore, they found that rail service suppliers did not appear to realise that their main competition was with road transport, and that they were failing to match the service, reliability and prices which the road and logistics sector continued to offer and improve upon.

The results over many years has been a gradual reduction of rail freight's market share across Europe. One exception has been the UK, where rail freight volumes within the UK have increased by 50 per cent in the last eight years, largely due to privatisation of the train operators and the introduction of competition.

However, cross-Channel rail freight where there is not competition, has declined dramatically since the opening of the Channel Tunnel 10 years ago, to about 1.5 million tonnes a year, compared with a 1994 forecast of 6 to 8 million tonnes.

What is Needed for European Rail Freight to Succeed?

In Europe generally, customers have concluded that the only effective solution to the problems of service quality and price of rail freight is competition above tracks. The European Commission's open access Directives (2001/12 and 14) reached the same conclusion and, where this has occurred, for example in the UK, in parts of Germany and across the Brenner, rail freight volumes are increasing and customers are becoming more satisfied.

[1] Union Internationale des Chemins de Fer, Paris, Study on Infrastructure Capacity Reserves for Combined Transport by 2015, May 2004.

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Where this has not occurred, such as in France, many customers remain deeply dissatisfied with the inability of the state and the national railway to provide an acceptable service, or to allow competition above track and to set up a regime where the barriers to new entrants are not impossibly high.

For rail freight to succeed and grow, those customers who have the choice between using road and rail must have the confidence that their supplier(s), one or more train operators, are able to deliver. They are less concerned about who is to blame when things go wrong than with ensuring that some organisation is responsible for getting their goods from origin to destination.

This is not possible under the traditional arrangement whereby one national railway hands over a train at the frontier to another; rarely is there any prior notification of the arrival of a train. Nobody has overall responsibility for performance, or for putting things right when they go wrong.

In locations where there is the choice of more than one operator, one can find that some of the private operators have obtained operating and safety licences in several Member States, and can offer a terminal-to-terminal service, and take full responsibility for it, dealing with several infrastructure managers on the way.

Customers welcome this approach and in location where choice is available (parts of Germany and Netherlands, north south across Switzerland or the Brenner and, of course within the UK but not through the Channel Tunnel), more traffic is running and more reliably.

Infrastructure Capacity

For the infrastructure itself, there is of course no point in introducing competition, but there is an ongoing need to ensure that infrastructure managers (IMs) treat all their customers, the train operators, fairly and equally.

Many IMs argue that congestion on rail infrastructure will hamper rail freight growth. The European Council of Ministers of Transport Report on their 125th Round Table[2] argues that "the saturation of infrastructure was largely due to the inertia of the incumbent networks and their inability, for example, to change the safety and administrative procedures for freight convoys."

Responding to the Specific Questions Posed in the Inquiry

What are the current barriers to entry in the international rail freight market?

The current barriers to entry for freight train operators (FOCs) to enter the international market are high but they vary in different Member States. Generally, a new FOC must obtain an operating licence and safety certificate from each national authority of the Member State in which it wishes to operate. In addition, the operator must have traction that can operate in the Member State concerned; this means not only the correct electric traction voltage but also signalling systems for the countries or routes concerned, as well as drivers trained on these routes. This is also the conclusion of the ECMT Round Table Report.

In some Member States, one finds that only traction manufactured in that country is capable of being approved on technical grounds and, generally, new operators find that they cannot obtain second-hand equipment to reduce the cost of entry because this equipment is owned by the national railway and, even if not used, will not be sold to a potential competitor.

There may also be barriers in the shape of "not enough capacity", and this can of course be because the IM does not deal fairly between requests from its national operator and independent new entrant. Both these issues are covered in references 1 and 2 in some detail.

To what extent are these barriers a result of a failure to fully implement existing EU Directives in all Member States?

The above barriers to entry are principally the result of a failure of Member States to implement the open access Directives in a consistent and timely manner.

[2] European Conference of Ministers of Transport "*European Integration of rail freight transport, Round Table 125*, published 2004 by ECMT 2 Rue Andre Pascal, 75775 Paris Cedex 16, France; Page 104, paragraph 2.3)

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Some Member Sates, such as France, have fully implemented the Directives, but have failed to ensure that new entrants can overcome the technical and commercial hurdles summarised above. Germany has not yet implemented the Directives, but does allow competition among FOCs, but there are many examples of alleged abuse of monopoly position by the dominant national operator, and of collusion between DB Cargo and the infrastructure manager DB Netz in commercial negotiations that should remain confidential.

Other consequential changes required include the removal of border crossing delays. For some time now, a private sector operator was able to operate trains in Poland and Germany, but not across the frontier because the national railway argued that it had exclusive rights negotiated with the frontier control authorities to operate trains across the frontier. Similarly, the national operator claimed exclusive rights to operate the last kilometre into Hamburg port.

That is why it is so important that the open access Directives are implemented in respect of terminals so that, whoever owns or operates them, there is a legal obligation for the owner to allow any licensed operator to use them provided that there is sufficient capacity.

Is further action necessary at a European Union Member State national level to ensure enforcement of EU Directives?

For the reasons stated above, we believe that urgent action is necessary at both levels to ensure uniform and complete implementation of these Directives.

The Commission, along with Member States' governments, must grasp the problem of lack of enforcement and ensure urgent resolution on a consistent basis. Performance clauses as proposed in the Third Railway Package, may be a means to an end, but in themselves are a much less attractive solution than the availability of competition.

Is further European Union legislation necessary to make the policy of introducing competition into international rail freight effective?

We doubt whether further EU legislation to ensure the introduction of competition in international rail freight is necessary. The proposed third railways package which would include measures requiring all rail freight contracts between train operators and their customers to include performance clauses requiring the train operator to pay compensation in the event of delays. Whereas the intentions of this are laudable, by far the best solution is to ensure that there is real competition available between and in all Member States so that a customer can change operators if not satisfied with the services provided by one of them.

What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?

The UK Government has still not implemented the open access Directives, although it may argue that, since there is competition above rail already, there is not so much urgency. However, there is no on-rail competition through the Channel Tunnel, and the current charges for rail freight, a consequence of contracts signed between Eurotunnel and the then two nationalised railways, BR and SNCF, more than 20 years ago, are a continuing deterrent to growth, since they fail to reflect the current competitive market rates for cross-Channel freight by road, either by ferry or Eurotunnel's shuttle service.

Implementation of the Directives in the UK must enable rates for rail freight through the Tunnel to be competitive with other modes, and barriers to access, both technical and commercial, to any operator who wishes to run services through it must be removed.

Since the UK rail connection to the rest of Europe goes into France, where there are different but equally challenging difficulties for new entrants, the UK Government must also enter into serious negotiations with the French Government to ensure that their duties to promote the use of the Channel Tunnel for rail freight are delivered.

August 2004

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Examination of Witnesses

Witness: Lord Berkeley OBE, a Member of the House, Member of the Steering Committee, of the European Rail Freight Customers Platform, examined.

Q69 ***Chairman:*** Good afternoon, Lord Berkeley. Thank you very much for sparing the time this afternoon and also for the evidence that the European Rail Freight Customers Platform has produced for us. Is there anything you would like to say in advance, before we ask questions of you?
Lord Berkeley: Thank you, my Lord Chairman. Thank you for inviting me. I think I owe an apology on behalf of the Chairman of the European Rail Freight Customers Platform, Georges Di Lallo, who would have been very good as a witness because he also runs Arcelor, which is the biggest customer of SNCF in France. I will try and answer as best as I can on his behalf and on behalf of the rest of the Platform. I apologise for him not being here.

Q70 ***Lord Fearn:*** Lord Berkeley, what are the principal shortcomings in terms of price and quality of service of rail freight in Europe at the present time, and at the same time to what extent have the reforms of recent years alleviated these shortcomings?
Lord Berkeley: The real problem with rail freight, as you will have heard, is that rail freight is in competition with road freight, and sometimes waterborne freight; and in some countries rail freight remains the monopoly of a nationalised industry, with all the pretty poor service quality and sudden hikes in price that one has got used to over the years, not just in the railway industry but in many other industries. That is why, of course, it has been privatised in this country and has been very successful. The reform in recent years in Europe of course did include the open access regulations, which helped because people like SNCF were supposed to publish separate accounts for the train operation, for rail and the infrastructure—and in Germany and other countries—but it is nothing like enough. The open access Directives in 2001/12 & 14 have the potential for moving it forward. In the UK, since privatisation, certainly eight, nine or 10 years ago, rail freight volumes have gone up by 50 per cent. Equally important, market share between road and rail has gone up from 7 per cent to 11 per cent; so we have increased our market share. On the continent, figures are quite hard to come by but the best that can be said in most places on the continent is that the overall volumes have remained static, which means that the market share has effectively gone down because the total volume has gone up. This is looked at against the demand for movement of freight, which certainly out of China is expected to be an increase of over 10 per cent every year. The demand is going up! I heard this during our recent visit to Canada. It is quite frightening in some ways, and somehow the industry has got to cope with it. There have been some good new services in the UK. There have been good services in Germany, with the independent operators who have been able to start there. Italy is moving in that direction, especially down Italy, but in other countries—Spain, and France, which is key for UK and Spanish traffic to get to the Continent—France remains a serious problem. There is a great deal more to do.

Q71 ***Lord Fearn:*** In regard to Italy you used phraseology that meant they have gone ahead rather quickly. Have they?
Lord Berkeley: Ten years ago, if you sent a wagon to Italy, you did not expect to see it come back; it got lost in the system. Now they have split the passenger services from the infrastructure, and there are three freight companies working—not nationwide but they are working. They may be not truly private in our sense and may be owned by Swiss Railways or Austrian Railways or some other companies, but at least there is an element of competition. I think they have increased the traffic across the Brenner Pass, which has been a major bottleneck, very significantly, and this is a step in the right direction. Italy is still pretty chaotic when it comes to sending boxes or receiving boxes, as reflected by the service that some of the customers have got from within the UK to and from Italy. There have been endless delays and problems. This is probably because there is not yet the competition between Italy and France to the UK that there is on the other route. Italy-France is just one operator, and part of it is SNCF, so we have still got a problem there.

Q72 ***Lord Haskel:*** Lord Berkeley, the Minister of the Department of Transport recently said that in the Government's view the rail freight market within the European Union should be fully open access by 2007. Will it?
Lord Berkeley: That is a good question. The first thing is that international traffic in Europe means traffic between Member States; it does not mean outside the European Union, and that is the definition. Open access for international traffic should have already happened. I think the Minister was talking about domestic traffic within Member States. There should be open access now on international traffic, and I do not see very much of it. Domestically, as I said, there is open access in this country, and it is very successful. There is some in Germany and into Belgium and the Netherlands. There is nothing between Germany and France. Recently a private operator called Rail4Chem was to be awarded a contract by

Eléctricité de France, the French electricity generator that has a lot of power stations along the northern French frontier, to move coal from Rotterdam by rail; they won the contract from EDF, and I understand that the French Government said, "No; you will not get this contract; SNCF will." There is open access across the Brenner Pass, as I said, between Germany, Austria and Italy. The real problem is that there is no particular expectation it will all be there by 2007, although there will be progress in some countries. Until there is uniform progress across all Member States, 2007 will just be another step in the right direction—we hope!

Q73 ***Lord Haskel:*** What are the main obstacles standing in the way? You did say that you do not see this working.
Lord Berkeley: My Lords, there are lots of main obstacles. The first is implementation of the open access Directives 2001/12 & 14; secondly, making sure that the provisions of those open access Directives are translated into domestic legislation in a fair and proper manner; and, thirdly, enforcing the beastly things! There is no point in having lots of laws if you do not enforce them. It applies just as much around freight as anything else. France has implemented all these regulations, but, unfortunately, they have drafted the regulations for safety certificates in such a way that you have to be French to get a certificate; and even SNCF has had a certificate refused quite recently for a new service, even though it wrote the rules. Clearly, the rules need a bit of adjusting! Other countries have not implemented the Directives, like Germany, and neither have we for cross-Channel traffic. All these things need to be implemented, and then new operators must be helped to get started, because the barriers to entry are still huge and are different in each Member State. In regard to getting across the frontier—to give you a quick example—Rail4Chem, or one of the independent German companies, got a licence to operate in Germany and another one in Poland. It was not allowed to operate between Germany and Poland because DB Cargo had a monopoly of getting across the frontier—they have a little deal with the customs people. You frown, but I am afraid it is true. It has been resolved now. Ditto, getting in and out of the port of Hamburg. Until quite recently there has been a ransom strip, as you might call it; the last mile of the track into the port could only be operated by DB Cargo; so if Rail4Chem came in, the customer had to pay for DB to haul it the last kilometre into the port. That is thoroughly anti-competitive, in my view.

Q74 ***Lord Haskel:*** How do you enforce the last mile?
Lord Berkeley: It would normally be done in the first instance, I think, by the regulatory authority of the Member State concerned. If that did not work, the competition people in the European Commission should be doing it. I am very pleased to say that I had a meeting with one of the people involved from the Competition Directorate a couple of weeks ago, who did say that they were looking into all these issues, and would not hesitate to take action against companies or Member States that contravened it. Competition investigations do take some years, on the whole, but the more pressure that can be put on them and, as I have told my Platform colleagues, the more information we can give them of examples of where it goes wrong, is the only way that it is going to work. It is terribly important that that point is made to all the Member States. However, the Commission needs to indicate that it is not just creating new legislation all the time but making sure the existing legislation works properly.
Chairman: We are going to come to those very points in a moment.

Q75 ***Lord St John of Bletso:*** Lord Berkeley, in response to Lord Fearn's question you mentioned that volumes are going up and by that, obviously, demand will go up. We read in the ERFCP's response that demand for freight will increase by nearly 40 per cent between 1998 and 2010, and that there needs to be more reliable and cost-effective rail freight. Obviously, this goes on to the big question of more competition. In paragraph 15 of the written evidence you say: "For the infrastructure itself, there is of course no point in introducing competition, but there is an ongoing need to ensure that infrastructure managers (IMs) treat all their customers, the train operators, fairly and equally." Do you believe that complete separation of infrastructure from operations is necessary to achieve a competitive rail freight market throughout Europe? Would strong independent regulation suffice?
Lord Berkeley: First of all, can I make a point to amplify paragraph 15. I said there is no point in introducing competition, but of course between London and Italy there is competition: you either go via France and then straight to Italy, or you go through Switzerland and then you can avoid most of France. To that extent there is competition but, I think, that is not what the real question is about. The infrastructure managers have made a lot of progress in working together, so that when a train is about to arrive at the frontier, the next infrastructure manager knows it is coming. This is not rocket science, but it is not even commonplace yet; however, it is happening on occasions. You can now book a path all the way through, an infrastructure path from origin to destination, through one organisation; so to

that extent it is helping. I think you do need to have complete separation. The reason I say this is that there is separation here, and it works well. A year ago when we were in Germany with an all-party group, we met Rail4Chem and BASF, the big chemical company. They own part of Rail4Chem, an independent company, and they had recently wanted to put on an extra train through Rail4Chem from Ludwigshafen to Berlin, and so they asked Rail4Chem to apply to DB Netz, which is the infrastructure manager, for a pass. Two days later they got a call from DB Cargo, which is Rail4Chem's competitor, saying, "we hear you want to run another train to Berlin". In other words, if there had been a Chinese wall, it did not work at all. There is the big boy, who could easily kill the little fledglings in Germany, still saying, "we can under-price this". The chemical industry is so fed up with the German railway system that they encourage these smaller operators to develop. To me, there has to be total separation, but it has to be also coupled with strong independent regulation; you need them both. They are in the private sector, and there is money at stake, and any secrets put across like that would just drive the small operators away. We were told by the customer that Rail4Chem offered a 25 per cent reduction in price compared with DB Cargo and a much better quality of service. If we want rail freight to survive, these people have got to be encouraged to prosper, and therefore there has to be competition and therefore separation.

Q76 ***Lord St John of Bletso:*** How important therefore is it that rail freight customers have an independent rail freight regulator, and is existing European legislation adequate to achieve this throughout Europe?
Lord Berkeley: In theory, the regulation is adequate to achieve this, but again it comes back to how each Member State interprets and implements the European legislation as to whether it works. This is the problem. It may be that the Commission would have to come back in the future and say, "this is not working because each Member State is doing it in such a different way that there has to be a better commonality of structures, making them all work together". Perhaps it is early to say that, but I think this is something that should be flagged up for the future if things do not improve soon. There is no regulator in France to speak of. There is one in Germany, but I think they have just restructured and I do not know too much about it. Maybe it will get better—but it is something to watch. It should work, but we will see.

Q77 ***Lord Geddes:*** You have almost answered my question, Lord Berkeley—one regulator or 25?
Lord Berkeley: I am glad you did not say 27, because Malta and Cyprus do not have railways.

Q78 ***Lord Geddes:*** I was thinking it would be a bit a bit difficult to go across the water to Malta by rail!
Lord Berkeley: You are aware that they have asked for a seat on the board of the European Railway Agency, along with Cyprus.

Q79 ***Lord Geddes:*** Let us stick to 25 for now. Let us stick to the question, Lord Berkeley.
Lord Berkeley: Ideally, you would have one regulator throughout Europe. I look at the railway safety regulations that are coming in and it comes back to the question of a combination of political interference and political fear among Member States as well as the Commission. Are you going to get the highest common factor or the lowest common denominator? On railway safety, I have a fear which could run across to rail freight—although it is primarily rail passengers, I suppose, but rail freight has to comply—that they will make everything so safe that the safest railway will have no trains on it, which is not the objective. It has to be reasonably safe, with a risk analysis done in accordance with European rules. Our Regulator does an enormous amount in this country, and has been very helpful in getting into the detail. It has taken eight years to get this far, so if I am critical of some of the other Member States, who started a lot later, it is probably not surprising. I know that our Regulator does meet all the other Regulators, where they exist, for regular meetings. It would be nice to think that they could agree all these things without an enormous bureaucracy in Brussels, which is what I would be worried about. What I would like to see is commonality of rules and purpose. If that has to be achieved through the Commission, I think it is sad, but politics being what they are, it may be necessary for them to go back and re-visit it in more detail. There must be a bottom line below which you could not go at a European level, because freight just wants to run without all these constraints, some of which are totally passenger orientated.

Q80 ***Chairman:*** You touched yourself on the question of effectively implementing the existing single market legislation. You said that that is what the Commission should be concentrating on, and I assume you agree with that?
Lord Berkeley: Yes.

Q81 ***Chairman:*** Is the Commission actually vigorously implementing and monitoring existing legislation to the degree you would want?
Lord Berkeley: Of course, the Commission will say that it is down to Member States to implement the legislation which, in the way these things are written,

is probably true. I would like to see, first of all, the Commission pressing much harder on all the Member States. I know they have got infringement proceedings against a number of Member States for not implementing these Directives, but to go through the legal system will take years. There is a lot that they could do themselves through the Council of Ministers and through the European Parliament to raise these issues and ask what is happening. If that does not work, then they will have to propose yet more legislation which will go into more detail so that we have a common process and common more detailed legislation for implementing the open access regulations, which is not in the 3rd Railway Package—they have left that to one side and put other things in the package. It needs to move forward. The Commission's latest move has been to seek bids from a consultancy study to see how the implementation has taken place in different Member States. I do not know the details of it, but I heard about it a couple of months ago. It might be worth finding out, and if I hear any more I can certainly write to you. That is a start. Britain has the Presidency, starting next July. On transport, would it not be nice if rather than come up with many, many lovely new ideas, if our contribution was to get these things up and running consistently and comprehensively across all Member States? I know I am looking up in the sky, but it would be very nice, Lord Chairman.

Q82 ***Lord Geddes:*** Lord Berkeley, you and I go back a long way as far as Sub-Committee B is concerned, and I would like to put on record how grateful I was, and continue to be, for the terrific assistance you gave me during my Chairmanship in 1996–99. I valued it then, and I still value it today. In your reply to Lord Haskel you got quite a long way down what I call the abuse route, but I would like to tease out a bit more. You made an interesting comment subsequently about the ability now to be able to plan a route, or book a route. We have heard in previous evidence that that is great in theory, but dare I say it, certainly in one particular continental European country, they suddenly say, "sorry, but we have a train that is going to take priority over that, so you cannot do it after all". Can you expand on this whole question of the abuses that in your experience exist on the continent, or indeed in this country, if you know of any? I think I know the answer to my second question, but I would still like to hear it from you: you are obviously very keen on competition, but given the circumstances, what merit can you see of the introduction of the compulsory quality provisions into freight railway contracts, as suggested in the 3rd Rail Package?

Lord Berkeley: Thank you, Lord Geddes, for your kind remarks. I also enjoyed working with you and it is a privilege to be back here, on the other side of the fence, if I can put it that way.

Q83 ***Lord Geddes:*** The same side!

Lord Berkeley: The same side. Getting a train path across many Member States is of course key to running a decent service. It achieves what the customer wants, for the goods to get there quickly, on time, reliably and safely. To give you a recent example, there is a new service that has just started between Cologne and Istanbul, going through many Member States and other countries in between. In one trial they saved about 30 hours off the service, just by planning it properly and sorting out the frontiers and everything else. It demonstrated what can be done. In the open access environment there is a further step which is that if you are a big customer, in the UK, that customer can reserve a train path London to Glasgow while he puts together a package of bringing the road vehicle in and by whom, how it is going to transfer and when it needs to go, he can book the timetable slot. He cannot get a train operator because he has not got a licence but at least he can go out to one of the operators we have in this country—four, five, six, or seven—and get the best price from them. This is not legal in the Continent because it was rejected from the 2nd Railway Package because of pressure from countries like France, which did not want customers to do it. I would just like to make the point that customers still want that. The big customers of Europe want to be able to plan their logistics and then they will get prices from the train operators for what they want to do. It is terribly important to plan the route. Again, in this 2001/14, there is a clause which states that international rail freight should be given priority. That is probably the very reason you asked the question. One of the Members of the Committee mentioned that in France there are regional railways that are funded by the local authorities, and naturally they will want to run as many trains as they can over the network—and freight does not perhaps bring them any benefit if it goes straight through. That is why this clause is in this Directive to counteract that—you want to go all the way through so you get priority in the timetabling. That, combined with some speedier transfer across the frontier—it does not take long to change an engine—but the real problem is that the people picking the train up should know that it is coming and have got a driver and are ready—that is the way to do it. If this Directive were implemented properly and enforced, freight would be all right, especially on the main routes, which is where it matters.

Turning to the 3rd Railway Package and your question on quality, it has been debated by the customers and the train operators. There is a big difference of opinion between people. The Community of European Railways, which is mainly the old national railways, are dead against it, and some of the independent railways think it is a good idea. The Platform expressed the view that it was a good idea in principle but that the detail was wrong. The principle is as a means to an end of introducing competition; and the end is competition, like it is on the road. It is quite simple. This might be seen as a means to an end in Member States where there is no competition. Therefore, the Platform has said that there must be an opt-out possible if a customer does not want to participate in this requirement. The customer must be able to opt out. Secondly, the Directive is much too detailed. They talk about so many euros for so many hours' delay, but that is not the sort of thing you put in a Directive. Apart from inflation, it is completely wrong. As a means to an end, and politically, if the British Government opposes this thing, they are seen to be working together with the French Government in opposing it—and probably everybody will follow suit. Does that not give some lovely messages to SNCF? They will say, "We need not bother now." The services from SNCF are still appallingly bad in many instances. Politically, my view is that this Directive needs to go forward, but needs to be significantly modified. If the Committee would like to see our response on the 3rd Railway Package, I can send it through.

Q84 ***Lord Geddes:*** You have mentioned the "F" word—France—on a number of occasions. Just how bad is France in this respect? Witnesses we have had before you—and I am sure witnesses who will come after you—all come back to the same theme: France is the bugbear. Do you agree with that?
Lord Berkeley: Yes, I do, I am afraid. It is a terrible thing to say. Réseau Ferré de France spoke at a conference I organised last month, and I believe they are trying very hard to be different from SNCF and to welcome new operators. The real problem is that SNCF always seem to have a shortage of drivers and/or locomotives. The number of times I have been in France and seen these big locomotives with "SNCF freight" on the side pulling a passenger train. You think, "how many freight trains are in the sidings?" They are quite capable of running trains on time—because I organised a Parliamentary visit down to Perpignan three years ago and we saw the fruit and vegetable train that leaves Perpignan, temperature-controlled, every night for Paris—sometimes four trains every night—and it has never been late, except for one night in ten years when farmers dropped turnips on the line, which is probably acceptable. They can do it, but it is a question of the will. The feeling, I think you will find, if you are able to interview the chairman of SNCF or ministers in France, is that they all want to do it, but they are desperately concerned about the industrial action that might occur if they did do anything. Who is going to be in there first as a train operator? Is it going to be Rail4Chem or Eurotunnel; will it be Transfesa, who you interviewed last week? They are keen, but who is going to take the plunge? How long can France hold out? The situation is very bad, and it is part of the reason why the Channel Tunnel is going so badly, because the customers do not know when the train will arrive half the time. We feel cut off from the rest of Europe by France, the same as the Spanish and Portuguese do.

Q85 ***Lord Geddes:*** Would it be fair to interpret the action required in this context is internal in France, and not from Brussels?
Lord Berkeley: Yes, it is internal in France, but the Commission could put even more pressure on than they are putting on at the moment. I believe the new Transport Commissioner, who is French as you know, has expressed his concern about the slow progress in open access; but he of course does not have to deal with the general strike that might occur. Somebody is going to have to deal with it. The feeling is that once it has been dealt with once, it might get better; but there is a great frustration, ten years after the Channel Tunnel opened, that we are still in this position, suffering the appalling service that sometimes comes out of there.

Q86 ***Lord Swinfen:*** You said that international rail freight should be given priority. Over whom—just local freight, or passengers as well?
Lord Berkeley: What I believe I said was that the Directive 2001/14 gives international rail freight priority. I did not say it—I am just repeating what is in this Directive. It is priority over everything else.

Q87 ***Lord Swinfen:*** You are suggesting it does not happen?
Lord Berkeley: I am, yes, in some countries.

Q88 ***Lord Swinfen:*** Would you like to enumerate the countries?
Lord Berkeley: France at the moment, Germany; Italy I do not know enough about.

Q89 ***Lord Swinfen:*** Have you any idea why?
Lord Berkeley: Because passenger trains carry people who have votes—simple as that.

Q90 ***Lord Walpole:*** Lord Berkeley, I will ask you two questions about the Channel Tunnel and a supplementary question, which I would like you to answer at the same time. What is the potential freight through the Channel Tunnel and what does the British Government need to do to secure it? Are the access charges a barrier to freight through the Channel Tunnel, and again, what could the British Government do to overcome this problem? The supplementary question is this. Sitting still on the M11, listening to the radio and wishing I had come by train instead today, I heard a very interesting piece about the price of carrying yourself across the Channel Tunnel where it does not matter if you go by ferry or Eurostar, or any other way, in a car or whatever: it has gone down about 50 per cent in charges. Are you subsidising all that, you freight people? You must be paying as much as you were when the Channel Tunnel opened.

Lord Berkeley: Yes. I will answer that question. It is highly complex. I will get there, and I will take it in the order that you asked the questions. I am on record as suggesting that if the Channel Tunnel was being operated properly, in a proper competitive environment, without all the hassle that has gone on, it could probably be expecting to take about ten times the volume it is doing at the moment. I can go into the detail of that if you like.

Q91 ***Lord Walpole:*** Do you mean freight?

Lord Berkeley: I mean rail freight. Forget about the shuttle, the lorry freight; this is rail freight—ten times. I can go into more detail.

Q92 ***Chairman:*** A note would be useful.

Lord Berkeley: You would like a note! I thought you probably would. It is quite complicated. Are Eurotunnel access charges a barrier to rail freight through the Channel Tunnel? It is very difficult, because of the structure that was set up when the tunnel was being developed—and as some of you may know, I used to work for Eurotunnel at that time—to tell the source of the charges, in other words what Eurotunnel charges and what the other charges are. All I can say is that five years ago we commissioned some research which did indicate that if you wanted to send a container from Birmingham to Paris by rail or road, probably the rail element through the tunnel was two to three times what it was if you sent it by lorry on the shuttle or ferry. You would have to do the deductions, because there are no prices quoted yet by Eurotunnel of their own rates because of the usage agreement with EWS and SNCF. That is what the customers believed was roughly the difference. What can the British Government do? I ought to explain the problem about the current charging regime. I am sure that Mr Smith, in his evidence, will be able to tell you a bit more about this. Next May the current arrangement where the British Government funds what is called a minimum usage charge for the British half of the tunnel for freight, in place of EWS, stops. Unless something is done to take this forward, EWS will be faced with paying £20–25 million a year even if they run one train. That period goes on for about 18 months, until the end of 2006. I hope that the Government is going to sort it out. I cannot see any company wanting to spend £25 million just like that. More importantly, at the end of 2006, the minimum usage charge stops for passengers and freight; so Eurotunnel will lose £60–70 million worth of revenue a year, and heaven knows what will be the consequence of that. You are right in saying that the cost of going across the Channel as a passenger has gone down. That is probably because of competition, although P&O have announced they are cutting some of their ferries, and so that might change things. The real problem with the competition between road freight and rail freight is that the road rates are set in a free market, whereas the rail freight rates are fixed by the usage agreement that was signed in the mid-eighties between British Rail, SNCF and Eurotunnel as a back-door financial guarantee for the company Eurotunnel, as we all know. What the future holds is quite difficult to know. The uncertainty is nearly killing the business at the moment. It is very serious. Some people say that Eurotunnel might go into liquidation and then it will pop up with rather less debts than it has at the moment. The operation of the system is perfectly rational and reasonable, and it should be profitable, in competition with the ferries. It is this enormous debt they owe at the moment which is the problem. I am not suggesting that the British Government should bale them out. I have a few small shares in Eurotunnel, but, frankly, if you are a shareholder and it is going bust, then that is your problem. I hope that they will at least facilitate the continuity of the operation and then introduce the open access Directive in a way that will encourage competition, which will enable the operators and Eurotunnel, in whatever form it is, to get a reasonable return on what they are doing. At that stage, then the traffic should grow significantly. The next two years could be a bumpy ride for everybody, which is worrying.

Q93 ***Lord Shutt of Greetland:*** You, like me, will have had the experience of sitting in a motor car and somebody saying that the wagon in front should be on the rail; and then you look carefully at the wagon and see that it is taking furniture to somebody's house or something. I have some problem about this definition of what is freight and what is possible. It is not that long ago that I read that there is a moratorium in this country on private sidings at the moment. People are not able to get access to the system and so on. Are there any problems like that in other countries?

Lord Berkeley: Yes. I am not quite sure if it was a moratorium on private sidings. There is a shortage of them in some places in this country, mostly in the South East, where one will want to deliver things. Clearly, if you take more freight by rail, you have to have terminals to lift them on or off, or unload them. Goods like furniture are more difficult to take by rail, unless you put them in a container. More and more things are put in containers—and swap bodies are technically very similar—which is probably the easiest way to do it, except for the bulk flows, or if you have pallets, in which case you use wagons. The real answer to your question is that anything that can go into a container or swap body in enough volume to run a decent train length, is fit to go by rail. A wagon load is the concept of single wagons and marshalling yards that you come across. Sometimes they work. In some continental countries they are, frankly, disastrous. If you can get a train load right across Europe or within this country or through the Channel Tunnel, be it containers or wagons or whatever, it can go by rail freight, and it should be economic. One of the projects that some of our members are going to look at this autumn is to try and capture for rail the fruit and vegetables that come from southern Spain. About 60 trucks a day come into this country in the season: why not take them by rail? We have to make sure that it works through France, and they do not sit in a siding for three weeks; but that is all part of tracking and tracing, which the road freight industry is very good at, so it is not very difficult. That would save 60 lorries a day, and it might take two trains but it might take one.

Q94 ***Lord Shutt of Greetland:*** Are you saying that the infrastructure is there for any freight that is likely to be offered?

Lord Berkeley: Within the gauge limits and the height and weight limits, but virtually anything, if it is going far enough and in big enough volumes, which is basically a train in general terms.

Chairman: Thank you very much indeed, Lord Berkeley. As we expected, you have been very good value, as it were! We are very grateful for your evidence and for coming to represent the ERFCP this afternoon.

SUPPLEMENTARY WRITTEN EVIDENCE BY EUROPEAN RAIL FREIGHT CUSTOMERS PLATFORM—PLEASE SEE PAGE 154.

Memorandum by English Welsh and Scottish Railway

Introduction

It is the intention of English Welsh and Scottish Railway (EWS) to demonstrate to the Sub-Committee that the liberalisation of the European rail freight industry is essential for its survival and for its ability to thrive and provide an attractive and viable alternative to crowded and increasingly congested roads for the movement of freight. As the UK's leading rail freight operating company, EWS has first-hand experience of trading successfully in a liberalised corporate environment. We understand the conditions necessary for liberalisation to succeed—and through our dealings with continental operators, we understand the extent to which the right conditions are in place yet for a liberalised freight railway to flourish there. It is clear to EWS what remains to be done, both on the continent and in the UK.

English Welsh & Scottish Railway (EWS) is a private-sector company and the UK's leading rail freight operator, running 8,000 trains every week and hauling over 100 million tonnes of freight per year. EWS is the only rail freight operator to provide a full nationwide service—and it links the UK with the continental European railway network via the Channel Tunnel. EWS is a national employer, with 5,800 staff based across the whole of Britain, and has a fleet of nearly 500 locomotives and over 14,000 wagons.

EWS was founded in 1996 following the liberalisation of the UK railway industry under the Railways Act 1993, itself based on the principles of the European Union's Directive 91/440. Today, EWS regards freight as one of the successes of railway liberalisation. As well as the £500 million committed by EWS, a further similar amount has been invested in rail freight by the other private-sector players including operators and end-user customers. Since 1993–94, the volume of freight moved by rail has grown by over 50 per cent and rail's share of the UK surface freight market (ie road + rail) is now close to 11 per cent—the best performance for 20 years. EWS has identified further substantial opportunities for growth in both existing core market sectors and also in parts of the market where rail has modest presence.

Key activities include the movement of bulk commodities such as coal, construction materials, petroleum products, iron-ore and steel to meet the needs of UK heavy industry—and of a wide range of high-value, non-bulk products ranging from new cars and newsprint to mineral water and premium parcels. For non-bulk customers, EWS operates 800 trains every week, many conveying goods for several clients. Services for premium parcels customers are run at 110 mph to ensure short journey times.

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EWS is the only UK rail freight company to operate through freight trains linking the UK and the continent directly via the Channel Tunnel. These trains convey a wide variety of goods including mineral water, automotive components, steel slab, china clay, new cars, perishable foodstuffs, furniture and almost any manufactured products that can fit in a container.

The EWS Experience of Railway Liberalisation in the UK

EWS is convinced of the benefits of railway industry liberalisation:

- UK industry: in place of a single supplier of rail freight services are now four private sector operators offering a wide choice of services at competitive prices. Two more companies have indicated their intention to enter the market and should give further choice, all helping to make rail an attractive alternative to road haulage.
- The wider community. Rail is a safer and more environmentally-friendly mode of transport than road for the movement of freight. By offering an efficient and competitive alternative to lorries, rail can reduce road congestion and free capacity for other users.
- Freight train operators: Freight is often a minority user of rail routes: the separation of rail infrastructure ownership and control from train operation has made capacity allocation unbiased by any tie with an incumbent and enabled fair conditions of access. This has given EWS the confidence to invest in the long-term future of rail freight and has encouraged customers and suppliers to do likewise.

Vital to the process of liberalisation is (i) full independence of infrastructure capacity provision and train operation and (ii) the presence of an independent Rail Regulator to ensure that players in the industry are fair in their dealings with each other and that no one company exercises undue power or abuses its position. EWS wishes to register its support for the Government's intention—as set out in the Rail Review—to retain these features of the industry's organisation. EWS hopes that the SRA's (Strategic Rail Authority) Capacity Utilisation Policy will be retained and that the Rail Regulator's powers and independence will not be undermined.

Rail Liberalisation Elsewhere in Europe

EWS regards the liberalisation of international rail freight as an important issue.

EWS's international freight business operates traffic between the United Kingdom and mainland Europe via the Channel Tunnel. This business is conducted in partnership with the other European railways although the transit through the Channel Tunnel is just in partnership with the French Railways (SNCF). Volumes are currently increasing again as the market steadily recovers from the near collapse of operations due to the illegal immigrant problem, and now approach two million tonnes of cargo moved through the Tunnel by through freight train per year.

EWS believes that the European rail freight market represents a significant growth opportunity, encouraged by the European Union's pro rail freight policy and the opening of all European networks to open access operation in 2007. Through Channel Tunnel freight has the potential to grow substantially. In the medium to long-term there may be opportunities for EWS to operate on mainland Europe in its own right or in partnership with one or more of the public or private European rail hauliers. A further option would be to form an alliance with a mainland European customer.

The recent enlargement of the European Union reinforces the attractiveness of the market given the market share enjoyed by rail freight in the accession states. In the markets for non-bulk freight, rail is particularly competitive over the longer distances that trade flows between the UK states such as Poland and the Czech Republic offer.

Sight should not be lost of the fundamental logic that underpins the European Union policy of rail freight liberalisation. For decades, rail has steadily lost market share to alternative modes, in particular road. The inherent flexibility of the heavy lorry (HGV), the enterprise shown by hauliers, the development of improved roads, legislation allowing larger, heavier and faster vehicles and the European Union's own measures to remove barriers to international trade have all helped make road more competitive. In contrast, many state-incumbent, monopoly rail operators have been slow to respond by matching road's service quality, speed and price.

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The increased use of road has created its own problems such as environmental damage and traffic congestion delays. The latter in particular has grown to become a threat to the European Union's overall economic efficiency and its ability to compete with other world trade blocs. The reversal of rail freight's decline is regarded as essential if EU industry is to have a viable alternative to congested roads and if the wider community is not to suffer adversely from road's environmental impact. By the late 1980s the European Commission formed the view that rail freight providers would only improve their offer to the market if spurred to do so by on-rail competition.

The First, Second and Third Rail Packages of legislation are intended to open up first the international and now the domestic EU rail freight markets. The liberalisation process has worked and is delivering its aims in the UK. The Committee should seek to understand the extent to which on-rail competition elsewhere in the EU freight market really is making rail more attractive to end-users and thus helping rail to increase its market share again.

The EWS Response to the Committee's Questions

1. *What are the current barriers to entry in the international freight market?*

The relatively limited extent of new-entrant operation across the EU as a whole suggests that liberalisation is proceeding slowly and that new-entrants remain deterred from competing in the market. In France for example there is virtually no competition with the SNCF. Across the border in Germany there are several small freight operators, a few of which (such as Connex Cargo Logistics and Rail4chem) have grown through acquisition or merger to offer services across the country and across borders. Even in Germany, the state-owned incumbent, DB Cargo, retains just over 90 per cent market share. EWS estimates that less than 10 per cent of all the EU's international freight is operated by new-entrant companies.

From its experience and observations, EWS finds that a number of barriers remain which serve to deter entry. Together these create a level of risk and uncertainty which may prevent private-sector operators from entering the international rail freight market.

The current barriers include the following:

— Regulatory: the absence of an effective independent body in each Member State able to curb uncompetitive behaviour by dominant operators or by the infrastructure provider.

— Infrastructure capacity allocation and management: the lack of true independence of these activities from the interests of the dominant operator when both are state-owned.

— Technical: the prevalence of different signalling and electrification systems which require the provision of specially-equipped locomotives for through cross-border operation.

— Operational: the existence of different standards for train operation such as length, axle-weight and speed.

— Bureaucratic: EU Member State customs procedures give "fast-track" clearance to established state-owned incumbent operators but insist on lengthy checks on private-sector new-entrant trains.

— Cost: the application of common standards requires the re-equipment of existing motive power or its complete replacement. The benefits of common standards may be outweighed by the expense of meeting them.

— Risk: new-entrant operators regard the uncertainty over the cost and time-scale of implementing liberalisation measures as a risk in itself which only adds to the commercial risks already faced when entering the market.

2. *To what extent are these barriers a result of a failure to implement existing EU Directives in all Member States?*

Some of these barriers should erode over time as EU liberalisation measures are introduced and take effect. International timetable pathways have been established on many key axes, common technical standards have to be agreed and implemented, administrative bureaucracies have to be re-organised and experienced staff put in place. Others—such as the variations in infrastructure design (axle-weights, signalling and electrification systems)—will take many years to remove or may only be overcome through the use of expensive multi-purpose locomotives. However, EWS remains concerned that the provisions of existing EU Directives are not yet being implemented sufficiently to achieve the entry of new operators into the market and thus the creation of on-rail competition. In particular:

— In many Member States the rail freight market remains dominated by a single state incumbent operator and a single state infrastructure provider. Unless there is true separation of management between the two, the risk remains that bias will occur in the allocation and control of track capacity which disadvantages new-entrants. In the UK, this separation has been achieved thoroughly and successfully by the complete abolition of the state incumbent railway organisation and total separation of ownership, control and day-to-day management of train operation and infrastructure provision. The existence of large, dominant rail freight operators is in itself not necessarily a barrier to new entrants. Small companies can co-exist with larger incumbents—whether state-owned or not—provided that competitive activity is subject to effective regulation, so that a dominant market position is not abused. In the UK, the Office of Rail Regulator has performed this role successfully and has intervened promptly when uncompetitive activity may have taken place.

— A similarly effective regulatory body is vital to protect the interests of smaller operators in each Member State—the more so where state-owned incumbents may enjoy financial support not available to private-sector companies. The regulator should be competent, adequately resourced, capable of prompt action, able to enforce its rulings through the use of coercive measures if need be, and free of state interference when freight operators are still in state ownership. Rulings should be fair and consistent both within each Member State and between states. EWS does not believe that there is yet the equivalent of the UK's Office of Rail Regulation in all Member States. In the case of accession states it is not always clear that even the concept of an effective regulatory body outside direct state control is yet accepted.

3. *Is further action needed at European Union or Member State national level to ensure enforcement of EU Directives?*

In the light of EWS concerns expressed above, action is required at both EU and Member State levels to ensure that true separation of infrastructure provision and train operation is achieved and effective independent regulation put in place. Private-sector risk capital is unlikely to be available to new entrants and to ensure that rail freight is suitably resourced unless track access allocation and control are carried out equitably and the competitive behaviour of dominant companies is subject to independent scrutiny.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

EWS believes that the achievement of fully liberalised rail freight need not require significant further legislation, although there may remain the need to adjust existing measures in the light of experience. Some features of the legislation in the Third Rail Package are unnecessary and will prove counter-productive, if well-intentioned. Examples include:

— Mandatory Performance regimes

This Directive seeks to establish compulsory clauses in each contract between rail freight operator and customer relating to minimum service levels. The UK experience shows that rail freight's growth is the result of competitive market forces which allow each customer to negotiate freely its own conditions with the rail freight operator of its choice. These contracts may cover a range of issues such as price, journey time and value-adding services and may or may not include a performance regime as such. When quality of service conditions are included, they are constructed to meet the precise requirements of the customer concerned, are almost always confidential and will vary from one contract to another.

Making such a requirement mandatory would damage rail freight's competitive position since (i) those customers that chose not to include performance regimes in their contracts will be penalised since rail freight operators must then protect themselves against potential payments for poor performance and face little alternative but to increase their prices, (ii) an imposed performance regime may not be flexible enough to match precisely the conditions of those contracts that have been negotiated freely between customer and rail freight operator, and (iii) to distort the cost-base of one part of the transport market is discriminatory: there is no similar requirement placed on the road haulage industry. That would have the effect of deterring private sector investment in rail freight.

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— Interoperability

Measures to improve barriers to open access by encouraging interoperability have formed part of the EU's Second Railway Package. These involve the creation of new European Technical Standards for Interoperability (TSIs) and a uniform approval process. Throughout the Community these standards would replace existing national standards on the lines selected by Member States to form part of the Trans European network. EWS accepts that the intention here is well founded: greater standardisation and uniform approval processes should result in lower costs of production of equipment such as locomotives, wagons, track components and signalling systems for the industry.

Through our participation so far in the establishment of TSIs, it is clear to EWS that the standards may be set unrealistically high and that this may oblige the use of equipment that is costly to purchase. Unless careful analysis of the relative costs and benefits of each TSI is undertaken with the full and active participation of those who must purchase the equipment—ie the train operators—there is a risk that in seeking these standard arrangements, costs may be unnecessarily increased. If the cost base for rail freight operators is raised without full justification then rail will be less price-competitive with road haulage and business will be lost from rail rather than attracted to it. This issue is particularly important to those Member States such as the UK where geography means that through international freight will always and inevitably remain a small proportion of the total amount handled.

— Driver Licensing

The EU regards the lack of harmonised standards for driver management as a barrier to opening the rail market to competition and seeks to address this through measures in the Third Railway Package. At present it is seldom possible for drivers to operate a through freight train from one railway administration across a border to another. This enforces a change of driver which causes a delay and can prevent the efficient utilisation of staff and undermines the benefits of through operation of locomotives and other measures such as reductions in border bureaucracy. It is also difficult for drivers to move their employment from one administration to another without the need for sometimes lengthy and expensive retraining.

However, the EU now proposes to extend a common set of driver competency standards to all such staff—including those employed purely on domestic duties. Given that standards inevitably vary between administrations, such an extension of new requirements will result in an extensive and expensive programme of training. It is not at all clear to EWS that these costs are—or ever would be—outweighed by the benefits that the EU feels would be obtained. Furthermore, EWS has undertaken its own study of the safety benefits that would be obtained if all its drivers had to be trained to meet a set of competence standards for international freight trains. This study failed to find any significant benefit.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international freight as a result of this policy?*

EWS has two specific concerns about the Government's role in facilitating growth in international freight business:

— The UK railway network

International freight trains require appropriate capacity on the UK rail network. Train and freight terminal operators, rolling-stock suppliers and lessors and end-users all risk their own capital and require the assurance that the conditions and extent access on Network Rail's infrastructure will not change adversely in the future. The recent Rail Review does much to give EWS and these other parties the confidence needed for investment to continue. However, significant concerns remain and must be resolved by discussions between the Government and the industry. EWS will not be able to expand its international freight business unless there is capacity for additional freight trains between the Channel Tunnel and the principal UK industrial centres such as the West Midlands, West Riding, North West, North East and central Scotland. A "steady-state" railway with finite capacity would not meet these needs.

— The Channel Tunnel

There is the need for agreement to be reached by the parties involved on the future level of Channel Tunnel tolls paid by international rail freight. The charges for the UK portion of international rail freight are paid by the residuary British Railways Board (BRB)—an obligation created when the Channel Tunnel opened. These charges comprise three elements: (i) variable tolls relating to the volume and type of freight traffic conveyed, (ii) a contribution to Eurotunnel's operating costs, and

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(iii) a top-up fee known as the Minimum Usage Charge (MUC). Together these elements amount to around £26 million a year and last until 30 November 2006. Thereafter the MUC element falls away, leaving an annual charge of around £17 million a year should traffic remain at the current levels.

At present, the BRB (in practice the Strategic Rail Authority (SRA)) is not seeking reimbursement of these charges from EWS, an arrangement approved by the European Commission at the time that EWS acquired British Rail's international business. This arrangement ceases on 30 April 2005 and if no agreement is reached EWS will have to pay £26 million a year to access the tunnel.

Unfortunately international rail freight cannot bear this level of charges, in part because traffic levels have not reached expected levels as a result of the Asylum Seekers problem of recent years. Therefore EWS would have to cease international freight services if it was obliged to pay Channel Tunnel tolls.

EWS is in active discussion with the SRA and Department for Transport to extend the existing arrangement on tolls. Should we reach agreement we would need to gain approval from the European Commission—further evidence of the importance of the European Union to the development of international rail freight.

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Examination of Witness

Witness: MR GRAHAM SMITH, Planning Director, English Welsh & Scottish Railway (EWS), examined.

Q95 ***Chairman:*** Thank you very much for coming to be with us today and for the evidence that EWS sent us, which naturally we read with interest. We aim to finish at six o'clock, and have many questions, so if you could keep your answers reasonably to the point, that would be helpful. From your point of view, what are the three most significant problems faced by rail freight operators in international rail freight operations in Europe, particularly if I may say affecting Britain, where it is relevant?

Mr Smith: Service, service and service! The key for any freight haulier, by whatever mode, is to be able to meet the customer's expectations, and to deliver the goods at the time the customer requires. As Lord Berkeley has referred to, and as we put in our evidence, the quality of service for rail freight for mainland Europe is terrible, for a number of reasons: the priority given to the passenger railway; towards eastern Europe the quality of the infrastructure; the quality of the resources. If a customer is to choose rail, that can sometimes require considerable investment by the customer, and they need to be sure that that investment is going to earn a return, and that they are going to get their goods on time. We find in operating services as far as Calais, where the French railways will pick it up and pass it on to other rail freight operators elsewhere in Europe, that the service quality is not as good as it could be.

Chairman: I am sure we will pick that up during the course of the next 40 minutes or so.

Q96 ***Lord Fearn:*** The Minister for the Department for Transport recently stated the Government view that the rail freight market within the European Union should be fully open access by 2007. This was a question to Lord Berkeley as well: do you think that it will be?

Mr Smith: The legislation will be in place so that any national operator will be able to operate domestic traffic in any other Member State's railway. The legislation is there, but putting it into practice is another matter. It is arguably an issue across the entirety of Europe, which is that to make something work you have to have an organisation or a company that is willing to invest and take risk, and is willing to make an offer to the customer that they can then meet. The issue is not so much about the legislation, which is what the European Commission has put in place; it is about the willingness of the market and for rail freight operators to respond to that legislation. I do not know whether it will be there in 2007. Certainly, EWS, or strictly speaking EWSI, which is our international division, intends to take advantage of that legislation, both on international and domestic traffic. The extent to which other rail freight operators are in a position to invest and take on both the incumbent state operator and other private sector operators remains to be seen.

Q97 ***Lord Fearn:*** Are there any other obstacles that you can see?

Mr Smith: Essentially, the obstacle in every country is the state railway and the government that sits behind that state railway. It is probably quite easy to blame the state railways directly, where it is difficult to achieve open access. One has to look behind the state railways and look at the will of the government to open up their railways to on-rail competition. If that will is not there, both in railway legislation as in anywhere else, then it is doubly difficult to achieve.

Q98 ***Lord Fearn:*** How successful has the European Commission been in overturning or overcoming the barriers to a competitive rail freight market?

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Mr Smith: Our view is that the Commission has done what is in its power to do, which is to create the legislative framework. It is not for the European Commission to demand that the railway industry in a certain country changes its ownership or is fragmented; it can merely create the legislation that enables that to happen. Sometimes the European Commission may go too far and create legislation that it believes will be helpful but which would increase cost. Overall, it is EWSI's view that the Commission has created the right framework for a competitive environment.

Q99 ***Lord Shutt of Greetland:*** Mr Smith, in your paper, you say: "Vital to the process of liberalisation is (i) full independence of infrastructure capacity provision and train operation and (ii) the presence of an independent Rail Regulator . . ." You are very clear that there should be this split. Why are you so clear about that?
Mr Smith: I would be quite clear that different models work in different parts of the world. There is a fully competitive railway operation in North America, where there is a split between operations and infrastructure, and where the operator owns the track and has agreements with other operators to use each other's track. It is a "co-operate and compete" approach. Each player in that market has got market strength. The situation that has been developed in the United Kingdom post privatisation, and the situation that is developing in Europe, is that not all operators and not all markets have the same market strengths. We certainly see in this country that there is a need for independent economic regulation to protect private sector investment in rail freight against government intervention that will prefer the passenger railway for quite recognisable political reasons. Elsewhere in Europe we also see the separation of infrastructure and operations because there is a market imbalance and the market does not work effectively.

Q100 ***Lord Shutt of Greetland:*** You do not think that just regulation can cope with this?
Mr Smith: The problem with regulation is that regulator's powers can be changed by government and by Act of Parliament. One cannot always rely on the fact that the regulator will remain independent of political influence. That has always been a concern that we have had in the United Kingdom and we certainly welcome the fact that the regulator's independence in the UK was reinforced by the White Paper. But in Europe where the regulator can be part of the Ministry of Transport, can be part of government, then that genuine independence does not exist.

Q101 ***Lord Geddes:*** Could I ask you exactly the same question that I asked Lord Berkeley: one regulator or 25?
Mr Smith: The Regulator has a number of powers in the United Kingdom, not just relating to rail freight, and those powers are shortly to be increased by becoming the safety regulator as well. My view is that if the European Union has produced a common framework to which everybody works, I think the practical reality is that you will probably need a separate regulator for each country. I do not think the European Union has yet got the depth and breadth of knowledge to be able to regulate as a single regulator across the entirety of Europe.

Q102 ***Chairman:*** In the area of financial services regulation across Europe, they have a lot of complicated regulations for directors to implement and so on. The device that was adopted was for all aspects of the industry to get together and to talk through the guidelines as to how to make this actually work and the Commission then fairly quickly proposed, and was successful, taking those kinds of voluntary agreements and making them subject to comitology and they were implemented. Is anything like that feasible for rail freight in Europe? What you have described is a situation where the legislative framework is in place but the actual way in which it operates is so different in various countries that anyone who wants to operate across Europe cannot easily do it. How can you move to break this stalemate across Europe?
Mr Smith: I think the difference is that the financial services sector, along with other modes of transport, is not hidebound by a national state boundary, it will work across not only states in Europe but is a worldwide activity. Railways, by nature of their geographical existence and the way in which they have been developed since the 1850s, are very much a national activity tied to a national economy and in the past have been used to promote national interests. It is not many years since national railways were forced to purchase from manufacturers within that country rather than purchasing at best possible price. I do not think that the railway industry throughout Europe is yet mature enough to regard itself as a cross-border pan-European activity. I believe the legislation that the European Commission have put in place will lead us towards that, but I think it has a few years to go yet.

Q103 ***Lord Swinfen:*** Mr Smith, we heard from Lord Berkeley that he thought that the potential for rail freight through the Channel Tunnel was not being reached. I wonder what is your view on this is and, if you think it can be increased, what can our Government do to help secure this?

Mr Smith: Rail freight through the Tunnel is about 3 per cent of the cross-Channel market and it is a growing market as well, so there is—

Q104 ***Lord Geddes:*** Three per cent of the cross-Channel freight market?
Mr Smith: That is correct, yes. Clearly there is huge potential. There is a constraint, which is the physical capacity of the Channel Tunnel but, of course, that is not the only way to get to Europe and perhaps in years to come we will see a second tunnel built—that would be unlikely—or maybe the reintroduction of train ferries. There is a capacity limitation but certainly we are nowhere near that at the moment. Prior to the problem with the asylum seekers that we faced two years ago when most of the international rail freight just stopped because of the incursion of asylum seekers at the SNCF yard at Fréthun, we were moving about three million tonnes a year. In the last full year we moved 1.7 million tonnes and we expect just over two million tonnes this year. I go back to my answer to the first question: one has to improve the service quality and to be able to offer that at a price which is competitive with an alternative load, but the potential is significant. It is not just in what people might think of as traditional Channel Tunnel traffic, the containers and swap bodies that have been referred to, but in the areas where rail freight is competitive across the world you can move more goods and heavier goods by rail more efficiently than one can do by road. It is a matter of rail freight, either individual companies or across Europe, finding the markets—be it chemical, steel, construction materials—and moving those between countries in Europe. Elsewhere in Europe the manufacturing industry moving from western Europe to eastern Europe and the construction industry will go to the lowest priced supplier. What the transport industry has to do is to ensure that the lowest priced supplier can access the markets where there is demand.

Q105 ***Lord Swinfen:*** You said that a couple of years ago we were at three million tonnes freight a year.
Mr Smith: Yes.

Q106 ***Lord Swinfen:*** You did not actually suggest what it might rise to if properly managed.
Mr Smith: The forecast put in place at the time when the Channel Tunnel was built was for six million tonnes. One could certainly get higher than six million tonnes, it would depend on other users of the Tunnel as to whether the capacity was available and it would depend on the nature of the goods. Clearly a wagon can move very light goods, a wagon can move very heavy goods, so the absolute volumes I would not want to be drawn on because it depends how the market evolves. Certainly one can move significantly more than is being moved at the moment.

Q107 ***Lord Swinfen:*** You could significantly remove the freight traffic off the M2 and M20?
Mr Smith: Certainly we could make a dent in that. No-one in the rail freight industry has ever said that it is the sole solution to congestion on the motorway network in the UK but we can certainly have a go at it.

Q108 ***Chairman:*** At the moment you say that rail freight through the Tunnel is 3 per cent of all cross-Channel freight?
Mr Smith: Yes.

Q109 ***Chairman:*** At an optimistic level of growth, if all conditions are right, what proportion of that movement do you think could go through the Tunnel economically?
Mr Smith: I believe you could move up to 10 per cent of that before you ran out of capacity. That would be the limiting factor, not the market, because the market is huge.

Q110 ***Chairman:*** That is helpful to the Sub-Committee to know, that at capacity for rail freight purposes it would still only take 10 per cent of the freight movement.
Mr Smith: If one presumes that the use of the Tunnel remained for lorry shuttles, car shuttles and capacity for Eurostars. Clearly it is possible to change the proportion of the capacity of the Tunnel and were the entirety of the capacity of the Tunnel handed over to rail freight we could probably move significantly more, but I suspect that is unlikely.
Chairman: That sounds like an opening gambit.

Q111 ***Lord Geddes:*** Mr Smith, presumably that aspiration would also require open access through France?
Mr Smith: Yes.

Q112 ***Lord Geddes:*** You came up with a perfectly wonderful expression about 10 minutes ago, that such open access was "not as good as it could be". How masterly an understatement would you say that was and would you like to expand?
Mr Smith: Certainly I stand by that comment, Lord Geddes.

Q113 ***Lord Geddes:*** You have not answered my question. How masterly an understatement was that?
Mr Smith: Open access in France does not exist at the moment but I am aware of four rail freight operators who are applying for safety certificates in France, and my company is also looking seriously at becoming an operator in France. There are three essential

prerequisites. The first is to have an international operating licence, which we do have. The second is to have a safety certificate, which has to be applied for in triplicate, in French, to French Network Rail (RFF) for approval. Thirdly, to apply for access rights relating to particular traffic. It is not a simple process but nor is the process in the United Kingdom, so perhaps one should not be too critical about it. My view is that the French government is starting to realise that it will have to allow the French railways to accept open access, if nothing else but to help the French railways themselves become more efficient. The French railways do have financial problems as well as service problems and the ability to have open access operators to demonstrate a low cost operation will help them hugely. If we were to sit here in a year's time I think you would see four or five open access operators with access rights in France operating open access services.

Q114 ***Lord Geddes:*** Is there anything that this Government, our Government, can do to accelerate that process?
Mr Smith: It has a multiplicity of relationships with the French government on a number of issues, only a few of which relate to rail freight. I would suggest that through the European Council of Ministers a little pressure could be exerted to make sure that the processes in France are perhaps speeded up slightly. Certainly I am aware of a French company that applied for open access 10 months ago and is still waiting to get its approvals. The European Commission, the UK Government, I am sure could give a little nudge in the right direction.

Q115 ***Lord Geddes:*** I feel sure that in a previous incarnation you must have been in the diplomatic corps.
Mr Smith: Thank you.

Q116 ***Lord Swinfen:*** Mr Smith, I am just wondering, will EWS and the other four companies have to use SNCF locomotives and drivers?
Mr Smith: No, we do not have to. What we would like to use are the Class 66 General Motors locomotives that we use in the United Kingdom. That locomotive has been approved for operation in Holland, Belgium, Germany, Sweden and Poland; the French have not quite got round to approving its use yet. It is probably that General Motors have to provide them with a little more evidence as to why it is suitable. The French tend not to like diesel locomotives; their preference is for electric traction. In terms of drivers, we have drivers employed by EWS who could drive in France and whom we might use in the first instance. It would be good to have a market to hire in locomotives and drivers from SNCF, as we have in the United Kingdom, but certainly if we were to develop our own operation there we would want to recruit our own drivers and supply our own locomotives.

Q117 ***Lord Swinfen:*** To what extent are capacity constraints in terms of infrastructure and terminals a constraint on the growth of international rail freight in this country? Again, what can our Government do about it?
Mr Smith: I think there are two elements of constraint. The first is the capacity of the network generally, which in most areas is uncongested but there are very congested parts of the network, particularly in the primary routes, and that is why with the recent upgrade of the West Coast Main Line the railway industry has committed to providing 70 per cent more paths for freight trains. International freight trains are some of the biggest users of the West Coast Main Line because of the connection between London, the West Midlands, the North-West and Scotland, so ensuring there is sufficient track capacity for freight throughout 24 hours a day as well. Freight is always at risk of being pushed aside for Network Rail to gain engineering access to the network. If one is going to meet customers' aspirations, to pick their goods up at close of work and deliver the next morning then, by definition, we have to move at night. The other area is gauge, where the continental loading gauge, for reasons of history, is higher than in the United Kingdom. Our plan is to run high gauge trains through the Channel Tunnel and on the Channel Tunnel Rail Link as far as the freight connection just north of the River Thames at a place called Ripple Lane near Barking, so we can get high gauge European wagons there. What we would like to do in the long-term is to be able to move those high gauge wagons further into London and ideally further north. That is a not insignificant task; it is not a cheap task. At the moment the focus on gauge enhancement in the United Kingdom is to permit the movement of nine foot six inch deep-sea boxes from the deep-sea ports at Felixstowe and Southampton, but if we are going to be truly united with continental Europe through rail freight then the ability to move high gauge continental wagons elsewhere in the UK is essential.

Q118 ***Lord Swinfen:*** That means possible major structural changes to stations, bridges and tunnels, does it not?
Mr Smith: There are a variety of ways of increasing gauge. Recently there was the track lowering in the Ipswich Tunnel which allowed the nine foot six inch gauge containers to go through there. It is possible to interlace track so that the wagon passes underneath the bridge or the tunnel arch, which needs signalling, but there are many examples around the world of gauge enhancement being achieved in that way.

Q119 ***Lord Swinfen:*** Would it affect the platforms at stations or not?
Mr Smith: It can do, but it depends on the route that one goes on and the amount at which the throw or the kinematic envelope of the wagon would conflict with the platform edge. For example, on the West Coast Main Line, platform edges were shaved back quite considerably, not actually shaved but taken back quite considerably, to allow the passing of the tilting Pendolino train as part of the West Coast Main Line upgrade. It is not an impossible task and in some places it is already in place.

Q120 ***Lord Swinfen:*** Would you have to change platforms to continental platforms almost at ground level?
Mr Smith: You would not have to go to the step up that we see on the continent. You may have to draw some platform edges back. No route is the same in the United Kingdom and we are not saying that the Government should spend money that it has not got in immediately blasting across all routes throughout the United Kingdom, but I think we should identify the major centres of population, of consumption, of production, and start there. Our view is that if we can just get across to the major freight centres in west London, around the Wembley and Willesden areas from the Channel Tunnel Rail Link at Barking, that would be a good start.

Q121 ***Chairman:*** I gathered from our Spanish witnesses last week that elsewhere in Europe they are investigating freight-only lines, even developing networks, and there is some discussion going on in the Commission on the survey potential there. Is that something that you are aware of and can you tell us more about it? Are you involved in that?
Mr Smith: I believe that the European Commission's intention is to have freight primary routes perhaps, not freight-only lines. Most of Europe, like the United Kingdom, is a mixed traffic railway with a variety of passenger traffics and a variety of freight traffics, but by identifying freight primary routes, perhaps freight can get the priority running that it does not enjoy at the moment. As far as the United Kingdom is concerned, as part of the rail review process we have pointed out to the Government that routes, such as the Glasgow, South Western and Settle and Carlisle route, the North-East/South-West route across England, the route from the Channel Tunnel and the Haven Ports, all could be identified where freight trains perhaps might be seen more frequently than passenger trains. In Europe, with more and more high speed running with more and more capacity on what you might call the classic lines, those could become freight primary routes. Freight will never run, and does not need to run, at 140 or 120 miles per hour. There are certain parts of Europe where 100 or 90 miles per hour provides an attractive service but what freight needs is the reliability to keep going and to have the guarantee of the paths.

Q122 ***Lord Shutt of Greetland:*** There has been a lot of discussion over the years about the Great Central route being reopened and so forth. Is that just a pipedream? Would that really help?
Mr Smith: I think the concept of reopening that route is interesting but it would be incredibly expensive. The suggestion was that it would be reopened at a gauge where one could carry a complete lorry on a train, that there would be a lengthy tunnel underneath London and the traffic on that would be competing with traditional rail freight, Eurostar shuttles and cars. I think the issue with that route is the expense. The concept of having a route which is primarily for freight is very attractive but I think we do have to live in the real world, which is why I am not pressing the Government to open up the entire network to continental loading gauge, just one stage at a time.

Q123 ***Lord Shutt of Greetland:*** You referred in your written evidence to inter-operability and that you are worried that action on that may raise the costs for British operators without compensating benefits. I think there is a feeling that perhaps the practitioner will not be listened to. Can you expand on this? What can the British Government do about it?
Mr Smith: EWSI may well be a lone voice amongst the rail operators in the UK in supporting the general principle of inter-operability because as an international operator we can see benefits from common gauge, common braking systems, common systems of communication, but this is one of those areas where occasionally the Commission does get a bit carried away with itself and starts suggesting schemes which will be very expensive for a government to implement and impossible for a private sector operator to implement. In that part of our paper our primary concern was the European Rail Traffic Management System—ERTMS for short—which is a signalling system, that I am sure your Specialist Adviser can brief you on, which would be incredibly expensive to implement both in terms of communications systems and the amount of technical equipment that would need to be put inside locomotives which would fall to the operator to provide. As yet it is unproven technology. Indeed, the Swiss put it in as a trial system on one of their lines and once the trial is over they are going to rip it out and reinstate the traditional signalling so that it is compatible with the rest of their network. Sometimes the Commission can see a great technical idea, rush ahead with it, and perhaps does not think enough about how something can be funded.

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Q124 ***Lord Shutt of Greetland:*** Is there anything that the British Government can help with on this?
Mr Smith: We have made representations to the British Government who, on the one hand, support the concept of inter-operability which for purely domestic operators in the UK has perhaps limited attraction but with the increasing internationalisation of rail operation is more important, and at the same time we have pointed out to them the areas where the expenditure would be excessive and the benefits not seen. The Department for Transport have an international department who do represent the UK's interests in Brussels and I believe they are effective but they are only one voice amongst 25.
Lord Shutt of Greetland: Thank you very much indeed. I do not think I need go on to the other point, my Lord Chairman.
Chairman: Just touch on it briefly.

Q125 ***Lord Shutt of Greetland:*** You did raise concerns about the cost of the European driving licence. Is an obvious answer not to make it applicable only to drivers of international trains?
Mr Smith: Our view is that drivers want to be promoted, drivers may want to transfer, so a driver of an international train may not always be the driver of an international train and a domestic driver may aspire to be an international train driver. Connected with the question earlier about whether we would be able to hire drivers from SNCF, if we did not have drivers who were qualified to operate internationally, then we would be obliged to go to the state railway to supply them, but in having an international driving licence there is more freedom. What we object to in this process is the setting up of an expensive independent body to verify and to register drivers with international licences. We believe this is an area where self-certification and audit would be a far cheaper and far quicker way of implementing this policy. Again, it is one of these areas where the European Commission has grabbed an idea and perhaps gone a little too far with it.

Q126 ***Lord Walpole:*** Can I just say, Mr Smith, although I am not absolutely clear about this, I came down by train today and it does seem to me the chance of being drawn by one of your engines is fairly great on ONE Anglia, is that correct? Do you let them have them because they are having problems?
Mr Smith: We lease a number of EWS engines to ONE Anglia and to other operators as well. We do not just haul freight trains, we hire our drivers out and we hire our locomotives out. I believe ONE Anglia are moving across to using all of Virgin's old locomotives.

Q127 ***Lord Walpole:*** Yes, I think so.
Mr Smith: As someone who has got a flat in Cromer who uses that service on a regular basis, I share your concern.

Q128 ***Lord Walpole:*** Are you satisfied that the new structure of the rail industry in Britain, as announced in the recent White Paper, will give adequate priority to international freight services?
Mr Smith: It was slightly disappointing that the White Paper did not refer to international freight services but, by and large, I think it was good for rail freight because it offers the following things. One of its six principles was to create stability and certainty for rail freight operators, customers and investors. What it did say was that rail freight operators in the UK should have long-term access agreements, and shortly we will be applying for our long-term access agreement. Unlike the passenger, a rail freight customer will invest for up to 20 or 30 years and they need to be certain that there is always going to be room on the network for rail freight. The second was certainty of access rights, be it for international freight trains or domestic freight trains. The third, and arguably the most important, is that the charges that rail freight operators pay to use the track, which is significantly less than it costs to go through the Channel Tunnel, will be at stable and affordable levels. The Rail Regulator's review of freight access charges in 2001, which determined that rail freight would pay its wear and tear costs on the UK rail network but no more than that, was a significant boost to the rail freight industry and certainly gave a lot of our customers the encouragement to reinvest and to enter into long-term contracts.

Q129 ***Lord Walpole:*** Can I just ask, does the track actually wear out more quickly if you use a selection of different sorts of vehicles on it, some of which may not have quite the same bogeys on them as others?
Mr Smith: Absolutely. Wherever you go in the world, the laws of physics are the same. If you have got something with dodgy suspension, whether it is a freight train or a passenger train, they will bang the joints when it goes over them and if you have a really smooth suspension it will not. Damage to the track is a mixture of the volume passing over it, the axle weight and the speed of the train and it is a complicated mathematical formula that I—

Q130 ***Lord Walpole:*** So the quality of maintenance of the vehicles is very important?
Mr Smith: Absolutely, yes.

Q131 ***Chairman:*** Could I thank you again. Is there anything that you would like to add in conclusion?

Mr Smith: I think there is one further issue which you touched on with Lord Berkeley, which is the issue of the Channel Tunnel. Whilst we would hope to operate in mainland Europe in due course, perhaps even on a stand-alone basis, we have got to get through the Channel Tunnel to do that. Resolving the issue of Channel Tunnel tolls, to which Lord Berkeley referred, is critical. To have a solution for the future of Eurotunnel is equally important. We are having constructive discussions with the Department for Transport and the Strategic Rail Authority to get the toll issue resolved but until it is, it is perhaps difficult to be completely confident that international rail freight has a strong future. However, I do believe that the issue will be resolved because, as Lord Berkeley said, traffic levels at the moment could not bear the additional £26 million in Tunnel charges. In the long-term, providing there is a solution to Eurotunnel's future that meets everybody needs, I am absolutely confident that international rail freight will grow significantly and certainly my company intends to play a full part in that.

Q132 ***Chairman:*** We share your aspirations and we hope very much that the picture that you have just drawn is one that comes about. Thank you very much indeed; we are very grateful to you for your evidence today.

Mr Smith: Thank you, my Lord Chairman.

MONDAY 25 OCTOBER 2004

Present	Cohen of Pimlico, B	Shutt of Greetland, L
	Eccles of Moulton, B	Swinfen, L
	Fearn, L	Walpole, L
	Haskel, L	Woolmer of Leeds, L (Chairman)
	St John of Bletso, L	

Memorandum by European Rail Infrastructure Managers (EIM)

The European Commission was late in evolving a transport policy involving rail transport. It had observed that rail was losing market share in the international freight scene and concluded that a major cause was the lack of quality, essentially in punctuality. Delays were being measured, not just in minutes, but in hours and sometimes days.

The EC concluded that one of the main factors for the shortcomings in rail service was structural. Each railway was sovereign in its own country, and whilst it competed with other modes (road, inland waterways, etc), there was no "intramodal" competition between the state-owned railways. Rail was the only mode of transport where intramodal competition simply did not exist.

In 1991, the EC prepared proposals that started to open the rail market (in Directive 91/440), opening the market to intramodal competition to freight traffic, if only for international intermodal traffic, whether it be by private companies or incumbent national systems.

There was little "take-up" on this opportunity. The Commission made further proposals. To establish fair conditions under which new, private companies could compete with the established, "incumbent" national systems, the Commission and the European Parliament voted through proposals that required the separation of infrastructure management from train operations. The thinking was that this was a prerequisite for the opening of the market. The continued existence of nationally-owned train operating companies was seen as a great deterrent to new incomers in a market that in itself was an expensive one to penetrate. (There are many different signalling systems, traction current supply systems, and the purchase of a locomotive, which normally has an operating life of at least 20 years is a major hindrance to entering established rail markets).

This event, commonly known as the "First Rail Package" became law in March 2003. By that time, the infrastructures of Finland, Sweden, Norway, Denmark, the Netherlands, Britain, France, Portugal had already become separate from their national train operations. Since then, Slovenia, and the Czech Republic have followed. Other national systems have moved in the direction of infrastructure separation, but not to the fullest extent. The German Railways—key to the heart of European rail operations—has created a separate DB Netz (Infrastructure Company), but this reports to the same Board that administers the operations of its passenger and freight activities. The same can be said of the Austrian, Italian, Belgian and Luxembourg Railways. All these systems are moving towards full separation, but have not yet finalised the process. The Spanish Government was in the act of separating, infrastructure from train operation, planned for this year, but the sudden change of Government following the terrorist attacks put this process back. It is understood that the process of separation will take place, probably within one year.

A further difficulty revealed at an EIM conference jointly held with the Association of European Rail Freight Operators (ERFA) and the Intermodal Association (UIRR) in March this year has been the experience suffered by "would-be" operators who have to submit their equipment (eg locomotives) for validation and certification, and who find this task is often still in the hands of the incumbent railway with whom they wish to compete. This has resulted, in a number of cases, to lengthy delays in certification and acceptance.

In the newly-joined countries, all are expected to complete the separation of infrastructure and train-operating activities.

How far has the opportunity for competing with the established national freight train companies been taken up?

The answer is "at a different speed in different countries". (Not a surprising answer, but it needs understanding).

In the UK, at the time of privatisation, separate companies dealing with the containerised transport (Freightliners Ltd) and conventional freight (EWS) were created. Since then, Freightliner has moved into the "Heavy Haulage" business of block train operation in competition with EWS, just as EWS has entered the combined transport market. In addition, Direct Rail Services (DRS), based originally on the haulage of nuclear traffic, has entered the market, as has GB Railfreight and Advenza.

In France, the position is different. Only very recently, Europorte (a subsidiary of the the Channel Tunnel Company—Eurotunnel) gained the first operating licence for international freight operation through France and another company (CFTA—a subsidiary of Connex) has also been awarded a licence. Neither company has yet operated freight services in France.

In Belgium, one private operator has started operations, whilst in the Netherlands, some 10 private operators run container trains from Rotterdam to inland destinations, one of whom is the German national state rail operator Railion.

In Scandiavia, competition exists in Sweden between the state-owned operator (Green Cargo) and nearly 20 other train operating companies.

In Norway, the only non-state-owned system is the private company operating heavy-haul iron ore trains in the far north at Narvik.

In Finland there is one private company hauling its own traffic, but no competion as such with the national operator.

In Denmark there are four newly licensed operators. It has to be noted that Danish Railways recently sold its freight activities to German Railways under their title Railion. Similarly, Railion acquired the national freight activity of the Dutch national system.

The situation in Germany is particularly interesting. Whilst the infrastructure of DB (the national railway) is still owned by and responds to the same Board as the incumbent railway, more than 300 private train operating companies are now established on DB Netz tracks. They haul not just the traffic of individual companies, but are also active in "general" traffic in full and free competition with DB itself.

In Austria, there are at least eight or nine private companies competing in international rail traffic. One is interesting (they are all interesting!) as it is a Viennese tramway company that has sidings leading into industrial sites, and now operates its own trains largely to German ports.

In Italy private operations have taken hold, notably via the Ferrovia Nord Milan Company. Some 30 companies have been licensed, not all yet obtaining their Safety Certificates. Most are aimed at regional passenger services, but the Rail Traction Company (RTC) has gained a firm foothold on the Italian side of the Brenner route, providing freight transport between Italy and Germany, and capturing 25-30 per cent of the existing flows as well as gaining new traffic. Through co-operation with their Austrian partners, service quality has improved.

In Switzerland, private operations, as in certain other countries, have taken a different path. Groupings of big, international systems (DB/BLS) have got together to form internationally controlled groupings to manage the international operation of trains across frontiers. Such groupings are showing good progress, but make new penetration of the market difficult for newcomers. (I make it clear that this is a personal opinion—JE).

Similarly, Deutsche Bahn (DB) has acquired the national freight operations of neighbourng countries (in Denmark and the Netherlands) through its subsidiary Raillion. The impact of this action has certainly improved the international control and marketing of services in the countries involved, but has also made new entrance by independent companies more difficult. Tonnage hauled, however, has grown. Whilst there were early fears that new operators would merely "cherry-pick" existing rail freight tonnage, these have since been dispelled and the emergence of new operators has grown the traffic levels to beyond that previously carried. The amount of traffic growth varies from country to country. The UK is recording some 45 per cent, or more, freight tonnage since privatisation and the emergence of competition. In Germany, tonne kilometers have grown from 69,597 million in 1995 to 79,450 million in 2003 (+14 per cent), according to the DB's Competition Report issued in March this year. Significant tonnage growth has been noted in Sweden since the advent of competition.

General Conclusion

The groundwork necessary for the introduction of liberalised, competing freight services in Europe, notably the full separation of infrastructure from train operations, has been implemented in some countries, but not in a number of important systems. However, the concept of introducing independent train operating companies has caught on, although considerable doubts remain where the national railways remain integrated. The "German" model which retains the same Board control over both infrastructure and "incumbent" train operations is followed in a number of countries. Competition has, however developed in Germany, but to a lesser extent in other countries.

It is important that key issues are monitored:

— Full market opening must be pursued in all countries, some of which have been reluctant to embrace the doctrine;
— Competition must be kept "active" and Europe must be vigilant against possible domination of the market by the major state railways;
— The processes of safety certication and equipment approval must be simplified and speeded up. Above all they should be in the hands of independent authorities, not the State railways; and
— The difficult question of the level of Access Fees (presently entirely dependent on National transport policies) must be addressed from an international viewpoint.

J Evans
European Rail Infrastructure Managers'

August 2004

Examination of Witness

Witness: Mr Marc Falchi, Secretary General, European Rail Infrastructure Managers, examined.

Q133 Good afternoon, Mr Falchi, can I convey to you the warmest of welcomes on behalf of our Sub-Committee and thank you so much for coming along to give oral evidence today. Thank you also to EIM for submitting an interesting memo to us in advance. We are extremely appreciative. It would be helpful before putting questions to do two things. Firstly, for you to make any preliminary remarks that you wish to make by introduction; and, secondly, for you to give us some indication of who the members of EIM are.
Mr Falchi: First, I have to apologise in advance for my English. I will do my best, but sometimes it can be difficult for me. Second, I am very honoured to be here and to attend to give you this evidence. Membership of EIM is at the moment eleven members, of which nine are infrastructure managers from EU 25 Member States. I can quote all of them: Finland, Sweden, Norway (which is not a Member State), Denmark, UK, Netherlands, France, Portugal, Spain—but only the high-speed network because RENFE is still integrated and not yet a member, and then Slovenia which is a new Member State, and Eurotunnel, which is not only an infrastructure manager—so eleven members. I have to say also that this association was created at the beginning of 2002 by splitting CER—before this date CER was the common lobbying body of all the railways in Brussels, and we split because it was impossible at this time, and it is still, for infrastructure managers, and especially the independent infrastructure managers, to have their voice heard, when it is different from the railway undertakings in CER; so they lobby the European Council, the European Parliament and the Commission.

Q134 ***Chairman:*** Of those nine new Member States—which of those companies would you describe as independent companies?
Mr Falchi: All of them.

Q135 ***Chairman:*** Are they?
Mr Falchi: Yes. The only one to be a special case is Eurotunnel; the other 10 are fully and entirely separated from any railway undertaking.

Q136 ***Chairman:*** How many of them, if any, are privatised in whole or in part?
Mr Falchi: Privatised? It is a very difficult thing. When you say "privatised", in the UK it can be something different from the continental context. For example, you say—

Q137 ***Chairman:*** Not owned by the state.
Mr Falchi: Not owned by the state, but what is owned by the state or not? Is Network Rail owned by the state or not, in your understanding? In my understanding, with my French background, all these companies are state-owned companies or almost state-owned companies. None are privatised, even the Spanish one.
Chairman: That is extremely helpful. As you know, we have a lot of questions to ask, and there is never enough time. Baroness Cohen is going to start.

Q138 ***Baroness Cohen of Pimlico:*** Mr Falchi, we note from your evidence that there is a certain amount of concentration going on among the infrastructure owners, with the Germans buying up some infrastructure in Denmark and in Holland. Does this matter? Is it excessive? Is there any action necessary to avoid concentration?
Mr Falchi: German Railways, Deutsche-Bahn, is spreading in Europe, but not on the infrastructure side, on the railway undertaking side. I use the European language, but I can use UK language, as a

clerk, not as an infrastructure controller. The only case where infrastructure has been taken over by someone else is Estonian Railways, which has been bought by an American citizen; it is the only case. In all other cases, the infrastructure is still state-owned, or almost still, state-owned. Where you are right is that the German Railways, DB, is buying a lot of other undertakings, particularly freight companies in various countries—not here, but in the Netherlands, in Denmark; and they are discussing whether or not to buy GreenCargo in Sweden. They are also trying to expand in the Czech Republic, but that is not yet done. At the same time, on the continent the most open market is the German market, where there are now more than 200 railway undertakings particularly on freight. In Germany there are a lot of freight companies—not only German freight companies but there are also a lot of passenger train freight companies, most of them being French. DB always says, "look at the French; they can invest and buy companies and operate in our market but it is not possible to do the reverse". To answer your question whether there is a threat, I would say not yet. I think the problem is that on the freight market there are only two companies at the moment playing at the European level, and these two companies are the German Railways and the Swiss Railways. Some others are coming in—the Italians are beginning to do the same—but the problem is that only these two companies are doing it yet. It is the EIM position that the situation will be difficult if no UK or French company comes in within the next few years, because if they do not, in the end the German Railways will dominate the freight market—it is obvious.

Q139 ***Baroness Eccles of Moulton:*** Mr Falchi, we have been told by a number of witnesses how difficult it is to gain access to operate through certain countries, and I am afraid here I have to mention France again, which is of particular concern to us because our only access is through the Tunnel, obviously. It would be very interesting if you could tell us whether in your view these difficulties are being overcome and what steps have been taken recently, or are being planned to be taken soon, to overcome the problems, again especially in France.

Mr Falchi: The first thing between the UK and France is the Eurotunnel. I go back to this, because Eurotunnel is still a problem, and a big problem, particularly for freight. More widely, at the European level the legislation is now there in order for the freight market to be open in two or three years' time. Even if I do not believe in this index, the German Railways and the University of Humboldt in Germany publish every year a liberalisation index, which you can find on the website of the Commission. It shows that liberalisation is going on. The countries in which we have no competition at all are France and Spain, but things could change this year or next year, 2005, because Member States have to implement the First Package, and the Second Package will also be there. Practical steps for France: I think you know, because it has been published in the English press, that Eurotunnel has created a subsidiary called Europorte 2, which has a licence to operate in France. Europorte 2 has asked for a safety certificate in France, and will have the safety certificate in the coming weeks, maybe days—now. Three companies are at the same level, so the licence is there; the safety certificate is going on. The French minister has published a decree that says that within two months they have to give an answer to the companies asking for a safety certificate. Of course, the two months is when the dossier is completed, because sometimes you have to complete a dossier, but to give the example of Europorte 2, it was something like four months between the formal application and the granting of a safety certificate, so things are happening. More than this, in the French market, Europorte 2 in mid-December of this year—so in 40 odd days—will have at its disposal a lot of paths; in advance of getting the safety certificate, they asked for paths and they will have some paths, so the French market is opening.

Q140 ***Baroness Eccles of Moulton:*** Does SNCF issue safety certificates?

Mr Falchi: No, and yes! No, because formally it is the French minister for the moment, until a safety body or a safety authority is created—and this is coming. The French minister grants the safety certificate, and the people involved in safety and the French minister—I do not know exactly the figures now, but it is 10 people, say, so a small body. The French minister will deliver the safety certificate on the report issued by RFF, which is the independent infrastructure manager. Of course, the technical work to make sure that the locomotives are compliant with the French networks, will be done by SNCF because for the moment the competences are there. Things will change, but for the moment it is "no" and "yes". When RFF was created in 1997—and I joined it after 20 something years in SNCF—my first job there was to be head of operation and safety. I was involved at the beginning of this, and I know the people in charge; and ultimately it will no longer be SNCF. Even if SNCF did a review on this, the other bodies are now in a position to say, "we do not believe in this; we do not trust you and we will make our decision". I can give you examples if you have time.

Q141 ***Chairman:*** Did you say you could give examples?

Mr Falchi: Yes. In 1999 we had an example of a discriminatory position where, between France and Switzerland in the area of Geneva, the Swiss authority wanted to create a link between—I do not remember the name of the city in France—and Geneva. They wanted to use a Swiss locomotive and a Swiss train. At that time, they had to ask SNCF, and SNCF said "it is not possible because, because, because . . . ." The case came through us, RFF and the discussion between SNCF and the Swiss authorities was destroyed—excuse me for my English—because of SNCF's behaviour, but, in the end SNCF and the ministry had to say, "now this locomotive and this train can go through France". Things have changed now because now everything is written in law, at that time it was not.

Q142 ***Lord Swinfen:*** Mr Falchi, you talked to a large extent on the safety certification with regard to France, but what about the rest of the EU, the other countries? Are the existing proposals sufficient to ensure fast and non-discriminatory treatment of applicants?
Mr Falchi: I will ask another question! Is it possible to have locomotive or train certification in the other countries? In the EU 15, yes; in the EU 23 (let's exclude Malta and Cyprus which have no railways)—not everywhere. In the EU 15 it is possible everywhere to have locomotive or train certification. Fast and non-discriminatory—I am not sure about Spain, but I think in the other countries, yes, very obviously, because the safety authorities are there, the independent infrastructure managers have been there for years and doing their job; it is possible also the answer to the question is fast, but fast is not yet there. The best example I can give you is the Ikea experience. Three years ago Ikea created a train operating company between Sweden, Denmark and Germany, only with the three countries. It took more than a year for them just to hand in all the papers for the safety certificate, not because things are so different, but in the end they had to give all the same information to the three safety bodies, but in different shapes and different languages. It took a lot of their money and time. In principle, the answer to your question is "yes", but we need harmonisation of this because for a train operating company that wants to do business in more than one country, they have to have a safety certificate in each country, at the moment it is obviously very difficult. Even in the UK it is difficult, and I can give you examples of people coming from elsewhere in the UK where it is not so fast and not so easy. It is one of the biggest difficulties for the European market. I do believe that it will be the remit of the European agency, and I hope they will work as fast as they can on this, because it is one of the biggest issues for the train operating companies.

Q143 ***Lord Fearn:*** What are your views on appropriate tariffs for track access; and do two-part tariffs discriminate in favour of the large operators?
Mr Falchi: What do you mean by "appropriate tariffs"?

Q144 ***Chairman:*** What do you think are appropriate? How do you think track access should be charged?
Mr Falchi: My view is that there are a lot of questions around this. Most of these issues are political because tariffs and access fees are mainly decided by the Member State. They decide this based mainly on the mechanism to finance the infrastructure and the development involved. My view is that it is a difficult issue for the association because the situation is very different if you compare, for example, Norway where the tariff is almost zero, and in Sweden and the Netherlands it is also very low. It is the reverse in the UK, where the tariffs are very high. The tariffs are so different because the way in which the infrastructure is financed is different, and the decision has been made by the Member State—the government and the parliament. I have done some academic economic transport studies. I am also an engineer and have been a railwayman for 35 years now. I will use one of your acronyms—KISS (keep it simple and straight)—and for me to keep it simple and straight, comparing the modes with each other, the way in which road is financed in every Member State is very simple. Member States or their local operators are paying for the road renewal and development. The other is the regulated or organised mode—air traffic. Most of the infrastructures of the airports and traffic control are, at the moment, financed by Member States or local authorities. At the European level there are differences between Member States. Just to keep it simple, what if the financing of all infrastructure was 100 per cent public, and if the Regulation was made on the basis of what we have agreed in regulated modes, so priority rules for path allocation or slot allocation for the aircraft? I know part of the UK example and part of the French example, our finance for infrastructure is as complex as yours, but very different. The result is that for freight train operating companies in France the tariff is very low, but public; and in the UK it is non-public and not so low. For a train operating company wanting to operate from Wembley, for example, (and in 1999 I was engaged in this) going to eastern Europe, through say the Austrian/Hungarian border—if you put yourself in the position of a general director of a train operating company, it is a mess. In the UK, path allocation is not public and transparent; fees not known; Eurotunnel, the cost is very great; path allocation in France—okay, now it is coming. The fees in Germany are very high. In Austria they are very low. It is not exactly an answer

to your question, I know, but the main problem is financing the infrastructure and the devices; the tools used now in every country are so different that the consequence for a train operating company is too difficult.

Q145 ***Lord Fearn:*** What about two-part tariffs?
Mr Falchi: In France, we have three parts! I am one of the designers of this system. I would say the problem is not one of two or three parts; the problem is if you have a fixed path, not related to a single path—so if you if you ask for a single path or 10 or 10,000 paths, if the price is obviously created in proportion of what you are asking for, it is not the problem; the problem comes when there is a fixed path, which was the French system two years ago. There was a not so low fixed path, and the consequence of this was that between A and B it was one price for SNCF, each path, and it was a very different price for the other competitors. This is unfair and discriminatory. You have to build your system in such a way that the path allocation is not a commercial business because, in the reverse, if your policy is that path allocation is a commercial business—in any business you can have a price for a big buyer and a price for a small one.

Q146 ***Lord Fearn:*** It does discriminate in favour of—
Mr Falchi: No, it is a commercial attitude. It is commercial behaviour. Of course, you can have a better price for big clients. Just to give you an example, if you go to your tailor and buy 10 suits, you do not pay the same price as if you buy one. It is exactly the same thing. If path allocation is not commercial business, in this case it is discriminatory. If it is a commercial business I am not so sure it is discriminatory.
Chairman: We will be coming to one of the possible consequences of the view you have just expressed later on.

Q147 ***Lord St John of Bletso:*** What is the scope for a level playing field in future on transparency on pricing, and what is pricing benchmarked against?
Mr Falchi: I cannot answer your question—I can give an opinion, but when you see what is happening in Brussels on the charging issue, a lot of very intelligent, clever, sound economic studies—more or less taken into account in the White Paper—say the infrastructure can be charged on a social cost analysis, but the Member State's policy—and this is the kernel of the issue—to finance infrastructure is so different from one country to another that I can see no common basis for the moment. If you want, you can trust in the new Commissioner who has said, "I will tackle this issue in a very practical and pragmatic manner"; but in my view if you want to transfer traffic from road mainly to rail, we have to make it simple for the train operating company, the big ones, the small ones and the new players. Of course the level of fees is important, but you, and Eurotunnel, are the worst of the class, because your fees are very high. If it is too high, you are out of the market. It is not only the charges, because the German Railways are speaking of this; it is the taxes. If you look at the VAT in Germany between Deutsche-Bahn and the low-cost airlines, the VAT is not the same. The low-cost airlines pay much less on fuel than the German Railways, so it is not an even charging of taxes. If the purpose is to shift traffic from road to rail, make it simple in the market at the European level: because I do believe that for rail freight the market is no longer for one country, it is at a European level and it is very difficult for them—too high, too complex, and not transparent.

Q148 ***Lord Haskel:*** Changing the subject to track capacity, we have been told that this is far from simple and straight. Can you tell us if the existing measures are sufficient to ensure a reasonable priority for international freight trains in the allocation of track capacity between competing operators so that they can plan their journeys and work to time?
Mr Falchi: If you mean between competitors, between freight competitors, I think the answer is "yes" because as far as I know there is the tax issue, but there is no discriminatory behaviour between freight companies. That is not the problem; the problem is how international freight traffic is treated against passenger regional traffic. This is the main issue. The study is not yet finished, but it could be interesting for you to know that on the Rotterdam-Milan corridor the ministries in Netherlands, Germany, Switzerland and Italy are doing a study to see how far this issue is real and how far there is real competition between passenger regional traffic and freight traffic. The answer is very obvious to any railwayman. In the main conurbations at peak time, and also around peak times, freight is limited by the speed and number of the passenger trains. Path allocation is such that there is no real priority for the freight train. To give you an example, it is almost impossible to have a train starting from Rotterdam or Antwerp from between 6 a.m. to 9 a.m. because passenger trains are coming all the time. The market needs more. Why is this? It is because in the path allocation process all these trains are put on the same level. The priority for an international freight train is the same level as for the passenger train. For regional passenger traffic it is like that in the UK—the legal contexts are not the same, but the result is the same. There is a contract between Member States, regional authorities and the train operating companies, and these contracts are for seven, 10 or fifteen years. If you change something in the contract which gives

more priority to freight, it could be a lot of worry in re-discussing everything, and the Member State authority in charge of this will do nothing. They will just say, "no train path for international freight". It is the same in a congested area. Of course, if you are in the middle of France, there is no problem, but in a congested area it cannot work. Is that clear?

Q149 ***Lord Haskel:*** Can anything be done?
Mr Falchi: Yes! It could, but it is so difficult. To solve the problem—this is a personal opinion, but it is an increasing opinion amongst the people involved—we need to reinforce or to go deeper into the details in Directive 2001, No.14 because it deals with path allocation and says very few things about priority rules. I think it has to be improved. It could be said, for example, that because the development of the freight market is international, because there is this kind of conflict between commuter trains and international freight traffic, one of the solutions could be that a greater share of a path is given to freight in advance, in a time frame for the freight operators, so that you have trains starting when the ships are there. You unload from the ships and put the containers on the train, and then they can go. If they wait hours or one day in order to start, of course when compared to road they will always lose. You have to have a path ready for this kind of traffic at the right time. This is impossible in the situation as it is. One solution could be that a share is given by law to freight, or reserved for freight; and if freight does not use the capacity it can be given to other competitors. If this reserve is not given to freight, it is impossible for them to have this path, because do not forget that you have to ask for a path one year in advance! The timetabling is such—look at Directive No.14—that it is one year in advance if you are to be sure to have a path. Of course, you can always ask now for a path tomorrow, but you have what is available, and if nothing is available you will lose. You have to reserve capacity for freight in advance. Of course, this will affect the capacity given to the passenger trains. In this case, Directive No.14 is such that the Member States propose increasing capacity, and it is very often easy to increase capacity for passenger trains, local passenger trains, much more so than for freight trains. You have to go deeper into this Directive. In addition, the time-scales are not the same. Freight traffic is either now, or in one week, or in one month. It is only regular traffic like automobile traffic between plants in Europe that is on a regular basis and can be designed one year in advance. Freight is very often on the spot, and on the spot you are the last to be served. It is only because of this time frame that the legal argument should be for the legislator to save capacity for freight.

Q150 ***Chairman:*** I only want a brief response to this question. Without in any way implying blame or fault, that implies that rail infrastructure managers like yourself find it very difficult to treat freight operators and freight operators' customers as customers. After all, if you really do have to book a path a year in advance to have a good chance of getting a path, that is an extremely inflexible situation for freight which, after all, is serving flexible industries. What you have told us so far is that, frankly, the system, for various reasons you have explained, means that people like yourself cannot manage capacity to meet the needs flexibly of the ultimate users of freight—the ultimate users.
Mr Falchi: You are right.

Q151 ***Chairman:*** That is not an issue of blame; it is an assessment.
Mr Falchi: Yes, you are right.
Chairman: That is extremely honest.

Q152 ***Lord St John of Bletso:*** You mentioned in your opening remarks that EIM is made up of independent members. Is the current legislation sufficient to ensure a strong independent regulator in each country? Obviously that regulator's role would be to ensure non-discriminatory access to the infrastructure, but also hopefully there will be more accountability and transparency on pricing for track access, to go back to my previous question.
Mr Falchi: We could say "yes" and "no", once again. You have at the moment organisation and path allocation process priority rules and charging which are very different when you look at the EU 15. It is very different in each country, from one country to another. As far as I know, from the legal viewpoint everything is compliant with the EU legislation because if it were not the case the Commission would have sued some Members' organisations. Of course, they do not like the way in which some railways are organised, but from the legal point of view everyone is compliant, although it is not the spirit of what is written. The UK example is quite different, and the German example is quite different. Take the Swedes: the separation is very clear between all the organisations. In my view, the legislation, as it is, is not clear enough and not detailed enough. It is most important to organise a good basis for train operating companies. In my last position in SNCF I was asked to explain how we at SNCF could be compliant and allocate paths in a very transparent and non-discriminatory manner. I can do this, but I know also how tricky it can be. Our organisation's view is that in the other Member States the independence of the infrastructure manager, in short, is not sufficient. The way in which the financing of the infrastructure manager is ensured is not sufficient everywhere. Even in France the process for allocating

paths is not so clear because RFF is the body that in the end will allocate the paths, but most of the job is still done by SNCF people. I fear that if the process stops here, it could be difficult in a few years' time because the Chinese wall between Deutsche-Bahn, DB Netz and DB Cargo—the Chinese wall, I can explain to you, is not an Internet Chinese wall—any information going to DB Netz goes straight to DB Cargo—of course. When you have a very complicated tariff charging issue, if it is not public and transparent, you can also have discriminatory behaviour.

Q153 ***Lord St John of Bletso:*** The answer is "no"; that the legislation is not sufficient—
Mr Falchi: In my view, if every country were to apply it in the same way in the same spirit, it could be sufficient; but the fact is that this is not the case.

Q154 ***Chairman:*** Is that because in each country there is not an independent and strong regulator?
Mr Falchi: Not a sufficient number.

Q155 ***Lord Shutt of Greetland:*** I wanted to come back to an earlier point before I come to my main question. I have been listening very carefully to you. When you mentioned the whole business of the Rotterdam-Antwerp-Milan route and the problem of passenger trains at about six in the morning to nine o'clock, what in your view has been lost to rail freight because you cannot get in at that time?
Mr Falchi: Lost to railways? I am not sure—

Q156 ***Lord Shutt of Greetland:*** What trade is likely to want to travel from Rotterdam and Antwerp to Milan that cannot go by rail because of the problems of congestion in those areas?
Mr Falchi: So many. This main freight corridor is the biggest corridor in Europe. There is a lot of traffic between Rotterdam and Milan. The market share for freight for rail is approximately 6 per cent. Everything goes by road, on the motorways. Just to give an example, millions of intermodal units are going from Rotterdam to Germany, and then to Switzerland and eastern countries, and then to Milan and the north of Italy. This traffic is continuous. I do not have the figure in mind but the market share for rail is 15 per cent—very little of it—and it is decreasing every year. Previously it was because no train company was operating from Rotterdam to Milan. Things are changing because you have to change locomotives at the border, and you change driver—you re-start. It is the same thing in Germany: you change two or three times and then in Switzerland once or twice; and then you go into Italy. Now, because they are more or less competing, you can make the journey with one or two train operating companies. They have increased the speed, the efficiency. This is coming. But the paths are not there—that is all. If you ask for a path, you can ask but you get nothing.

Q157 ***Lord Shutt of Greetland:*** I have to move on, but at some point could you give us a list of the traffic that wants a path but cannot get one. That would be helpful to us. You have mentioned the whole business of changing engines and that sort of thing, and one of the points that we have been considering is interoperability. It sounds a good idea, but will it raise costs and reduce competitiveness for rail freight if people have got to invest in technology which is suitable for here, there and everywhere in terms of all the different countries that locomotives might go through, or the whole business of signalling and so forth? Will it not be an expensive thing and put prices up?
Mr Falchi: My last position in SNCF was to be seconded to the European Association for Railway Interoperability (AEIF), the body in charge of writing the technical specification for interoperability. I have two answers to your question. First, we need interoperability because we need locomotives that can go from Wembley to somewhere in Germany, and then overland from there. It depends on the companies, but one-quarter or more of train freight operating costs are locomotives and drivers. The freight business is mainly an asset management business because you have huge assets—locomotives and drivers. Asset management within national borders is less and less profitable and will become less and less profitable. So for the freight market interoperability is needed, but that does not mean—and it is a problem—mandatory technical harmonisation on everything. On your question on the control command signalling—TSI—of course it is a big discussion at the moment in Brussels with all the trade bodies, the Commission and the Member States, because they tried to make mandatory the implementation of a new signalling system for all trains, locomotives and all infrastructure. The cost is very high—you are right. If you compare the cost of locomotives to this cost of this device—because you have to put the computer on with a lot of things around—the cost on average could be €250,000 and if you compare that to the cost of the locomotive it is not so big. With this cost you can increase your market because instead of running your trains only within the UK, you can go to Germany, Austria and Hungary; so you can benefit from interoperability. My feeling is that without the control command and signalling systems, TSI is the most costly of all, it is impossible to cross the border. You have to change locomotives at each border. Increasing your market is impossible, but you need it. In my view, because the main focus is the train operating company we have to implement it in

a way which is the most profitable for them, which means that it is not mandatory—but it is never mandatory because Article 7 of the Interoperability Directive says that you can always, based on competitive analysis, say, "this would not be mandatory for me", and even if it is mandatory in the EU legislation, you can apply Article 7 of the Directive. That is the first thing. The second thing is that because the same locomotive can run on the UK network and in Europe on a line equipped with this device, we, as infrastructure managers, implement the system as fast as possible because then the lines will be open more quickly for competition of locomotives running from A to B. At the same time, we have to implement this device in super position to the existing device in order that people running locally or nationally, can continue to operate with their trains. Do you understand what I mean? The benefit can be there, not only in terms of cost; but to be there we have to implement the system on a lot of lines.

Q158 ***Lord Walpole:*** I assume you work on railways because you want them to continue working, but how do you view the prospects of international freight traffic, particularly traffic passing through the Tunnel; and what needs to be done to make it successful? You have got to, do you not? That is a fact. We cannot go on having lorries chuntering around our main roads; we have got to get them on to long-distance trains.

Mr Falchi: Eurotunnel is a problem in itself because to carry a container from A to B by crossing the Channel is much more expensive by train, due to Eurotunnel fees, than by any other means. It is a problem for the UK particularly, but also for others. If we forget the Eurotunnel case, my view is not an optimistic view. My view is that freight—rail transport—will collapse very quickly if some of the measures we have spoken of during this afternoon are not undertaken. To gain market share, we need train operating companies doing similar things at the European level. Only one or two are doing it. The business-oriented companies, the UK companies, are for the moment stuck in the UK, they are not going outside the UK. To go outside their own country everyone needs either to tackle the differences of the technical system or, better, implement TSI interoperability. This needs very quick and efficient measures now, but also a path allocation process which is fair for freight. We need changes in the way things are implemented and business is done. I am not very optimistic for freight traffic—not at all.

Chairman: If I may say so, that is a frank and possibly a realistic view. Of course it is not where the Commission hopes rail freight will be, but it is a view that you feel we need to hear. Mr Falchi, you have been very generous with your time, and far from being concerned about your English at all, you have demonstrated a superb ability to communicate some complicated thoughts and ideas. We are most grateful to you for that.

Memorandum by Community of European Railway and Infrastructure Companies (CER)

Introduction

The Community of European Railway and Infrastructure Companies (CER) is grateful to have been given the opportunity to present evidence to this House of Lords inquiry. The main document responds to the specific questions before the inquiry; two annexes provide more detailed evidence on the subject.

This evidence is provided on a corporate basis.

CER brings together 36 railway undertakings and infrastructure companies from the European Union, the accession countries (Bulgaria and Romania) as well as Croatia, Norway and Switzerland. It is based in Brussels and represents its members' interests vis-à-vis the European Parliament, Commission and Council of Ministers as well as other policy makers and transport actors. CER's main focus is promoting the development of rail as essential to the creation of a sustainable transport system which is both efficient and environmentally friendly.

CSR's membership has increased in recent times, through separate railway infrastructure companies (created after the first railway package) and further private train operators joining the organisation.

1. *What are the current barriers to entry in the international rail freight market?*

1.1 In terms of European legislation, the first railway package opened the market from March 2003 for international freight operations on the defined Trans-European Rail Freight Network. Progress on implementation by Member States has however been quite uneven.

1.2 The second railway package, adopted in April 2004, goes on to open the whole European rail network, first for international traffic from January 2006 and then to national traffic one year later. Thus all remaining direct barriers to entry will in principle be removed in less than thee years' time.

1.3 CER would like to emphasise its commitment to the overall aims and principles of EU transport policy, and to acknowledge the progressive liberalisation of the rail sector.

1.4 However, European legislators have recognised that other, more practical, barriers exist, both for new entrants and for existing railway companies intending new approaches to international rail freight services in an enlarged EU. The second railway package included a Safety Directive whose principal objective is to tackle—through the establishment of a railway agency within the same legislative package—the problems created by different railway safety management approaches—methods, safety targets and safety management systems—that are frequently controlled by national safety authorities as much as by railway companies themselves.

1.5 The second package also recognises that the process of interoperability development—the progressive harmonisation of railway system design—cannot be achieved by the railways and the supply industry alone. The railway agency will bring together rail expertise and Member State representation to tackle the political and financial challenges presented by such widespread system change.

1.6 These practical barriers will remain for the near future. Recognising the nature of the task, the second railway package sets time-scales that vary between five and seven years for completion of the work described earlier. Until these issues are resolved, it will remain a practical challenge to obtain safety certification and rolling stock approval for the flexible geographical application intended by EU transport policy.

1.7 CER welcomed the adoption of the second railway package, and contributed actively to the resolution of the legislative process. The Agency now needs time to complete its work, and to be successful, in the interests of all freight operators in a liberalised market.

2. *To what extent are these barriers the result of a failure fully to implement existing EU Directives in all Member States?*

2.1 It is clearly too early to assess the implementation, let alone the effect, of the second railway package in light of the compliance and stage dates set in the legislation.

2.2 In terms of the first package, this question is really a matter for the Member States, as they are responsible for implementation. CER understands that there has been delay in the process. It is not clear to CER whether this phenomenon is limited to railway legislation or whether it is symptomatic of a wider problem.

2.3 As far as CER Members are concerned, it is a generally held view that an improvement in the discipline with which legislation is enacted would be welcomed, as this would bring clarity and certainty to the framework within which business plans can be developed.

3. *Is further action needed at European Union or Member State national level to ensure enforcement of EU Directives?*

3.1 CER has no comment to add to those made in question 2.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

CER would like to consider this question in two ways.

4.1 Firstly, CER strongly believes that the railways have been the object of sufficient rail-specific legislation in recent years. As described earlier, it is clear that the successive first and second railway packages will effectively overlap with each other during their implementation. The third railway package, proposed in Spring 2004, includes a final proposal—on European train crew certification—to tackle a practical obstacle to freight liberalisation.

4.2 No more rail-specific legislation is needed to create the basic framework conditions for liberalisation.

4.3 *Annexe 1* to this submission sets out CER's general philosophy in respect of freight liberalisation and illustrates that competition exists already between operators on Europe's railways. The railways have for some years now been required by European law (Directive 91/440) to operate according to normal business principles; as well as the existing intramodal competition referred to in *Annexe 1*, they have long had to face fierce market competition from road and other transport modes.

4.4 The railways need to continue adapting to the new legal framework without further rail legislation. CER is therefore very concerned that further rail legislation is proposed by the Commission—in the form of a prescriptive regulation on rail freight contractual commitment obligations.[1].

4.5 While CER absolutely understands the principles of contracting for quality and the need for customer focus in a competitive environment, a standard regulation intrudes into the commercial relationship between freight customer and supplier. It is very hard to reconcile this approach with the practically simultaneous policy objective of liberalisation.

4.6 CER therefore calls for the Commission's proposal to be rejected. *Annexe 2* contains a more detailed explanation of CER's position on the proposal.

4.7 Secondly, the question before the House of Lords Inquiry points to the need to make the policy of introducing competition to international railfreight more effective. CER believes that the effectiveness of the policy should be judged against overall transport policy objectives, of shifting the balance between transport modes in favour of more environmentally friendly modes that support sustainable development.

4.8 In this context CER feels strongly that further transport legislation is necessary to shift the balance and give rail—whether new or established operators—a fairer competitive position, in particular against road freight transport. CER has for some time been pressing for EU legislation on the crucial issue of infrastructure access charging for all transport modes. Rail is currently the only mode required by law to raise comprehensive system access charges, under the principles of Directive 91/440 and the more detailed terms of the Directive 2001/14 in the first railway package.

4.9 It is therefore very disappointing that there has been so little progress with the specific measures set out in the European Commission's 2001 Transport Policy White Paper. There is no sign of the framework Directive on cross-modal charging principles proposed in the White Paper, and progress on the Eurovignette Directive for road freight is deadlocked, despite the fact that the current proposal does not fully address the stated aims of the White Paper.

4.10 Urgent political action and EU legislation is needed on both of these measures.

4.11 Finally, there remains the headache of funding, in particular for rail infrastructure. CER welcomed the final resolution in April this year of the revision to the Trans-European Transport Network Guidelines and funding rules. The inclusion of 21 rail projects in the Guidelines underlines the importance of international rail freight to the Community's transport policy objective.

4.12 While this is perhaps less a case for further EU legislation, progress on these priority projects is vital, to start tackling the capacity issues that will seriously inhibit any growth occasioned by the policy of freight liberalisation.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth in international rail freight as a result of this policy?*

CER would comment here on two issues for action, in addition to the points made earlier in this document.

5.1 Firstly, there is a very specific problem for international rail freight to and from the UK, in the shape of Channel Tunnel access charging. CER understands that, as things stand at present, UK financial support for the Eurotunnel access charge will not continue beyond the general time-scales for full freight market opening established within the second railway package. This is an acute example of wide variation in the level of access charges payable in various parts of the EU, and one which will surely present a serious commercial obstacle to any international freight operator.

5.2 Secondly, it is worth mentioning the need to establish clear and effective national capacity allocation priorities for international freight traffic. This will be particularly important on the very busy railway network in the southeast of the United Kingdom.

Colin M Hall
Deputy Executive Director CER

August 2004

[1] Proposal for a Regulation of the European Parliament and of the Council on compensation in cases of non-compliance with contractual quality requirements for rail freight services—COM(2004) 144.

Annex 1

Fierce competition has always existed between SNCF and DB for the very strategic Benelux-Italy flows, where each operator developed commercial strategies to attract flows on their respective side of the Rhine. Similarly, SBB, Trenitalia and Railion are still competing strongly with each other for traffic between France and Eastern Europe. On a smaller scale, SNCB and SNCF have often competed for flows from Antwerp to the south of Europe in order to attract tonne-kilometers on the itineraries most favourable to each one. Similarly, SBB and SNCF are still contesting the route to be taken by the UK-Italy flows. "Strategic route management" has always been and still remains a major weapon for competition between long-established companies.

In addition, it is to be noted that the biggest companies do not hesitate to enter into direct competition on each other's territory. One of the most significant examples of this phenomenon is the association between the Swiss historic operator SBB Cargo and the German private railway HGK into Swiss Rail Cargo Germany, which operates trains between Switzerland and the Netherlands in direct competition with the German operators (including Railion). SBB Cargo also competes with the Italian operators (including Trenitalia) through its Italian branch Swiss Rail Cargo Italy.

Mirroring the SBB Cargo–HGK joint venture, Railion Deutschland, through its association with BLS Cargo, is now operating freight trains in Switzerland.

On their side, Trenitalia Cargo have entered the German rail freight market through a stake in the German private operator TX Logistics.

Liberalisation has Stepped Up Since 15 March 2003

This process of co-operating with small local operators from foreign countries is the way which most railways (state-owned or private alike) have chosen to tackle new unknown markets. Although this way of proceeding looks seamless from the outside, it is quite clear that, in effect, historic railways have definitely entered into competition with each other. Acquiring or forming an association with small local actors is a common strategy used in all types of businesses in order to get acquainted with any new market.

This common approach may partly explain why a company like Railion has not yet ventured into the French market. The non-existence of smaller operators in France makes it indeed more difficult for a foreign company to acquire the technical know-how and market knowledge to enter such a big market. However, even in France, concrete signs can be seen, notably with the first railway licence granted to Eurotunnel this year. Eurotunnel is now applying for a safety certificate from the Channel Tunnel down to Italy. On the passenger side, DB is testing its ICE high-speed train on French tracks.

Being the preferred approach developed by the market forces to acquire the necessary skills and know-how on foreign territory, the "merger and acquisition" process now seems to be the way ahead. However, once this is done, the competing railway may even push the experience further so as to run its own trains end-to-end into foreign territory. This is the case of Railion Deutschland, which is starting to drive into Switzerland, building up on the experience acquired in its association with BLS Cargo.

What Lesson can be Drawn from 15 March 2003? Competition, Alone, will not Bring About Modal Shift!

As a result of what has just been described, today, more than 60 per cent of the European rail freight market is exposed to competition (partly via new entrants, but mostly through historic companies competing with each other). This is not, however, without some difficult consequences and the much expected modal shift is far from being the result of this phenomenon.

Indeed, not surprisingly, the new entrants have taken positions on the most profitable flows (block trains on major corridors and shuttle services between industrial sites). This "cherry-picking" strategy has obliged historic operators to concentrate on the traffics at risk, leaving aside other less strategic ones. In addition, the obligation put on historic railways by the European Union and National Authorities to balance their accounts and possibly make profits has led them to concentrate on their core traffic. As a result, the least profitable traffic (single wagonload and other less-than-trainload traffic) tends to be neglected or simply given up. This obviously works against the development of rail freight and was not taken into account by the legislator when opening up the international market.

In addition, the infrastructure bottlenecks and the often very high cost to pay for infrastructure access and use does not encourage rail operating companies to stick to their least profitable, nevertheless useful (from a socio-political point of view) traffic. Politicians, however, expect rail freight to take a major place in the transport world of tomorrow. Therefore and far from asking the European Union and the national governments to rule over the railways, as in the old days, CER pleads for more political attention to the very crucial issue of rail infrastructure. In this regard, and considering the longstanding investment gap existing between rail and road since the war, the revision of the TEN guidelines can only be seen as a first (yet encouraging) step. A lot remains to be done!

CER Statement on Rail Freight Liberalisation 11 March 2004

Competition has never been a foreign concept in the railway world, as the railways have always been exposed to heavy competition from other modes (especially from road). In addition, and contrary to common belief, in most Member States, intramodal competition in rail freight has been a reality for quite some time! The official opening of the international rail freight market on 15 March 2003 did not therefore mark as much the start of the process of liberalisation as another important milestone on an historic and sometimes long-started journey.

Before 15 March 2003, the Railways were Already Subject to a "very multifaceted" Intramodal Competition

It is obviously hard to avoid mentioning first the much-quoted example of Germany, where the co-existence of private operators alongside the state-owned railway has always been true. On 15 March 2003, among the 150 private operators or so operating freight trains in Germany, 10 were already considerable in size.

Great Britain, Sweden, the Netherlands, Denmark, Italy, Austria (and Switzerland, outside the Union) are other examples of countries where private operators were already present well before 2003.

As a result, competition has already been quite fierce:

— on major rail freight corridors such as the North–South corridor through the Brenner,

the North–South corridor through the Gotthard–Lötschberg,

the Rotterdam–Milan Corridor,

— and within some countries: UK, Germany, Sweden. the Netherlands, Austria

Historic Railways are also Competing Strongly with each Other

On these major corridors or wherever other profitable traffic can be identified, older private companies (like HGK[2] or Connex Cargo Logistics) and new entrants (like FNME[3], RTC[4] or Shortlines) have been an important factor for increased market dynamism.

However, it should not be ignored that the most significant potential for competition falls, and will mostly remain, in the hands of major operators.

Examples of Rail Freight Competitors in the EU (before May 2004) + Switzerland

— This list is not exhaustive: only companies with the most significant freight volumes are listed (for example in Germany, only a few of the 150 companies operating freight trains today are listed). Strictly local companies are not included.

— All companies possess and use safety certificates to operate domestic and/or international Freight Trains.

— Major historic companies (whether still state-owned or privatised) are underlined.

[2] HGK: Häfen und Güterverkehr Köln GmbH.

[3] FNME: Ferrovie Nord Milano Esercizio.

[4] RTC : Rail Traction Company.

GERMANY	AUSTRIA
Connex Cargo Logistic	Cargo Serv, VOEST Logistik Service GmbH
B-Cargo—SNCB (through Rail4Chem)	GKB—Graz-Köflacher Bahn
ERS—European Rail Shuttle	Lokomotion
HGK—Häfen und Güteverkehr Köln	LTE
Mindener Kreisbahnen GmbH	**Rail Cargo Austria**
RAG Bahn und Hafenbetriebe	**Railion Deutschland** (through Lokomotion)
Rail4Chem	RÖEE AG
Railion Deutschland	RTC (Rail Traction Company)
Städtische Hafenbetriebe Neuss	Salzburger Lokalbahn AG
SBB Cargo (through Swiss Rail Cargo Köln)	St + H Stern and Hafferl
TraXion A/S	Steiermarkbahn Transport
Trenitalia (through TX Logistik AG)	StLB Steiermärkische Landesbahn
TX Logistik AG	**Trenitalia** (through LTE)
Verkehrsbetriebe Peine—Salzgitter GmbH	WLB Wiener Lokalbahn AG
Wanne-Herner Eisenbahn und Hafen GmbH	Zillertaler Verkehrsbetriebe AG
Westfälische Landes-Eisenbahn GmbH	
Württembergische Eisenbahn-Gesellschaft mbH	
NETHERLANDS	UNITED KINGDOM
ACTS Nederland B.V.	*Advenza (Starting)*
D&L—Dillen & Lejeune	Direct Rail Services
ERS Railways	**EWS—English Welsh & Scottish Railway**
Rail4Chem	**Freightliners**
Railion Nederland	Freightliners Heavy Haul
Railion Deutschland (through Railion Nederland)	GB Railfreight
Shortlines	
SWEDEN	ITALY
CargoNet (through RailCombi)	DFG—Del Fungo Giera Servizi Ferroviari
Green Cargo AB	FNME—Ferrovie Nord Milano Esercizio Rail Italy S.r.I.
Inlandsgods AB	**Railion Deutschland** (through FNME & through RTC)
Malmtrafik i Kiruna AB	RTC—Rail Traction Company S.p.A.
Orsatåg AB	**SBB Cargo** (through Swiss Rail Cargo Italy)
Railion Denmark	**Trenitalia S.p.A.**
RailCombi	
Shortlines Väst AB	
Skövde-Karlsborgs Railway	
TGOJ Trafik AB	
DENMARK	FRANCE
Hads-Ning Herreders Jernbane	**SNCF Fret**
Lemvigbanen-Vemb-Thyborøn Railway	*Eurotunnel (coming up)*
Lollandsbanen	*Rail4Chem (coming up)*
Nordjyske Jernbaner A/S	
Railion Denmark A/S	
Railion Deutschland (through Railion Denmark)	
Vestbanen (Arriva Tog A/S)	
BELGIUM	LUXEMBOURG
B-Cargo—SNCB	D&L Dillen & Lejeune
D&L (Dillen & Lejeune)	**EuroLuxCargo (CFL)**
SWITZERLAND	
BLS Cargo	**Railion Deutschland** (operating trains on their own)
Hupac	**SBB Cargo**
Railion Deutschland (through BLS)	etc . . .

Annex 2

PROPOSED REGULATION ON RAIL FREIGHT QUALITY[5]

POSITION[6] OF THE COMMUNITY OF RAILWAY AND INFRASTRUCTURE COMPANIES (CER)

1. *The European Commission's Proposal*

The published proposal is concerned with the setting up of a mandatory system of penalties for rail freight services. It includes provisions on liability, penalty levels and monitoring schemes.

2. *CER's assessment of the proposal*

2.1 General

CER is firmly committed to freight quality improvement: but is strongly opposed to the Commission's proposal. CER questions the legal basis for such an initiative, which discriminates against rail compared to other competitive transport modes.

Far from achieving its alleged purpose of encouraging a modal shift from road to rail, this Regulation, should it be adopted, would simply overburden the rail system administratively and financially, to the extent of actually deterring some existing and potential customers from using the rail mode. Experience already shows that compensation systems imposed by law do not of themselves improve quality, much to the contrary (see the British case).

This intervention of the public authorities into what usually pertains to normal business life harks back to the "old days" (when the railways were fully state-run) and is quite difficult to understand one year exactly after the "liberalisation" of the rail freight market (the precise purpose of which was to "deregulate" the rail freight market and "get rid of administrative constraints"). Furthermore, the existing international legal framework provided by the CIM[7], which is applicable (beyond the European Union) in 41 countries, already imposes rules on the railways which are twice as strict as those applicable in the road sector: this renders an even stricter—by six times—and potentially conflicting Regulation all the more unnecessary.

2.2 Responsibility for rail freight transport quality

In the railway sector (and probably more than in any other transport modes), responsibilities for quality are multi-layered, involving several actors of the transport chain from the Customers themselves through Railway Operators to Infrastructure Managers (and, beyond, as far as Public Authorities). Each of these actors plays a part in the quality delivered to the end customer; each of them depends heavily on the others to achieve the desired end result. Also each of them, notably those closest to the customer, are unambiguously committed and firmly determined to use and control quality as one of their major marketing arguments and as an essential tool of competitive differentiation in their commercial strategy. Against this background, CER is very concerned about the Commission's intention to set up a compulsory system of penalties on the layer which is most vulnerable and most dependant on the others, namely the "customer-operator" layer.

2.3 CER initiative on freight quality

The move to "regulate back" the rail freight sector also seems to conflict with the European Commission's apparent support up to now for the railways' own endeavours to take up full "entrepreneurial responsibility" in the field of freight quality, in particular through the implementation of the CER-UIC-CIT[8] Freight Quality Charter (adopted on 4 July 2003). It is all the more surprising as this voluntary commitment of the railways has, in the context of the railways' ongoing process of quality improvement, already brought about visible changes after only six months, and led to a substantial increase in the number of quality agreements signed between railways and customers. The European railway community therefore sees the proposed Regulation as a definite step backwards after the progress brought about by previous legislation.

5 Regulation of the European Parliament and of the Council on compensation in cases of non-compliance with contractual quality requirements for rail freight services—COM(2004) 144.

6 Extracted from the CER Position paper on the Third Railway Package, published in May 2004.

7 CIM: Convention Internationale Marchandises (regulations governing the international transport of goods by rail).

8 UIC—Union Internationale des Chemins de Fer, Paris (the world-wide railway association responsible for improving interoperabilty and co-operation between railways on technical and commercial matters)
CIT—Comité International des Transports Ferroviaires, Bern (the railway association responsible for the legal framework for international passenger and freight rail transport).

2.4 Impact on costs and competition

From an economic analyst's point of view, it is quite clear that the proposed Regulation would have a profound impact on the economy of freight in general and of rail freight in particular.

Regarding the cost aspect, an evaluation of its actual economic impact on operations is currently being carried out. At this point in time, it is however already possible to say that the cost associated with the implementation of such a Regulation could lead to substantial price increases and could seriously distort the competitive situation of rail towards road (which would not be subject to the same regulatory straightjacket). In the "worst case" scenarios, a significant part of the total rail freight revenues would be absorbed, severely jeopardising the economic viability of rail freight as a whole. It is therefore important that, before taking definite decisions, the political stakeholders are well aware of the potential harmful cost implications associated with such a far-reaching Regulation.

2.5 Impact on infrastructure management

As the railway system is susceptible to secondary (knock-on) delay, the effects of the Regulation are not isolated to freight. In practice therefore the Infrastructure Managers would need a comprehensive regime to analyse delays and recover penalties from other Railway Undertakings, as well as accounting for payments for infrastructure delays. While such regimes exist (for example in Great Britain) experience has shown that this would almost certainly lead to further transaction costs, a proliferation of internal disputes and even legal action, without necessarily improving performance. All these extra costs would be a drain on resources which would be much better used in effectively improving quality.

There is also a likelihood that, to minimise claims from Railway Undertakings, Infrastructure Managers would seek extra pathing or recovery time for delayed trains. This would inevitably result in a decrease of the availability of infrastructure capacity, the opposite of what is required to achieve transport policy goals. This problem would be particularly acute where low access charges have been introduced to encourage modal shift and capacity has been stretched.

2.6 Impact on customers and rail freight growth

From a strict business point of view, as saturation is already apparent on many parts of the European rail network, severely limiting the potential for quality improvements, the proposed Regulation would lead existing operating companies (whether historic or recent) to reduce their freight activities in order to relieve congested areas and automatically improve quality (thus avoiding penalties). They would also be encouraged to concentrate on regular domestic flows for which production processes can be better streamlined and secured, leaving aside more diffuse "production-disruptive" ones (single wagonload traffic and other non-regular flows in block trains) and a large number of international flows (carried out through a chain of subsequent carriers). Alternatively, as already mentioned above, they may increase their selling prices to integrate the risk of having to pay penalties. In both cases, the effect would be a reduction of rail freight.

In this context of traffic reduction, the already narrow margin of the freight operators would be further reduced, as the marginal cost of the use of the most capital-intensive resources (locomotives, wagons) would increase, encouraging operators to gradually disengage from rail freight (and put the smallest, most recent ones out of business). On this background of threatened margin, potential newcomers would be deterred from entering the rail freight market, resulting in an adverse effect on the development of intramodal competition expected by the European Commission and most actors on the market.

In the end, all this would obviously limit the customers' ability to choose between various operators and products. Having little regard to individual customers' needs and expectations, the proposed Regulation forces all customers into the same regulatory straightjacket. Especially, those customers who place more importance on price than on performance will simply no longer be able to afford rail. Regulation will deprive the market actors of their ability to use "quality" as a marketing tool of competitive differentiation and of their natural capacity to regulate quality through contractual agreements. In this respect, the proposed Regulation heavily restricts contractual freedom and Article 71 of the European Treaty referred to in the text does not seem to provide a convincing enough legal base to justify such a heavy EU intervention into contractual freedom.

2.7 Customer reaction to the proposal

More generally, CER regrets that, in developing this Regulation, the European Commission has not taken into account the reservations of most customers, who were far from unanimously supporting such a heavy intervention into the natural functioning of the market at this point in time but were rather in favour of leaving more time to the railways to implement their Quality Charter.

2.8 Conclusion

For all the above reasons and on the basis of a number of other more detailed technical points (which CER is ready to provide to those interested in this issue), CER strongly opposes the proposed text and seeks its rejection.

Examination of Witness

Witness: Mr Colin Hall, Deputy Executive Director, Community of European Railways (CER), examined.

Q159 ***Chairman:*** Good afternoon, Mr Hall. Thank you very much for coming and for the evidence we received from CER, we are very grateful to you for that. I am sorry we are a little late in taking your oral evidence and I do apologise. We have until around 10 past six, I fear, and as we are running a little late, we only have forty minutes. I hope we can get through matters expeditiously. Is there anything you would like to say to us before we start throwing questions at you? Can you tell us something about the membership of CER?
Mr Hall: There was a very brief summary on the CER in the evidence that we submitted, but certainly, I will add a little more to that. The membership is a combination of different types of railway companies across the EU and, indeed, outside the EU to include some of the current accession countries, for example Bulgaria and Romania. We have a combination of membership which ranges from what we call the integrated conventional railways, the major railways of Europe, the DBs and SNCFs of this world, to the new small operators, the most recent example of that being Connex, the freight and passenger train operator. Very shortly, we will have railway undertaking—as we call them—membership in all of the EU countries. The Swedish Association of Train Operators will be joining CER within the next month. On the infrastructure side, we have the infrastructure management elements of the conventional integrated railways. I can go into more detail about that if you would like? Also, we have membership of the separate infrastructure management companies which were created by the new Member States in a number of cases, that in the Czech Republic, Slovakia and in the accession countries, Bulgaria.
Chairman: That is very helpful. Thank you.

Q160 ***Lord Fearn:*** Good afternoon, Mr Hall. In your written evidence, you referred to the quite uneven implementation of the first railway package across Members States. What needs to be done to correct this?
Mr Hall: That is an interesting question to put to us. I must say that the answer to this question was written earlier in the summer, when I think the evidence of progress might have been a little less than it is now. I am slightly embarrassed to sit in front of this Committee and see from the evidence of statements from the Commission that, technically, the UK has not yet transposed the first railway package. I think the main issue is one of principle. If you are trying to introduce quite a fundamental change in the way the railways are structured and operate, and that is the intention of the legislation, then it seems to be to everybody's benefit if we can all move forward at the same sort of speed; and with the knowledge that we are facing the same conditions in different countries. As an European association, we see the disadvantages in the present state of affairs where legislation is slow to be implemented. However, on the situation as I think it stands now on the first railway package; if you look at the countries where, technically, it has not been completely transposed, then I think it is slightly ironic that the United Kingdom, Germany and Austria (which is in a transition phase) do have an amount of competition on the tracks already. On reflection, we would want to think about just how significant the uneven implementation was.

Q161 ***Lord Fearn:*** I do understand how difficult it is, but if you have any other thoughts, please let us have them.
Mr Hall: The only common sense thought that comes to me is that members of the EC Rail Committee from the Member States who do have a good record of compliance with European legislation, should use whatever powers they have in their relationships with the European Union to press for the same sort of progress elsewhere. I know that is a rather general answer, but I am not a parliamentary procedural expert and I cannot tell you exactly how to do it.

Q162 ***Chairman:*** When you refer to CER membership, you talk about traditional integrated rail companies.
Mr Hall: Yes.

Q163 ***Chairman:*** Is that not an absolute contradiction to the first railway package and is the idea splitting up the infrastructure and train operations?
Mr Hall: No, it is not.

Q164 ***Chairman:*** How can you have a traditional integrated business if they are supposed to be split apart?

Mr Hall: Providing that they do comply with the legislation, and they do, which requires that there is accounting separation, then there is nothing illegal about the structures that are in place. In referring to those kinds of railways, I use the shorthand for describing what are the well-known operators on the European railway scene. I was not in Brussels at the time when the infrastructure package, as it was then known, was negotiated. What finally came out of the infrastructure package did not mean that companies could not operate on a so-called integrated basis. If you take the German model, the Deutsche-Bahn model, you have a holding company and you have an infrastructure management department as a separately organised and accounted operating unit. Deutsche-Bahn are very sensitive about their competition position, which is not surprising as they are the biggest rail operator in Europe. They also have the largest number of railway frontier points as well; so in a sense, they are sensitive to international relations.
Chairman: I am very sceptical of that view, I have to tell you, but it leads us very neatly on to Baroness Eccles.

Q165 ***Baroness Eccles of Moulton:*** Good afternoon, Mr Hall. You described to us your huge membership, which obviously has many varying vested interests in their own particular part that they play in European railways. The question is how do you regard institutional separation of infrastructure from operations as necessary to achieve non-discriminatory access to the rail infrastructure and, is it achievable, bearing in mind what you have told us?
Mr Hall: I do not believe it is essential. The process of change started in the 1990s, but there has been very little evidence to suggest that one particular model of managing and operating structure in the railway is, in fact, more effective than any other. There are three or four companies that have moved to the holding company model, as opposed to full separation; but if we look at some of those countries: if we look at the German situation; the Austrians are moving to a holding company model from the 1 January; and we have the same sort of thing in Italy. I represent all CER members but I think the best thing I can say is that I do not see any particular disadvantage to competition there compared with some other countries—where we also have members—where, in fact, there is full separation of the infrastructure management and train operation companies. I simply do not see the evidence that says full separation is the best way to liberalise the railways.

Q166 ***Baroness Eccles of Moulton:*** If we are going for a full and believable liberalisation, is it not very tempting for vertically integrated companies to give their operators a small advantage over other people wanting to use their tracks?
Mr Hall: It is easy to make that sort of presumption, I can understand that, and there is an element of common sense in thinking that that might be the case. But in reality, these companies have to comply with the law. I do not just speak for European law, but for national law as well. The companies that are structured in the way that we now see them operating are extremely sensitive to that. In CER, we have copies of reports produced on the status of competition within Germany as an example. I do not know if you have seen anything of that sort, you probably have: but if you have not, I would be happy to provide a copy. They know that, as a large organisation, they have to be transparent in the way they deal with, and fulfil, their obligations. I guess, from time to time, things will happen, there will be "skirmishes in the woods" where, for whatever reason, you end up with things not being managed as smoothly as you would like. It does not mean institutionally the organisation is against the objectives that are set for it.

Q167 ***Baroness Eccles of Moulton:*** If this is reality as opposed to aspiration, then we are a lot further along the road than I had imagined.
Mr Hall: I think there is some way to go. Part of the reality is that the freight market liberalisation and in particular the full legal opening by 2007 is not yet with us. It may be the case here in the UK: but it is not yet with us in the rest of Europe. In the negotiations over the second railway package, our Association did play a part in helping to negotiate a compromise over the timing of the market opening. We keep saying—and I ask you to accept this as a sincere position—that we are not against liberalisation. The railways have to compete; and in fact for want of other competition, they have started to compete with each other now, in advance of Europe-wide legislation. You find the Italians, the Swiss and the Germans all getting into contracts on what you might consider to be each other's "patch". The reality is that the network, if you take the German example, is open in practice.

Q168 ***Chairman:*** Let me take an example. In a country where you have a large track operator and a large train operator, if a relatively small competitor train operator discusses with a major user of rail freight a possible contract to shift freight, and that company went to the track operator to discuss possible paths and so on, and then a week or two later the rail company, which was part of this integrated business, somehow magically learns of this and goes to the original business that wanted freight moving, and unbeknown to the small competitor knows all about the discussions that are happening, do you not

think that would be worrying? Surely there is a problem with integrated companies because anybody who wants to compete with the train operators has got to go and discuss commercial confidential information with a track operator. Are you saying that problem never arises, because I can tell you we have had evidence that it does. Would you be worried if that happened?
Mr Hall: I think I would be concerned. As I said earlier, I think when you are making change, there are going to be steps and stages you have to go through before the situation matures.

Q169 ***Chairman:*** You are saying you are happy with the situation as it is, you do not think they should be split? If you were a small train operator and you wanted to break into a cheaper market, would you be happy that you have got to go and have discussions with the rail track company that is part of the same group as your principal major operating competitor? Would you be happy to do that?
Mr Hall: If I knew I had the rights and my opportunities were protected under the law, then it would depend on the business that was on offer.

Q170 ***Chairman:*** Do you think they are properly protected under the law at the moment?
Mr Hall: Yes, I think they are. They have rights and there are railway undertakings that have exercised those rights, when things have not gone in the way they would like. They have protection.

Q171 ***Lord St John of Bletso:*** My question leads on from that. In your written evidence you mentioned that over 60 per cent of the European rail freight market is exposed to competition and you spoke about the cherry picking, the strategy of operators and more possible traffic. How important do you regard a strong independent regulation as a way of ensuring fair play between the competing operators?
Mr Hall: I do think that is very important. I do not want to give too simple an answer, but clearly that is one way in which this potential risk of imbalance can be dealt with. Again, the concept of a regulatory body was introduced with the first railway package. I think the comment I would make—and maybe this is me drawing on my thinking in regard to the UK—is that, when we talk about a strong regulation perhaps the best way that process can operate is if the Regulator sets the framework within which the industry parties can do their business, and do it in a fairly transparent and non-discriminatory way. I think it would be a sign of failure if every single instance where there was suspicion and concern was ending up with a regulatory body. A scenario where the regulator is actively involved in approving the "rules of the game", the codes of business practice that have to be applied by the parties in the industry, (and, indeed, approving any changes to them) allows the industry to take a better hold of its own destiny but still with the assurance of the regulator at the back of the field.

Q172 ***Lord St John of Bletso:*** To what extent is there going to be provision in the future for a level playing field? All the evidence we have heard about, so far, is that we just see an industry which is going from bad to worse in terms of market shares, and it is not just the issues of reliability, it is pricing and it is so complex. We had some very interesting evidence on the whole principle of KISS, "Keep It Simple and Stupid". I think it is a very important issue, when one looks at liberalisation and the market going forward, to see what could be done to provide greater transparency and a level playing field.
Mr Hall: Yes, indeed. The level playing field issue is an often-repeated concept; but we do have serious concerns that if the European Transport Policy is to be taken seriously, then there are steps that have to be taken to address the uneven playing field. The very least that should be happening is that we are moving forward with the kind of measures that were proposed in the EU Transport Policy White Paper. Sometimes, it does seem ironic to me that the first thing we have done in terms of restructuring the railways is we have made sure the rail infrastructure is separate, and that there are charges in place; and that is all right then and everybody pays their charges: but you cannot say that about the other transport sectors. If you had a bad day at the office you could imagine that creating the separate rail infrastructure charges might have made matters worse, depending on how national governments treat that opportunity. If you look at the charges that are raised across Europe, they vary very considerably. For example, I would not like to be the sales manager for the Bulgarian infrastructure company, because their charges are beyond anything that a proper market could stand; and of course it has not been a proper market.

Q173 ***Lord Haskel:*** We have had quite a lot of evidence about the need for interoperability between your members. This need for interoperability is to cut costs and improve performance. We have been told that this means investing in locomotives, training, signals and all sorts of things. Is there any danger that measures to improve interoperability may have the effect of raising costs in reducing the competitiveness of rail freight?
Mr Hall: I think the simple answer to that is yes, but it is a question of how serious a risk that is. The conventional international rail freight operation, based on borders and exchanges of crews and locomotives, was built for a different era, for a different set of political, social and economic

circumstances. In that conventional situation the wagons themselves were, and still are, interoperable, they can go anywhere. The issue, particularly if you are trying to improve the quality and the transit times, is more about the time that it takes to cross the border; and the link with the bottlenecks, the congestion that you get into when you stop trains at the border, and putting them into marshalling yards. We do not have many of these problems in Britain: but in continental Europe some of the traffic can get heavily delayed by that process, by what some people now see as an artificial border, but it is still a system reality. There is a need to improve the transit arrangements at borders, and some of our members have already made relatively modest, but nonetheless significant, investment to improve the arrangements. An example of this is between Germany and France where there is a major transit route from the Mannheim area to the Metz area. Here rather than hopping from marshalling yard to marshalling yard—having to change resources again on one side of the border, going through to change again on the other side of the border and then carrying on to another yard— there has been judicious investment on interoperable locos and crew to streamline that movement. This investment is happening at the moment, in advance of the European legislation. However the answer to your question remains yes: particularly if, with the new European Railway Agency, there is insufficient attention paid to cost benefit analysis of the implementation of the specifications for all the different aspects of interoperability, whether it is communication, power or the signalling system. The process started some years ago, with interoperability legislation for the high speed routes and it is now extending to work on conventional rail. I have to say to you that there are difficulties currently in reality on particular interoperability aspects; such as the signalling arrangements and the introduction of a European train management system, (fully automated, the sort of thing you have if you go through the Channel Tunnel with the Eurostar), when these concepts are extended to the conventional network. That is very expensive: and so, at CER, we are very activity supported by a number of our major members, and we are in high level discussions with the Commission on this subject at the present time. Again, this is fine, but how practically can we do this without putting an intolerable financial burden on the business.

Q174 ***Lord Haskel:*** There are a lot of technical problems to sort out. The frontiers are not just a matter of bureaucracy?

Mr Hall: No, absolutely not. The railway is a disciplined and physically inflexible system of transport that operates with interactions between the infrastructure and the trains that are not found in any other mode of transport. Once you have designed them for a particular set of circumstances, in many cases well before the European Economic Communities came into existence, then there is a heavy cost involved in addressing that. It is a cost for freight in particular. CER has the view that if you going to be serious about freight transport policy, then freight has got to cover its cost and the road transport market, in particular, is too cheap. We hear this from road freight operators and we hear it in this country when we talk about the fuel costs going up, but nobody wants to raise their prices because somebody else could come along and take the business. All of that has an impact on the railway. There are very slender margins and this is where the wholesale equipment of the infrastructure has to be checked very carefully to make sure it is done in the right place at the right time, when equipment needs to be renewed on major corridors for example.

Q175 ***Lord Haskel:*** If this interoperability has been achieved on passenger traffic, can that not be passed onto freight or are they two completely separate things?

Mr Hall: They are not completely separate. There is a different set of standards and requirements for high speed train operation. Yes, you can with conventional operations, providing the business is there, but for quite a number of international operations now the freight is arguably the heavier volume: the railways in Europe have suffered from the impact of airline competition, and particularly low cost airlines, in recent years. It is not necessary, but it can piggy back on passenger development.

Q176 ***Lord Swinfen:*** Mr Hall, in Annex two of your evidence on the proposed Regulation on rail freight quality you dealt very fully, for which we are grateful, with the possibility of penalty levels. Is there not a case for compulsory compensation for quality shortcomings in those rail freight markets in which competition fails to emerge?

Mr Hall: There is an open question there, is there not, about if competition fails to emerge? Maybe look forward to two or three years time, when we have the market open, but we find that we do not have a multiplicity of operators, because of the volume, maybe the costs involved and the competitive position versus road. I tend to view the proposed Regulation as being almost a "punishment" for the railways for the fact that the market is limited.

Q177 ***Lord Swinfen:*** What is the position where you have got time-sensitive freight? We have had anecdotal informal evidence given to us of a complete train of perishable goods, food, and the whole load had to be written off because it did not go through on time. It was in cooled containers, the train ran out of

fuel, everything perished, everything had to be thrown out.
Mr Hall: We are talking about quality.

Q178 ***Lord Swinfen:*** I am talking about quality of rail freight and if you have not got a competitive market—I understand it did not happen in that case—are there not grounds for compulsory compensation?
Mr Hall: I think that I would not dispute that there are some individual horror stories that could be told on rail freight. I am not going to try and debate that. The CER's members understand the principle of quality and they are doing a lot to try and to improve quality in areas where it has not been acceptable to the customer. CER launched a Europe wide freight quality charter in 2003 to try to establish a common set of principles throughout the railways of Europe. We have already seen a significant increase in the number of contractual quality commitments that have been entered into between railway companies and their customers. I think if we are talking about time-sensitive goods, these are contracts between commercial concerns and it should be possible, if the price is right, to negotiate a set of quality commitments that would provide compensation for the kind of situation which you described. The reality is that the customer does not want compensation, he wants a quality service, and so do the railways. I think the principal point is, yes, quality clauses have their place, and they are in place to an increasing extent in European freight: but to have it set by an absolute Regulation, when there are many types of traffic, where the offer of the business is such that it is quite hard to provide an assured pathway—there are plenty of examples of that in the UK—is simply not consistent with the notion: "this is now a liberalised and competitive market". It seems to me we are sending two very different signals to the market. One is,"Right, you are big boys now, you are open to competition, you have got to get it right or the competition will take the business away": and then we are being told, "now we are going to regulate you all and tell you what sort of penalty clauses you have to have for which types of traffic". We find that a bit difficult to understand, because managing change is difficult, even without these very contradictory signals.

Q179 ***Baroness Cohen of Pimlico:*** We have half an answer to the next question. What can be done to speed the financial implementation of the necessary improvements to quality and capacity to the rail infrastructure? I guess I mean bottlenecks, bits where the thing stops.
Mr Hall: CER welcomed the conclusion of the quite lengthy negotiations about the revisions to the Trans-European networks projects and I am sure you have probably heard all about that. That is a very positive move. The funding problem remains. The European Commission recognises that and is itself trying to make both actual budget money available, and be more flexible in the criteria as to just how much money within its European Union budgets can be used for Trans-European transport network projects. The issue still, nonetheless, puts a heavy burden on the Member States because the Commission's funding proposals—and they are still only proposals at this stage, to provide £20 billion of European Union money towards the projects over the next six years—is still only £20 billion of the £140 billion that would be needed to deliver those parts of the Trans-European Network Projects which would be due to be completed by 2013. There is a major funding challenge for the Member States. I think maybe when you are talking about part of the answer, finding those sorts of sums of money out of public money is difficult, public private partnerships or some other funding vehicle may help. I think the point here is if having established these priority projects and agreed them through a lengthy process; if the European Union cannot then put the money behind that, then there is something wrong with the way the Union is trying to move its transport policy forward in favour of the modes that support sustainable transport development, compared with road freight in particular. That leads you back to the 2001 White Paper, where we were expecting that there would be a Directive produced on the general principles of charging for infrastructure access (remembering we are the only guys that have to charge for every kilometre the train travels) but that has not materialised. It is not clear to us today whether that is just delayed because it is politically very difficult, or whether it has just gone altogether. The proposal on the table at the moment for a Eurovignette, a better approach to road freight tolls, is completely deadlocked. Rather than looking for huge sums of public expenditure to fund infrastructure, if there was the will to change the structure and have economically driven charging on a comparable basis across the modes, that could radically change the whole framework. That seems to me to be much more important, if you are taking a long-term view, than looking at issues around contract quality; I sincerely believe that. I remember one of the first quality contracts that was signed in this country was with the Royal Mail and that was quite some years ago now but it has not kept the traffic on the railway.
Chairman: You covered it fully in your paper, so let us not go back to it.

Q180 ***Lord Walpole:*** I think this is a straightforward question. What solution would you suggest to the problem of high access charges to the Channel Tunnel?

Mr Hall: Reduce the price.

Q181 ***Lord Walpole:*** I think we would all agree with you.
Mr Hall: It does seem to be a classic, extreme case of high access charges. Of course we know that it was a special case, because it was advancing transport in a way you could not describe as conventional infrastructure. The Channel Tunnel route is one of the Trans-European network projects, but I think the reality is, unless the severe imbalance can be addressed, the market potential is never really going to be achieved. It is easy for me to sit here and just say: "well, just reduce them": but the problem was the expectation that the charging regime, which was a key part of the way the project was funded in the first place, would cover the investment costs through the fare box, if you could call it that. Certainly, with hindsight, we face a different reality.

Q182 ***Lord Walpole:*** I am not going to go into figures now but it is not being stretched at the moment, is it?
Mr Hall: No, because it is too expensive.

Q183 ***Lord Walpole:*** It is not being stretched by cars, lorries, Eurostar or anything else?
Mr Hall: If I remember correctly, I think the original business plan for freight was around 28 trains a day in each direction or something of that sort, and now we have got 10. There were terrible problems, as you all know, with the asylum seekers, but I think the freight operators, from the British end, face the abolition of the support that is in place from the Strategic Rail Authority. At the very least if that proposal is maintained, then that would be a disaster.

Q184 ***Lord Shutt of Greetland:*** I cannot weigh up what sort of an answer you are going to give me, whether it will be a rosy view or a gloomy view. What do you see as the long-term prospects for international rail freight within the EU? I suppose if you have a rosy view, what needs to be done to make these a reality? If you have a gloomy view, there is still an answer to it, but what is your view?
Mr Hall: My view is going to be rosy, and I am going to start at the rosy end because the one thing that we are now creating with the European Union is a market that, in terms of its sheer size, is something that becomes comparable to the US, at least in terms of overall size and distance. Some of the markets have a different distribution of the markets compared with the US. On the one hand, the basic distance that is such an obstacle to long distance passenger travel is a major opportunity for freight. If you take a long view over the development of the market, and the resolution of some of the transitional problems that the Eastern European countries—the new entrants—face in the market, then there is a natural advantage that rail freight has. The principles and structures that are being put in place now, through the creation of the Agency, can address some of the very real problems that get in the way. Sometimes the railways have different safety standards and systems in each country, that are passionately defended by the national safety authorities and the railways. There is now a pan-European structure being put into place to address those issues, not just at the railway level, but at inter-governmental level as well. If you take a long view, and see that structure is steadily making progress, and if we can make progress in the area of the funding, the idea of developing a fairer arrangement for infrastructure charging across the modes, then in the long-term I think there is a positive future. There is a lot of work to be done and if you said to me: "Is it going to happen in five years?" I think I would go back to the gloomy side and say: "No, I do not think so". Some of the investment costs are very large, so you can only make changes when the network needs to be renewed and replaced. It is a combination of both, no one measure alone will take it forward. When the 2001 White Paper was published and rail was identified as the strategic transport mode, particularly for rail freight because of its environmental advantages, that was a very positive and constructive place to start and we have got to keep pressing that forward.

Q185 ***Chairman:*** I am extremely pleased to hear that you are optimistic about that. As you rightly say, over the next few years there could well be a continuing decline in the shares of freight, that is if I have got you right. You did seem to put a lot of emphasis—and I do not disagree with you—on the relative need for proper pricing of all methods, if I have picked up on the gist of your evidence. Unless that is not right, the necessary investments and substantive investments in the infrastructure should be freight as opposed to passengers is not likely to be forthcoming on the scale needed. I hope that was a fair summary?
Mr Hall: That is a fair summary. There will be markets that we will continue to compete in, but if we are taking the Transport Policy seriously, and trying to shift the balance, then it does need these other measures.

Q186 ***Chairman:*** Could I say a very warm thank you on behalf of the Sub-Committee. You were courteous in waiting as we were late and, you have been even more courteous in being full and helpful in your replies. I am grateful to you.
Mr Hall: Thank you very much, my Lord Chairman.

MONDAY 1 NOVEMBER 2004

Present	Cohen of Pimlico, B	St John of Bletso, L
	Fearn, L	Swinfen, L
	Haskel, L	Walpole, L
	Shutt of Greetland, L	Woolmer of Leeds, L (Chairman)

Memorandum by European Rail Freight Association (ERFA)

THE SPECIFIC QUESTIONS:

Preliminary remark: The following comments refer to the situation on the Continent, the different situation in the UK will be treated in question No. 5;

1. *What are the current barriers to entry in the international rail freight market?*

- Barriers erected by Member States.

  Some Member States don't support the entry of new companies, or even obstruct it. The motivation could be protection of their own state company or consideration for Trade Unions. Many tools are used:

  - Not creating efficient administrative bodies to allocate licenses, security certificates and approvals for rolling stock, especially locomotives.
  - Delay in allocating all these certificates, and administrative obstruction.
  - Bodies in charge of the allocation of the different certificates are dependent on the experts of the incumbent railway company.
  - The system of pricing for the use of rail infrastructure discriminates against new entrant railways (eg the French system incentivises high volumes so that only SNCF can take profit from this).
  - The same phenomena can be found in pricing for electricity, fuel or even for the use of the electricity supply line, if the private railway buys its energy from a third party. Member States are often imposing these pricing systems or at least tolerating them.
  - State aid is given to the incumbents in different, sometimes hidden forms: covering deficits, bailing out from time to time, public funds misused, guaranties for credits, thus better rating, restructuring with public absorption of costs.
  - Crossing borders hampered by treaties between States.
  - The competent public authorities (national and European) don't follow competition cases with the necessary emphasis and rapidity.
- Barriers erected by the incumbents:
  - It is quite normal for them to use all the lobbying power they have as important state-owned companies, employers and investors.
  - Thus they are able to combine the power of the administration, the Trade Unions and the industry relating to the way in which the railway is operated. The fault in this system is that the Member States don't prevent them from doing so.
  - Integrated Networks are not fully neutral, separated ones are often not better.
  - Abuse of dominant positions is usual (eg to force by pricing measures a client to give 100% of his traffic to the incumbent). The state aid gives the incumbents the possibility of dumping in order to defend their monopolistic position.
  - The same state aid gives the incumbents better opportunities to invest in better production tools.
  - State aid enables some state-owned companies to buy private competitors and even other state-owned railways with the effect of creating the danger of a European monopolist instead of a former national monopolist.
- Barriers erected by practical circumstances :

— The railway business is very capital intensive, but the yield is low. This brings specific problems for new and private railways in getting access to the capital market, in obtaining attractive costs for outside capital. This factor often hampers the development of new entrant companies. This circumstance combined with the above-described advantages of the state-owned railways (state aid) is a very high barrier to entry in the rail freight market.

— The new entrant railways have a vision for their services, which differs from the classical one that is based on co-operation between national railways. The new entrant railways want to provide transport from the sender to the destination. Thus they are more challenged than the historical companies by the problem of the absence of interoperability and the financial burden of surmounting them.

— Trade Unions are mostly hostile to private railways and use their influence to limit their development.

2. *To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?*

It is beyond any doubt that the discipline in implementing existing EU Directives, especially Directives 2001/12/EC to 2001/14/EC is generally relaxed and differs from country to country. DG TREN evidently does not use all its power to enforce the Directives fully in all countries. The Commission does not pursue even blatant discrimination such as the French pricing system for the use of infrastructure. The differences also come about because the existing Directives give Member States too much liberty in arranging state railway systems, as it is in case of Article 3 ("infrastructure manager") and Article 6 paragraphs 2 and 3 of Directive 91/440/EEC, as amended by Directive 2001/12/EC.

In many countries the independence of the infrastructure manager and fair and non-discriminatory access to the infrastructure has been introduced only superficially. The integrated railways are both the operator of transport and the operator of infrastructure. For this reason, private operators have, in many cases to negotiate access to the infrastructure and the timetable with their competitor. The charges for timetables, train paths and often electricity therefore constitute an in-house overhead item for the trains of the integrated company, but those charges are effectively collected only from external operators.

All the attitudes enumerated in question 1 are often contrary to European law, general rules and specific rules in the field of railways; they are certainly not in line with the spirit of the European Transport Policy in railway matters, which is based on intramodal competition and open access.

3. *Is further action needed at a European Union or Member State level to ensure enforcement of EU Directives?*

The situation in individual countries lacks close and independent examination from the level of DG TREN. It is clear that the evaluation report date of 15 March 2005 set by Article 14 of Directive 91/440/EEC, as amended by Directive 2001/12/EC, is too distant, and, taking into account the time-span needed to ensure corrective action, the efficiency of the supervision can only be very low. The examination of the real state of competition and non-discrimination in the European rail market should be continuous, and be carried out also by DG COMP. The Commission must not be content with the legislation they proposed and which was adopted. An active follow-up of real implementation n conformity to its spirit is needed.

In many cases of illegal behaviour the national competition authorities are competent (subsidiarity). If they fail or are too slow, the Commission must take the case over.

Some parts of the existing "second railway package", such as safety or interoperability measures, may even act as a sort of back strike against private operators, as those measures were strongly influenced by the incumbents and adjusted to their wide funding sources. DG TREN using the instrument of the European Rail Agency (ERA) must ensure that all the technical specifications for safety and interoperability (TSIs) have a neutral character.

The joint agreement by Community of European Railways (CER) and European Transport Workers Federation (ETF) to give their recent agreement on working hours binding force to private operators as well is another field, where Community action to support intramodal competition is needed.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

With the adoption of the second rail package the most important parts of the legislation in the field of rail freight are in place. We see two smaller needs: the Directive on driver licences, which the Commission has already proposed, and a regulation that obliges the infrastructure managers to commit themselves as far as the quality of their services is concerned.

The current proposal of the Commission on quality of services that intervenes in the relation between the operator and the client is superfluous.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

We want first of all to express our opinion that in the United Kingdom all the critical points we mentioned in respect to Member States don't apply. Furthermore there is no incumbent that could misuse its former monopolistic position. The national rail freight transport is not suffering as it does on the rest of the continent.

The prime obstacle for internationalisation of rail freight between the United Kingdom and the rest of the continent can be seen in the channel tunnel. It is not always apparent why this efficient means can not be more widely used for rail freight. There seems to be a host of reasons such as safety considerations (terrorism and fire, for instance) and especially the practical difficulty of entering the French rail territory (RFF). The United Kingdom Government should address these issues.

August 2004

Memorandum by Freightliner Group

1. Introduction

This evidence is submitted by the Freightliner Group, which consists of two licensed rail freight operating companies, Freightliner Ltd and Freightliner Heavy Haul Ltd.

Freightliner Ltd is the UK's largest intermodal rail operator, and moves some 600,000 intercontinental containers a year between the major container ports (particularly Felixstowe, Southampton, Tilbury and Thamesport) and thirteen inland destinations.

Freightliner Heavy Haul Ltd has been working in the rail bulk market for four years, and now operates more than 1,000 trains a week carrying coal, rail infrastructure materials, cement, cars and vans, domestic waste, aggregates and petroleum products throughout Britain.

2. Involvement in International Traffic

Although the containers carried by Freightliner Ltd are international they arrive in and depart from, Britain by sea in the course of their journeys to and from Asia, America, and Australasia. Neither of the companies in the Group carries, or aspires to carry, traffic between Britain and other Member States of the European Union (EU) by rail, and we are therefore relatively indifferent to the impact of EU legislation on international rail traffic in Europe.

In our view, the legislative and regulatory barriers to entry into the European market from Britain are secondary to the economic and safety barriers presented by the Channel Tunnel.

3. Current Barriers

There are three sets of barriers which make us unwilling to consider carrying goods by rail through the Channel Tunnel.

3.1. The safety requirements of the tunnel mandate technical requirements for the locomotives which are disproportionately costly. As a result, only one small fleet of locomotives, expensive to acquire and expensive to operate, meets the specifications.

3.2. The current structure of tolls and guaranteed payments to Eurotunnel makes it impossible to obtain competitive prices for passing through the tunnel.

3.3. The generally low levels of rates for the movement of goods between the UK and Europe make it an unattractive market to enter. It should be noted in this context that the major traffic objective in the UK is London and its surrounds; length of haul from the Channel coast is unattractive when compared with the distances available on the other side of the water.

If these problems could be overcome attention would then turn to the extent to which Member States are complying with the open access and other European Directives, but from a UK perspective this would be pointless without resolution of the Eurotunnel issues.

Robert Goundry
Director of Strategy

12 July 2004

Examination of Witnesses

Witnesses: MR KLAUS-J MEYER, Secretary General, European Rail Freight Association (ERFA) and MR ROBERT GOUNDRY, Director of Strategy, Freightliner Group, examined.

Q187 ***Chairman:*** Good afternoon, Mr Meyer. May I thank you very much indeed for coming to meet with us today and also thank you and your organisation for the written evidence you sent in? We have around 45 minutes and we have many questions to ask you. Is there anything by way of introduction you would briefly like to add to your written evidence before we begin?
Mr Meyer: Perhaps some words about the organisation. My name is Klaus Meyer; I am Secretary General of the European Rail Freight Association. This is an organisation which is two years' old and is the organisation of the private, independent, European freight railway operators. We have 20 direct members and four associations which represent some 120 other companies. The objective of ERFA is to raise the competitiveness of the whole rail freight sector by intermodal competition. Intermodal competition is the most normal and natural situation in the whole economy, including transport, but in former times there was one exception, rail, and the UK introduced intermodal competition and the European legislation followed. We are convinced that intermodal competition and the increase in private rail companies is the last chance for rail freight and the UK example confirms it. I think that is enough for now. At the moment we have one British member, Freightliner, but after the next board meeting English Welsh & Scottish Railway (EWS) will also become a member and perhaps a third one at the beginning of next year.

Q188 ***Chairman:*** Of course, we have a representative of Freightliner with us today, Mr Goundry.
Mr Meyer: We are proud to have Freightliner as a member because they are really successful.
Chairman: Thank you very much.

Q189 ***Lord Fearn:*** How successful has the European Commission been in overcoming the barriers to a competitive rail freight market in Europe?
Mr Meyer: The Commission is happy to have brought the legislation through. The system of licences and certificates with a rail regulator as a legal institution is not perfect but is a workable system. An improvement in this field might be better separation of infrastructure and operation and we also need common rules for the allocation of safety certificates, but success is limited because not all Member States are convinced that the famous intermodal competition is the right way. We therefore lack full implementation and application of the legislation, really the spirit of competition. We have the impression that many Member States try to bypass the legislation. A solution would be for the Commission to take contractual infringement to the European Court of Justice, but this takes a long time and success is not guaranteed. For this reason the Commission is hesitating and perhaps also because they do not have the necessary courage. I must say openly that the Commission must struggle more for the real application of the existing legislation. One of the problems is state aid, which I have written about in my memorandum, and the Commission did not even try to hold an inquiry into state aid. Are they afraid of the Member States or are they too orientated towards the legislation? Yes, they have succeeded in passing the legislation, even most of the third rail package will pass: the problem is that they feel free now. They have succeeded and the legislation is there, but much work needs to be done on implementation. If Mr Barrot becomes the Commissioner for Transport in the new Commission, he has promised that he will not go down the road of legislation but implementation. I hope that even with all the problems now with the Barroso Commission, Mr Barrot will stay with transport.

Q190 ***Lord Fearn:*** Yet it is working quite well. You say it is not perfect, but it sounds as though it is working quite well anyway.
Mr Meyer: Not in every country. We have an example. In the UK you have at least 300 or 400 locomotives of the General Motors Class 66. It is proven and accepted in the UK, the same locomotive is accepted in the Netherlands, in Germany, but if you want to take this locomotive on the French rails, they ask for the whole examination to be done again, including crash tests. If you want to have a safety certificate in some countries, it is impossible to get a safety certificate; really impossible, they refuse.

1 November 2004 Mr Klaus-J Meyer and Mr Robert Goundry

Q191 ***Chairman:*** In which country is that a problem?
Mr Meyer: That is in Belgium. If you write a letter to the Ministry requesting a safety certificate you will be told to address yourself to SNCB, to the railway.
Chairman: You raise many issues there to which I am sure we shall return as the session goes on.

Q192 ***Lord Swinfen:*** Is the certification required for each individual locomotive or just for the class?
Mr Meyer: For the class.

Q193 ***Lord Shutt of Greetland:*** In the paper you sent to us you refer to barriers and you say that integrated networks are not fully neutral; separated ones are often not better. Where do you stand in terms of the separation of infrastructure from operations? Is it desirable or not?
Mr Meyer: It is desirable. We have a really absurd situation. In Germany the network is integrated; there is no separation. However, for the moment the Deutsche-Bahn Netz, the infrastructure manager, is absolutely neutral. On the other hand you have the French infrastructure manager, Réseau ferré de France, which is separated from SNCF, but it is used as an instrument to filter market entry by private railways. Why is there this situation? It is because the question of separation is now discussed by the German parliament and by the German public and in this situation Deutsche-Bahn Network will do what they can to give an impression that they are neutral. In France, however, they have chosen an elegant way of hiding the fact that they do not want competition on the French infrastructure against SNCF. There would have to be a revolution in France to bring in competition on the railways. In my view the separation is necessary, because with the separation you can reduce the potential for discrimination, but it is not sufficient. It must be completed by a real feeling that you want competition, that you want intermodal competition. It is difficult for the state to allow competition against a state-owned company and they do not see that competition is also good for the incumbent. The incumbent also becomes better with competition.

Q194 ***Lord Shutt of Greetland:*** If tomorrow morning in France they decide to operate exactly as the Germans, will that not be to your satisfaction?
Mr Meyer: Yes; yes.

Q195 ***Lord Shutt of Greetland:*** That being the case, why are you not happy for everybody to be like the Germans?
Mr Meyer: Where do you have a guarantee that the German policy will remain the same? When the discussion is over, the problem then is if Deutsche-Bahn wants to go public, but with the network. When they are a limited company on the stock exchange with the infrastructure, it becomes difficult to separate them again. Who then guarantees the neutrality? I think separation is necessary, but it is not sufficient on its own. There must also be the political will to have intermodal competition.
Lord Shutt of Greetland: Thank you very much; I understand your point.

Q196 ***Chairman:*** Do the Directives now insist that separation must occur?
Mr Meyer: Unfortunately not.

Q197 ***Chairman:*** Not at all?
Mr Meyer: No, not at all. The Directive asks for separation to be in the accounting. Public money or state aid which the company receives for infrastructure may not be used for the operations.

Q198 ***Chairman:*** If they are not completely split, how can a competitor railway company, an operator, have confidence, if they go to the infrastructure operator to discuss possible new business, that the infrastructure operator will not, however carefully, inform their own group company that there is some competition on the horizon?
Mr Meyer: Absolutely. This happened at the beginning, even in Germany. They talk about Chinese walls between the infrastructure side and the operating side, but often our members asked for a slot and the next day the client informed the private company that the state-owned company had already tendered for this transport. It is becoming less and less frequent now, because this political discussion about separation has engendered an element of neutrality for the moment. There is no guarantee for the future.

Q199 ***Lord St John of Bletso:*** Your written evidence gives many examples of abuse of dominant position by existing operators. I am aware of Article 82 of the EU Treaty on Competition and now we have moved increasingly to the SLC (Substantial Lessening of Competition) test for mergers. Do you feel that there is a need for new competition legislation to protect against abuse of dominant position, or do you think that the existing legislation is sufficient? Is a more vigorous application of this law a potential solution to this problem?
Mr Meyer: It is the same as my first answer: the legislation is sufficient, the legislation is in place, the rules exist in the rail packages and also the legislation in the field of competition. The reasons for the abuse are manifold. There is a lack of courage on the part of the Commission to insist but, I must say, that is also a current problem with our members. Often they ask me to go to the Commission and tell them this or that. The Commission say that if they have no formal complaint they cannot begin an inquiry or process

and our members often do not have the courage to make a real complaint because they are afraid that they will be penalised in the future. The case of the French pricing for the use of their infrastructure is a striking example. One of our most active companies really wants to go to France and for the moment they are prevented by the pricing system. However, they told me that they do want to go to France, but if they make a formal complaint now, they will encounter many, many difficulties in the future. So we are trying to find another way. For the moment we are trying to find a legal way for the association to put in a complaint, but legally that is not so easy. It would be one solution.

Q200 ***Lord St John of Bletso:*** Surely one of the ways of getting around that is for the rail operators to have an independent rail regulator who could depoliticise the situation.
Mr Meyer: Yes; absolutely.

Q201 ***Lord St John of Bletso:*** If there were such a regulator—I am referring here not just to the freight industry but also to the communications industry, on which we have had several Select Committee reports—they could apply *ex ante* legislation. Do you think that existing legislation is currently adequate to achieve this throughout Europe?
Mr Meyer: My answer is the same again: the legislation is okay, but if the Member State does not create an independent regulator, as many have, or if the regulator is not independent, there could be difficulties. In France the regulator is the minister and the minister is also responsible for the results of SNCF; in other countries there is no regulator at all. The German regulator has 120 cases against Deutsche-Bahn to deal with. An active regulator has much to do. It is perhaps better in the UK because competition is accepted as the norm and there is no incumbent and separation of infrastructure and operation has been achieved. In other countries there are cases, often small cases, but there are cases for the regulator and the regulator has much to do. The regulator must be really independent.

Q202 ***Lord St John of Bletso:*** Do you think that there could be a regulator across the whole of Europe? I see that being a problem in individual countries. That is what you really want to have, when talking about the freight industry, which is really in the doldrums at the moment. We have had evidence from certain of our witnesses saying that there have been massive problems in France. What the consumers are looking for is an independent regulator, not just in one particular country but right across the region.
Mr Meyer: It would be an ideal situation, but to install one you would have to gain the agreement of all the Member States and I do not think they would agree.

Q203 ***Chairman:*** You referred to the position of the regulator in Germany and the position in France. You will be well informed about the position in each of the Member States?
Mr Meyer: More or less; yes.

Q204 ***Chairman:*** Would it be possible for you to send us a written memo setting down your understanding of the position regarding the regulator in each Member State?
Mr Meyer: An evaluation?

Q205 ***Chairman:*** No, just briefly whether there is an independent regulator, who the regulator is, whether they are independent, whether they are active or not; just very briefly, an overall assessment. This is terribly rude of me, but we are meeting the Commission on Monday next week and it would be very helpful to have your understanding in advance, because we shall ask the same question of the Commission. That would be very helpful to us. The Clerk will have a word with you afterwards.
Mr Meyer: Okay. So you need it this week?

Q206 ***Chairman:*** If you could; if you cannot, then it is better to have it late than not at all.
Mr Meyer: I am travelling until Thursday, but I will try. Perhaps I can find somebody who will do the work.
Chairman: Thank you very much; I am most grateful to you.

Q207 ***Lord Swinfen:*** You comment in your written evidence that some aspects of legislation on interoperability and safety may damage independent operators. Could you enlarge on that and explain what you mean?
Mr Meyer: You put this in a rather different way. It is not the interoperability which is the problem, but that reaching interoperability is more difficult for the small private railways than for the big companies which have access to capital. Let us take the interoperability of the new signalling system, the security of the signalling system. The infrastructure part is paid for by the infrastructure company; okay. However, for each locomotive there is an investment of at least €200,000 and that is a lot of money for a small company for each locomotive. The classical railways on the continent still have a system of co-operation, which means that the French railway goes to the frontier and then the Italian railway takes over the train. Our philosophy is to remain the responsible operator from start to finish, so we try to use only one

locomotive for the whole journey. In principle therefore we need locomotives which can go on different systems and for each safety system—not the electricity, the safety system –we have to pay between €150,000 and €200,000. If you go from Rotterdam, for instance, just to Italy, you have to have three systems on board.

Q208 ***Lord Swinfen:*** So that is €600,000 for each locomotive?
Mr Meyer: Per locomotive.

Q209 ***Lord Swinfen:*** And that does not include the cost of training the drivers?
Mr Meyer: It does not include the cost of training the drivers.

Q210 ***Lord Swinfen:*** And the price will rise again?
Mr Meyer: Yes, naturally. The driver also has to learn the different systems. If you go from Rotterdam to Milan, the driver has to be changed. One driver cannot drive for more than, let us say, six or seven hours.

Q211 ***Lord Swinfen:*** I appreciate that, but you may reach a time when the drivers will sleep on the train and come back on duty and they will still have to know the system the whole way and be capable of taking over if there were an emergency, I assume. If one of the other drivers got taken ill, for instance.
Mr Meyer: The driver cannot stay on the train. They have to leave the locomotive and sleep elsewhere. This is not the same as for lorry drivers: the second driver can sleep in the cabin but not on trains.

Q212 ***Lord Swinfen:*** That never happens on the railways?
Mr Meyer: No.

Q213 ***Lord Swinfen:*** Do you not think it will happen in the future?
Mr Meyer: I do not think so. There is no space in the locomotive. The safety system takes up space. The electrics system at the moment does not take up much space, it is only little, but the safety system is considerably larger.

Q214 ***Lord Swinfen:*** How big? About 5 feet x 5 feet?
Mr Meyer: Yes.

Q215 ***Lord Swinfen:*** Thank you very much; that is quite interesting. The costs are quite horrendous when you are thinking of that for every single locomotive. I can understand that.
Mr Meyer: At the moment we have a big problem with the Betuweroute, the new Dutch line from Rotterdam to the German border. It is planned to equip it only with the new European system, the Electronic Rail Transport Monitoring System (ERTMS), but this is an island and if you have a locomotive going from Rotterdam to elsewhere, you need a separate system for those 120 kilometres from the ERTMS. We are trying to make a case for continuing the system on the German side, but German railways are not willing, or are not able, to finance the infrastructure for this. We are now trying to persuade the Community and the Dutch ministry to pay for the onboard installations for this system.

Q216 ***Lord Swinfen:*** I take it that is the same for every single country, not just between Holland and Germany but on into Austria or France?
Mr Meyer: The idea is that this will be the future single system in Europe.

Q217 ***Lord Swinfen:*** You give me the impression that nobody is actually willing to take it on at the moment except for Holland.
Mr Meyer: Yes.

Q218 ***Lord Swinfen:*** Is it a question of who is going to pay for it?
Mr Meyer: Yes. They may put it on the infrastructure in Switzerland but alongside the existing system; you would be able to continue to use the old locomotives on the old safety system. This is technically possible.

Q219 ***Lord Swinfen:*** Are you then not doubling the cost?
Mr Meyer: No, then you have time. You can buy new locomotives when the ERTMS has been installed over greater distances and in the meantime you can use the old locomotives.

Q220 ***Lord Swinfen:*** How many years is this going to take?
Mr Meyer: Ten, 15 at least; maybe more.

Q221 ***Lord Haskel:*** Could we turn the conversation round to the question of quality? You say in your memorandum that you think that the proposals for the Third Rail Package, as far as quality is concerned, are superfluous. Given that there is a continued dominance of the market by national operators who do offer poor service, what do we do about this? You do suggest that there should be a Regulation requiring infrastructure managers to commit themselves to their quality of service. Perhaps you could explain why you think this is better than the other proposal?
Mr Meyer: First, on the relationship between the customer and the operator, there I was opposed, in agreement with all my members, to the Commission's proposal for two reasons. The first reason is that practically all our members already have quality clauses and sanctions in their contracts. If it were

compulsory for everybody, we would lose a market advantage. This was the first reason. The second reason is that I want to orient the Commission to be active in the implementation of the Regulation and that means in supporting the intermodal competition. I think the best way to raise quality and productivity is intermodal competition. I wanted the Commission not to dissipate their energy on this new proposal, but to put all their energy into implementation of the existing Regulations and that means more competition. These were the two reasons why we opposed this. I must admit that for the moment you are right: there is in any case no alternative competitor for the shipper. There are cases where the goods are so rail orientated that they cannot be transported by any other means. It is true that the shipper often only has one possible supplier. In that case this supplier is so strong that he would never accept a very strong quality clause. These are the cases which the Commission has in mind for this Regulation, but the power of the supplier is so strong that he will not accept really strong commitments. On the other side, there is no level playing field in the relationship between the infrastructure manager and the operator, at least as far as our members are concerned. On the one hand there is a monopoly, the infrastructure, and the monopoly is a state-owned monopoly. On the other hand you have a private company, perhaps a small private company. We have an example. One of our members is operating a train from Rotterdam to a terminal near Milan. The train arrives every morning on time at the Swiss-Italian border and then it takes several hours, often five or six hours, to cover the last 60 kilometres. The infrastructure manager is not willing to give any commitment on punctuality. I think we must have this obligation on the infrastructure manager to say yes, I will bring the train to the destination by ten o'clock. He must be obliged to give this commitment because he is a monopoly and a monopoly must be balanced by legislation. In the other relationships, at least in time there will be a level playing field between two contracted parties. This is the difference between the two relationships.

Q222 ***Lord Haskel:*** Are you suggesting that until such time as you can get competition where the monopolies are, there should be some kind of basic quality arrangement which the European Commission should try to impose?

Mr Meyer: Yes; yes, absolutely. The infrastructure managers have understood. Last week I attended a meeting in Paris organised by UIC, the Union International des Chemins de Fer, the worldwide organisation of railways but state railways, the infrastructure integrated companies and others. They have understood that this is needed and they will start to develop that now. We are invited to take part in working on a code of conduct or a charter. I am not convinced that it is strong enough.

Q223 ***Lord Haskel:*** Presumably this quality charter would refer mainly to timekeeping, that is the main element?

Mr Meyer: Yes; timekeeping is the main issue here, absolutely. Accidents happen, that is normal.

Q224 ***Lord Haskel:*** Reliability?

Mr Meyer: Yes.

Q225 ***Lord Shutt of Greetland:*** I am just trying to work out whether some of the things you are arguing for are ultimately practical. For example, you mentioned the locomotives here in the UK which could go to the other side of Europe, but there is such a thing as tiredness amongst the drivers and how long it might be sensible for such people to drive. Supposing these locomotives break down 20 miles short of Milan, is there then any fraternity between anybody in Italy who is able to take over in such circumstances? How practical is it?

Mr Meyer: It is certainly for the moment not practical to go with a locomotive from the UK to Italy. It is not possible because of the safety systems and so on. Even if you take a diesel locomotive, the Class 66, they must be equipped with the different signalling and safety systems. It can happen that a locomotive breaks down, but normally you get help from the manufacturer's workshop, Siemens, Alstrom and so on. They can normally offer help. That is a problem if you have no partner in a country. If you go alone into a country, it is really a big problem. It is better to have a local partner; let us say co-operation between the German company and the Italian company. In our association we try to bring those companies together.

Q226 ***Lord Walpole:*** Could we look at the drivers themselves? You support the proposals for them to have international driving licences for trains, although some operators have argued that in the current form it will raise costs more than benefits. Can you explain your position on this?

Mr Meyer: Yes. The European driving licence is certainly a good thing because the free movement of drivers from one company to another will be easier and also the movement from one country to another: interoperability, but also taking employment in another company. The supplementary training is costly, that is right, and I think it is accepted in the Directive that companies or drivers who do not cross borders, who do not go abroad, are excepted, they are not included in the Directive. On the other hand we must also try to make the whole procedure and the administration a little easier. There are requirements in the proposal which a lorry driver never has to meet.

Are the risks for a locomotive driver really so much higher? He has the rails, he has the signalling system, in many countries the locomotive is controlled directly by the signal; it cannot go through. A lorry driver can make many mistakes which can have very important results and victims. I think what the Commission have asked for could be reduced a little; perhaps it has not been excluded because of the influence of the classical railways.

Q227 ***Baroness Cohen of Pimlico:*** We have heard a good deal about the shortcomings of other European countries, but we are all very conscious that one of the problems for your members is the kind of difficulties involved in getting through the Channel Tunnel. Would you like to expand on those? What are the principal problems that your members are encountering with the Channel Tunnel?
Mr Meyer: It is not the Channel Tunnel it is France; it is the French network.

Q228 ***Baroness Cohen of Pimlico:*** Are the owners of Eurotunnel innocent in this matter? I thought there was a problem with high charges.
Mr Meyer: No; no. As I understand it, the Channel Tunnel is not the problem. The problem is that in practice you cannot go through France for the moment. Even some British companies stop their activities at the end of the tunnel; EWS for instance goes through the tunnel but no further. The problem is not the tunnel, as far as I understand it.

Q229 ***Baroness Cohen of Pimlico:*** We observe that the freight traffic through the tunnel is very much less than was originally predicted. We know that charges are thought to be high, but is it your view that the real problem is that you cannot get through it?
Mr Meyer: Yes. I have heard from a very important shipping company for the automotive industry, Volkswagen, which has factories in Spain and the UK is a market for them that they have tried everything they can to find a private operator going from Spain through France to the UK. The problem is France. There is another company, Transfesa, a Spanish company, which is also very active in the United Kingdom. They are not an operator, they rent wagons but they are not a railway operator because they are afraid to become one. We have a French member of our association, Connex Cargo Germany, and I asked a director of this company why they were not the first to go through France, as they were a French company. He said, "No: because I am a French company, I do not want to kill the first railwayman who lies on the tracks when the first private train comes through".
Chairman: We did receive evidence from Freightliner and I am going to have my recollection helped.

Q230 ***Baroness Cohen of Pimlico:*** I am sitting on the Freightliner evidence. Freightliner produced three sets of barriers which they thought were really making life very difficult. The safety requirements of the tunnel were quite difficult and involved technical requirements for locomotives which were very, very costly, as a result of which there is only one small fleet of locomotives which actually meets these specifications. Whatever the French are doing, it seems to me that we are doing something wrong too and I am trying to get at this. The prices, our toll structure and guaranteed payment structure going through Eurotunnel make it very difficult to get a competitive price; in fact I think you take the price you are given, I do not think there is a competitive price. Then there is a point which I find slightly more complicated, which is that people delivering to this country really want to deliver to London and the journey is just not long enough; you would be better off in a lorry. Do I have this right and is there anything the British Government could do? I am quoting from the Freightliner evidence. We have also received evidence from other places on the level of charges and general awkwardness of Eurotunnel. The safety requirements are slightly new to me and the idea that it may not be worth pushing freight through the tunnel anyway because you mostly want to go to London.
Mr Goundry: I am Robert Goundry and I am Director of Strategy for the Freightliner Group, which is a British freight operating company which has two operating companies; I wrote the evidence to which Baroness Cohen refers. There is a matter of perspective in this. If you are sitting in Germany or Belgium or Italy and want to go through the Channel Tunnel, or in Spain indeed, the first obstacle you reach is France, so that naturally looks as though it is the most serious obstacle. Once you had got through France you would find that there were still difficulties with the Eurotunnel system as well. At the current time English Welsh & Scottish Railway (EWS) is the only British freight operator which works through the Channel Tunnel. They do that with the assistance of very, very substantial Government subsidy. EWS is not actually, nor are their customers, paying the full charges. There is a complicated system of a guaranteed annual minimum user charges and the arrangement in the Anglo-French Treaty is that Eurotunnel is guaranteed to receive this payment, almost regardless of however many trains go through. As the minimum user charge is being met by the Government, it is reduced in effect by the number of trains which run through. EWS receives direct subsidy. A new operator receives a quotation from Eurotunnel, inasmuch as they are willing to give you a quotation—and that is another long and complicated story which I will not go into unless you want me to—which is effectively the minimum user

charge divided by the number of trains they are currently running; I think; as far as I can understand it. It is a charge for 30 miles which is way, way outside anything we would regard as being reasonable for running a train through and certainly much more than the comparative charge for taking a lorry either through Eurotunnel or on the cross-Channel ferry.

Q231 ***Baroness Cohen of Pimlico:*** That is the point: it matters because it is uncompetitive with the ferry or driving.
Mr Goundry: Exactly; yes.

Q232 ***Chairman:*** Remind me. That comes to an end when?
Mr Goundry: The minimum user charge (MUC) arrangement expires in 2006. The government subsidy to EWS was due to expire in May 2005, although I think I understand that there is some arrangement to see it extended until they can grapple with the whole problem of the financing of Eurotunnel, because in every respect the forecasts for traffic have been disastrously wrong. The lowest conceivable estimate in 1994 or thereabouts for the passenger traffic this year was that it would be 12 million passengers. They are actually doing something around six million and the freight is exactly the same. It is optimism piled on optimism, piled on folly, frankly.

Q233 ***Lord Walpole:*** What sort of percentage below capacity is this, or is that an impossible question?
Mr Goundry: It is a question which is possible to answer, but I cannot answer it for you off the top of my head. It is well below capacity. The capacity is partly taken up by express passenger trains, the Eurostars, which consume more capacity than a freight train would because there is a speed differential. Even the passenger trains, many, many of the Eurostar trains, are very poorly loaded, particularly the ones to Brussels.

Q234 ***Baroness Cohen of Pimlico:*** What would improve this position? Inasmuch as this is our Government, what could be done to make it easier for rail freight to get through the tunnel?
Mr Goundry: It is quite difficult because it is governed by the Anglo-French treaty; so our Government cannot act in isolation, it has to act with the French government.

Q235 ***Baroness Cohen of Pimlico:*** But what could be done?
Mr Goundry: That may well restrict what can be done. The problems are so intertwined that even if the tolls were themselves competitive, you would still have this problem of having a very limited number of locomotives, all of which belonged to competitors, which met the safety requirements of the tunnel. The key safety requirement is that if a locomotive or a train breaks down or catches fire, it must still be capable of moving itself out of the way. So the Eurostar trains have power cars distributed all through the length of the train and if one fails the rest of the train can propel it. Although the freight locomotives look as though they are one locomotive, in fact on board them virtually every system is duplicated. It looks like one locomotive, but there are in fact two locomotives. This means that they are very, very expensive to buy and operate and maintain and so expensive to buy that in my view no more will ever be bought and there is a very limited pool now.

Q236 ***Baroness Cohen of Pimlico:*** One sees why you have a Regulation that a train must move itself where it is under the sea in a tunnel. I just wonder what the way round this is?
Mr Goundry: There is an emotional response to being under the sea in a tunnel. In Switzerland in particular, and in Italy, there are many, very long tunnels which are not under the sea but under mountains and none of these requirements exists and there have not necessarily been major catastrophes. Given that it is a two-bore tunnel, if one bore is blocked by a broken-down train, there is another way round it. There will of course be delays, and you should try to design and build railway equipment which is reliable. One of the beauties of the Class 66 diesel locomotive is that it does not very often break down which is an encouraging thing and it is easy to put right when it does break down. Nobody can afford to buy locomotives of the complexity of the Channel Tunnel ones and offer a competitive service, bearing in mind that the road haulage option for the cross-Channel routes is extremely competitive and extremely lowly priced.

Q237 ***Chairman:*** Mr Goundry and Mr Meyer, you have been generous of your time and generous with your answers. Is there anything you would like to add by way of final remarks before I conclude the session?
Mr Meyer: No, thank you.
Chairman: May I thank you both most warmly? I asked you the almost impossible, given your schedule, but if you could send us the information I asked for at some point in the next two or three weeks, preferably by next Monday, that would be helpful. May I thank you both for being with us today? Thank you very much.

Supplementary written evidence from Mr Klaus-J Meyer, European Rail Freight Association

REGULATORY BODIES

Introduction

A Regulatory Body is to be established/set up in every Member State.

The main task of the Regulatory Body is to ensure a fair and non-discriminatory access to the rail network and services. The legal basis for the creation and competence of the Regulatory Body can be found in Article 10.7 of Directive 2001/12/EC and in Articles 30 and 31 of Directive 2001/I4/EC.

Organisational Independence

The Regulatory Body is a body independent from any infrastructure manager, charging body, allocation body or applicant. It is independent in its organisation, legal structure, funding and in its decision making. Decisions taken by the Regulatory Body shall be subject to judicial review.

Main Tasks

The Regulatory Body shall be an appeal body in relation to decisions taken by an infrastructure manager or a railway undertaking regarding discriminatory access conditions. Any applicant or interested party may lodge a complaint with the Regulatory Body if it feels that it has been treated unjustly, has been subject to discrimination or injured in any other way.

The Regulatory Body shall ensure that the charges set by the infrastructure manager are non-discriminatory. It shall supervise any negotiation between an applicant and an infrastructure manager on the level of the charges and intervene if necessary.

The Regulatory Body shall monitor the competition in the rail services market. In its monitoring function it shall decide on complaints or on its own initiative on appropriate measures to correct undesirable developments.

The Regulatory Body shall have the right to request relevant information from the infrastructure manager, applicants and any third party involved within the Member State concerned, which must be supplied without undue delay.

Co-operation

At European level and with the help of the European Commission, the Regulatory Bodies shall exchange information about their work and decision-making principles and practices with the aim to develop a common approach in order to avoid conflicting decisions.

List of the Regulatory Bodies established as of 15 June 2004

Austria: Schienen-Control Österreichische Gesellschaft für Schienenverkehrsmarktregulierung mit beschränkter Haftung (GmhB) & Schienen-Control Kommission Website: www.scg.gv.at

The Czech Republic: The Track Authority Website: www.du-praha.cz

Denmark: Jernbaneklagenaevnet

Estonia: Raudteeamet
Website: www.rdtamet.ee

Finland: Ministry of Transport
Website: www.mintc.fi

France: Mission de Controle des activites ferroviaires

Germany: Eisenbahn-Bundesamt (EBA)
Website: www.netzzugang-eba.de

Lithuania: State Railway Inspectorate

Latvia: State Railway Administration

The Netherlands: Nederlandse Mededingings autoritet (NMa)
Website: www.nmanet.nl

Poland: Office for Rail Transport

Portugal: Instituto Nacional do Transporte Ferroviario (INTF)
Website: www.intf.pt

United Kingdom: Office of Rail Regulation
Website: www.rail-reg.gov.uk

Norway: Statens Jernbanetilsyn/The Norwegian Railway Inspectorate
Website: www.jernbanetilsynet.no
and Samferdselsdepartementet
Website: www.odin.dep.no/sd

Switzerland: Commission d'arbitrage dans le domaine de chemin de fer/Schiedskommission im Eisenbahnsverkehr/Commissione d'arbitrato in materia ferroviaria/Arbitration commission for rail traffic
Website: www.ske.ch

November 2004

Memorandum by The Office of Rail Regulation (ORR) and the International Rail Regulator (IRR)

Introduction and Scope of Powers

1. This evidence is submitted jointly by the Office of Rail Regulation (ORR) and the International Rail Regulator (IRR). For ease of reference the evidence is set out under the specific questions but, as some areas overlap, the evidence should be read as a whole. The Committee will be aware of the Government's recently published White Paper "The Future of Rail". ORR is not yet able to analyse what specific impact implementation of the Government's proposals may have on matters discussed in this evidence.

2. ORR is an independent statutory body established under the Railways and Transport Safety Act 2003. It exercises, in Great Britain, a range of statutory powers under the Railways Act 1993, as amended by the Transport Act 2000. ORR's principal function is to regulate Network Rail's stewardship of the national rail infrastructure. It is also the licensing authority for operators of railway assets and approves agreements for access by operators to track, stations and light maintenance depots. ORR has concurrent jurisdiction under the Competition Act 1998, with the Office of Fair Trading (OFT), to investigate anti-competitive agreements and practices in the rail industry. It has a general duty under the Railways Act to promote competitive markets for the benefit of users of the railway.

The IRR

3. The IRR is a separate legal entity from ORR. ORR's Chairman currently holds this position. The IRR acts as an appeal body for capacity allocation and charging in relation to international services and is the licensing authority for international licences. Unlike for the domestic regime, the IRR does not approve international access agreements in advance.

Channel Tunnel Rail Link

4. Neither ORR nor the IRR has competition powers in respect of the Channel Tunnel Rail Link (CTRL). These are exercised by the Office of Fair Trading (OFT). In respect of the Tunnel itself, the French and UK Governments act jointly on regulatory and competition matters. In practice this means that the OFT undertakes competition functions jointly with the French National Competition Authority, and that regulatory matters are likely to be delegated to ORR and its French equivalent. In relation to through trains that run on Network Rail's network, ORR and OFT have concurrent competition powers, exercised jointly with the French NCA.

Q1. *What are the current barriers to entry in the international freight market?*

5. Freight markets within Great Britain (GB) are largely liberalised. A recent independent study by IBM Business Consulting Services produced a Liberalisation Index (http://europa.eu.int/comm/transport/rail/research/studies en.htm) showing GB as having the most liberalised market (for passenger and freight) compared to other European Union (EU) Member States (MS), Norway and Switzerland. The Index also showed that Sweden, Germany, Netherlands, Denmark, Italy, Switzerland and Portugal were making good progress in opening their markets (generally). Countries such as France, Belgium, Norway, Austria and

Poland were judged to have made significantly less progress. Greece, Ireland and Spain were deemed to have the highest existing market barriers.

6. Currently, there is only one international freight operator in GB—English Welsh and Scottish International Limited (EWSi). This company provides an international service from the UK through the Channel Tunnel (the "Tunnel"), and has held an international licence since August 1999.

7. To date ORR/IRR has not received a complaint about barriers to entry into haulage of international rail freight travelling to or from the UK through the Tunnel. (IKEA Rail approached ORR in April 2003 about starting a train haulage service in Spring 2004. Subsequently, they decided not to proceed with an application for a licence and ORR does. not know why that decision was made.) Therefore our comments are confined to practical and operational considerations for entry into haulage of freight by rail in the UK and to issues that we are aware have been raised at MS level. Not all the issues mentioned are specific to the haulage of international rail freight.

Barriers to Entry Within Other Member States

8. The following are the current barriers we have identified:

- The lack of transparency arising from capacity allocation administered by vertically integrated railways, both in relation to domestic and cross-border trade, particularly in countries where there is no effective sector regulator capable of acting *ex ante* to influence behaviour in the market;
- The lack of structural separation, which acts as a severe hindrance to effective competition affecting the fair allocation of capacity to rail facilities and the charges for that access;
- The difficulty in gaining access to:
  - track (including mainline track, terminals, sidings and marshalling yards), particularly where there is competing interest between the incumbent and the open access competitor and insufficient capacity for both;
  - maintenance facilities, although the entrance of new maintenance companies to the market could ease this situation; and
  - refuelling points for freight diesel locomotives or to an electric power supply;
- The absence of rolling stock leasing companies in most MS (other than GB). This continues to lead to complaints about access to incumbents' rolling stock;
- The difficulties experienced with access to drivers and traction;
- The lack of interoperability between rail systems. Technical and operational barriers favour incumbent operators and manufacturers and hamper the entry of new players; and
- Regulatory hurdles encountered in MS, including the difficulties of obtaining a licence and safety certification. Nine out of the 23 MS with railway systems have issued no licences to new entrants. The role of the flag carrier in safety certification and rolling stock acceptance procedures has also led to complaints.

Practical Issues Arising for International Rail Freight Traffic Entering UK Markets

9. *Locomotives and wagons*—the only locomotives cleared for the Tunnel and the national network are the Class 92 electric locomotives, which have Tunnel-compatible TVM430 in-cab signalling. Most continental freight wagons cannot operate in the UK due to the restricted loading gauge. Thus most freight traffic consists of intermodal containers that are transferred from rail to road for final delivery. With sufficient wagon and locomotive capacity in service to support all existing customer requirements, leasing companies have been reluctant to support "speculative purchases". Thus there is no existing pool from which to lease.

10. *Infrastructure capacity to and from the Tunnel*—the opening of section 1 of the CTRL led to the removal of Eurostar services from part of the domestic network and a subsequent rearrangement of South East Train's domestic passenger services. While this resulted in more space for freight through much of Kent, the number of services of all types through the crowded London area did not change. Consequently, this has had little beneficial effect overall as most freight has its origin or destination north of London. The completion of section 2 of the CTRL in 2007 and the complete removal of Eurostars from the conventional network between the Tunnel and London will free up more capacity, and a marginal reduction in the number of domestic services using some London termini may result if some domestic services are provided over the CTRL. Both of these effects will likely result in increased capacity being available for freight. Further, although because of speed differences it is unlikely that freight services could be accommodated over the completed CTRL route during the day, freight could be operated over it at night.

11. *Tunnel access charges*—it is widely acknowledged that the high level of access charges paid by operators for the use of the Tunnel is holding back traffic growth, and that lower rates would considerably increase the size of the economically viable cross-Channel rail freight market.

12. *Drivers*—a shortage of drivers combined with an increasing number of services has led to a bottleneck emerging, which all operators (passenger and freight) have been attempting to resolve. A prospective new operator training new staff from scratch would face a lead-time of approximately fourteen months per driver. Route knowledge is also an issue.

13. *Regulatory Barriers*—for the larger entrant regulatory barriers are likely to be strategic (in terms of project planning and timing) rather than absolute but there are significant costs for the small entrant, particularly the costs of purchasing third party liability insurance to the UK's current railways standard of £155 million. Procuring a licence to operate on the UK network is not unduly onerous. Generally ORR can issue a licence within two months of receiving assurance that industry agreements (including the appropriate level of insurance and a safety case) are in place. The safety case has, however, in the past added significantly to project time-scales for entry. Even for a limited activity it can take about 12 months to achieve. The Safety Directive, when implemented, will require a decision on safety certification within four months of receipt of the final documentation required which should speed up the overall process.

Q2. *To what extent are these barriers a result of failure fully to implement existing EU Directives in all Member States?*

14. The first railways package (consisting of Directives 2001/12/EC, 2001/13/EC and 2001/14/EC) includes a range of measures to liberalise international rail freight and to establish common policies and procedures across MS—the separation of essential functions between infrastructure managers and operators; a common format and tests to be met for licences for train operators; and matters concerning capacity allocation and charging and the establishment of an independent regulatory body.

15. While the UK is late in transposition (due March 2003), it is compliant in many areas including full separation of functions and having a regulatory body. ORR understands that only nine MS have notified transposition of the full set of Directives in the first package and three of those (Belgium, the Netherlands and Spain) are subject to infringement procedures for incomplete transposition. Nine MS do not yet have regulatory bodies in place.

16. Full implementation of the package would not specifically address the practical considerations detailed in paragraphs 9 to 13, but would potentially have some impact. The following highlights ORR's policies in relation to freight.

Charging for Freight Access to the Infrastructure

17. The GB freight-charging regime is consistent with the principles and purpose of the first package. ORR's current policy on freight access charges ensures that any freight operator able to pay the efficient level of incremental costs they impose on the network (estimated in 2001) will be able to operate. The charges are non-discriminatory as they ensure that all freight operators pay the same level of charges for equivalent traffic.

Access to the infrastructure and a timetabled path

18. Use it or lose it mechanisms ("UIOLI") domestic freight and passenger access agreements incorporate UIOLI provisions consistent with Directive 2001/14 that provide for access rights to be given up if not used for a specified period of time.

19. Transfer mechanism for freight operators—a competing operator may apply to the infrastructure provider requesting that an access right be transferred in cases where business moves between operators. The existing holder of that right may object on the basis of a "reasonable on-going commercial need", which will be assessed by the infrastructure provider in accordance with criteria that have been the subject of consultation with train operators and approval by the regulatory body.

20. Rights review meetings for freight—the infrastructure provider may call a meeting with the train operator at six-monthly intervals on the basis of a notice specifying those rights which the infrastructure provider considers should be surrendered or reduced on the basis of no continuing on-going commercial need. Any failure to agree will be referred to arbitration and the loss of rights would be subject to ORR consent. This may be a more flexible way of dealing with problems of non-use than the UIOLI mechanism, whilst also protecting the legitimate concerns of an incumbent operator.

Q3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

21. Full implementation of the first package by the UK will potentially facilitate the development of international freight markets by introducing the common format for operator licences to GB operators and by recognition of the common licence across MS, by clarifying the regulatory regime in respect of the CTRL and by implementing the provision for undertakings to request access to, and services from, a facility where there is no viable alternative. Although ORR recognises that such applications may be rare, this would permit entrants who currently have no other recourse to appeal to ORR should such access be refused. ORR continues to work with the Department on implementation matters, including the application of the first package in the context of rail freight markets.

22. The Commission should continue actively to enforce its existing legislation, and challenge those MS who fail to demonstrate improvements in the liberalisation of their markets.

Q4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

23. The second railways package, due to be implemented in 2006, also has the potential to facilitate the growth of international freight, in particular by accelerating full liberalisation of those markets from 2008 to 2007 and by harmonising high speed and conventional interoperability requirements. It also requires implementation of the Safety Directive which will modernise and harmonise safety regulatory structures and methods across MS, requiring a full review of GB's safety case regime.

24. The Commission's proposed third package, currently under negotiation, may bring further harmonisation eg in train driver licensing.

Q5. *What action should the UK Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

25. ORR cannot comment on behalf of the UK Government. ORR will, however, have a continuing role as a regulatory body and as a National Competition Authority. It will continue to enforce its concurrent powers under the Competition Act 1998 where it finds evidence of anti-competitive agreements and abuses of a dominant position, and pursuant to the Modernisation Regulation 1/2003/EC will apply Articles 81 and 82 where there is an effect on trade between MS. ORR will also continue to monitor railway markets in Great Britain and, where appropriate, use its concurrent powers under the Enterprise Act 2002 to refer a market to the UK Competition Commission should there be reasonable grounds to suspect that any feature, or combination of features, of a market for goods or services prevents, restricts or distorts competition in the supply of services relating to railways. ORR will continue to participate in relevant European forums to co-operate and share best practice with other regulatory bodies and NCAs.

Chris Bolt
Chairman of the Office of Rail Regulation and International Rail Regulator

August 2004

Examination of Witnesses

Witnesses: MR CHRIS BOLT, Chairman, MR MICHAEL BESWICK, Director of Rail Policy and MS ANNETTE EGGINTON, Head of Competition Policy, Office of Rail Regulation (ORR), examined.

Q238 ***Chairman:*** Good afternoon Mr Bolt and your colleagues. Thank you so much for coming along today and for your written evidence in advance. As you would imagine, we have lots of questions. Before we start, is there anything you would like to add by way of introduction? Perhaps you might also introduce your two colleagues.

Mr Bolt: I am Chris Bolt, Chairman of the Office of Rail Regulation and also, in a personal capacity, International Rail Regulator. On my right is Michael Beswick who is Director of Rail Policy at ORR and on my left, Annette Egginton who is Head of Competition Policy at ORR and also has responsibility for European matters. Just briefly, by way of introduction, the Office of Rail Regulation is a new regulatory body which came into existence on 5 July this year to replace the individual rail regulator. The board of ORR is five people at the moment, myself and four non-executive directors and we exercise the same functions that the rail regulator has done previously under the Railways Act 1993. The primary role of ORR is currently focusing on the regulation of Network Rail, both in terms of its stewardship of the national rail network and in terms of access to the network. I said that I hold the position of International Rail Regulator in a personal capacity, but in practice, the work is done through the same people, particularly the people with me today. That role is different from the ORR role where, instead of approving access agreements as we do for domestic services, I have a role in consulting on international access agreements and dealing with appeals on those matters, but do not have the same powers that ORR has under the Railways Act. As you may know, there are proposals, if the European rail Directives are transposed in a particular way, for the two roles to be combined because the distinction between domestic access and international services will disappear under those arrangements.

Q239 ***Chairman:*** That is very helpful. I cannot say I entirely understand the relationship, but I am sure that at the end of the session I shall be much wiser. Before we get into things, in your written evidence, you said, in relation in the latest White Paper, *The Future of Rail*, that your office had not yet been able to analyse what specific impact this might have on rail freight and so on. We are two or three months on now since you did your written evidence, are you any further on in your analysis of that?

Mr Bolt: In some respects I think we are. The White Paper talked about a new deal for freight and I should emphasise that these remarks are very much about the Great Britain rail network, rather than specifically international services. What that means is still being worked out in detail, but the idea that freight operators should have potentially longer-term access rights for a core part of the rail network, the core freight routes, is one that has gained a fair bit of support. ORR will be consulting, probably before Christmas, on the criteria we might use in looking at applications for long-term access agreements from freight operators, setting out the conditions that we might want to attach to that to make sure that there is still competition between freight operators, but it gives the rail freight sector as a whole the right opportunities to develop rail freight as a business. Obviously, the other side to that is what freight operators pay by way of charges and tomorrow we are publishing a consultation paper which is the first stage in looking at the structure of Network Rail's costs and the implications that might have for access charges. Although freight access charges are fixed in the existing agreement until 2007, it is obviously important in terms of giving medium-term certainty, how those charges might change over the medium term. Again, the principles in the White Paper are that where freight uses a mixed part of the network, it should continue to pay charges on broadly the current basis, but recognising that if there are enhancements to the network for freight-only purposes, that freight operators would have to pay the full cost of those enhancements.

Chairman: That is a very useful starting point and I am sure we shall take up lots from that. Lord Shutt is going to start the questions.

Q240 ***Lord Shutt of Greetland:*** I wonder whether we could start on process. This is hypothetical, I regret it, but there we are. Let us assume we have got a situation where there is somebody in Manchester and they are shifting 100 road wagons a week from Manchester to Milan and they all need replacing. This person says "Well, I think I'll give rail a go, but I'm not buying any private wagons or anything like, because I'll give it a go for six months and we'll see how it goes". This person firstly has got to find somebody who becomes the operator. Is there any choice in that? How many doors are there to knock at for a start? When someone has been found, what has to happen in order that this trade can be carried and that it can get to Milan? What would the difference be if these were perishable goods as opposed to non-perishable goods? Would there be a difference? How does all this come to pass, if that decision is made today that "Well, I'll give rail a go"?

Mr Bolt: A nice list of questions there. The answer clearly reflects what I was saying right at the beginning about the different roles under domestic legislation and for international services and it is, as

Mr Goundry was saying in the last session, that there is currently only one operator going through the tunnel which can carry international services. On this-side-of-the-tunnel portal it is a different matter: there are currently four licensed freight operators and others looking at entering the market. So if it was simply a matter of getting freight to the Channel Tunnel entrance from the UK side, there is that choice of operator. Let us assume we are looking at a single end-to-end service, the first and most important issue is whether you can actually identify a single path which gets you from one end of your service to the other. The operator would, in principle, need to arrange access through each of the Member States, but there is an organisation called Railnet Europe which is picking up on the requirement in the Directive for Member States to co-operate on providing access and that organisation has a catalogue of routes and the Manchester to Milan one is one of those that would be covered in that catalogue. Even if you could identify a path if there were opportunities to get it with the frequency that you were describing, simply identifying access is only one part of getting the whole service operating. When it is a matter of looking at the domestic part of that route, there are well-established procedures, including powers to come to ORR for direction to provide access, licensing powers which would cover the operating side of that equation. That is much more difficult where you are looking for an end-to-end service of the sort you are suggesting. So, getting the access identified is the first, but only a limited part of that operation. I think that explains why there are relatively few long-distance international services through the tunnel, because in practice, unless EWS has effectively a joint venture operation with European operators and it is developing that sort of relationship with SNCF, it is actually very difficult to go to one person and get that end-to-end service. As for perishables, Mr Beswick may be able to add to that.

Mr Beswick: Very clearly it is really the same story: rail freight in Great Britain does carry perishable traffic and carries it successfully. Clearly, in order to carry perishable traffic successfully, you have to have reliability in the transit and you have to do a deal with the infrastructure operators on the route to ensure that you are getting that reliability of transit. We have got processes in place to do that in Great Britain, but they are less well developed elsewhere.

Q241 ***Lord Shutt of Greetland:*** This is all very well. You are putting me off a bit really. If I am in the shoes of this potential trader, I think 100 wagon loads a week is a fair bit of trade. OK, I will stick with you, but how long is it going to take before you sort this out?

Mr Bolt: I think you have almost answered your own question. It is a complicated process. It could take a long time and I agree that is not a very encouraging answer to you when you are looking at transferring traffic from road to rail. It is the reality, unfortunately, of the position we have got, given the way the Directive is set up and the fact that we do not have the equivalent of the Great Britain regulatory framework yet established in other Member States which would give the same opportunities to move relatively quickly to give access, provided there is capacity on the network.

Q242 ***Lord Shutt of Greetland:*** You are not giving me any encouragement. Is it days, weeks, months, or could it be more than a year before we can sort out whether we can shift this traffic this way?

Mr Bolt: I think the experience is that it is certainly months and could be longer, but we do not have much experience.

Ms Egginton: We do not have practical experience of transporting international rail traffic, no, but it really does depend on whether the current operators are incentivised enough to do it because actually it is not we who are going to be pursuing this piece of traffic through the tunnel, it will be the operators themselves. So if EWS see a business opportunity, or any of the other operators but practically EWS for the reasons that we discussed previously, if they see the incentive to negotiate with the various infrastructure managers to get a path through, that traffic will be carried. It really is a question for EWS in a sense as to how long that would take.

Q243 ***Chairman:*** I am anxious to move things on because we have so many questions to ask. Just let me make one observation to you and then perhaps we could return to the idea later on. What has come across to us from other evidence so far is that the infrastructure operators across the Member States have almost no incentive to be customer orientated. They have no incentive to think about what the real needs are of industry and the wholesalers, retailers and distributors. You are presenting a picture that gives much the same impression and indeed even, almost, that the regulators have not. The people who want to try to move things around, the rail operators, have got to try to fight their way through this jungle of different Member States and nobody they are dealing with other than them have got any incentive to be very efficient and to minimise the cost and speed things up. That is the impression we have.

Mr Bolt: I hope, my Lord Chairman, that it does not sound as though I am being defensive. Clearly ORR with its responsibilities in Great Britain, which it takes very seriously, can deal with those issues up to the entrance to the tunnel. We obviously, through, for example, participation in the European

Regulators' Group, talk to the bodies in other countries about our experience. Those bodies generally are not as well developed as in Great Britain and, in some cases, Member States have not set up the independent regulatory bodies yet. Until that happens, the practical problems that we have been talking about will almost certainly remain.

Chairman: Again, I would sooner return to this, otherwise other colleagues will not get in; but I will return to it.

Q244 ***Lord Swinfen:*** A slightly different aspect of this. To what extent can the Office of Rail Regulation and you, as the International Rail Regulator, act to ensure that there is adequate capacity of track and other infrastructure within Great Britain for international rail freight operation. I am thinking in terms not only of the track, but of train length, axle weight, gauge, things of that sort.

Mr Bolt: There is clearly a number of things that we can, and are, doing in that respect. The last interim review of Network Rail's access charges set out the deliverables that Network Rail had to work to for the next five-year period and that included, for example, no reduction in the capacity on different parts of the network and, by capacity, I mean issues like axle weights and loading gauges and issues of that sort. That is, in a sense, simply saying that what is available at the moment should not decline. Two questions follow from that. One is: what can be done to improve that, where there is a clear requirement from rail freight and to ensure that freight operators can get access to capacity where it exists at the moment? The powers that we have under the Railways Act, the access provisions through Sections 17 and 18, provide a very clear basis that if a freight operator approaches Network Rail, there is capacity available, and if it cannot agree terms, then there is a mechanism through Section 17 of the Act to come to ORR and we will look at that application against the public interest duties which are in Section 4 of the Act. If we are satisfied that the capacity is available and there are appropriate terms for an access agreement including price, then we can direct Network Rail to make that access available to a freight operator. When it comes to enhancing capacity, I think this is one area where the framework that is set out in the White Paper should make the future arrangement clearer, in terms of giving Network Rail the leading responsibility to develop strategies for particular routes, which look at future demands for both passenger services and potential rail freight uses. So if there is a clear case for providing for growth in capacity on the network, either passenger or freight, that is identified, it is consulted on properly with interested parties, that is operators, freight users as well as Government, that becomes a clear specification of what Network Rail is working to and we can make sure, if that is properly funded, that Network Rail then delivers capacity enhancement. So there are a number of things that we can do in respect of the Great Britain network.

Q245 ***Lord Swinfen:*** To take the example of freight traffic between Manchester and Milan that Lord Shutt mentioned. Quite obviously, if you have freight traffic between Manchester and Milan, you are quite likely to have European locomotives and trucks coming into this country and running on British Rail. Can that work today, or do we have to alter our infrastructure to do it; and if we have to alter the infrastructure, what are you, as the International Rail Regulator and your Office of Rail Regulation in Britain doing about that at the moment?

Mr Bolt: To emphasise, the area of involvement is more through the Office of Rail Regulation in terms of the domestic controls provided by the Railways Act rather than the International Rail Regulator who simply deals with third party appeals against agreements between train operators and the infrastructure provider in respect of international services. Clearly, the gauge, for example, on different parts of Network Rail's network is different. The route through to the Midlands from Felixstowe has recently been enhanced for nine-foot-six-inch containers. That is still not European gauge, but that is the output that the Strategic Rail Authority said it was prepared to see funded at the time of the last Network Rail access charge review. For the future, if there are further enhancements on that route, for example to move to European gauge, it would be a question of the provision of funding for that. Freight operators could fund it directly, and there is a basis for that, then we could make sure that Network Rail undertook the work. I think in practice on that route, nine-foot-six is likely to be the limit, certainly for the medium-term and the priority is turning to other parts of the network, for example the routes down to Southampton, where the settlement from the last review, reflecting what the Strategic Rail Authority said it was prepared to see funded, does not include that sort of enhancement.

Q246 ***Lord Swinfen:*** I must admit, I am a bit disappointed because I drive up and down between just this side of Dover and London on a regular basis and I would love to have the freight traffic off the road from Dover and Ramsgate and on to the rail.

Mr Bolt: If there is capacity on the network, then freight operators can come to us and we can make sure that they get access on appropriate terms. If the capacity is not there, the question obviously is how any enhancement is going to be funded. If it can be funded, ORR can make sure it happens.

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Q247 ***Lord Fearn:*** I listened with interest to what you were saying to Lord Shutt and the word "choice" was very much one that I seized on. Let us take the Channel Tunnel itself. A phrase has been twice used now "It stops at the Channel Tunnel"whether it be legislation or whatever. What choice has the operator got now for traffic which is going to travel through the Channel Tunnel? Is there going to be one? There are difficulties are there not? There is only one type of locomotive going through at one time, is there? What choice is there going to be?
Mr Bolt: I have made it not sound terribly encouraging. Some of your questions are actually not best directed to me, either in my ORR or IRR capacity, because the Channel Tunnel is not something for which I have any responsibility. It is regulated through inter-governmental agreement between the UK and French governments. In the same way the Channel Tunnel Rail Link (CTRL), where there is debate about freight access to that link, is not something I have any powers or ORR has any powers on, other than in the limited sense of an appeal route through the IRR side as described previously. If there are issues about charging or access to either the Channel Tunnel or CTRL, those are dealt with either directly by the Government or by the Office of Fair Trading as competition authority. The regime in the Railways Act that I was describing earlier requiring access to the network does not apply to either the Tunnel or to CTRL. So in practice, the position is as you are describing: there are limits to choice through the Tunnel and only one UK operator operating freight through the Tunnel. That is not something that ORR or I as IRR have any role in changing.

Q248 ***Lord Fearn:*** Are you allowed to say whether you think that is a good thing or a bad thing?
Mr Bolt: In terms of the Great Britain network, we have set out very clearly in ORR our view that a choice between different rail freight operators is a good thing. We have seen, for example, that EWS, which previously carried mail traffic, lost that contract and Great Britain Railfreight now has a contract to run some mail trains and clearly the Post Office, as a user of the network, feels that in switching operators there is a benefit and it will get better service.

Q249 ***Lord Fearn:*** Is the mail the only example you can think of?
Mr Bolt: Mr Beswick can give you more details.
Mr Beswick: For instance, what happened in the coal traffic in the UK is that Freightliner Heavy Haul is now a haulier of coal and that is competition and that is a good thing, opening up choice in shifting coal around. We do not have that for the Channel Tunnel traffic.

Q250 ***Chairman:*** The picture you present, I am sure faithfully, of the Channel Tunnel situation would be rather disconcerting to the general public. It is that you can be very active in trying to ensure that there is competition in rail freight within Great Britain, but where common sense says rail freight should have an advantage, long distances, carrying major routes through Europe from the UK, there is a mish-mash of bodies and authorities, none of which is you; except with a different hat on There is the International Rail Regulator, there is an inter-governmental agreement, there is the Office of Fair Trading, but on the face of it, that is an absolute mish-mash. What is the point of you working hard to ensure that freight can get anywhere, except into Europe? As I understand, rail freight has 11 per cent of the domestic market but less than two per cent of what goes into Europe. Is anybody concerned about that? How does rail freight increase its market share into Europe, when on the face of it, there is nothing like your ORR trying to achieve that? Does that seem to you, as professionals in the field, a problem? I do not ask you for the answer, because the answer quite reasonably is for the politicians to decide to some extent. Does that seem to be a problem?
Mr Bolt: Yes, I think it does seem to be a problem. There is a practical issue clearly that, even if all the paths for the Channel Tunnel which were designated for freight were fully used, it is still a pretty small proportion of overall UK rail freight. That is no reason not to see those paths being used to the full. If we were in a position where the EU rail packages were fully implemented and we had regulatory bodies covering the Channel Tunnel and France and other Member States which had the same sort of powers and approached issues in the same way that ORR did, then the practical problems of developing new services would be very much less.
Chairman: One last question on the Channel Tunnel from Lord Walpole.

Q251 ***Lord Walpole:*** I do not know quite how you are going to answer this, because you said it was nothing to do with you. How are the access charges to the Channel Tunnel itself, regulated? What action do you think the Government could take if it wished to reduce them? I know it is nothing to do with you at all.
Mr Bolt: The simple answer is that they are "regulated", in inverted commas, through the inter-governmental agreements. So, it is very much a matter for the UK Government and the French government, if they want to change the basis of charge, to negotiate those changes.

Q252 ***Lord Walpole:*** But what are this company which Lord Shutt is trying to get to move all his stuff from Manchester to Milan going to do? Are they

going to have a chat with the governments of France and England to find out what we are going to do about the charges for the Tunnel? Where do they find out?
Mr Bolt: Where do they find out what the charges are? They would have to approach Eurotunnel, or an operator who was able to run through the tunnel, who would have that negotiation with Eurotunnel that Mr Goundry was describing earlier. I agree that it is not a very satisfactory system.

Q253 ***Lord Walpole:*** It seems incredibly woolly, does it not?
Mr Bolt: The fact is that the construction of the Tunnel was set up on a particular basis and the provisions in the Railways Act for clarity of charging, transparency of charging and for regulatory control over charging was not set up in the same way.

Q254 ***Lord Walpole:*** Do you not think you ought to take this over as well?
Mr Bolt: If both governments were to propose a change which put the Channel Tunnel on to exactly the same basis as other parts of the network and we had the same sort of regulation on the French side that ORR has on the Great Britain side, I think some of the practical problems would be less.

Q255 ***Lord Walpole:*** Would this not be sensible?
Mr Bolt: I would have a personal view on that. I think it is a question you would need to address to the Department of Transport.
Chairman: I think you have gone as far as you probably can, but that is helpful nevertheless. Lord Haskel.

Q256 ***Lord Haskel:*** May I revert to an area where you do have some authority, or some say, and that is the rail freight terminals in Great Britain. What is the position regarding open access to these rail freight terminals? Are there any European Directives which control this? Do we satisfy those Directives?
Mr Bolt: The practical position we are in is that there are 1,000-odd freight terminals and they range in size from the major new ones like Daventry to much smaller facilities. Most of the facilities were exempted from the provisions of the Railways Act, at the time that the Railways Act was brought into force, by the decision of Government. It is only more recent ones, but that particularly includes ones like Daventry, which do have open access provisions where operators can come to us under the terms of the Railways Act and if they cannot agree access with the facility owner, can ask us to direct that access is made. That is the position we are starting from. Clearly the first package did address the question of access to freight facilities and I think our interpretation of that is that, when fully transposed— and that is one element of the package which does not have its immediate parallel in the Great Britain system— it would extend the ability for freight users to seek access to other operators' terminals. So the fact is that the first package has not been fully transposed into UK law because in many areas we are actually ahead of what the first package would require because of the Railways Act provisions. The question of freight terminals is one where potentially the first package, when transposed, would move the current framework on and allow much wider open access to freight terminals.

Q257 ***Lord Haskel:*** What about the terminals where you do not have authority? Is it up to the freight company to negotiate with the owner of the freight terminals?
Mr Bolt: Essentially yes. There may be circumstances, if you could show that a particular terminal was so crucial to a particular part of the business that the refusal of the owner to agree to access was an abuse of dominance, where you could address that matter to the competition law. However, there are real questions about where that would actually apply and it is obviously a much less direct process than is available through the Railways Act where, if someone cannot agree access terms, they have a clear right under the Railways Act to come to ORR for a direction under Section 17.

Q258 ***Lord Haskel:*** Who are the owners of these freight terminals?
Mr Bolt: In many cases it is the existing freight operators. Annette, do you have any details on the breakdown?
Ms Egginton: It does vary. EWS, for example, operates a significant quantity of these terminals, but so do other UK freight operators. Terminals formed part of the package of assets, the operation of which was passed to the private freight sector at privatisation of British Rail. The new multimodal terminals which Mr Bolt just referred to, such as Daventry and Hams Hall, are owned and operated by entirely private individuals and are open access facilities.

Q259 ***Lord Haskel:*** If I were the owner of one of these terminals and a freight operator, I would not be obliged to allow my competitor to come and use my freight terminal?
Ms Egginton: No you would not, but one of the things that Mr Bolt was referring to was under the first package. If there is no viable alternative, there is an ability for you approach us on appeal to ask for us to intervene. Viability is different to that interpreted under the Competition Act, inasmuch as it is railway confined, that is, if you are running a railway service, you require that terminal, and if there is no other

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viable alternative, you have an ability to appeal. The Competition Act is less specific than that, because relevant markets may be transport markets for the purpose of assessing whether a terminal is essential. It is not quite as sharp at all for railways and that is what the Commission was thinking of when it developed that Directive, that it would be confined to railway markets and rail service requirements.

Q260 ***Lord Haskel:*** It sounds very long winded.
Ms Egginton: It has clearly not been operated yet, but it should be less long winded than what we have currently. Certainly if the facility is exempt from the Railways Act and not an essential facility under competition law, then it is one step forward.

Q261 ***Chairman:*** From your knowledge of the industry, do you expect any such appeals? Do you think this will be an effective tool when it is used?
Ms Egginton: I would not expect there to be a flood of appeals. Those appeals would clearly have to come from an operator seeking access, as we discussed previously. There is hardly a flood of them knocking at the door of freight terminals trying to get into the UK. I would imagine that it is not going to be a huge amount of activity.

Q262 ***Chairman:*** You do expect it to be used?
Ms Egginton: It is a tool which is able to be used.
Mr Bolt: Clearly, in terms of access rights, we have built in flexibility. If a freight user switches from one rail freight operator to another and there are provisions for the access rights to switch, what in a sense you want to ensure is that if those freight flows are dependent on access to a freight terminal, the access to the freight terminal would switch in similar circumstances, so you have end-to-end competition as a reality for freight users, so they have the choice for the whole of the service.
Chairman: That is the kind of thing I had in mind.

Q263 ***Baroness Cohen of Pimlico:*** Do you believe it to be central for effective regulation of access, that, as in the UK, infrastructure and operators are in totally separate organisations?
Mr Bolt: There is a balance to be struck. One of the points which came out of the White Paper was that train operators and network operators need to be talking enough to each other; that the way particular parts of the operating network delivers proper services and if there are conflicts, operational problems on the day, those are resolved. What we have seen with the UK framework is that those practical operational issues can be addressed and in terms of some of the other questions that we have been talking about, access to the network, having separation between the infrastructure manager and the train operator, particularly where there are competing users on a single path of the network, makes the whole issue of getting access to the network much more straightforward. I think that is why ORR's position would always be that for the majority of network at any rate, where there are those competing uses and freight operators are in competition, having separation between the infrastructure operator and the train operators will make that whole process work much more effectively, ultimately to the benefit of the freight users.

Q264 ***Lord St John of Bletso:*** We read in your written evidence that the recent independent study by the IBM Business Consulting Services showed Great Britain as having the most liberalised market for passenger and freight compared with other EU Member States. Can you tell us what regulatory bodies there are similar to yours? My Lord Chairman mentioned that there were no other similar bodies to yours, but what bodies are there in other European countries with powers and responsibilities comparable to your own? How far is this required under existing Directives? Mr Meyer, our previous witness, Secretary General of the European Rail Freight Association, was sceptical of the ability and the muscle of existing or potential operators in other parts of Europe to challenge those operators with a dominant position.
Mr Bolt: It is clearly the case that the Office of Rail Regulation and the Office of the Rail Regulator previously has a longer history and developed its expertise and case law much more than other Member States. Although there is a requirement for a regulatory body in all Member States now, in many cases in practice, it is part of the transport ministry. All Member States are developing the independent regulatory body that is required under the Directives but in many cases have not got very far down that route. The sorts of the bodies that are being created also range quite significantly in size from 10 people up to the 100 or so that ORR represents. The answer to your question is that the development is very patchy. Many of the Member States have been looking at how ORR operates as a potential model for an independent regulatory body, but it is a matter of how resources are devoted to that and expertise, as well the powers that that regulatory body has and the requirements in the Directive would not go as far as ORR's powers under the Railways Act. It would be more of an appeals route rather than the range of directive powers which ORR has.

Q265 ***Lord St John of Bletso:*** How long do you think it will take for there to be truly independent regulatory bodies throughout Europe? Is this achievable? Secondly, you mentioned the First Railway Package earlier on in answer to Lord Haskel's question. Are you confident that the Second

Railway Package, to be implemented in 2006, will facilitate the growth of international freight?
Mr Bolt: I am not sure I should like to predict how long it would be for regulatory bodies or Member States to develop the professionalism and expertise and experience in dealing with cases that would resolve some of the problems that we were talking about earlier. To some extent it is a matter both of the attitudes of the Member States themselves and of the Commission in raising standards in all Member States up to a common level. We are certainly working with the Commission and with the regulated bodies in other Member States to explain what we are doing as an attempt to spread what we would see as best practice. It will take some time for that best practice to spread. In terms of the Second Package, I will just say a few things and my colleagues might want to add to it. The Second Package addresses some issues which will help to reinforce the trends that we are all looking for. There are some issues in there which I know some of the freight operators have been concerned about in terms of mandatory performance regimes and driver licensing and issues of that sort. I am sorry, that last one is in the Third Package. There is certainly some evidence that the Third Package might go too far in some requirements, but we would genuinely support the Second Package in terms of reinforcing those moves and helping to develop the consistency across Member States that would help to get the end-to-end international services operating more effectively.

Q266 ***Lord St John of Bletso:*** Do you therefore, bearing in mind that it is going to take much longer than you would have hoped to get these independent regulatory bodies, believe that competition law is totally inadequate and should be redrafted?
Mr Bolt: When you say competition law...?

Q267 ***Lord St John of Bletso:*** I am talking about competition law in freight services across Europe. There is no point in having legislation unless it is fully enforceable.
Mr Bolt: The way the competition provisions work within Great Britain is that we actually see this as an ability, because we are a combined economic regulator and competition authority with joint competition powers, to see the competition law and the rail Directives reinforcing each other. So there may be instances where the specific rail provisions are more effective than competition law, as we were talking about earlier: in others the reverse will apply. I think the fact that as far as I am aware we are the only rail regulatory body in Europe which also has competition powers, may be something which other Member States will want to look at to make sure that specific rail Directives and competition provisions are reinforcing and operate together in a way which gets access to the network to allow rail freight services to develop.

Q268 ***Lord St John of Bletso:*** Do you want to make a comment about the competition laws?
Ms Egginton: I could. Most Member States of course adopt Articles 81 and 82, so our competition laws are fairly consistent across the board. We would say there is still a role for *ex ante* regulation rather than *ex post* regulation which has limitations in the way that we described earlier. I would not say that either should be scrapped fundamentally, but they should both be applied.

Q269 ***Lord St John of Bletso:*** Yes, that was what I was really getting at: having a sectoral regulator who could apply *ex ante* legislation, that is essentially what you would be looking for?
Ms Egginton: Yes.
Mr Bolt: It is clearly part of the UK's approach to implementing competition law with the Competition Act and the Enterprise Act that sectoral regulators should exercise those powers concurrently with the Office of Fair Trading (OFT) because of the benefits of looking at alternative routes to enforcement and to promoting competition. That opportunity does not exist to the same extent where competition law is looked at by one body and rail issues by another body.

Q270 ***Lord St John of Bletso:*** I declare an interest. I am a lawyer by training; I specialised in social law and obviously one of the problems in the European Union is that it is such a lengthy procedure that you want to have a position where a regulator can apply *ex ante* legislation which can be *ad nunc* rather than *a tempore more* in the future.
Mr Bolt: Which is one of the reasons that specific powers like Section 17 in the Railways Act to require directions for access may be much quicker and more direct that the general competition law.
Chairman: Lord Shutt wants to come in with a supplementary. He is the only guy from Yorkshire I know who keeps talking from the perspective of Manchester. I shall have a word with him afterwards!

Q271 ***Lord Shutt of Greetland:*** We can change it; we can rewrite the script. I am just wondering if we are being altogether fair. In the context of rail freight, what is the major element of regulation that you are working on at present that is really of current concern for you?
Mr Bolt: In terms of rail freight, there are two issues that we are working on at the moment which will have the biggest impact going forward. One is looking at the criteria for approving long-term access rights and in a sense the contractual framework that goes with that to make sure, through things like the

network code, the multilateral part of the contracts, that freight operators can, in a sense, get onto the network on a level playing field with other operators. That is one thing. The other, which goes alongside it, is making sure that the basis of access charging is clear, transparent, properly understood and, if there are enhancements in the network for freight purposes, which freight operators are prepared to pay for, or where there are freight grants available, that Network Rail then gets on and delivers those enhancements.

Q272 ***Chairman:*** In paragraph 17 of your written evidence, you deal with the question of access charges and transparency and the sentence is very carefully worded, as I would expect "... non-discriminatory as they ensure that all freight operators pay the same level of charges for equivalent traffic". That is consistent with dual pricing is it not? Say one operator has a lot of traffic and they negotiate one lot of access charges for infrastructure and then someone wants to break in, but is inevitably a much smaller operator, could the infrastructure operator not say that somebody with a lot of traffic is entitled to a lower price than somebody with a small amount of traffic?

Mr Bolt: No, I do not think the intention behind our access charging provisions is that there is some sort of national quantity discount. It is looking at the costs of access to different parts of the network for different traffics and making sure that if one freight operator is losing business, or if a freight user is looking at a choice between one freight operator and another freight operator, the basis of access charging is not distorting that choice, it is the service which the freight operator is providing, the freight operator's own efficiency in running trains, which is driving that competition. We do not want to bias competition between freight operators through the access charging regime.

Q273 ***Chairman:*** So dual charging systems would not be acceptable?

Mr Bolt: The important point in that sentence is "equivalent traffic"; it is recognising that charges for coal may be different from charges for container traffic, but they should not be discriminatory between different operators.

Chairman: Baroness Cohen has been very patient; she has the last question.

Q274 ***Baroness Cohen of Pimlico:*** I am not sure this is a very interesting question. We are late in transposing the First Railway Package. Does it matter and what can we be doing about it?

Mr Bolt: In most respects, it does not matter.

Q275 ***Baroness Cohen of Pimlico:*** That is what I thought you would say.

Mr Bolt: The Great Britain regulatory framework is in advance of the First Package in most respects. I think there are three or four issues where it potentially matters: the access to freight terminals that we talked about earlier is one; clarifying the regulatory position of Channel Tunnel Rail Link (CTRL) is another. There are issues about safety regimes which may be affected by transposition, but they are relatively minor issues. What can we do about it, to the extent it matters? It would be desirable to be fully compliant with the Directive. I think the answer is, again, that we have to address those issues with the Department for Transport which is responsible for the transposition.

Q276 ***Baroness Cohen of Pimlico:*** Does it need any legislation?

Mr Bolt: It will need secondary legislation.

Q277 ***Chairman:*** When we urge other Member States to implement Directives and so on, it is slightly irksome to us if we say that to them and they point out that we are not fully compliant.

Mr Bolt: Given that we are well in advance of the First Package on most issues, not to be fully compliant does not make it as easy as it would otherwise be to advocate the Great Britain model in all Member States.

Q278 ***Chairman:*** What is the lack of clarity about the position regarding the Channel Tunnel Rail Link that you referred to?

Mr Bolt: One of my colleagues will fill in the detail. The essential issue is that the Channel Tunnel Rail Link is not covered by the access provisions of the Railways Act. The competition issues are dealt with by the Office of Fair Trading and ORR does not have concurrent powers. The only provisions for international services are the appeal routes to me as international rail regulator, if a third party objects to the notified agreement. Given the proposals for developing use of the Channel Tunnel Rail Link for both domestic service and potentially for freight to clarify how that works and ideally to put it on exactly the same basis as other domestic services would help to develop the freight market on a level playing field.

Q279 ***Chairman:*** We are not about to resolve that.

Mr Bolt: It could be resolved by Government, as it transposes the first package, if Government wished to. For the Channel Tunnel Rail Link: the Channel Tunnel itself is different, as we were saying earlier.

Q280 ***Chairman:*** We will no doubt ask the Minister on Monday when we see him. Thank you so much, you have been extraordinarily patient. We have kept you longer than we should and I apologise for that, but you have been very helpful to us. Is there anything you would like to add?

Mr Bolt: I do not think so My Lord Chairman, thank you very much.

Chairman: Thank you so much. The meeting is closed.

MONDAY 8 NOVEMBER 2004

Present	Cohen of Pimlico, B	Shutt of Greetland, L
	Eccles of Moulton, B	Swinfen, L
	Fearn, L	Walpole, L
	Geddes, L	Woolmer of Leeds, L (Chairman)
	Haskel, L	

Letter to the Clerk of the Sub-Committee from Mr Heinz Hilbrecht, Director of Directorate-General for Energy and Transport and Mr Lowri Evans, Director of Directorate for Competition, European Commission

HOUSE OF LORDS SELECT COMMITTEE: INQUIRY INTO EUROPEAN RAIL POLICY

Thank you for your recent invitation to submit evidence in connection with Sub-Committee B's inquiry into the implementation of the European Union policy of open access for international rail freight services.

We have pleasure in enclosing a joint reply to your questions.

17 August 2004

Memorandum by the Directorate-General for Energy and Transport and Directorate for Competition, European Commission

1. *What are the current bariers to entry in the international rail freight market?*

Entering the international rail freight market can be onerous and costly for a number of reasons. Railways are a capital intensive business with historically low profit margins and rates of return. Owing to the different technical and operational specifications of the national railway systems in EU Member States the investment needed in rolling stock and staff can be considerable. This may be a particular stumbling block for smaller railway undertakings. In fact, since the opening of cross border intermodal rail freight in 1993, followed by conventional freight services in March 2003, there have been very few new entrants on the market. Besides this general entry barrier there is a number of process-related features that can constitute barriers to entry.[1]

Access rights

Directive 2001/12/EC grants open access rights to licensed railway undertakings for international rail freight services on the Trans-European Rail Freight network. In some Member States of the EU such access rights have not been established legally as the national implementation measures have not been adopted yet.

Licensing

For railway undertakings, the process of obtaining a licence can be complex and time consuming. In some Member States, insurance requirements are particularly onerous. Insurance requirements differing widely from Member State to Member State can constitute a barrier for smaller railway undertakings.

Safety certification

There are differing safety certification philsophies across Member States and new international operators are subject to repeated approval processes when entering the market, requiring the provision of evidence that is not then mutually recognised between Member States. There is little indication of formal liaison between national safety certification bodies during the certification of international operations thus exacerbating the lack of cross acceptance in terms of both traction and operating approvals. National networks are not fully technically interoperable and hence railway undertaking must comply with national standards. In some Member States therre is inadequate transparency of the national technical requirements and the approval process to be applied. This is expected to change thanks to the transparency obligations imposed by the Rail Safety Directive 2004/49/EC adopted in April 2004.

[1] DG COMP and the national competition authorities (NCAs) recently conducted a market survey into barriers to competition in rail freight. Its main findings also confirm the main elements presented in this note.

As national network characteristics favour existing national, historic rail operators new entrants can be subject to extensive assessment in order to prove safe operations, over and above that experienced by existing historic railway undertakings. The resultant cost of seeking safety certification for international operation can then be excessive, especially for smaller newcomers.

In at least one country the incumbent railway undertaking provides its opinion on the technical instruction of the safety certification dossier to be established by the infrastructure manager for the national safety authority. This practice that could have some deterring effects on newcomers will be discontinued when the safety Directive 2004/49/EC will be implemented.

Path Allocation, Available Network Capacity and Track Access Charges

A large number of national networks continue to be dominated by vertically integrated railway undertakings which *de facto* enjoy grandfather rights. Furthermore, newcomers often feat that they will not receive the same fair treatment in comparison to their capacity request being dealt with by an independent infrastructure manager. It is therefore very important for Member States to ensure by all adequate means the independence of essential functions such as the allocation of train paths and the setting of track access charges. This shall be ensured when all the provisions of the rail infrastructure package Directives will have been implemented (Art 13(2)).

Moreover, some rail freight operators have exclusive rights (by law or on a contractual basis) to use other specific infrastructures, such as track and loading facilities at inland terminals and ports, effectively hampering third party access to those locations. The implementation of the rail infrastructure package (in particular Art 10(6) of Directive 2001.12/EC) by all Member States should eliminate this entry barrier.

Charging mechanisms and infrastructure costs are not yet fully transparent across all Member States, In some Member States, the infrastructure charging schemes which have been put in place appear to favour the national incumbent at the expense of new entrants. National competition authorities, rail regulatory bodies and the European Commission have been and are combating such practices to ensure non-discriminatory rail market access.

Agreements between railway undertakings

There have been complaints from newcomers that agreements concluded between national rail operators related in particular to rules and access to certain facilities for cross-border rail traffic could be discriminatory. These agreements were concluded mostly at a time of monopolistic state railways and appear effectively to exclude new entrants in some cases. For this reason the European Commission is undertaking a study to determine the extent of the problem and to propose remedial action.

Availability of Services

New entrants into the freight market will require access to sidings, marshalling yards, depot facilities and fuelling points. They may also require access to existing rail services at ports and terminals. Further, they may wish to lease rolling stock, hire drivers, crew, and support services, or procure training for their staff. Currently these types of services are often still in the hands of national operators. In some cases, new entrants may have restricted access to such facilities compared to existing national operators. Most of these barriers will be overcome once the EU rail legislation will be completely enforced in all Member States. In some cases, complementary action may be necessary such as setting up of neutral facilities for train crews and drivers.

2. *To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?*

The 1st Railway Package of Directives (2001/12/EC, 2001/13/EC and 2001/14/EC) requires Member States to put in place fair, transparent and non-discriminatory rules governing train path allocation and charging; access rights for designated terminals and ports and other key facilities such as refuelling points; to ensure the independence of safety certification, licensing and other essential functions; and to set up an independent Regulatory Body at national level to act as an avenue of appeal and to hear complaints.

A number of Member States have not or not fully transposed yet all of these Directives into national law. Obviously, in some of these countries the failure to implement the EU legal framework leads to barriers of entry related, for instance, to access rights, licensing, charging capacity allocation and access to services. However, in other countries not having formally transposed the Directives, such barriers do not or only partially exist because these countries had defined a legal framework similar to the EU one based on national

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initiative. In other Member States where the EU legal framework has been transposed, no entry has been observed yet.

Directive 2001/14/EC sets requirements for obtaiing safety certification; these requirements are now superseded by Directive 2004/49/EC, adopted in April 2004. This Directive lays down more detailed requirements on safety certification and Member States are still in the process of transposing this legislation. However, it is clear that few Member States have implemented the earlier safety certification requirements of 2001/14.

DG COMP and the NCAs are currently engaged in fact finding to see whether the representations received during the recent market survey have any validity and, if so, whether action on those matters not covered by the sectoral regulatory framework may be possible under the competition rules.

3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

The Commission continuously monitors the implementation of the Directives through the regulatory committee, the Developing European Railways Committee (DERC) and the Rail Market Monitoring Scheme. Member States are required to provide regular progress reports on their transposition of these Directives and to notify national implementation measures. The Commission publishes the latter on its web site.

Immediately after the adoption of the 1st Railway package in Spring 2001 the Commission took the initiative in the framework of the DERC to establish a number of working groups and task forces composed of experts from Member States and the Commission to exchange experience and best practice with respect to the implementation of the most important provisions of the package.

The Member States which have not yet notified the Commission of (all) transposition measures for Directives 2001/12/EC, 2001/13/EC and 2001/14/EC are Germany, Greece, Ireland, Luxembourg, all the new Member States which entered the EU in May 2004, and the UK. For this reason, the European Commission has started infringement procedures against Germany, Greece, Ireland and Luxembourg and the UK for failure to notify. These infringements have been referred to the European Court of Justice.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

Possibly. Art 10(8) of Directive 91/440/EEc, as inserted by Article 1(d) of Directive 2004/51/EC, requires the Commission to present a report by January 2006 on the implementation of the Directive and on rail market developments generally and, if appropriate, to make new legislative proposals.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

The UK has yet to notify the Commission of national legislation transposing the Rail Infrastructure Package Directives as well as the second railway package of April 2004. Concerning the implementation of the Rail Infrastructure Package Directives, the UK should in particular address the issues of a regulatory framework in line with EU legislation for special infrastructures such as the Channel tunnel, as well as for Northern Ireland. The UK Government also still has to set up the appropriate national legal framework ensuring non-discriminatory access to tracks and supply of services in terminals and ports.

Second, we are aware of concerns on the part of rail operators in Great Britain about the time and expense involved in obtaining safety certification,[2] and of the fact that the insurance cover required for train operators is the highest in the EU. These areas merit attention. Also, the UK rail network has specific infrastructure and operating characteristics requiring railway undertakings to implement specific technical or operating requirements, for instance, related to structure gauge and axle load. These requirements are not always fully transparent or visible, in particular to newcomers who do not have a long experience with operating on the infrastructure. These requirements must be made fully transparent and explicit in order to ensure that they are clear for all and, in particular, for new market entrants so that escalating costs in the certification of rolling stock and operations are prevented.

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[2] Eg Interim Report of the ongoing study "Acceptance criteria and assessment methodologies for safety certificates delivered in accordance with Directive 2001/14/EC, Art 32.

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Examination of Witnesses

Witness: MR HEINZ HILBRECHT, Director of Directorate-General for Energy and Transport, European Commission, examined.

Q281 ***Chairman:*** Good afternoon.
Mr Hilbrecht: Good afternoon, my Lord Chairman.

Q282 ***Chairman:*** Thank you so much, not only for coming but for being early and enabling us to make an early start. It is just possible that there may be some Divisions while we are having questions and, as I am sure you know, that tends to interrupt things a little. Thank you, again, for your written evidence which we have read with interest obviously; it was very helpful. I wonder if you would like to say any words of introduction. If you do, could you include in your remarks your assessment, briefly, of whether or not the Commission feels that international rail freight within Europe is actually a matter of any real significance for the UK? If it is, why is it important?
Mr Hilbrecht: My Lord Chairman, thank you very much for having me here, it is a pleasure for me. I think that international rail freight is of significance to all member countries, including the UK in particular, because from the studies we have done we see that the big market potential for rail and for rail freight is in international traffic across the borders. If you really want to explore that big potential I think you have to address the questions which are linked to crossing the borders, to interoperability, to barriers to entry and so on. Of course, the UK has a particular problem in that for the link to the continent there is only one possibility, you have to go through the Channel Tunnel, but nevertheless I think also the international traffic from the UK down to the south, and also to the east through Germany and into eastern Europe, can be of much more importance than it is today. I would expect that in the longer run the UK would benefit from a better international rail freight system in Europe.
Chairman: Thank you. We may return to those points later on but that is a very helpful introduction.

Q283 ***Lord Fearn:*** Good afternoon. Despite the high level of legislative action on the part of the Commission to promote competition in the international rail freight business, we have heard from witnesses so far that implementation is "patchy". What is the Commission doing to ensure full implementation in all Member States?
Mr Hilbrecht: First of all, yes, I think the implementation is patchy for the time being, that is a fair statement. On the other hand, you have to bear in mind that the first railway package is quite a complex piece of legislation, particularly the Third Directive, 2001/14, on railway charging and path allocation. If I remember correctly, the whole package is about 36 pages of fine print of legislation not including the maps in there. We have a situation where, within the Member States, we come from positions which are quite different one from the other. For me, the biggest surprise is not that it takes quite some time for some Member States to apply the First Package; the big surprise for me still is that they got the First Package through the Council and Parliament altogether in the first place. I do not know that we would be able to do it again today with the new member countries that are less favourable to change. I think I am quite happy that we have this on the books, that the First Package is there. Before the date of implementation, which was in spring 2003, we had installed working groups to prepare the Member States. Some have taken advantage of that help which we offered and others took a longer time. It is a little bit surprising to me that two countries that basically were in favour of the First Package, my own country, Germany, and the United Kingdom, are among those that have not yet notified implementing measures. Even so, they have implemented quite a lot, free market access and so on, but they have not formally notified their implementation decrees to the European Commission and we have launched infringement procedures to three or four of the member countries who have not notified anything at all. In recent weeks the European Court of Justice has taken negative decisions against the UK, Germany, Greece and Luxembourg. We have already followed up on the legal side. We are now preparing new infringement procedures against other countries like Spain and Belgium. Also, we have checked on the background of the notified measures in different Member States and have entered into a dialogue with those member countries where we have seen problems or we have concerns. We have exchanged letters with a number of those member countries. For example, twice now we have exchanged correspondence with France on their tarification scheme. In France they still have a two-part tariff system in place. I am happy to say that we have achieved agreement with France on the substance. They agree that it should be changed now but they say because of the public service contracts with regions they cannot do so before 1 January 2006. It is up to the new Commission to decide whether this is a sufficient reason or not to launch a formal infringement procedure, and I cannot judge that. We have a number of cases which we are now preparing which, over the next weeks and months, will lead to formal infringement procedures. We have already done a number of them and others are going to follow. It is a complex piece of legislation. If you look at the discussions which we have had in the meantime on the Second Package I think it would have been

unwise to wave the big stick too early. Now we have the Second Package in "dry towels"; it has been adopted by the European Parliament and Council and now we should look more earnestly and prepare legal action against those who are not implementing at all or incorrectly implementing the First Package. This is going to happen. By the way, the new Commissioner, M Barrot, in his testimony before the European Parliament said that one of his priorities will be to follow up on the correct implementation of the First Package. This will be a top priority for the next weeks and months.

Q284 ***Lord Fearn:*** I am surprised to hear that Germany and Great Britain are in that list. Is there any reason for that?
Mr Hilbrecht: I can only guess. I do not know for sure. In my opinion, in Germany there could be two reasons but I am not totally sure about this. I think that one problem is in Germany they have not opted for a complete separation of the infrastructure manager from the railway company but have opted for a so-called holding model whereby the infrastructure manager is a part under the roof of the holding. To get all of this right and to make it compatible with the First Package legislation is not easy and I suppose this has delayed the process and the discussion is still ongoing, particularly as in the German parliament part of the parliament is for a complete separation and not for a holding model. Certainly this is a big issue which needs further discussion and probably has caused some delay. Another problem has to do with the infrastructure charging system in Germany which probably needs some adaptation to be compatible with the Directive of the First Package. With regard to the UK, frankly, I do not know. In the UK the basic work has been done. There are probably some questions with regard to the infrastructure charging but nothing should be so important as to cause such a delay. Honestly, I do not know why there is a delay in the United Kingdom.

Q285 ***Lord Geddes:*** What a pity, I thought perhaps you might have been able to tell us what our problem is and the answer to it. Herr Hilbrecht, you made some very interesting comments in your opening remarks and certainly I think the earlier comments you made would be music to our ears, that one of the real battles is to break down the barriers across borders. In this country, as you know well, we have got, or are getting used to, the importance of regulators and what a really tough regulator can and should do, but in our evidence we have heard a lot of comments about the dominant position of other national rail questions. My question really is to do with the independence of regulators in various countries within the EU. It may be a bad example, but we have been told that existing rail regulators are simply small offices in the transport departments of the governments. Those may be extreme cases but I would like your comments on that. What further action does the Commission think needs to be done and is appropriate regarding regulation? How could one beef up the role of national regulators? To throw a wobbly into my question, do you think that there is a necessity for a European regulator?
Mr Hilbrecht: First of all, I would like to nuance my reply a little bit because I know that in some member countries over the past years there have been some situations which have been very uncomfortable for new entrants competing with the big dominant railway carriers. I am thinking particularly of Germany, for example. There are only a very few cases of clear-cut abuse of a dominant position. I think to have a case where people think that they are unfairly treated which is perhaps a little bit mal adroit, or which is not intentional, has to be considered differently than a real, clear-cut case of abuse of a dominant position. There are only very few cases where we have proof of abuse of a dominant position so far, and I will return to this and I will cite examples. It is very clear that in particular in those countries, in Germany and also in the UK, where you have more than one active railway company, the infrastructure manager and also the regulator have been more active and more concerned about the level playing field and fair competition than in other countries where you do not have a second or a third railway operating besides the dominant carrier. From the echoes which I hear, these informal complaints or this uneasiness has died down in many of those countries where the regulator and the infrastructure manager have tried to be fairer and more correct. For example, I hear surprisingly few complaints from Germany today. I heard a lot two or three years ago, I do not hear very many complaints today. At the European level we have had only three cases of clear-cut complaints to the Director General for Competition. Two of them came from a German railway operator who is operating occasional passenger traffic, not freight traffic. One of these cases has led to a decision by the Commission; the other case is still pending. There is a case by the International Union of Private Wagon Owners which is still pending which I do not know very much about. There are very, very few cases where we have had formal complaints. Some people say that the small companies are afraid to complain against the big carriers because they fear retaliation but the German example shows that it is surviving. It has made a complaint against Deutsche-Bahn and won a complaint against the Italian company, FS. It has won one case and not suffered too many problems from that. Those small companies that are complaining about unfair situations should really

prove it and go and make a complaint. This was how it was done in the aviation sector and I do not see why it cannot be done in the railway sector. I think one should be very careful about this. What is important, however, is to have a good regulator. That has been helpful in the UK and in Germany, for example. We now have 16 other member countries that have established a railway regulator. About half of them have established the railway regulator as an independent administration and the other half as part of the ministry. Again, I think one should—

Q286 ***Lord Geddes:*** If I could just interrupt you there. That makes only eight out of 25.
Mr Hilbrecht: That is correct. Sixteen in total and about half—

Q287 ***Lord Geddes:*** That is only half.
Mr Hilbrecht: Half are independent and the other half are part of the ministry. We discussed this when the First Package was adopted and Member States were very reluctant to create a new administration because they said if we do not have competition in our countries for the time being, we cannot establish a new administration with half a dozen people who are waiting there and doing nothing all day long, waiting until perhaps in one, two or three years' time there is a railway company. Of course, it is a chicken and egg problem. You may say you need the railway regulator first to create the atmosphere and then you will have new companies coming. You can also see it the other way round and say you can start with a small department within a ministry and then if it becomes more important it will create the dynamics for an independent rail regulator. Again, it is a question of whether companies have reasons to complain and at this time I can only say there are no complaints because they do not test the liberties which they have got. In France, which has established a very small regulator of three or four people with a secretariat attached to it, two of them are independent, a judge from the outside, so they try to show an independence, for the first time they have two freight companies who have got a licence and are waiting now for their safety certificates. One got the safety certificate, which is Europorte 2, the daughter of Eurotunnel, on 22 October. The other is a daughter of Connex waiting for the safety certificate and hopefully they will get it in a few weeks or months' time. We see that people are slowly coming in. I hear that Rail4Chem, a German company, is also trying to explore entering France. I do not believe that the non-existence of a completely independent rail regulator will prevent railway companies from entering the market. They should test it. They need a little bit of courage maybe, a little bit of money. We know that there are barriers to entry because it is a capital intensive industry but I think that they should have the courage to test it and if it fails we can go after the Member States and against the dominant carriers if there is abuse of the dominant position. If nobody goes for it and nobody complains it will be very difficult for the competition authorities to do anything about it. They can only become active if they have a substantive complaint. By the way, one of the countries, Slovakia, has no regulator at all so they are in violation of the Directive for the time being, but they have a competition authority which has already put a fine on the dominant carrier in Slovakia. Even there, the railway regulator is not the panacea for everything. It is useful, very helpful and we should push for it, but I understand Member States who say "Let us be more proportionate and start first in a small way within the ministry and then develop it later if there is a need". Incidentally, we have established a working group of the rail regulators; they all come together and meet, try to exchange best practice and learn from each other which has had a very stimulating effect for those countries who think that perhaps it is not such a priority.

Q288 ***Lord Geddes:*** I take it your answer to my question about a European rail regulator is *nicht*?
Mr Hilbrecht: I think it is too early, we will have to see. We are just about to establish a European agency for technical questions, for interoperability questions, I think the time is not right now to jump into a European rail regulator. I would wait another four or five years and then re-evaluate the situation but, for the time being, I do not see the need for it.
Lord Geddes: Thank you.

Q289 ***Lord Haskel:*** You seem to suggest that the competition is going to come from other operators in other countries going into another country. Is it the dominant players in those countries who are going to go into another country to form the competition or is it the smaller players who are trying to expand their markets?
Mr Hilbrecht: For the time being, disappointingly, it is not the big carriers who are going into the other markets. I always say that they behave like the members of an old boys' club and they try not to hurt each other. I would like to see SNCF go into Germany and Deutsche-Bahn go into France. This is not happening yet—not yet.

Q290 ***Lord Haskel:*** Do they have some kind of agreement between them about that?
Mr Hilbrecht: I do not think that there is a formal agreement, no, but it is a gentlemen's agreement perhaps.

Q291 ***Lord Haskel:*** An informal agreement?
Mr Hilbrecht: Yes maybe, but it is not a formal agreement. Among the dominant carriers, the only one that has clearly a European perspective for the time being is Railion, that means Deutsche-Bahn. They have realised, as I said at the beginning, that a good perspective for rail freight is international traffic. They have bought freight operations in the Netherlands, in Denmark and elsewhere and they have tried to consolidate their market and get into other countries that way. Apart from Deutsche-Bahn we have only very tentative attempts by the Italian carrier, FS, who has now tried to go together with a small subsidiary in Germany and we have the Swiss carrier, SBB, who is also part of the European market, who has tried to go together with an Italian carrier to better exploit the international traffic. There is a nucleus for this development but for the time being the big carriers are not trying to make too much competition for each other.

Q292 ***Chairman:*** We have got a lot of questions so, extremely helpful as those long responses were—
Mr Hilbrecht: I am sorry.
Chairman: No, they are very, very helpful and you have covered a lot in there but it would help if we could keep the questions and the responses a little shorter and then we could get through more.

Q293 ***Lord Swinfen:*** Herr Hilbrecht, we have had other witnesses telling us about the problems of safety certification, and you brought it up in your written evidence. What action is the Commission taking to overcome this problem?
Mr Hilbrecht: You are right, safety certification is one important potential barrier to entry. I think there are different levels where we have to address it. The first point very clearly is that we have to establish a set of European standards for the rolling stock. That is what we do in the so-called interoperability process, establishing technical specifications for interoperability, TSIs. We have had a set of technical specifications for the high speed sector and later this month we will have a second set for conventional rail and other sets of such technical standards will come. If we have such a commonly agreed set of technical standards then the possibilities for Member States to deviate from them and have their own standards, and use this as a barrier to entry, would be vastly diminished. It is an absolutely basic development to have a common rule, a common set of technical standards for interoperability which will allow them to cross the borders more easily. Nevertheless, under the Safety Directive which has been adopted as part of the Second Package, apart from the safety standards for the rolling stock, a company will need a safety certificate. The safety certificate has two parts. One part is a European general safety certificate and a second part will always be needed at the national level because you have to check whether the security structure, the management of the company and the rolling stock fits for that particular line. All lines are a little bit different, they have different radii and so on, so you have to check whether the rolling stock can really roll on that line. You will never be able to have only one European safety certificate, in addition you need a national safety certificate. What is important is that the procedure will be sped up by the Directive, which will have to be implemented by spring 2006. For the time being, some of the Member States still take quite a long time to issue these national safety certificates but as of 2006 they will only have four months to grant this safety certificate. We will have the technical standards and we have to speed up the procedures. Also we have created a new working group where the safety authorities will work together. They will meet for the first time this December so we will know exactly where the problems are. We have a study, which will also be finished by the end of the year, on the methods and the techniques being used by the different Member States to check on safety and security so that we know where the problems are and where we need to fine-tune the system. We have been quite active and we hope that within the next one or two years the system will become much smoother than in the past.
Chairman: Lord Walpole has a question that you have touched on slightly but I think he wants to ask in more detail.

Q294 ***Lord Walpole:*** Yes, indeed. Mr Hilbrecht, can you tell us about another barrier that we have been told about, which is the wide diversity of the level and structure of infrastructure charges and the presence of two-part tariffs in countries like France. Is the Commission planning to look into this in great depth?
Mr Hilbrecht: Yes. I think one of the important questions which we have to analyse is how Member States construct their infrastructure charges. I am less concerned about France because I think they have a basic agreement that the two-part tariff which exists there will have to finish sooner or later, at the latest in 2006. I am more concerned about the infrastructure charge in my country because it is rather high in Germany. Germany pursues a full infrastructure cost charging philosophy whereas the Directive says that the train company should only pay the costs which are directly provoked by the running of the train, a sort of marginal cost approach. There is an exception in Article 8 of the Directive which then says that member countries may deviate for specific sectors. It would be interesting to see how Germany is handling that. I foresee that there will be a number of discussions to be held. With regard to the two-part tariff: Article 8, paragraph three of the Directive says

that for equivalent traffic the marginal and the average charges should be comparable and that comparable traffic within the same market segment should be levied at the same charge. The Directive does not explicitly disallow two-part tariffs but for me it is very difficult, if not impossible, to make a two-part tariff system compatible with Article 8(3) which I have just quoted. I think the French have recognised that. To study the effects of two-part tariffs you do not have to look across the Channel because, if my memory is correct, the largest rail freight operator in the UK has a special deal with the infrastructure manager here whereby it pays only a lump sum per year and a very small average cost per kilometre thereafter. I think this is a blatant two-part tariff and I would be very interested to see what the UK Government is going to show us in their notification as to how such a system can be made compatible with the Directive. I think we will have quite interesting discussions with them.

Q295 ***Chairman:*** If my memory serves me right, I think that was the case but I rather think that arrangement has now ceased.
Mr Hilbrecht: I am happy to hear that. My information is not up-to-date, I apologise.

Q296 ***Chairman:*** You have usefully provoked an enquiry and I shall check and report to this Committee.
Mr Hilbrecht: I am happy to hear that.

Q297 ***Lord Walpole:*** There is no doubt that some types of vehicle going at certain speeds do, in fact, do more damage to the infrastructure than others, do they not?
Mr Hilbrecht: Yes, of course.

Q298 ***Lord Walpole:*** You cannot charge someone for having not particularly good rolling stock, can you?
Mr Hilbrecht: There is the possibility to have a charging system that differentiates according to the rolling stock. The rule of Article 7(3) or (4) says that the charge should be in relation to the damage caused by the rolling stock, so I do not see why for somebody who has more damaging rolling stock than others, that could not be integrated into a transparent charging system. What should not be done is to internalise external costs as long as external costs are not taken into account by the competing mode, that means by the road haulage sector. A differentiation according to the damage, if that can be defined *a priori*, I do not see why it could not be done.

Q299 ***Chairman:*** In the Commission I assume you have got a checklist for all 23 Member States with railways and various criteria. How many Member States have you ticked on the box for transparency and reasonableness of the infrastructure charges—approximately?
Mr Hilbrecht: I could not answer that off the cuff, I must say. I have particular concerns with France, Germany and the UK, although maybe my concern about the UK is a bit outdated. With regard to other countries, traditionally they have very low infrastructure charges. All the Scandinavian countries have quite a transparent system. I do not think that we have major concerns with the other countries for the time being. I would not advance a figure here and say how many.
Chairman: That is fine.

Q300 ***Baroness Eccles of Moulton:*** Herr Hilbrecht, I want to return to a question that you touched on earlier when you were talking about the complexity of the first Directive and the progress in Germany towards separating the infrastructure and operations. Could you please tell us whether the Commission believes that complete separation of infrastructure and operations is the best way of ensuring fair access to the infrastructure for new entrants? If that is the case, what are the prospects for overcoming what we know to be opposition in certain areas?
Mr Hilbrecht: It is no secret that the Commission's original proposal was aiming at a complete separation and it would be dishonest if I said that I am now completely happy with the text as it stands. From our point of view, complete separation would be the better solution. I have to admit that we have proposed complete separation of the infrastructure not as a first best solution but rather as a second best solution. Ideally, if we had room and space in Europe we would have a system where different railway companies would compete on their own infrastructures. That is a little bit like what we see in the United States where between the big three industrial centres we have the companies competing on their own infrastructures but for geographical reasons in Europe that is not practical. That is why we opted for a second best solution saying that we should have separation from the infrastructure knowing that there are good arguments which are in favour of keeping a company integrated: it is easier to manage, you can have better foresight for investment planning and so on. All this can be overcome with the appropriate mechanism, we think. The Council and the Parliament did not follow our suggestion, they adopted a third best solution which is only the separation of the essential functions, in particular infrastructure charging and path allocation. We have to live with that. I am not advocating the reopening of this discussion, in particular because I do not see any possibility of finding a majority to change it, not with ten new member countries who are rather

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conservative in that area. We should live with what we have now and re-evaluate the situation in three or four years' time when we have to make our interim report on the application of the First Package. For the time being, I do not see any possibility of coming back to that decision which was a difficult decision between the European Council and the European Parliament in any case.

Q301 ***Baroness Eccles of Moulton:*** Could it be that in certain cases it is very important to unbundle the link between infrastructure and operation because in other places it would be perfectly all right to leave it as it is in that you do not have to have the same rule for everybody?
Mr Hilbrecht: It is very difficult at the European level to have a decision á la carte. Who is going to decide which is the country that needs unbundling and which is the country that does not need it? From a practical point of view, even though it may be a wise approach, I do not see how that can be implemented.

Q302 ***Baroness Eccles of Moulton:*** Might it be better than the third best which sounds rather low down the list of bests?
Mr Hilbrecht: It depends how things are being implemented. I said at the beginning that, for example, in Germany the holding system, which is a little bit of a test case for a number of other countries which are split half and half—half are going for total separation, the other half are following the German example of the holding—if the holding is correctly done the number of informal rumours and complaints will die down, as has happened quite considerably in Germany because the German infrastructure manager, DB Netz, has closely observed and tried to behave as if they are totally independent. For the time being, I think we have to wait and see how other countries do it.

Q303 ***Chairman:*** A lot of the vertically integrated railway businesses are also state owned, nationalised.
Mr Hilbrecht: That is correct.

Q304 ***Chairman:*** As you say, each can have their own perfectly justifiable system of charging for the use of the infrastructure but how can you honestly expect a vibrant, competitive European market with large state owned, national champion vertically integrated businesses? What incentive have they got to be competitive?
Mr Hilbrecht: You take me into a difficult situation because the Treaty says the Commission has to be neutral with regard to ownership questions. We have never advocated, and we could not advocate, privatisation because this would go far beyond what the Treaty would allow the Commission.

Q305 ***Chairman:*** I said how can you really expect to have a competitive market emerge on international freight? Where are the pressures? After all, competition only happens because there is pressure to be competitive. Where is the pressure? Witness after witness after witness has come before us and, I have to tell you, have been very gloomy. Rail freight is falling in market share in Europe, that is the reality.
Mr Hilbrecht: Absolutely.

Q306 ***Chairman:*** We are talking about how to improve things. Most people have been pretty gloomy. Is not the problem at the root of it that the big operators are vertically integrated, state owned? What is the pressure to be competitive?
Mr Hilbrecht: The only pressure which we can hope will develop over time is that new companies come up and even the big companies will start to compete with each other. We see the cracks in the barriers and we can only hope that if one starts going into the market the others will retaliate and then you will see competition. We are not yet there. I have said publicly, and to the railway companies several times, that I think they have about 10 years to change. My personal opinion is that if by the middle of the next decade the railway companies have not changed drastically, maybe the political climate which is very favourable to them today will change also. Who wants to pay subsidies forever to a system which cannot reform itself? I am not here to paint a rosy picture to you. I agree with you but I can only hope, and there are small flowers starting to come out but it is not much for the time being, there you are right.

Q307 ***Lord Haskel:*** Mr Hilbrecht, in your introduction you spoke about crossing borders and in response to an earlier question you spoke about the barriers in safety certification as far as crossing borders is concerned. It has been put to us that whilst improving interoperability is welcome, and particularly the proposals of the European Rail Traffic Management System, these proposals may impose costs which are far in excess of the benefits. What measures are you taking to ensure that there is an appropriate relationship between the costs and the benefits of interoperability?
Mr Hilbrecht: The proposal to have technical specifications for interoperability covering command and signalling systems, the ERTMS for the conventional rail system, will be discussed on 23 November in the Committee of Member States, Committee 21. It is true that in some respects, in some cost-benefit analyses they have come out negative. We think that those cost-benefit analyses have not taken the whole picture into account, they have taken a very short-term view of the issue. There are two issues which have not been reflected very well by the cost-benefit analyses. One is that the command and

signalling system which we propose, the ERTMS, provides a much higher level of safety than the so-called Class B system, the TPWS, the system which is being installed today in the UK, can provide. Let me give you an example: the Class B system, TPWS, basically can only check whether a train is at a given place. It is a simple magnet which checks whether a train is running a red signal or not. There is no speed control which you can provide with an advanced system like the ERTMS. I have to express my condolences to you and to the UK for the horrible accident which happened last Saturday. If you discuss how to prevent this, of course, ETCS or ERTMS would not have prevented that alone but what you could do is instead of eliminating all level crossings, you could install a detector which would be linked to ETCS and which would warn the train in advance that there is an object on the level crossing. You cannot do this with TPWS because TPWS is not equipped for that. ERTMS is a system which gives you far more operational possibilities than the existing Class B system. That is the first point. The second point is that today we see more and more suppliers walking away from the maintenance of the existing Class B systems. You have the same development with the introduction of the digital communications system, the GSM-R, which is the other part of the ETCS, where, following cost-benefit studies, we thought the whole migration would be done somewhere in the middle of the next decade but today we have 100,000 kilometres equipped with GSM-R, the digital telecom system, 16,500 kilometres in the UK alone, and the full migration will be done within three or four years, by 2007–08, much faster. Why? Because the suppliers walk away from the maintenance of the analogue communications system, they say it is too expensive, they do not want it, technology is advancing and so on. We think that you will see the same development with the Class B systems. I have had two meetings with representatives of the Community of European Railways, of the manufacturers' federation, UNIFE, and the AIF, the interoperability committee, over the last six weeks. We have agreed on a basic network of 20,000 kilometres in Europe to be equipped on the conventional rail with ERTMS. If the detailed cost-benefit analysis which has to be done by Member States within the next year shows that on a specific part of that rail network the cost-benefit really is too negative then they can derogate from it, but nevertheless there is a basic agreement that 20,000 kilometres should be equipped within the next 10 years. For the first time, there is an agreement between the railways and suppliers on the basic costs of implementing the system. There have been wide differences so far. We see that we can make progress there. We expect that ERTMS will come. We have 11 countries in Europe now which are partly, or totally, implementing ERTMS because they see that this is the way forward and maintaining the old systems will cost more and more money. We are very disappointed that both the Commission and the UK have put 300 million—I say euros some people have told me it is pounds—down the drain in development and pilot costs to test ERTMS in the UK since 1995. You can only blame the Commission that we have been so patient and have continued financing that. The TPWS, which was promoted as a cheap and easy solution, which was supposed to cost only £150 million, is now at £575 million or even more. I am very sceptical when I hear about cost-benefit analysis which take a very short-term view and does not take the long-term and strategic aspects into account. Now you are going to test ERTMS again on the Cumbrian Line and we will see what that brings but I think that one should really take a strategic decision and see that for interoperability reasons and for safety reasons, as the Cullen Report in 2001 stated, there is no alternative to ERTMS. This is a common trend which we see across Europe.

Q308 ***Chairman:*** That is very thorough but we are running out of time.
Mr Hilbrecht: I am sorry for being so detailed but it is a very important subject.
Chairman: I can assure you that I let you go on because it is so important and I am grateful to you. You have raised a number of very important issues upon which, I can assure you, we will reflect.

Q309 ***Lord Shutt of Greetland:*** Costs and charges. We have been talking about the railway and the costs and charges, but what about road haulage? It has been put to us that inadequate proposals have been put forward to implement the declared policy of the Commission of fully internalising the external costs of road haulage and that even the stalled revised Eurovignette proposals do not achieve it. What are the Commission's plans regarding infrastructure charges for heavy goods vehicles?
Mr Hilbrecht: We have made a new proposal to revise the so-called Eurovignette Directive. There have been two main leading philosophies in Europe. One—and Chris Nash is an advocate because he was chairing a consortium of research institutes which helped develop this philosophy for us—is social marginal cost charges where a company would not pay the full infrastructure costs but only the costs of the wear and tear plus the internalisation of external costs, in particular congestion, emissions and noise. The other philosophy says we should only cover the full infrastructure costs but not the external costs. There are not many people, apart from the railways themselves, who advocate full infrastructure costs plus internalisation of external costs. That is the odd man out, so to speak. We have opted for a solution

that my Commissioner thought was best, and so I favour it very much. The proposal developed by Chris Nash and his colleagues of social marginal cost charges, the Commissioner thought would not find a majority in Parliament and Council: she advocated a solution which is quite an intelligent one, namely to say we have a cap on the infrastructure costs, namely that the average cost should not lead to a higher revenue than the total infrastructure costs, but there is the possibility of variability between those congested areas where you have emissions and other areas where you have clean air, nevertheless the total volumes across the country should not go beyond a ceiling, even with variability of the charge. Strangely enough, and Chris Nash may correct me, the average charge under the social marginal cost proposal and the average charge under our proposal is the same, roughly speaking, about 15/20 cents per kilometre. What is different between the social marginal cost charging proposal and our proposal is that the variability of the charge is much higher if you take the full congestion charge into account; it can be three, four times higher or even more than the average charge whereas, under our proposal, we have introduced caps to limit this variability. There is a 100 per cent ceiling for the time of day and congestion and a 50 per cent limit with regard to emission classes. *De facto*, the proposal which we have made allows us to a large degree to look at the internalisation of external costs and take them into account at the point of use, even though we do not go as far as our research consultants recommended in the first place. It is a difficult proposal and, unfortunately, the Council could not achieve agreement. It was very close at the last Council meeting in October to achieving an agreement but so far the Council has not achieved that. But it is not correct to say that the element of internalisation of external costs is not taken into account at all.

Q310 ***Lord Shutt of Greetland:*** Where does this proposal lie now? Is it dead?
Mr Hilbrecht: No. It is on the table of the Council of Ministers. The European Parliament has had a first reading on it. The Council of Transport Ministers has discussed it two or three times. They have narrowed the gap on differences but they have not yet achieved total agreement. We would hope that if the Dutch Presidency does not take it up again in December, next year either the Luxembourg or the UK Presidency will look at it again and continue the discussion. It is not dead by any means.

Q311 ***Baroness Cohen of Pimlico:*** First I must apologise for being late. It was, I am afraid, a failure of the United Kingdom rail industry. A catenary had come down somewhere north of Cambridge and I imagine it will be chaos tonight. We have heard a great deal about the ordinary difficulties that attend on transporting freight about, that passenger transport is inevitably given priority because freight is slower and gets in the way. My question concerns the measures being taken to implement the Commission's policy of identifying and investing in a network of international rail routes on which freight would have priority, which really begins to feel like the only hope. How is this coming along?
Mr Hilbrecht: When we discussed the First Package, we would have wanted to give freight a clearer priority than as it is now formulated. It is said, in very vague terms, that the infrastructure should take due account of the importance of freight in allocating the slots, so it is not a very strong priority. What is important, and what is developing quite nicely, is that we have now a working together of the infrastructure managers in a new grouping called RailNet Europe where they discuss the allocation of international train pathways. That is developing very promisingly. In the past, the classical way of attributing pathways was that you first took the regional passenger traffic and then the national passenger traffic, then the national freight and then the international freight and you would have been very lucky to find pathways which met at the border. Now with RailNet Europe there is a top down approach. First you look at the suitable corridors across the border and try to build the national pathways around it. That is the idea and I think it is a very promising start. With regard to a dedicated freight network, we have already done certain research activities, another will start in 2005 called New Opera. It is a research project that defines the criteria for a freight network to know how much traffic should be the threshold for the definition of the network and so on. This is a long-term project, the project will be over in two or three years' time. It is also very important that in the discussions we have had very recently with the railway companies and with the industry on the implementation of ERTMS, the 20,000 kilometre network I mentioned earlier is considered by a number of railway companies also as the core for a freight network. Besides ERTMS on this network, one would also address what other investments are needed to improve the situation. For example, the German Deutsche-Bahn not only is ready to introduce ERTMS on the line right and left of the Rhine but they also want to improve the system to have lines which are suitable for freight traffic. Therefore, the ERTMS development leads to the idea of having specific corridors for freight. This is something which I think is very promising but it is a long-term issue, we will not have this within a couple of years. People are working on it and I think it is at least a good start and we are on the right track.
Baroness Cohen of Pimlico: Thank you very much.

Q312 ***Chairman:*** Thank you so much, you have been full and very helpful. Is there anything that you

would like to add that you think we should have asked you?
Mr Hilbrecht: I think you have asked very, very complete questions, there is nothing which I need to add at this stage.

Q313 ***Chairman:*** In that case, on behalf of the Sub-Committee I would like to thank you very warmly indeed. You have been full and very, very helpful in your replies and it is much appreciated.
Mr Hilbrecht: It has been a pleasure for me, my Lord Chairman. Thank you very much.

Joint Memorandum by the Department for Transport and the Strategic Rail Authority

Introduction

1. This evidence is submitted jointly by the Department for Transport and the Strategic Rail Authority.

2. The rail freight market in Great Britain is the more liberalised in the European Union (EU), notwithstanding the delay in transposing the provisions of the First EU Rail Infrastructure Package into domestic law. The progress achieved in liberalising the rail freight and passenger markets has been described in several independent reviews of rail policy in EU Member States—most recently, in the IBM Rail Liberalisation Index 2004, an independent study by IBM Business Consulting Services. Liberalisation of access to the domestic rail market along with the privatisation of British Rail's (BR) freight operations in 1996, has effectively established a level playing field between incumbent operators and companies wishing to enter the market. As a result, initial compeition between freight operators formerly belonging to BR has now been augmented by competition from new market entrants. Rail freight companies have invested to improve efficiency and equipment resulting in increased traffic levels. Since privatisation rail freight has increased by 42 per cent in terms of freight moved.

3. The procedure for entering the rail freight market in Britain is well documented and clearly structured. Key decisions to grant safety certificates and operating licences are the responsibility of independent public agencies, with no economic interest in incumbent rail freight companies. Companies wishing to run rail freight services within Britain require an operating licence from the Office of Rail Regulation (ORR). To obtain its licence, a company must possess a valid safety case accepted by Network Rail; information is available to assist applicants in preparing their cases. Once its licence has been granted, a company can apply to run rail freight services by entering into an access agreement with Network Rail. Each access agreement is subject to scrutiny and approval by the ORR to ensure that it promotes the public interest, and that it does not impact adversely on other rail network users. ORR also approves access agreements for ancillary freight facilities and light maintenance depots that may be required to support the operation of main-line freight services. Fair competition is policed by the ORR using powers it holds concurrently with the Office of Fair Trading.

4. There are four active freight operators in Britain: English, Welsh and Scottish Railways (EWS), Freightliner, Direct Rail Services and GB Railfreight. Other companies are still evaluating opportunities for market entry. Only EWS provides international freight services through the Channel Tunnel (through its subsidiary EWS International).

5. International traffic through the Channel Tunnel has suffered in recent years, principally due to prolonged service disruptions caused by the actions of clandestine immigrants in France. This proble, has been resolved following the installation of improved seurity measures in France and the UK. In 2003, the first full year of operations without disruption, EWS reported a 22 per cent increase in total tonnage moved over the previous year. Unfortunately, Channel Tunnel freight traffic has never reached the levels originally forecast. This is due, in part, to persistent rail service quality problems in continental Europe, but may also be a consequence of the inherited access and pricing arrangements from before the opening of the Channel Tunnel. Access to the tunnel by other rail freight operators in competition to EWS International is not prevented but it has been difficult to sell.

6. Since 2003, Channel Tunnel infrastructure capacity used by international rail services has been included within the Trans European Rail Freight Network, to which open access is guaranteed under the terms of the First EU Rail Infrastructure Package. To comply with its obligations as a rail Infrastructure Manager, as stipulated in the First EU Package, Eurotunnel has recently published its first Network Statement. This Statement provides comprehensive information on the Channel Tunnel usage regime including details of access charges and key features of the technical and safety regimes applicable to operators. This should encourage access.

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7. On 15 July the Government published its White Paper "*The Future of Rail*" which sets out a blueprint for a new streamlined structure for Britain's Railway. Under the new structure it is intended that freight operators will be given greater certainty about their rights on the national network, and a group of key routes may be identified on which freight will enjoy more assured rights of access. Implementation of these proposals will follow consultation with relevant stakeholders and should not be detrimental to the liberalised nature of Britain's rail freight market.

8. The Government considers that experience in Britain clearly demonstrates the benefits accruing to freight users and operators from liberalised access to the rail market. It fully supports the opening up of the international rail freight sector to systematic competition on an equitable basis, between rail freight operators and considers it important that the EU makes early progress towards meeting this goal. The Government is pleased to note that a legislative framework now exists for full market liberalisation as a result of the recent agreement on a Second Package of EU Rail Directives. This provides for full market opening for international freight services by 1 January 2006, and for all freight services by 1 January 2007.

Response to Questions

9. In the following paragraphs we set out the Committee's questions and the Government's response to each of them.

Q1. *What are the current barriers to entry in the international rail freight market?*

10. There are four broad categories of barrier to entry, as follows:

(a) The absence of a single neutral, transparent and comprehensive rail infrastructure access regime across EU Member States.

11. Currently, there are significant variations between rail access regimes in EU Member States. These variations include the definition of the range of rail infrastructure, ancillary services and facilities to which regulated access is granted; the procedures for approving new access arrangements, and the conditions of access applicable to new entrants—including the structure and level of infrastructure charges.

12. Opportunities for market entry on any international rail freight corridor will be constrained by the least transparent and comprehensive access regime involved. A major barrier to entry may be the perception of discrimination against new entrants where the body allocating the infrastructure capacity is itself part of a company operating freight services. For example, in France SNCF and RFF have signed a contract for services which specifies that SNCF is also responsible for infrastructure maintenance and plays a decisive role in the allocation of train paths. This perception is exacerbated where there are competing demands for track capacity and ancillary facilities, and little history of effective regulatory intervention. Particular areas of concern include:

(i) the criteria used to allocate capacity to new entrants: new entrants being assigned train paths that impose cost penalties due to long transit times and inefficient use of rolling stock (eg limits on train size).

(ii) the definition and scope of the rail infrastructure and ancillary facilities and services to which competitive access is granted: access being restricted to a minimum (eg use of main line tracks only) with no access rights to facilities that are necessary tfor the efficient operation of international freight services (eg major freight terminals, train holding and inspection facilities, marshalling yards, maintenance facilities, fuelling points and electric power supplies). Incumbent operators may simply refuse access to these facilities and services on the basis of shortage of capacity, or quote exclusionary prices. GB operators believe these types of restrictions to be in order to protect the competitive advantage enjoyed by an incumbent operator(s).

(iii) the structure and level of access charges: some access charging regimes may implicity favour incumbent opeators (eg by the imposition of substantial fixed charges accompanied by significant volume rebates, or by setting variable access charges at high levels). Such a charging structure may create affordability problems for new, privately financed, operators competing with major, publicly-owned railway service providers that benefit from public funding support. (According to Rail Liberalisation Index 2004—an independent study by IBM Business Consulting Services—in France: "The train path pricing system published by RFF is relatively complex, has a two tier structure and thus provides clear competitive advantages in favour of SNCF").

(b) The effects of the existing framework of inter-railway agreements for commerical and operational co-ordination, and accords with public agencies.

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13. For many years, national railway undertakings have co-operated mutually, under the auspices of the Union Internationale des Chemis de Fer (UIC), to develop a framework of multilateral agreements governing the marketing, administration and operation of international freight services. This includes standard international commercial contracts, procedures for the attribution and settlement of international revnues and costs, agreements for the cross-border acceptance of rolling stock, and international arrangements for the safety inspection of trains, the exchange of operational and traffic data and the management of railway-owned wagons. In some cases, multilateral UIC agreements are supplemented by specifically-negotiated accords between restricted groups of railways.

14. However, the philosophy of mutual co-operation between national railways, co-ordinated by the UIC, also limits the degree of interoperability between rail systems, by permitted the perpetuation of differing national technical and operational parameters. In turn this creates cost penalties for a prospective new operators (for example, the lack of qualified drivers, resulting in higher training costs; the requirement for more expensive rolling stock). In effect, this reinforces the competitive advantages enjoyed by incumbents. The success of initiatives led by the European Rail Agency, established under the provisions of the Second Package of EU Rail Directives, will be critical to improving interoperability.

15. The framework for multilateral agreements essentially establishes a set of "core" interfaces between large-scale railway undertakings operating a wide range of passenger and general freight services. It is not orientated towards the requirements of tightly-managed, open-access international freight operators, serving a limited set of customers. Although some inter-railway agreements reduce barries to entry by defining appropriate common technical and operational standards and administrative procedures, others are not binding on new operators requiring market entrants to negotiate their own requirements with infrastructure managers and service-partners. Furthermore, some inter-railway agreements may create cost penalties by stipulating bureaucratic procedures and in some cases may impose significant competitive disbenefits on operators, for example through the direct or indirect release of commercially-sensitive information to competing national railway operators.

16. Finally, arrangements for crossing borders can represent a particular example of an institutional deterrent to market entry. National incumbents have developed agreements with local Customs authorities for simplified procedures and advantageous conditions at EU external frontiers (eg with Switzerland). These are not necessarily available to new entrants who can thus suffer transit delays, with consequential cost increases and service attraction diminution.

(c) The absence of transparent, regulated, market entry procedures and the immaturity of rolling stock supply markets to support new entrants.

17. In some cases, the procedures and criteria used by agencies responsible for granting operating licences and safety certificates to market entrants are opaque, with few precedents available to indicate the time-scales involved and the compliance and transaction costs involved. Protracted approval procedures may expose new entrants to significant financing costs. As ORR has stated, no licences to new entrants have been issued in nine of the 23 EU Member States with railway systems.

18. A particular area of concern in some EU Member States, is the conflict of interest implied by the continuing role of the incumbent national railway undertaking in approving safety certification and undertaking rolling stock acceptance procedures for new entrants.

19. Procedures for rolling stock approval are considered to be one of the greatest barriers to entry for new railway undertakings. These vary widely amongst EU countries, in some cases taking several years and imposing significant costs and delays. Some external railway undertakings which have obtained approval of rolling stock often treat that experience as a competitive advantage over other operators.

20. New freight operators may also face difficulties in obtaining modern locomotives and wagons to start competitive services. This is likely if market entrants cannot reduce the commercial risk of acquiring rolling stock by negotiating longer-term contracts with clients. A large operator can spread investment risk over a large number of customs contracts. A new entrant operator cannot do so. Large incumbents may also have inherited equipment from their state predecessors (or themselves be state owned). The UK has long had a market in rail wagons and incomers have had no difficulty in procuring vehicles. Since privatisation companies—such as Fragonset—have also been set up which specialise in buying and refurbishing locomotives and making them available to the market for short or long periods. Some years ago the Regulator also agreed with EWS a Code of Practice for the disposal of surplus locomotives. Amongst other matters this ensures that competitors are not unreasonable prevented from acquiring locomotives and that those released are not unnecessarily made unfit for service.

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(d) The continued market dominance of publicly-funded rail freight operators.

21. The liberalisation of the rail freight market in Britain was accompanied by the restructuring of BR's former rail freight activities into new fully privatised companies. Each company operaqted on a "level playing field" in respect of access to infrastructure and enjoyed similar access to private capital markets to fund new rolling stock. All private companies face similar pressures from shareholders and lenders for business development, improved productivity and better financial performance.

22. With a few small-scale exceptions (eg privatisation of Estonian railways' freight sector; sale of Netherlands and Danish rail freight activites to German Railways' freight subsidiary) the implementation of liberalised access to the EU rail freight market has not been accompanied by a similar industry restructuring and privatisation. Consequently, the incumbent freight companies, often subsidiareis of national railway undertakings, still have a dominant position in many Member States. EU Member States (and regional authorities) have permitted or encouraged publicly-owned railway undertakings, to expand into the opportunities created by the liberalisation of the rail freight market. While there has been an increase in competition, the financial backing enjoyed by such companies is perceived by industry as giving them an advantage in the market through the scope to sustain aggressive responses to new competitors, in terms of pricing and service levels, and ability to access funds to invest in rolling stock and facilities to launch new services.

Q2. *To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?*

23. The rail freight market in Great Britain is the most liberalised in the EU (according to Rail Liberalisation Index 2004) notwithstanding late transposition of the First Package. Germany is in a similar position, although it is publicly-owned, national railway undertaking still retains a dominant position in the rail freight market. By contrast a number of countries that have transposed the Directives still have comparatively poorly liberalised markets. There are several possible causes:

- transposition is inadequate, which the Commission is currently assessing and may launch infraction proceedings;
- the Directives are not tight enough or the Commission is not being tough enough on interpretation—for example in relation to the separation between infrastructure managers (or capacity allocation bodies) and train operators; and
- the Directives do not cover all of the barriers described earlier—for example rolling stock availability and the supply of qualified drivers.

24. These may operate in combination and vary from one Member State to another. This is unlikely to become clearer until the Commission is more advanced with its assessment of transposition in each Member State, not just of the legal provisions, but also of their effect.

25. The IBM Rail Liberalisation Index 2004 states that countries that have not yet fully implemented the First Package can in practice, in some cases, offer better market access conditions than those that have already reported implementation.

26. For example:

- Belgium notified the EU Commission that it has transposed the first package during 2003, although not yet completely:
  - the SNCB business units of infrastructure and transport are separate only in terms of accounting;
  - the freight and passenger transport divisions are not yet separate.
- In France, although the Directive has been technically implemented, there remain many practical barriers to market access for new entrants:
  - approval of rolling stock can take up to 1.5 years;
  - safety case and rolling stock are valid only on specific routes;
  - test reports issued by other European countries are not accepted; and
  - there are no independent test bodies other than SNCF.

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- In Italy, an office at the Ministry of Transport is named as regulatory body as defined in Directive 2001/14. At present, the personnel resources of this authority are limited to one person and according to RFI (the infrastructure manager), it neither has the authority to impose fines nor to initiate investigations into charging principles.
- However, in Germany the practical market access conditions are considered "exemplary on an European comparison". Full transposition of the first package has not yet been completed.

Q3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

27. The main action is for the Commission to complete, as soon as possible, its assessments of the transposition for Member States where this has taken place and take necessary action for non-compliance. These assessments are not easy to make because each Member State's railway is organised differently and there are many possible approaches to meeting the requirements of the Directives. It may require a degree of probing, which only the Commission can undertake, to establish whether the transposition provisions in practice achieve the liberalisation purposes of the Directives.

Q4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

28. The European Commission has already adopted a range of legislative proposals aimed at introducing competition into international rail freight. Member States are currently in the process of bringing this new European legislation into force. Any future legislative proposals should be targeted at removing specific institutional barriers to competition. In this respect, we recognise the case for the proposed legislation covering the licensing of train drivers operating on international services. However, we see no merit in the Commission's proposal to regulate on requirements for service quality agreements between rail freight service providers and their customers.[3] The Government considers that the Commission's objective of improving the quality and efficiency of rail freight services should be directly addressed through the use of competition legislation to encourage market entry, and by promoting the restructuring of dominant incumbents in the international rail market. It should not, as an alternative, seek to impose commercially-unsupportable financial obligations on all operators, which may perversely penalise new entrants.

29. New legislation will not solve a key problem in some Member States of relatively weak regulatory bodies and competition authorities not always using the powers they have. The Commission, with UK support is encouraging capacity building by improving international contacts and exchange of experiences between supervisory and regulatory bodies concerned with rail transport.

Q5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

30. The focus of the European Commission's policy is to introduce competition into the international rail freight market and to ensure transparent public regulation of it. Within the EU, the United Kingdom has probably the most extensive practical experience in this area. The Government therefore continues to play an active part in sharing that experience with the Commission and with other Member States.

31. The European rail freight market was only formally liberalised in 2001. Given the experience of the successes achieved by UK companies in the longer-established continental market for franchised rail passenger services, the Government is confident that UK freight operators will, in due course, take advantage of emerging international opportunities.

32. On one specific issue—that of interoperability—the Commission is proposing harmonisation of standards to reduce the technical barriers hindering the growth of the international rail market. The UK Government plays an active role in ensuring that this work is taken forward speedily and cost-effectively.

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[3] Elements of the Third Rail Package: Proposal for a Directive of the European Parliament and of the Council on the certification of train crews operating locomotives and trains on the Community's rail network *(COM(2004(142 Final)*; Proposal for a Regulation of the European Parliament and of the Council on compensation in cases of non-compliance with contractual quality requirements for rail freight services *(COM(2004) 144 Final)*.

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Examination of Witnesses

Witnesses: Mr Tony McNulty, a Member of the House of Commons, Minister of State, Department for Transport and Mr Philip Graham, Head of Rail Freight Branch, Department for Transport, examined.

Q314 ***Chairman:*** Good afternoon, Mr McNulty. I apologise for keeping you. I have got your message that John Prescott might stimulate a Division. I cannot believe it!
Mr McNulty: I think as soon as he sits down literally there will be one. I am told by the Whips that it is imminent.

Q315 ***Chairman:*** Could we make a start. Thank you so much for sending in some written evidence through yourself and the Department, which obviously we have read with great interest. We have lots and lots to ask you, as you might expect, but there is never enough time. We are aiming for 45 minutes of questions and if we can make that it would be enormously helpful. Do you want to say a few words by way of introduction?
Mr McNulty: No, I am fine, thank you.

Q316 ***Chairman:*** I thought it would be useful by way of introducing the subject to take your views on the importance of international rail freight in the UK economy. How important is it and what are the key international rail freight routes between the UK and Europe?
Mr McNulty: Firstly, I think it needs to be put into context because in any numerical sense at the moment the answer to that would be not terribly important but the potential remains enormous. It is about something like a 3 per cent share of what is potentially the maximum addressable international freight market of 60 per cent-plus. EWS will tell you that at the moment it accounts for about 10 per cent of their business. I met them just this morning and they recognise that there is still a huge potential in terms of that fully maximum addressable international freight market. There is still a way to go. It can, and should, be far more important than it is. In terms of particular routes: the UK, northern Italy and all steps in-between, the UK and Spain versus France, UK, Germany and Austria are pretty much the most utilised and potentially utilised routes. You will probably be aware that key commodities include things like heavy industrial products: steel; paper on those huge reels; some time-sensitive products, both including time-sensitive in terms of the production process as well as time-sensitive in other senses; valuable products; spirits and wines; ambient, ie non-chilled foodstuffs and drinks. The potential is far, far more than it is at the moment. You will know too that we feel that in terms of liberalisation the UK is ahead of the game rather than otherwise; we look forward to a very rosy future for international freight in years to come as the liberalisation takes bite European-wide.

Q317 ***Chairman:*** You are saying about three per cent of the current market. Naturally you would not want to be tied down to a particular figure but as a strategy, as it were, what would you regard as a sign of success in five or 10 years' time? Would that be doubled? In the UK, is rail freight not about 11 per cent or so of UK freight movement on rail? Is it feasible to see it getting to that within five or 10 years internationally?
Mr McNulty: I suppose the kind of strict, neutral and civil servant friendly answer to the question is significantly more than 3 per cent. As I say, I saw EWS this morning and at the moment they are the key player, if not the only player, in terms of international freight by definition. They remain incredibly bullish and I think would like to see significantly more than 3 per cent. It is very difficult to put a figure because it depends on so many other dimensions in terms of liberalisation and getting into other areas of the freight supply chain in terms of opening up operations in the European dimension, those sorts of things. Putting a finger up in the air, I do not know, if that is not doubled, and some within four or five years, then I think we would be disappointed.

Q318 ***Lord Haskel:*** I wonder why the Government is so keen on increasing rail transport. Is it that they see it as a sustainable transport system and they are concerned about the environment or do they want better use of the infrastructure? What is the motivation behind it?
Mr McNulty: Certainly those developments. Firstly, in terms of the environment, whether it is international freight or other freight simply in domestic terms, the more and more that is on rail in terms of the environment, the less that is in lorries and causing all sorts of damage from air quality through to pure infrastructure damage, etcetera. We cannot, and nor would we want to, eradicate lorry bound freight but the balance could be far better and far more environmentally friendly in that sense. This reads across all that we are doing in transport. If we are not going to keep building and building and building out of congestion then the most efficient way of distribution and logistics must be that we are optimising to full capacity what we already have. Certainly the answer, in short, in terms of rail bound freight is, no, we are not. There is significant scope to increase the capacity of more and more freight being on the rail network. Clearly that is a matter of

balance with passenger bound traffic and other things too. Is there scope for expansion? Is there reason to be optimistic in terms of growing the international freight dimension? There is. As I say, the more freight that is on rail—it is a crude analogy but it will do—the less that is on roads. We can be far more efficient in terms of our distribution and logistics in that regard.

Q319 ***Lord Fearn:*** What are the causes of the delay in the British Government transposing the First Railway Package into British law? How will this be overcome?
Mr McNulty: I think we are well on the way to overcoming it. We are largely compliant with the requirements of the First Railway Package. Part of the delay was the transmogrification from Railtrack to Network Rail and all that ensued in terms of definitions and everything else. It is settled now and certainly we are well on the way to progressing the transposition of both the First and Second Packages as a matter of some priority. That was the principal delay.

Q320 ***Lord Fearn:*** How will it be overcome?
Mr McNulty: It is overcome largely by a settled environment now post-Railtrack and on to Network Rail which will not be impinged upon by what we are seeking to do with the Rail White Paper in terms of, again, reconfiguring some of the structures and relationships inside the rail industry. The concern over Network Rail was principally about not simply its survivability and durability but definitions as to quite what it was in terms of private sector/public sector and all those other elements. That aspect has clearly been resolved and, as I say, moving forward with the transposition of the First and Second Packages will not be impinged upon, as I understand it, by what we are seeking to do with the Rail Review which, as you will know, is to step away from the SRA (Strategic Rail Authority) type model and shift things round a bit in terms of the Office of Rail Regulation, Network Rail and the Department for Transport.

Q321 ***Lord Fearn:*** Does that mean every Member State has very different legal positions?
Mr McNulty: The one thing I cannot do, nor pretend to do, is to speak for every other Member State. It really is a matter for the Commission in terms of the transposition of the Packages to ensure that there is compliance within each and every legal framework. There were difficulties of substance over our definitions and the background in terms of Railtrack but now with Network Rail and everything else those have been overcome. Transposition, you will know, is essentially how does what the Directive say impact on, and how do we interpret it, in terms of our own legal framework. We have done that successfully and I think we are progressing now that huge issue, which it was at the time, is out of the way.

Q322 ***Lord Geddes:*** Can you put a date or dates on such transposition?
Mr McNulty: I think things are slightly more complex than that in the sense that there are lead-in times and tails for every single element of it, so to put one definitive date I do not think I would be able to do so. If I take that back and look in more detail to see if there is a definitive date I will happily get back to the Committee, but I do not think there is in that sense. I will happily get back to the Committee, if that is convenient.
Chairman: That is very helpful.

Q323 ***Baroness Eccles of Moulton:*** Minister, my question goes a bit wider than specific entrants to this country. It is about the difficulties we hear of that new entrants are finding in trying to get access to the infrastructure of other countries, and this particularly applies to France. The question is what is the Government doing to put pressure on these countries in order that they should respect the spirit and the letter of the legislation?
Mr McNulty: In the first instance, without trying to swerve the question, it is a matter for the Commission to put pressure on other countries in respect of legislation. In our terms, what we can do in a concrete sense is make sure that now that we are in a position post the Railtrack issues that we were talking about, that we can lead by example at least. We do believe that, number one, as a backdrop liberalisation is absolutely necessary for the railway system, including freight, and that liberalisation does mean that there is as little impediment as possible in any of the national markets that make up the European Union. We can say that and exhort others to go down that road far more readily if our own stables are clean, as it were, and that is what we are trying to do. You will know that the Commission is taking, if not infraction proceedings against those who are, in their terms, transgressing and not fully implementing the packages, at the very least they are starting to look a good deal more closely at the claims by Member States as to whether they are implementing or have fully implemented. The strongest response I can make to the question is so long as we are, which we think we are, progressing along with at least the best of other states, if not ahead in UK terms, then that gives us all more licence to say to colleagues informally in the main rather than formally, I guess, that they should be doing the same and supporting the Commission, where necessary, in taking infraction proceedings where clearly other countries are not properly implementing the package. It is sometimes glacial, sometimes less than glacial but

things are moving in the right direction. In part, some of the concerns are about the whole interface that troubled us for a little bit, to be honest, with the Railtrack issue about where public sector/private sector sit and how with a hybrid model or public sector dominant model you can liberalise in quite the way that the thrust of the Directives implies. There are huge arguments at the moment in Germany, for example, about the whole role and ethos of Deutsche-Bahn, not strictly in terms of freight but more generally. Whilst at Lander level there has been nibbling around the edges it still needs to move on significantly. In the politics of it all, with a small "p"—I know you do not like politics with a big "p" here, so I will refrain from politics with a big "p", it is more genteel than at our end so I am trying to moderate my politics with a big "p" in that sense—there is a massive debate going on about Deutsche-Bahn in the future. We thought they were moving towards some kind of resolution, at least in terms of direction of travel over the summer, but they have pulled back from that again and put it off to 2006–07. Those debates at national level do underpin much of what we are trying to do at the European level. Getting our own house in order and exhortation and, where necessary, support for the Commission are the three elements that make that up. We cannot do the Commission's job for them and nor would we choose to do so.

Q324 ***Baroness Eccles of Moulton:*** It does seem as if there is not a great deal of optimism about the speed with which the other countries will unbundle and separate infrastructure and operations.
Mr McNulty: I am fairly optimistic, you have to be as a Government Minister. As I say, whilst some elements and some experience in the past have been glacial, I think it has moved on from glacial.
Chairman: Baroness Cohen is about to test that a little further, I think.

Q325 ***Baroness Cohen of Pimlico:*** I suppose really it stems from your remark about doing the Commission's job for it. If you could do the Commission's job for it, what would you advocate to get us nearer the competitive market in international rail freight? Does it need legislation or does it simply need enforcement? Are we not quite there in legislative terms as far as the Commission is concerned or if everybody would only do what the Directive is saying, including us, it would all be well?
Mr McNulty: As a starting point, I think full and comprehensive implementation of the First and Second Rail Packages to ensure effective liberalisation would take us a good way down the line so long as that was done on an EU-wide basis. Partly in terms of the point I made about glacial progress, I think what is not helpful is unrealistic time frames for implementation and perhaps we do need to take one step back and say, "Here is what we need, let us now be far more realistic in terms of by what time frames they can be achieved". Even allowing for both of those, I will say quite freely that the UK Government is concerned by the slow progress towards implementation of access liberalisation across the board. If you can wait with anticipation I will answer the rest of it momentarily.

The Committee suspended from 5.36pm to 5.42pm for a Division in the House of Commons

Q326 Chairman: Mr McNulty, you must be one of the fitter Members of the Commons.
Mr McNulty: I doubt that. It is very kind of you, Chairman, but you saw me put my cigarette out!

Q327 ***Chairman:*** It is more than possible that we may be interrupted to vote and if that is so, I apologise.
Mr McNulty: I am assured that we are okay for a bit although we are on a running whip. The other points I was going to make refer to what I had already suggested about the dominant position of publicly owned railways and how that sits with the thrust of the Directives and how, as a Government, our position is clear that the liberalisation implied by the First and Second Packages is clearly the direction that we want all of Europe to go. It is almost wait and see in terms of their assessment of the latest round of protestations from assorted EU members that they have fully implemented and wait to see what follows from that in terms of infraction proceedings or otherwise and, equally, as I say, perhaps a degree more realism about time-scales but sticking to them. It is very, very easy to have time-scales that are perhaps, on reflection, unrealistic but that, versus one that is slightly longer but more realistic and held to, is probably a matter of better public policy than shorter ones that are probably unrealistic.

Q328 ***Chairman:*** Taking that theme, say that a realistic time-scale of three or four years, what two or three significant changes would you like to see actually implemented over that period that will make a difference? I agree with you, and I think the Committee would, that being realistic and achieving things and doing things realistically is much better than hopeless, impossible targets. What would you like to see in three or four years? You know the area well now.
Mr McNulty: It is very kind of you to say so, I have been running it for eight weeks.

Q329 ***Chairman:*** Incidentally, I should have congratulated you when we first started.

Mr McNulty: Thank you very much. At a Member State level, perhaps led by the example of Deutsche-Bahn, we would like to see some resolution on the direction of such a significant publicly owned railway with all that might imply in terms of liberalisation. At the European-wide level I would hope, rather than another series of infraction proceedings and whatever else, further resolution by Member States to move towards the spirit if not the letter of the First and Second Packages. I think, if fully implemented across the European Union, they really do contain the building blocks for the liberalisation across the board that we think is required for the industry European-wide.

Q330 ***Chairman:*** Do you judge that the political will is there? After all, this industry is full of state owned, vertically integrated national champions with really little or no incentive truly to be competitive. There is not a lot of competitive pressure facing them. A lot of change is required if you are going to get a liberalised market. Do you think there is the will there now?
Mr McNulty: If I could cheat momentarily and dip back into last year's portfolio before the eight weeks, if we were sitting here as little as six, seven, perhaps 10 years ago on an inquiry into aviation we would be saying exactly the same. There were almost psychic and cultural as well as national interests around national flag carriers. It has taken time for that to slowly break up and move on to an EU level, to look at EU designation and subsequently, perhaps glacially, dealing with the US on an EU basis rather than simply as individual countries and ten years ago you would have said that was nigh on impossible, that if you challenged Alitalia or Air France you were challenging the nation. Things have moved in that way, which is why I think it will take something as significant as Deutsche-Bahn, one of the larger public sector railways in that sense, moving much more readily in the direction that the Directive has outlined. As I say, I am ever an optimist.
Chairman: Thank you very much. As you say, if you are not an optimist as a Minister then we will never make progress. We would like to ask you a series of things around the Channel Tunnel issue, not surprisingly. If we are to, in your terms, as you say, aim to at least double international rail freight in the next three or four years, that is not going to happen unless things happen through the Channel Tunnel. Lord Haskel would like to start the ball rolling.
Lord Haskel: Minister, certainly we say amen to that, doubling the rail freight in three years, and of course it is all going to have to go through the Channel Tunnel. We have been told that one of the reasons why rail freight is inhibited from going through the Channel Tunnel is that the access changes are so high that they are uncompetitive with road haulage. Do you agree with this and, if so, what is the Government going to do about it?

The Committee suspended from 5.48pm to 5.56pm for a Division in the House of Lords

Q331 Lord Haskel: To recap very briefly: if we are going to double the rate of international traffic in three years, and we all hope that is so, it is all going to have to go through the Channel Tunnel? We have been told one of the reasons that stops freight going through the Channel Tunnel is that the access charges make it less competitive with road traffic. My question was is this correct and, if so, what is the Government going to do about it?
Mr McNulty: In the first instance, there is a hiatus through to the end of November that we need to deal with, 30 November 2006. We have asked the Strategic Rail Authority to negotiate a fixed term extension to the current funding arrangements for EWS's Channel Tunnel freight usage charges to ensure at least some continuity of service until 30 November 2006. That is prolonging the current regime but we need that, amongst other things, to get some space to work towards greater liberalisation. Secondly, we are going to continue to support and progress EU rail freight liberalisation measures. Thirdly, we will watch with interest—we are not party to it—the negotiations between Eurotunnel and the railways users' contract to renegotiate a structure and level of Channel Tunnel freight usage charges that allows that greater liberalisation. You are entirely right in the sense that we cannot move towards that notion of greater liberalisation, especially in terms of international freight, when there is this one rail bound route that clearly we rely upon. I think with those three measures in place by the end of 2006, we should be in a far happier position than we are now. It needs to be said, too, that the ro-ro sector, the ferry sector, has responded, and responded very, very well, to the notion of competition from the Channel in ways that perhaps were not envisaged when we were going through all the early negotiations for when the Tunnel was constructed. They have also had opportunities in the sense of Sangatte and the difficulties with immigration and the problems that has caused for the Tunnel. That has perhaps brought into sharp focus the notion that there are alternatives. Specifically, for the Channel Tunnel, between the renegotiations and the broader issue of what we are trying to do on liberalisation anyway and hoping that all parties do get together to get to a far more competitive regime post-November 2006, that will help us on the route to the liberalisation that we want and the importance of the Tunnel in that dimension.

Q332 ***Lord Haskel:*** If you agree that the charges are uncompetitive, between now and November 2006 not a lot is going to happen.
Mr McNulty: Essentially not, not least because private sector companies are involved. In the first instance we do need to extend the existing contract to November 2006, amongst other things, to allow that window of opportunity for post-November 2006 for a happier position to prevail. Again, that does demand that all the progress we are talking about in terms of wider liberalisation across the EU prevails, including things like access to other Member States' markets and all the other elements about infrastructure and things we were talking about earlier. The Tunnel is very, very important but it needs to be seen in the broader policy context.

Q333 ***Lord Haskel:*** Yes, but everything is going to have to go through it: between now and November 2006 is a big chunk out of the three years during which you want to try and double international freight.
Mr McNulty: If all the other elements are not put in place as well as first implementation of the first set of packages, in terms of greater liberalisation, in terms of greater access to other areas, in terms of what we were saying about some of these public sector giants like Deutsche-Bahn and the interface with the private sector. All that needs to happen at the same time and alongside moving to a more regular and more competitive position with the Tunnel.

Q334 ***Lord Geddes:*** Minister, in the context of the Tunnel and, indeed, outside the Tunnel, how often do you—I do not mean you personally but the Department—have discussions with your French counterparts? When did they start in this context and what sort of results have come out from them?
Mr McNulty: There are discussions with our counterparts on a regular basis, not just formally within the associated Commission's informals and everything else but more generally. At official level, rather than ministerial, there have been meetings with Eurotunnel and others, there have been meetings with the other elements including the senior directors of Eurotunnel. These meetings are ongoing all the time. Given that the nature of the situation is ongoing all the time as well, in terms of coming to fruition and particular outcomes, again, I have nothing against you personally, Lord Geddes, I am going to say I should write further on that in terms of specific outcomes. Given the nature of the beast, there are meetings on a regular basis. In the general context, not simply in terms of international freight, it is a very important element in terms of our transport infrastructure.

Q335 ***Lord Geddes:*** It is not restricted to this country, let us be quite honest. The French have got, let us say, not a very good name as far as fair and competitive access charging is concerned. How confident are you that we will get to that idyllic situation? Again, if I could ask if you are confident, and you said quite rightly as the Minister you have to be confident, when do you think that we will get to that idyllic state?
Mr McNulty: I would hope that the window of opportunity afforded by the extension of the contract between now and 2006 does bring some urgency to resolution, if not to the idyll at least well on the way to it, not just in terms of the narrow confines of the Tunnel but in terms of broader liberalisation.

Q336 ***Lord Geddes:*** Thank you.
Mr McNulty: As for their tidiness or otherwise you ought to have the French over, I think.

Q337 ***Lord Walpole:*** Minister, the problems of going through the Tunnel are not just charges, there are other barriers like the current procedures for slot allocation and the safety regime which includes the fact that there is only one company in this country, other than Eurotunnel itself, that has locomotives that are capable of going through it. The Tunnel is nowhere near capacity whichever way one looks at it, whether it is carrying lorries through or motorcars or EWS or anyone else. How are we going to overcome these problems?
Mr McNulty: Specifically in terms of freight, the wider thrust to liberalisation and that break through for EWS and, indeed, any other carriers, if they go down that road, to that wider market. The potential market there is still huge. Currently we are at about 3 per cent in terms of international freight and, as you say, just the one carrier, EWS. The potential is certainly there. Almost every question leading up to your question is part of the answer. Yes, it is the specifics over Eurotunnel and where we go post-November 2006 but it must be about the wider liberalisation too. It must be about greater access to track and other elements of other countries. I was very intrigued that EWS certainly, and others maybe, are at least looking at setting up operations in other countries to try and, I guess, from their point of view, circumvent some of the obstacles and difficulties that they encounter by working directly with the dominant carriers in those countries. All those put together do push us in the right direction and the halcyon days or the idyll that we were referring to earlier.

Q338 ***Lord Walpole:*** A lot of freight journeys from this country to the continent, if they come from the south of the country, are not really economic unless you drive several thousand miles into Europe to

make the most of it. Obviously it is very important for complete trains with complete engines and wagons and everything to travel—I have forgotten what the figures are—at least 300 to 400 kilometres to be economic.
Mr McNulty: As I say—

Q339 ***Lord Walpole:*** The further the better, of course.
Mr McNulty: As I said in answer to the first question, I think the principal routes are well into Germany, Austria, north Italy and whatever new opportunities are opened up and afforded by the new Member States. That is partly a function of how saturated in all sorts of ways, in terms of capacity and opportunity, if you like, the golden triangle is anyway, the south east, north Germany, the Benelux countries. There are any number of ways that operators or their competitors would have long, long established routes of how to shift things around that particular core of the market in terms of logistics and distribution. It is partly a function of that too in terms of economics.

Q340 ***Lord Haskel:*** Just to come back to the question of charges, Minister. After November 2006, will the Channel Tunnel be able to fix its own charges so that they could be competitive with the cross-Channel ferries?
Mr McNulty: I believe that is the case.
Mr Graham: I think that is the case. I would have to check.
Lord Haskel: Unless they can do so it cannot be competitive.

Q341 ***Chairman:*** Can I ask the question a little more broadly. How are Channel Tunnel charges regulated and is the process currently consistent with the requirements of the First Railway Package?
Mr McNulty: Either it is or it is about to be, or was about to be, but the extension of the contract means that it will be after November 2006. That sounds deeply confusing so I think we will write more. That was not meant to be a parody of yesterday.

Q342 ***Chairman:*** If you can write to us on those points, that would be very helpful.
Mr McNulty: Certainly.

Q343 ***Chairman:*** At the root, and I understand the difficulty in enlarging on these things, but nevertheless from the Select Committee point of view this is important, we cannot double or triple or anything else international rail freight in this country unless it does go through the Channel Tunnel. Naturally we are greatly concerned about the prospects of that. I am delighted that EWS are optimistic, and I forget how you described your meeting with them in this last day or so, but people who are considering using international rail freight from the UK either must not know that there is a problem looming over the Channel Tunnel or they have enormous optimism that the problems will be overcome. If you are thinking of setting up international rail freight operations using international rail freight as opposed to ferries and lorries, knowing that for the next two years things will be desperately uncertain, it must be very difficult to build that up at the moment.
Mr McNulty: I think the buoyancy revolves around what I was saying about the opportunities beyond that once things do become far more regularised. There are huge opportunities, as your Lordships have suggested. There is much capacity still to be fully utilised about how we collectively, France and UK in particular, get to a stage where that optimism is realised.

Q344 ***Chairman:*** As you know, rail freight in Europe is falling as a proportion of market share. As the Minister, a politician, do you think that rail freight across Europe is most likely to receive a boost as a result of fuller charging to heavy goods vehicles for the costs that they impose on the system rather than, not instead of but rather than, as a matter of balance, the movements to liberalise rail freight? Effectively, liberalising rail freight at the moment is trying to help matters in situations where lorries are far more competitive and delivering on time and so on, than rail is.
Mr McNulty: I think it would be fairly difficult to unpick the two, both need to happen. You will know that we seek to introduce lorry road user charging to move in that direction. It is at least spoken about, perhaps progressed not as much, in other countries. You will know that rail freight in the UK is growing rather than otherwise. I was going to say that there is a need for a rebalance of the playing field, I was going to say, but you probably cannot rebalance playing fields, I apologise for that, a rebalance of the competitive edge that respective sectors have. I would not unpick them, I would say that needs to happen alongside. You will know too that there is a broader debate in this country. It is a way off in terms of road pricing in general. You will know that the Eurovignette discussions are still proceeding and we will see what happens with those. We had no success at Luxembourg. There are a number of things going on to try to redress that balance a little bit but liberalisation is at the core of that, although these other things will need to happen too. If not now, most other countries will be engaged in the same debates that we have started about the optimisation of the capacity that we have, whether it is road, rail or any other form of transport. Everyone is starting to understand that you cannot simply grow and grow

and grow in terms of the road or rail network in quite the way that we did perhaps in the 1960s and 1970s. I think the general tenor of the wider political debate is moving in the right direction as well.

Q345 ***Chairman:*** With your agreement, I would like to finish in 10 minutes' time, so we are working to a schedule.
Mr McNulty: That is a polite way of telling me to shorten my answers.
Chairman: I was going to say shorten the way the questions are put.

Q346 ***Lord Shutt of Greetland:*** On that very point, we had Mr Hilbrecht here earlier and I mentioned this point about the costs of road haulage and he said that there is a proposal which is on the table at the moment. I am not at all clear as to what it is that is on the table. What does it do in terms of the costs that it puts on the heavy goods hauliers? It may well be that that is substantial but I have no idea whether it is coppers or more and what difference it will make. If it is substantial, does that put even more pressure on because people will say, "Just a minute, we had better really sort this Channel Tunnel out if there are going to be these sorts of costs"? Have you got any feel for what these costs are? If it is substantial, what is going to happen to the money? I do not imagine it matters if it is coppers.
Mr McNulty: The rates will be fair. Essentially what the Eurovignette does, which is the proposal on the table, is broaden out to a European dimension what we are trying to do with lorry road user charges in this country. There was almost a deal at Luxembourg at the last Council that I was at but it fell on a series of technicalities revolving around the French and the Spanish and how their existing toll regimes in terms of their motorway networks would fit in with any Eurovignette. We are very, very close to a consensus. Clearly they are not punitive charges that would break the back of the road haulage sector but they are intended to be somewhere between your coppers and your big money to reflect at one level the wear and tear and other infrastructure difficulties with large lorries throwing themselves around the network and, in some ways, to restore some of the competitive balance between lorry bound traffic and rail bound traffic. They are not punitive and debilitating.

Q347 ***Lord Shutt of Greetland:*** Will it make a difference? Will it mean that people will say, "Just a moment, we had better think about rail"?
Mr McNulty: At least it will bring that competitive choice back into the equation to an extent, that is the prevailing view across the Union.

Q348 ***Lord Shutt of Greetland:*** What about the proceeds, what happens to them? Are they for road, for rail or what?
Mr McNulty: That was part of the subtext of the debate at Luxembourg, as to whether they should be hypothecated or otherwise. The broad consensus lent towards hypothecation, but then whether hypothecation meant hypothecation into a transport pot full stop, which some preferred, or whether the hypothecation should be as narrow as taking account of the wear and tear on a particular road or a network of roads, that debate is still part of the option. Clearly we lean towards the broadest hypothecation possible, that it is up to the national government.

Q349 ***Lord Geddes:*** The Treasury?
Mr McNulty: I meant Government, not the Treasury. It is broadly up to each Member State to decide where, within transport generally, any proceeds are rendered and spent. It is hard to quantify how much because of the different cost base in each of the respective countries anyway.

Q350 ***Lord Swinfen:*** Mr McNulty, I would like to go on to the costs of EU legislation with respect to interoperability and the proposed international rail driving licence because some operators have raised concerns with us. How do you and the Government intend to ensure that such measures are only implemented when the benefits exceed the costs?
Mr McNulty: In the first instance that will be our guiding principle for any agreement at European level. For example, on the train driving licence we think the notion of anything beyond the EU itself there is an extremely weak case for going right up to a fully international licence. Anything beyond the starting premise of interoperability of licences, interchangeability of licences between Member States to outside the European Union, I would think the costs would far outweigh the benefits very, very shortly. Costs will be our driving ethos, as I say. In terms of interoperability, the same would prevail. The Strategic Rail Authority certainly does a lot of work on the technical specifications of interoperability, the TSIs, and we are very, very grateful for that. The guiding point is costs versus benefits, practicability, because often, however nice it sounds in flowery Directives, the practicability of implementation is sometimes not terribly well thought through, and in general I think that is understood across the Union. We started to look at these issues that form part of the Third Package at Luxembourg but it was very, very early days and more or less just part of the progress report stage rather than coming to the Council in any formal sense.

Q351 ***Lord Swinfen:*** I hear what you are saying but you have not actually told us how you are going to ensure, which was the word I used, that the measures are only implemented when the benefits outweigh the costs.
Mr McNulty: As I say, I think amongst most members the prevailing view is—

Q352 ***Lord Swinfen:*** I do not want to know about most members, I want to know about our Government.
Mr McNulty: I am afraid we need to know about other members because this is qualified majority rather than unanimity. We will seek to resist anything where we consider the benefits are far outweighed by the costs and practicability and we will not sign up to them. That is where we will start from in the early stages of the various parts of the package that seem to go in that direction and, happily, we have a good deal of support for that starting point within the Council.
Lord Swinfen: All power to your elbow.

Q353 ***Baroness Eccles of Moulton:*** This question concerns the capacity and quality of the infrastructure for international rail freight services and what is the Government going to do to ensure that it is adequate at a time when, as far as we can judge, most funding for the rail sector is being absorbed by renewals?
Mr McNulty: Despite much going into renewals there is still much that we are doing. The West Coast Mainline, for example, was not just about passengers. That will provide capacity for something like 60/70 per cent more freight traffic than at present and will link far more readily the Tunnel to the north west and the north-west of Scotland, etcetera. You will know that the Felixstowe and Nuneaton gauge enhancement was completed on time and under budget early this year, about 30 million or so, and links the container ports far more readily to key freight terminals in the north and the midlands. There were capacity improvements in the Chelwell Valley part of the Southampton West Coast Mainline link completed in May 2004. I would accept that we do need to look far more readily at other elements of that Southampton West Coast Mainline linkage and we are seeking to do so. It is part of the overall direction that we are moving in to improve the railway network generally. We have not parked freight on one side, as it were, to sort out everything else and then we will come back to freight subsequently, if it fits in. In the work we are doing with the SRA now, and the Department will subsequently work with others, we need to understand about route utilisation strategies for each and every route and how freight fits in far more readily. It will be no surprise to learn that when I saw them this morning, EWS had significant views on that.

Q354 ***Baroness Eccles of Moulton:*** I bet they did.
Mr McNulty: I shall follow that up with interest. Our difficulty, probably, will be down the line when there is the success that I optimistically talk about, because success brings its own difficulties in terms of capacity utilisation and other factors. At the moment there is significant give and flexibility in the network for freight to run far more optimally than perhaps it would if there was more freight on it, so we will have to keep that under review as well. Yes, there is significant work happening on the overall network and infrastructure but freight has not been forgotten.

Q355 ***Chairman:*** The Commission have told us that they are engaged in discussions with Member States about 20,000 kilometres of track involving international rail freight, but in particular, looking at it in terms of the new ERTMS. They said in a sense that was the bedrock or the kernel of a European network for international rail freight. Is the UK party to those discussions? Do we have a view with them on a system, a network, for international rail lines that need to be upgraded over the years? Are we party to those discussions?
Mr McNulty: I am sure we are party to the discussions. Quite how much of the 20,000 kilometres is in the UK I do not know off the top of my head but it would be very interesting to see.

Q356 ***Chairman:*** You know of that idea? We do not have any views about other than trying to improve the existing rail freight lines, we have no plans at all anywhere in the foreseeable future for purpose-built or freight only lines, have we?
Mr McNulty: Nothing at the moment. You will know that we decided not to support the Central Railways Initiative and that was the last one that came up in any way, shape or form. Doubtless such schemes will return and we will have to deal with them as and when we see them in terms of their appropriateness or otherwise.

Q357 ***Chairman:*** Rail freight getting around London and using the Channel Tunnel link, in your view is that an important priority or will it be dominated by passenger movements?
Mr McNulty: We will always have to be alive to the balance between passenger traffic and freight. Clearly they serve two very different parts of the market and we keep that constantly under review.

Q358 ***Chairman:*** That is not quite what I asked.
Mr McNulty: I was mindful when I answered it that I was starting to sound like Sir Humphrey, I do apologise. I think that is about the best you are going to get off me at the moment.

Q359 ***Chairman:*** Is that right? Clearly the Channel Tunnel Rail Link and getting freight around London to the Channel Tunnel is very important.
Mr McNulty: Certainly it is important and that is why in an earlier answer I partly concentrated on Southampton up to the West Coast Mainline in the notion of getting through or around London. In that context, the balance between rail and freight on CTRL or any of the other enhancements and renewals we do on the network is paramount and part of our discussions.

Q360 ***Chairman:*** Thank you for staying with us so long. I am sorry that we disrupted you and your House disrupted us.
Mr McNulty: It was mutual in the nicest possible way.
Chairman: Thank you for your time and thank you to your colleague.

Supplementary written evidence from the Minister of State, Department for Transport

In the session that I attended on 8 November, I agreed to write with some additional items of information. I apologise for the delay in doing so.

The Committee asked about contacts between the British and French Governments and railways about issues relating to the Tunnel. I can confirm that, as you would expect, there are regular binational contacts about key aspects of the Eurotunnel Railways Usage Contract, including some elements of Channel Tunnel usage charges.

The Committee also asked whether Eurotunnel will be able to fix the level of access charges following the expiry of the Minimum Usage Charge in November 2006. Eurotunnel's railway toll structure and levels for the existing Eurostar and freight services—which provide a benchmark for the effective level of charges that potential new entrants might expect to pay to use the Channel Tunnel—are set in the Railways Usage Contract (RUC), of which the Minimum Usage Charge forms only a part. The RUC does not expire until 2052, and can only be renegotiated by mutual consent of all the signatories: ie the British Railways Board, Eurotunnel and SNCF.

It is true to say, however, that at current (and likely) traffic levels the Minimum Usage Charge effectively comprises a significant additional cost for EWS (passed on to the Government), Eurostar UK and SNCF. Its expiry in 2006 is tantamount to a major reduction in Eurotunnel usage charges for existing passenger and freight services. This will give signatories to the RUC significantly more freedom to develop their international rail businesses. In addition, Eurotunnel's Network Statement, as described below, now provides information on usage charges for new entrants into the cross-Channel rail freight market, outside the aegis of the RUC.

Finally, the Commitee asked about the regulation of Channel Tunnel charges. In accordance with the first railway package, and specifically Council Directive 2001/14/EC, the regulation of Channel Tunnel falls within the responsibilities of the Channel Tunnel Intergovernmental Commission (the IGC).

Eurotunnel has published a Network Statement in accordance with Directive 2001/14/EC. As required by the Directive, the Network Statement includes a section on charging principles and tariffs. However, Article 8.2 of the Directive does provide for exceptions to the general charging principles in the case of specific investment projects, and allows that these may incorporate agreements on the sharing of the risk associated with new investments. The charging structure agreed in the Usage Contract falls into this category.

I will write again shortly with the information that the Committee requested on the expected date of transposition of the first railway package.

17 December 2004

Additional supplementary written evidence from the Minister of State, Department for Transport

When I wrote to you on 17 December 2004 with information on issues raised during the session I attended on 8 November, I promised to write to you with information about the expected date of transposition of the First Rail Package (Directives 2001/12/EC, 2001/13/EC and 2001/14/EC).

8 November 2004

As you may be aware, on 7 October 2004 the European Court of Justice (ECJ) ruled that the UK had, by failing to adopt laws, regulations and administrative provisions to comply with the First Package of Rail Directives, failed in its obligations under those Directives and the Treaty. In reality, these Directives will have little effect on our railways which already comply with the vast majority of the Directives' requirements which aim to open up the European rail market to competition.

Nevertheless, the Government takes the issue of complying with the ECJ judgment very seriously and regards transposition of the First Rail Package as a priority. We currently expect to transpose these Directives by the end of 2005.

7 January 2005

MONDAY 15 NOVEMBER 2004

Present	Cohen of Pimlico, B.	St. John of Bletso, L
	Eccles of Moulton, B.	Shutt of Greetland, L
	Fearn, L	Swinfen, L
	Geddes, L	Walpole, L
	Haskel, L	Woolmer of Leeds (Chairman)

Memorandum by Network Rail

Further to the call for evidence by Sub-Committee B of the House of Lords Select Committee on the European Union into the "implementation of the European Union policy of open access for international rail freight services, as implemented in Directive 2001/12", please find below comments in relation to the first and second packages and the Committee's further questions.

These comments support the oral evidence provided by Network Rail to the House of Commons' Transport Select Committee inquiry into "European Union Competence and Transport" given on 16 June 2004 and available at: http://www.publications.parliament.uk/pa/cm200304/cmselect/cmtran/581 /406 1601.htm. I refer you to this for comments on Network Rail's wider perspective on developments in EU rail policy.

In general, Network Rail shares the Commission's aim of wanting to improve the performance and quality of European rail freight services and believe that the means to bring about the necessary performance improvements can be found within the measures to liberalise markets that are found in the first and second packages of reform. We also believe that competition generates sufficient incentives for private operators to have a high standard of service.

As the Committee will be aware, Directive 2001/12 modifies Directive 91/440 (consolidated version) on the development of the Community's railways. It requests the Member States to adapt their national legislation to enable the extension of access rights for international freight transport services to the national section of the Trans-European Rail Freight Network. The Directive also provides that different organisational entities must be set up for transport operations and infrastructure management. Essential functions, such as rail capacity allocation, infrastructure charging and licensing be separated from transport operations to enable new rail operators fair access to the rail market. This Directive also foresees that railway undertakings set up different accounts for passenger transport services and freight transport services.

Network Rail is designated as the "Infrastructure Manager" responsible for detailed allocation of capacity on the network, identification of congested infrastructure and making proposals to the "Member State" (currently the Strategic Rail Authority (SRA)) for how these could be resolved, supervised by the Rail Regulator.

Network Rail has implemented all the relevant measures required of it under the first and second railway packages, such as the publication of the Network Statement (available on Network Rail's website).

With reference to the Committee's specific questions, although many of the issues raised will need to be addressed directly by the freight operators, the following points can be made in relation to the five questions posed:

1. *What are the current barriers to entry in the international rail freight market?*

Aside from language differences, many of the barriers to entry into the international rail freight market are physical. These include:

(a) Safety Case:

We would anticipate that freight operators will find that the maintenance of a robust safety case increasingly complicated and expensive, as operations extend into additional markets with individual safety cases and different standards.

(b) Vehicle Acceptance:

The process of vehicle acceptance similarly needs to be simplified.

(c) Access to infrastructure:

Due to the nature and consistency of access contracts (eg pricing), any potential operators considering entry into the rail freight market will require extensive knowledge of the network/ industry in order to negotiate contracts.

(d) Channel Tunnel:

The Channel Tunnel provides a limiting factor to cross-channel access as only three types of electric traction are allowed to haul freight trains through the Tunnel. The charging regime for use of the Tunnel also provides a financial barrier to the movement of freight.

2. *To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?*

While barriers will certainly result from Member States failing to implement the existing Directives, even if there was full implementation, the Channel Tunnel would still be a barrier to UK freight operators entering the continent and vice-versa, as its stand-alone safety case restricts types of rolling stock permitted to use the Tunnel. The UK does however already have in place appropriate access charges and performance regimes where necessary which are governed by the UK regulatory regime.

3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

Enforcement action has already commenced against countries that have not implemented the measures contained within the 1st package.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

The roll-out of Technical Standards for Interoperability (TSI's) should make it possible for Freight Operators to operate throughout Europe, however the high cost of implementing some TSIs prevents it from being economically viable to do so.

5. *What action should the UK Government consider to ensure that the UK takes full advantage of the potential growth of international rail freight as a result of this policy?*

As a key physical barrier to increased traffic, if Government were to review additional actions that might be taken, it would be sensible for consideration to be given for a review of the Safety Case for access to the Channel Tunnel.

The difference in gauge between the UK and the rest of Europe, as ever, poses difficulties for freight movement. Should the aim be to enable the UK network, to convey the newer and larger international freight containers, further development of the UK's integrated freight transport policy (design of intermodal routes, gauging etc) would be required, along with consideration of how to fund the necessary enhancements.

Finally, when considering further reform such as the third package, Network Rail believes that until the provisions of existing legislation (91/440, 2001/12, 2001/14 and 2004/51) have been fully implemented in all Member States, any further EU regulation in the rail freight market would be premature and could have the negative effect of driving prices up and forcing customers out of the market.

John Armitt
Chief Executive

21 August 2004

Examination of Witnesses

Witnesses: Mr Paul Plummer, Director of Regulatory Affairs, and Ms Barbara Barnes, Head of Customer Service, Network Rail, examined.

Q361 ***Chairman:*** Good afternoon, Mr Plummer and Ms Barnes. Is there anything you would like to say before we go into questions?
Mr Plummer: No thank you.

Q362 ***Lord Fearn:*** The White Paper on the *Future of Rail* states that Network Rail will in the future be responsible for route utilisation strategies. How will the needs of international rail freight be taken into account in the process?
Mr Plummer: The purpose of the route utilisation strategies is to define what it is we are trying to achieve on each of the 26 strategic routes we have. In doing that, we will be discussing sensibly with all our customers and train operators, as well with Rail Freight Group and others, and in the context of international traffic specifically with RailNetEurope, to make sure we take account of those traffic flows.

Q363 ***Lord Fearn:*** Which is the main route?
Mr Plummer: The main route clearly is the route to the Channel Tunnel, which is important. Other routes are important such as routes to ports, and we will be developing plans to ensure that we take account of those requirements.

Q364 ***Lord Fearn:*** "Will be developing", so they are not done yet?
Mr Plummer: It is already part of our business that we do that. The White Paper changes it slightly and places greater emphasis on the work we do for the route utilisation strategies. In the past, we have provided input to that work which was done by the SRA (Strategic Rail Authority), but ultimately the work that has been done in the past will continue to be done. What should be different is that it should be more joined up, between what we are doing to our infrastructure and planning that, and what we are doing in planning the way in which the network is utilised, so it should be more effective.

Q365 ***Lord Geddes:*** To what extent, Mr Plummer, do you feel you can either morally or legally disagree with what is said in the White Paper?
Mr Plummer: We have had extensive discussions with the Department for some time on the background to the White Paper and leading up to it. Most of our thoughts were reflected in that, so there are not really major issues at all about which we have fundamental disagreements.

Q366 ***Lord Geddes:*** I know it is hypothetical, but if you had, what would you do about it?
Mr Plummer: During the discussions there were certainly issues where there were differences of emphasis, and we discussed those extensively with the Department. In some cases the emphasis would have changed as a result of those discussions.

Q367 ***Lord Shutt of Greetland:*** You mentioned 26 strategic routes, were they for freight? What is it that makes a route strategic? Can one somehow be crossed off the list of "strategic"; and how can another route get on that list?
Mr Plummer: The strategic routes are for the network as a whole, so there are no non-strategic routes, as it were. It is the passenger and freight traffic, so it is planning those services together in order to get the best out of the available capacity on the network. There is no indication that anything is more or less important because of being called "strategic". It is just a name, in the sense that we organise our business around routes, so we needed something to qualify it, and "strategic" was the best word we could come up with.
Baroness Cohen of Pimlico: "Bigger" might be better!

Q368 ***Chairman:*** On those strategic routes, how are priorities determined where there are conflicts between passenger and freight traffic? What are the principles that you bring into play?
Mr Plummer: I will ask Barbara Barnes to comment further in a moment, but clearly we have to take account of our existing contractual commitments. We have to try and make the best use of the resources that are there, which means fitting in different services in the best possible way. Obviously, we need to balance the longer distance and short distance services and routes, by-passing off the main route on to a trunk line and so on, so it is a complicated process that is evolutionary and builds largely on the existing pattern of traffic and trying to improve that, rather than starting from scratch all the time. With the route utilisation strategy we will be trying to take a more radical look to see if there are better ways of doing things to plan the service.
Ms Barnes: The important thing to notice is that we do this in co-operation with our customers so that they have a part in that process as well. It may well be, especially where the freight companies are concerned, that they need changeover time, so we need to understand what they want us to deliver for them in the future.

Q369 ***Chairman:*** Have you started that dialogue?
Ms Barnes: We are in that dialogue now. We are always in that dialogue with them and trying to understand what they need. Whether it is as good as

it could be is an open question. I certainly believe that we could do more, with their help, in trying to understand their future needs. As the Rail Review becomes more concrete and the Strategic Rail Authority falls away, we need to get better at doing that because at the moment the Strategic Rail Authority has responsibility.

Q370 ***Chairman:*** Which are the rail freight businesses or interests with whom you are in consultation?
Ms Barnes: We are in consultation with five freight operating companies at the moment, and there are a couple that are in the process of agreeing traffic, and we also get involved with the Freight Transport Association and Rail Freight Group. Therefore, the end customers as well—they also have needs—can talk to us about what they want to achieve, because sometimes that has happened before they talk to freight operating companies. Speaking to freight operating companies alone does not always give us a true picture, and we need to look wider than that.

Q371 ***Baroness Eccles of Moulton:*** I wonder, Ms Barnes, whether comparative liability between passenger and freight is a factor? As a travelling passenger, it does seem that sometimes the reliability or punctuality of the service is affected by a rail freight train breaking down. Is this just a false impression?
Ms Barnes: I believe it is. All trains suffer failure at one time or another, either through the trains or through our infrastructure. I believe that the number that is most readily understood at the moment is that about 5 per cent of delays of passenger trains are caused by freight trains on the network, so I think it is a false impression.

Q372 ***Baroness Cohen of Pimlico:*** I had rather forgotten about the Strategic Rail Authority, but of course the planning must have been a bit stuck between the two of you. How can I put this without sounding ungracious? Is it going to be easier without the Strategy Rail Authority, and, if so, when is it going to be easier?
Mr Plummer: As I implied earlier, it will help to be able to bring together the work that we were doing already as input to what the SRA is doing with the work we are doing to plan the infrastructure. That should help in making our overall plans more robust. We are looking at the infrastructure, the planning for services on that network, and the work that we would do as input to rolling stock specification for example; and the franchising process should become more joined up and should enable us to deliver a better service as a result. Already we are discussing extensively with the SRA in the old model so that we try and achieve that, but it will be easier under the new model, I believe.

Q373 ***Baroness Cohen of Pimlico:*** The new model loses to the SRA?
Mr Plummer: Yes.

Q374 ***Baroness Cohen of Pimlico:*** When?
Mr Plummer: The formal transfer of its functions requires legislation, but for many of its functions around its role of planning and leadership of the industry the transfer does not require legislation, so that would be much quicker to change. There are some existing route strategies that the SRA is developing now, and those will continue. It has been agreed that we will take on the new route utilisation strategies that are being developed from now effectively.

Q375 ***Lord Geddes:*** Barbara Barnes mentioned discussions with the freight operators. If you can generalise, what sort of lead-time do you need from a specific request from a freight operator to implementation?
Ms Barnes: It is hard to generalise because it depends on the circumstances. If it is a piece of traffic that is using existing infrastructure and it is just a matter of running one additional train, we often have services that can run next week from a request today—that is possible. If you are looking at a new piece of infrastructure having to be built, or where we have to transfer access rights from one customer to another, that will be a different lead time. Equally, if you have some port development that is a major development of some sort, with planning applications dependent on it, that can take even longer, so it depends. It is difficult to generalise.

Q376 ***Chairman:*** Where does freight come in your priorities? Government Ministers would probably put passengers first, second and third. How can you in reality on our rail network ensure that rail freight does get as much priority for meeting their needs, which will not be as big as passenger needs? After all, rail freight does not shout, and passengers do!
Mr Plummer: Certainly rail freight does shout, and we have a huge amount of discussion with various freight operators and other freight groups. There is a significant influence there. We are required by our licence to develop the network to meet all the needs of our customers, not just passenger operators. We have contractual commitments to freight operators which we cannot simply ignore. We do plan our network to meet all of those requirements as best we possibly can.
Ms Barnes: We endeavour to treat all our customers in a non-discriminatory manner. Freight is a different product to passenger, and they do not sit easily

together, but that is our job. We have to make it fit. Usually, we have no difficulty with that whatsoever. People understand we need a freight business and they understand we have to plan to deliver service to them because there are a number of major UK companies that are relying on this service to deliver their production, and very small companies that are relying on us to keep them going. We take that very seriously.

Q377 ***Chairman:*** Do you keep data on rail freight arrival and punctuality as you do for passengers?
Ms Barnes: Yes.
Chairman: It would be very useful if you could send us a note about the equivalent data you collected on rail freight movement and punctuality.

Q378 ***Lord Haskel:*** It would be very useful if we could come back to the White Paper. It talks of giving rail freight greater priority on key routes, but requires it to pay for this priority. Can you explain this? What is the implication for international rail freight?
Mr Plummer: The details of this are being worked through between ourselves, the Department, the Office of Rail Regulation and freight operators. One of the key points is that in terms of freight and international freight, we would treat them exactly the same in terms of the charging regime. There is no difference there. They would not be discriminated against in any way because that would be inappropriate. One of the principles being discussed is that where there is an existing passenger railway then freight would have access to that at effectively incremental cost. That is reflected in the access charging regime at the moment. Clearly, where freight is asking for additional capability to be delivered, then it would be expected to pay for the incremental cost of providing that capacity. Details of how that gets worked through into the charging regime are still to be developed.

Q379 ***Lord Haskel:*** Do you have any principles on which you will base these charges? You say you are developing them, but are you depreciating the infrastructure or charging for the extra hour, or do you do it by the time that they use the infrastructure?
Mr Plummer: One of the basic principles being discussed is that where there already is a network that is required for both passenger and freight, part of the costs of that network are attributable to freight, part to passenger, and part of them are attributable to neither in particular but they arise from having that network there. It would only be the incremental cost of the freight part that would be reflected in those charges to the freight operators. That basic principle is consistent with the existing charging regime so, again, it would be a refinement of that and a consideration as to whether that should provide longer-term stability for train operators, rather than it being subject to review more frequently.

Q380 ***Lord Haskel:*** If the freight is delayed for some reason, does this affect the charging? Is there a refund or anything?
Mr Plummer: The way in which the performance regime works for freight operators differs to passenger operators, but there are some incentive mechanisms relating specifically to performance.

Q381 ***Lord Swinfen:*** I am wondering about the comparable cost to the network between a freight train and a passenger train.
Mr Plummer: It does not depend upon it being passenger or freight; it depends upon the characteristics of the vehicle and the pressures imposed on the track. There is a detailed model that is used by the Office of Rail Regulation to calculate charges for different types of vehicles, which is totally transparent and is subject to periodic review by the ORR. It depends on those vehicle characteristics.

Q382 ***Lord Swinfen:*** You are talking about the rate at which an individual train will wear out a track?
Mr Plummer: Yes.

Q383 ***Lord Geddes:*** That has almost answered my question, but I do not think you answered Lord Haskel's first question. Do you base it on, for instance, per tonne/mile, length of train, time that it uses the track, both of them or all three of them?
Ms Barnes: For freight trains it is based on gross tonne miles, so the weight of the train, and that takes into consideration the length because if it is longer it is heavier. On the passenger side, it is per train mile because that is just the way we have worked it through. In equivalent terms it is a transparent tariff-based system, which is readily available to anyone who wants to run new traffic.

Q384 ***Lord Geddes:*** Does freight vary on time?
Ms Barnes: No. There is a capacity charge for freight companies. I think about 3 per cent of the total charge is a nominal amount of money that affects whether or not they are using a congested piece of network at a congested time, but it is not a significant amount of money.

Q385 ***Lord Swinfen:*** I am just wondering whether the planned speed of a train has a bearing on the cost because, obviously, if you have a heavy weight moving along the rail it is pressing it down and you have therefore got a kind of wave going, and the faster you are going the harder that wave will hit bridges and things of this sort, which is liable to cause more damage. Does speed come into it?

Ms Barnes: Yes. That is part of the algorithm that has gone into the charging model.

Q386 ***Lord Swinfen:*** So the high-speed trains pay more than the slow local trains?
Ms Barnes: The higher speed characteristics and the damage that the higher speed train will do to the network is part of the calculation that has gone into the charging model. For example, if you had a particular vehicle type that went at 70 miles an hour, compared to one that went at 125 miles an hour, and everything else was equal, then the 125 miles an hour one would be chargeable.

Q387 ***Lord St. John of Bletso:*** You mentioned the weight of the train and pressure on the track; how does that move on to the maintenance of the track? How is that calculated?
Mr Plummer: We would approach the maintenance need of the network separately from the charging mechanism. We would be doing inspection of the track and inspect other assets to ascertain what maintenance is required and what renewal is required. Some of the tools that we use would take account of the volume of traffic, so if there is a large volume of traffic, the network would need to know it would be expected to degrade faster than if it was a lower volume, and we would use that information in assessing frequency of inspection and so on. It is not a mechanistic relationship. I am not sure if I have answered your question or whether I misunderstood.

Q388 ***Chairman:*** What parts of the UK network are part of the trans-European rail?
Ms Barnes: From Dollands Moor through to Wembley and Imingham through to Liverpool, but I will have to come back to you on that one; I am not absolutely certain.

Q389 ***Chairman:*** It would be extremely useful to have a map, the kind of thing we could include as an appendix to our report, and obviously a verbal description.
Ms Barnes: I can provide that.

Q390 ***Lord Walpole:*** Will international freight trains be able to use the new Channel Tunnel rail link when it opens through to London; and what volumes of traffic are expected over that route?
Mr Plummer: In principle they would be able to use it. In practice, it would depend on the speed and the weight. Clearly, slower trains would use up a very large amount of capacity that could be put to other uses.
Ms Barnes: In terms of volumes, it would depend on the customers who wished to use it. At the moment we have 35 paths reserved on the network between Dollands Moor and London on conventional routes, and we are running about 12 a day at the moment. How much of that would want to go via Channel Tunnel rail link, if it is possible to path it that way, is as yet uncertain. We are in discussion with freight operating companies about their needs.

Q391 ***Lord Walpole:*** In the long run, presumably that track could take a lot more passenger traffic up to Edinburgh and other places, could it not?
Ms Barnes: Potentially, provided the market is there.

Q392 ***Lord Walpole:*** Then it will probably become saturated with passenger trains anyway, won't it?
Mr Plummer: There is likely to be a demand for it certainly.

Q393 ***Lord St. John of Bletso:*** We have heard of several problems of the Channel Tunnel from safety to track access charges, and issues of subsidies. In your written evidence you mention that the Channel Tunnel provides a limiting factor to cross-Channel access as only three types of electric traction are allowed to haul freight trains through the Tunnel. What scope is there to increase the volumes of rail traffic through the Tunnel?
Ms Barnes: The limiting factors at the moment are the charges made for use of the Tunnel. There is the issue about whether or not customers find it easy to get access through France, because access through France is not as prevalent as it is here. There is the issue about types of equipment people can use going through the Tunnel. The biggest limiting factor at the moment is the charges.

Q394 ***Lord St. John of Bletso:*** We heard that rail freight through the Channel Tunnel comes to 3 per cent of traffic. In percentage terms, what do you think could be the potential? The Minister says he hopes to double that amount coming through. Is that achievable?
Ms Barnes: We have capacity booked for 35 slots and are only using 12 at the moment, so we have provided for that. It depends if the market picks it up.

Q395 ***Lord Haskel:*** If you have 35 slots and you are only using 12, in most businesses you would then reduce the price and try and encourage more people to use your service. Do you adjust your charges to make rail freight competitive with road transport or trucks going over the Channel on ferries?
Mr Plummer: No, we do not. The prices are based on assessment of the cost. If you look in the other direction as well, we do not seek to put the price up where there is a significant margin from that traffic. It reflects the cost to the network in either case.

Q396 ***Lord Haskel:*** There is no variation of charges at all?

Mr Plummer: Not for those reasons, no.
Ms Barnes: Not on our side of the Tunnel.

Q397 ***Chairman:*** Apart from your goodwill and general remit, you have no commercial incentive to build rail freight. In other words, you charge it if it goes over and if it does not go over—
Mr Plummer: That is the same for all of our traffic. The charges are meant to reflect the cost, including a reasonable return on the investment that we make, regardless of whether it is passenger or freight.
Ms Barnes: The advantage for the operators is that it is transparent and they know what they will be charged. It makes it easier for them in making commercial assessments as to whether or not they want to go.
Lord Geddes: In that respect you are not competing with road as far as freight is concerned.
Chairman: As far as Network Rail is concerned.

Q398 ***Lord Geddes:*** Yes, Network Rail is not competing with road.
Mr Plummer: Not competing in the sense that we make a large financial incentive for there to be additional freight traffic. We are discussing with freight operators how we can make sure our incentives, the incentives of the company, and the incentive of senior management of the company can be aligned with those of freight operators. We have been having that discussion in the last few weeks.

Q399 ***Chairman:*** We have found that this applies generally throughout Europe and it is probably even worse than here: the track operator has no incentive to see itself as part of vibrant, commercial, aggressive rail freight or freight businesses. The evidence you have given today is impressive: you know what you are talking about and you have a good grasp of what is going on; but even in this country, which is pretty liberalised, Network Rail has no real driver to build up business.

Q400 ***Ms Barnes:*** If you went back in time to Railtrack days, there was an arrangement when Railtrack was first set up where we did charge a commercial price for the paths, and at that stage the amount of revenue that we obtained from the freight operating companies was double what it is now. It was decided that that was not in line with European legislation, and therefore it had to change, which is why we now have the tariff-based system, which just seeks to recover our modelled costs. To that effect it is simpler. We do have an incentive regime. We are incentivised through adjustments to the regulatory asset base if we do achieve a certain volume of growth. It is not a significant incentive as such, but there is an incentive.

Q401 Mr Plummer: It is important that the whole contractual and regulatory regime is designed so that we are not averse to additional traffic or changes in traffic. There is no disincentive for us to accept that traffic. We try to work very closely with the operators. I believe that they strongly supported the existence of the tariff-based approach rather than the market-based approach, and the alignment of incentives is potentially a further improvement.

Q402 ***Chairman:*** In answer to questions you said that charges are high. Presumably that is for other than EWS going through the Channel Tunnel. If a freight train went through the Channel Tunnel, how much would they pay in freight charges compared to what they pay going over the track before they get to the Tunnel? Give us an idea of what the high charges are, because you say that is the biggest problem.
Ms Barnes: I cannot quantify that. I can get back to you with that.
Chairman: That would be very helpful because it has come up as a significant issue time and time again.

Q403 ***Lord St. John of Bletso:*** In regard to volume of traffic, you mentioned the issue—on which I take your point—about the tariff-based system being transparent, which is obviously a valid point, and the incentive on volume of growth. I am looking at a charge for the current position of rail freight in the EU over the last 30 years; and we see that rail freight has gone down from the 70s, which was 20 per cent of the European Union tonnage, down to currently 8 per cent, and road traffic has gone from 34 per cent up to almost 44 per cent, with crude oil prices having almost doubled in the last year. Surely, there will be much more incentive, with the congestion-charging on our roads, for more traffic to go by rail rather than by road? That is why I am quite interested in what you say about incentive on the volume of growth. This is surely a better time than ever for there to be more volume of growth?
Ms Barnes: If you look at the UK market freight business has grown by 80 per cent since privatisation. If you look at where we are this year compared to the same place last year, we are up 5 per cent this year. The difficulty we have had with Channel Tunnel international traffic is that we lost a lot of traffic over the past couple of years, as you are probably aware, because of the issue of people trying to gain access to this country illegally. That disrupted the traffic through the Tunnel quite significantly, and quite a lot of companies ended up going to the wall because of it. We are just beginning to crawl our way back. The traffic coming through the Tunnel at the moment is 68 per cent up from where it was last year, so we are beginning to improve, but we are still have a long way to go, and we have paths that are booked and available to be used. Markets need time to stabilise

and feel confident. The situation at Sangatte caused a huge amount of problems for our customers, and dented the confidence of the market. It will take a long time to get back, even if we have everything in place that we need. I am confident that there is a market there and that there is a way to gain that market and make it grow for the benefit of the freight community. We are doing everything we can to help our customers do that.

Q404 ***Baroness Eccles of Moulton:*** To what extent do you think the expansion of the amount of freight traffic that can move throughout the UK network is restricted by the loading gauge problems, the differential between the European Union and the UK loading gauge? In your written evidence the implication is that a great deal will have to be spent in order to bring our loading gauge up to the standard of the European loading gauge. What do you think is the future for this? One specific area is the clearance from 9' 6" for containers. I know that is only one part of it, but what is your general view?
Ms Barnes: As you probably know, the SRA recently completed gauging work in the Ipswich Tunnel that now gives us a route through from Felixstowe to the West Coast Mainline for 9' 6" containers, which was quite welcome at the beginning. Certainly the international container market is moving rapidly towards standardisation. If we are to retain our market share of this type of traffic on rail, we need to find a way of giving gauge compatible routes from places like Felixstowe, Southampton and potentially from the Channel Tunnel port as well, which already has a slightly smaller gauge but is a bit better than Felixstowe and Southampton. We need to find a way of dealing with that. However, it does need somebody to fund the works, and we need to find routes to improve the funding arrangements so that some of this work, which can be quite expensive, can be undertaken. The SRA is looking at developments like Great Yarmouth that are currently in planning phases. We are looking for port developers to help fund some of these gauge clearance works on our network so that once the ports are built and they have planning permission we can get an increased gauge through to the east coast and west coast to allow those opportunities to be exploited.

Q405 ***Baroness Eccles of Moulton:*** Is pretty well all the international traffic container traffic, or is some of it bulk traffic that is affected or not affected by gauge differences?
Ms Barnes: Most of the traffic coming through Felixstowe and Southampton will be container traffic. The traffic coming through the Tunnel will be a mixture of container, automotive and other types of traffic. We generally do not find the heavier type of freight that traditionally we have been very good at in this country running through the Tunnel because there is no market for it. It tends to be containerised or smaller bulk items.

Q406 ***Baroness Eccles of Moulton:*** Is it really the container gauge problem that is the major one?
Ms Barnes: Yes.

Q407 ***Lord Walpole:*** I wondered if there was going to be any trouble in Great Yarmouth if the port is built.
Ms Barnes: A similar sort of situation arises.

Q408 ***Lord Walpole:*** There are problems?
Ms Barnes: Yes.

Q409 ***Lord Shutt of Greetland:*** I am going to ask you about shifting some goods from Manchester to Milan but, in order not to disappoint my Lord Chairman, I ought to be asking about shipping something from Halifax to Heidelberg or Bradford to Berlin! However, the interesting thing is that I cannot really ask that question. I do not believe that any rail freight has shifted from anywhere near Halifax or Bradford for over twenty years. I would not mind knowing, as a side issue, if there was anything you could offer in places like that, with half a million of population? How soon could something happen if there were serious freight to be offered? We have asked the question previously about Manchester to Milan. If there were a hundred containers every week on that route, what process would a new operator seeking slots need to go through? How long would it take, and in particular who would champion this?
Ms Barnes: You may have heard of a group called RailNetEurope (RNE), which is a group of infrastructure managers based in Vienna, with a head office there; there are 23 Member States that are members of RailNetEurope. It has a philosophy of having one face to the customer, so the customer does not see that they are dealing with a lot of different administrations, and they end up having the ability to run their traffic from Manchester to Milan if that is what they wish to do. Each infrastructure manager, who is a member of RailNetEurope, has what is called a one-stop shop, which is one person who will deal with the issue from Manchester through to the end destination, across all the borders that it may have to go through, with all the different types of contracts that might have to be negotiated. They will champion it for the customer. The customer can choose any one-stop shop to go to; they can choose to come to us if they want to; they could choose to go to Italy if they are going to Milan, or they could choose somewhere in the middle; or they could choose somewhere completely different. If, for example, it was a Finnish company that wanted to run traffic from Manchester to Milan, they could go

to their one-stop shop in Finland. We are at an early stage and it is not something that is particularly well tested in this country, although it has been tested on the continent where there are far greater volumes of international freight. It depends again on what they are trying to achieve and where they are trying to achieve it, and whether a path already exists. It also depends on how soon they want to run the service, because I suspect if they are running from Manchester to Milan they are talking about developing something equivalent to three or four months' time, in which case there should not be a difficulty putting something in place. At the moment, we do not have standard access contracts across the continent. We have separate and individual contracts, but we are trying to put in place, as a group, a standard access contract that would apply across every Member State, so that it makes it easier for the customer to deal with cross-border issues.

Q410 ***Lord Shutt of Greetland:*** You are really saying that starting from today we are talking about three or four months?
Ms Barnes: It depends what they are trying to achieve and also on the time-scale. If they want something quicker than that, we will try and do that.

Q411 ***Lord Shutt of Greetland:*** With my earlier point, that is almost easy, in the sense that we believe there is something connected in Manchester and similarly in Milan; but what if there were no rail connection at this end and we are talking about a fresh start: how long would that take?
Ms Barnes: It depends on what they are trying to do and whether or not they have to look into signalling systems. It would be hard to generalise—and it comes back to the question I had earlier—on something that is difficult to get hold of. It would depend on the circumstances. Obviously, if there was a need of a customer and we understood the specification, there is no reason why we should not work with them proactively to achieve what they want, and we will do that.

Q412 ***Chairman:*** When you answered the question about the Channel Tunnel you said there were three problems: charging and the safety—
Ms Barnes: The third one is people trying to access our country illegally that caused the market to fall.

Q413 ***Chairman:*** No, the future. The third one was the problem of getting access into and across France. That is what you said. If this one-stop shop is going to be effective, is it going to solve that problem?
Ms Barnes: That is an issue that will need to be resolved. At the moment we have a couple of our train operators who are seeking safety certificates for France, and once they get that they will be able to run their own services through France. In the meantime, what happens is that EWS uses SNCF as their operator for their existing services, and there is no reason why other customers could not do that if that is what they wished to do.

Q414 ***Lord Swinfen:*** Do you think the operators you keep mentioning will be successful in getting a path that will take them all the way through France in one go without stopping, and being held up for either hours or indeed days at a time?
Ms Barnes: That is the principle that RNE is working to. As I was saying earlier, freight traffic in Europe has reduced in recent years, and that is largely seen as a consequence of difficult border issues, hand-over issues, and the fact that customers are not able to get their services through in a timely and efficient manner. That is what the group of infrastructure managers, of which RFF, which is part of SNCF, is a member, is doing. They have committed to working with us on this along with the rest of the European Community.
Lord Swinfen: I was not thinking so much of crossing borders but of getting from one end of France to the other. We have had evidence that drivers will not go the whole way in many instances and will only go about 200 kilometres at a time, and then you need to change drivers, and sometimes even trains. I am wondering how that would work.

Q415 ***Lord Geddes:*** How many significant rail freight countries are not members of RNE?
Ms Barnes: I can provide you with the information and I will list the membership. If you look at the map of Europe, most of the European Union countries that you would recognise as members of the Community are members, and we have been looking at Turkey and other eastern European countries, which have expressed an interest in being members. It is quite comprehensive.

Q416 ***Lord Geddes:*** I am really inviting you, with my next supplementary quetion, to give the answer you want to give, but I will try and phrase it to stop you! In years past I was also, with a completely different hat on, a member of a pan-European association with enormously high hopes and wonderful dreams of doing all sorts of things. How realistic is RNE? Do you really believe it will achieve its goals?
Ms Barnes: Yes, I do, because the members that are most anxious to make it work are Germany, Italy and France. I therefore believe it has the potential to do what it wants to do.

Q417 ***Lord Geddes:*** I tried to push you earlier on time frames, and I will push you on the time frame of this. When do you think there will be this wonderful accord?

Ms Barnes: I think that in the European Union it takes people a long time to agree to anything to the nth degree. The indications are good at the moment. We are talking quite proactively about how we move more traffic by rail across the continent. As far as traffic into Britain is concerned, it is a low priority for them at the moment because they see there are bigger opportunities elsewhere, but we are involved and we are part of the process, and will continue to be so.

Q418 ***Lord Geddes:*** Can we just hold on to the continent for the moment. We have heard what you said about the UK, and you have given a wonderfully diplomatic reply but I am going to go on pushing you—will it be 10 years, five years, three years?
Ms Barnes: We have the ability now, through the one-stop shop process, to make this work better. It will be as quick as members want it to be. I think you will find there is pressure on the continent for increasing the volume of freight traffic. RNE does not just look at freight to passenger, so it is all about harmonisation of approach across borders. You will find that given European legislation there is opportunity to make it work.

Q419 ***Lord Geddes:*** You are ducking and weaving beautifully but you still have not answered my question.
Ms Barnes: I cannot give you an answer because—

Q420 ***Lord Geddes:*** What do you think personally?
Ms Barnes: It would be difficult to say. I do not really know. With anything European it will take its time and it will gradually grow one step at a time.
Lord Geddes: I will not try again!

Q421 ***Chairman:*** You made the very interesting observation that to those core countries, as they might describe themselves, UK international freight is quite a marginal activity and will not be high on their priorities.
Ms Barnes: It is not at the moment. I think it would be if they found flows of traffic that they wanted to move or for which they thought there was a market. That is part of the discussion we have.

Q422 ***Baroness Cohen of Pimlico:*** I am going to ask a question which relates to evidence that came in rather late. I am sure you are familiar with The Rail Freight Group, with whom Kelvin Hopkins MP is associated, the people who are pushing for a rail freight route.
Ms Barnes: Yes.

Q423 ***Baroness Cohen of Pimlico:*** Fundamentally it is about building new bits of railway here and there, and you would get a freight route. We have received quite a lot of evidence to this Committee about the real difficulty of combining freight and passenger traffic; and *prime facie* the idea of a new rail freight route sounds not unreasonable, or reasonably sensible. It is less sensible in terms of your statement that continental operators are not very interested in UK routes; but is this familiar to you? Are you thinking in terms of new routes for freight?
Mr Plummer: Certainly any new routes require very substantial funding and it would therefore be important for the Government to fund that. It is unlikely that freight operators themselves would fund that, but Government funding would be required, and that would be the first part of a discussion.

Q424 ***Baroness Cohen of Pimlico:*** I wonder if that is the answer, but is it not something you have been discussing?
Mr Plummer: We have certainly been discussing it, and will discuss with anybody who wants to develop a network how to help them facilitate that; but ultimately we are not funded to do it. If that funding has to come from Government, then they would need to make that decision.

Q425 ***Lord St. John of Bletso:*** Would that be a PPP?
Mr Plummer: It could be.
Baroness Cohen of Pimlico: That is not what they are suggesting. This one seems to be clear, that you need a good deal of Government money.

Q426 ***Lord Shutt of Greetland:*** Is there anybody in your organisation that has a hold on this and is running to Government, saying, "this would be worth doing; for goodness sake, let us get it done"? Is anybody in your organisation enthused by it?
Mr Plummer: Is this the—

Q427 ***Chairman:*** As it is evidence to the Committee, we will supply you with a copy. Would you let us know if this has been looked at or not?
Mr Plummer: We will do that.
Chairman: We are not asking you to go away and do something *de novo*. It would be helpful to us to know if you have been looking at it.

Q428 ***Lord Geddes:*** Having had this long and very interesting discussion on RNE and fond hopes for harmonisation, which I hope are right, to what extent will safety certification and vehicle acceptance be bound up into those negotiations? Will they be quite separate, and is there something the Commission ought to be doing, quite apart from the track operators and the infrastructure operators working on their own?

The Committee suspended from 5.14 pm to 5.22 pm for a Division in the House

Mr Plummer: There are things that the Commission is already doing in terms of separation of infrastructure manager and railway undertakings, the opening up of the market for freight and passenger operators. It will take some time—and I would find it very difficult to say how long—to see that really flow through in specific changes in most of the main countries. It is difficult to see what further significant change they would propose to make a big difference.

Q429 ***Lord Geddes:*** It is not so much the change that I was pushing for as the powers of persuasion.
Mr Plummer: The Commission, certainly in our experience, uses its powers of persuasion extensively. I am sure it is using them on the other countries as well, but it is taking time to see the changes that everyone would like.

Q430 ***Lord Geddes:*** The evidence we have received so far is that there are very real issues. Access is being effectively prevented, or ease of access is effectively being prevented—and one has to come right out in the open—most particularly by the French. Does this accord with what you have been told?
Mr Plummer: In this country we have a strong regime of independent economic regulation, which effectively polices the access arrangements. That arrangement in other countries is, at best, fledgling, and as that evolves it should help to see more effective persuasion and influence to provide effective open access arrangements.

Q431 ***Chairman:*** In your written evidence you say that freight operators will find the maintenance of a robust safety case becoming increasingly complicated and expensive as operations extend into additional markets with different safety cases and different standards. You say that the process of vehicle acceptance similarly needs to be simplified. Those are problems not in the UK you are saying, but in the rest of Europe; and you would optimistically say that RNE would help overcome those.
Mr Plummer: We have very open access in this country, and that is pretty well recognised by the Commission. In terms of the problems freight operators see in Europe, it is more a matter for them to comment on rather than us.

Q432 ***Chairman:*** You have commented on it in your evidence; I was quoting your evidence.
Mr Plummer: I recognise that. I am not denying that. I think the details of that and how important those factors are you need to explore with them.

Q433 ***Chairman:*** But they do not apply to this country. There are no problems for the operators as far as safety issues, costs and complications or about vehicle acceptance.
Ms Barnes: There are issues about vehicle acceptance of vehicles that are currently used quite widely on the continent when they come over to this country because our infrastructure is configured slightly differently to that in Europe. For example, you may have a wagon in Europe that has a different type of suspension to that which we would normally see over here, and it causes complications occasionally. That is why we need to think about how to simplify wagon acceptance processes.

Q434 ***Chairman:*** In regard to the Channel Tunnel, you said it has a stand-alone safety case that restricts types of rolling stock permitted to use the Tunnel. That was one of the problems that you mentioned. Can you run us briefly through the stand-alone safety case? How does that differ from the safety standards you apply?
Mr Plummer: We would rather send you something on that, if you do not mind.
Chairman: Yes. The devil, we have discovered in this inquiry, is very often in the detail. It is precisely the detail that makes it difficult for freight operators, as you said in your evidence. It would be very helpful if you could do that.
Lord St. John of Bletso: When you are doing that, could you say in regard to the rolling stock permitted to use the Tunnel, with the advances in technology whether are there likely to be greater varieties of rolling stock using it going forward? It seems very restrictive, and we are looking to try and extend the use of rail freight through the Tunnel.

Q435 ***Lord Swinfen:*** Concerns have been expressed to us that interoperability provisions could raise the cost to British operators more than they would benefit. What needs to be done to avoid this happening?
Ms Barnes: If it is a matter of cost to the train or freight operating companies, it is difficult for me to comment on that. Obviously, if you end up with different standards applying, then complexity usually brings additional costs, but I do not have the detail to respond on that.

Q436 ***Lord Swinfen:*** You say in your written evidence that you think the high costs are preventing some technical standards for interoperability—they prevent it from being economically viable to do so. Would you like to enlarge on that, because you have already given it in your evidence? Why have you said that?

Mr Plummer: I do not have it in front of me at the moment, but there is a general point behind the question. One of the things we are concerned about in relation to obligations being imposed on freight operators in this country, is that access in Europe is not as open as it is here. Freight here is operating in a very competitive market. It would not be appropriate to impose regulations from Europe in general on to the freight market, which ignores that competitiveness here. It is replacing the need for those regulations. In terms of the specific point, I would be happy to send you a more detailed response backing up the comment in our evidence.

Q437 ***Chairman:*** I have one last question, I am afraid on the Channel Tunnel because it is such an issue. What part do you play, in Network Rail, in any discussions with the Channel Tunnel incumbent and through RNE to seek to address problems of rail freight going through the Channel Tunnel and linking the UK and Europe, and overcoming problems of taking business forward?
Ms Barnes: We have regular meetings with Eurotunnel about their aspirations to increase freight through the Tunnel. At one stage they were considering becoming an operator on their own account. We have had a number of discussions with them and other operators about possibilities of increasing traffic through the Tunnel; we would wish to see that because we have paths which are currently reserved, waiting for this traffic to turn up, and I would like to see that happen. Anything that we can do to facilitate or help we will do. If it is a matter of putting in place track access agreements between ourselves and operators, or between ourselves and Eurotunnel. We are, again, more than willing to help. We regularly have discussions on that basis.

Q438 ***Chairman:*** Network Rail is confident that if the Channel Tunnel link itself could be resolved and the problems of charges, numbers and kinds of vehicles that go through and the safety issues on this side of the Channel Tunnel, we could and would easily deal with quite a lot more international rail freight traffic.
Ms Barnes: Providing issues of gauge were resolved, yes. If it is not gauge-dependent, the answer is "yes".

Q439 ***Lord Geddes:*** Is it so that operators on the East Coast Mainline are within the foreseeable future going to revert—my word—from electric to diesel locomotives? If that is so, would that help international rail freight?
Ms Barnes: Do you mean freight operators?

Q440 ***Lord Geddes:*** Freight operators and passenger operators.
Mr Plummer: As far as I am aware, there are no plans in relation to passenger operators, and I am not aware of anything in relation to freight either.
Ms Barnes: No.

Q441 ***Lord Geddes:*** I heard tell that the electrification was not quite what it might be.
Mr Plummer: There are certainly issues about electrification and its renewal over a long period of time, because substantial money is needed to renew those assets. Clearly, at some point it would be an issue as to whether it would be more appropriate to change to diesel locomotives, but that is not a major issue at the moment as far as I am aware.
Chairman: Thank you for your patience and your replies when you have had the information to give those replies, and thank you for your generous offer on a number of occasions to follow up with some supplementary evidence to us. On behalf of the Sub-Committee, thank you again.

Supplementary evidence from Network Rail

In relation to the additional information that the Committee requested, I am pleased to enclose a map of Rail Net Europe's territory and the Trans-European Network of routes. These are available from RNE at: Joint Office, RailNetEurope, Annagasse 12/5, A-1010 Wien, Austria; or from http://www. railneteurope.com/.

Please note that the RailNetEurope list of Members and respective States that the Committee requested is as follows:

BS	Banedanmark	Denmark
BV	Banverket	Sweden
BLS	BLS Lötschbergbahn AG	Switzerland
CD	Ceske Drahy	Czech Republic
CFL	Société Nationale des Chemins de fer Luxembourgeois	Luxembourg

CH/OSE	Chemins de Fer Hélleniques/Hellenic Railways	Greece
CFR	Companie Nationale des Chemins de fer Roumain	Romania
DB	DB Netz AG	Germany
EUROTUNNEL	EUROTUNNEL	France/England
JBV	Jernbaneverket	Norway
ÖBB	Österreichische Bundesbahnen	Austria
RoeEE	Raab—Oedenburg—Ebenfurther Eisenbahn AG	Austria/Hungary
GySEV	Györ-Sopron-Ebenfurti Vasut-Rt	Austria/Hungary
PKP-PLK	Polskie Koleje Panstwowe	Poland
ProRail	ProRail	Netherlands
Network Rail	Network Rail	Great Britain
RHK	Ratahallintokeskus	Finland
RENFE	Red Nacional de los Ferrocarriles Espanoles	Spain
REFER	Rede Ferroviária Nacional, EP	Portugal
RFF	Réseau Ferré de France	France
RFI	Rete Ferroviaria Italiana	Italy
SCANDLINES	Scandlines	Germany/Sweden
SBB	Schweizerische Bundesbahnen	Switzerland
CFF	Chemins de fer fédéraux suisses	Switzerland
FFS	Ferrovie federali svizzere—Infrastructure Division	Switzerland
SNCB	Société Nationale des Chemins de fer Belges	Belgium
NMBS	Nationale Maatschappij der Nationale Spoorwegen	Belgium
SNCF	Société Nationale des Chemins de fer Français	France
SZ	Slovenske Zeleznice	Slovenia
VPE	Vasúti Pályakapacitás-elosztó Kft	Hungary
ZSR	Zeleznice Slovenskej Republiky	Slovakia

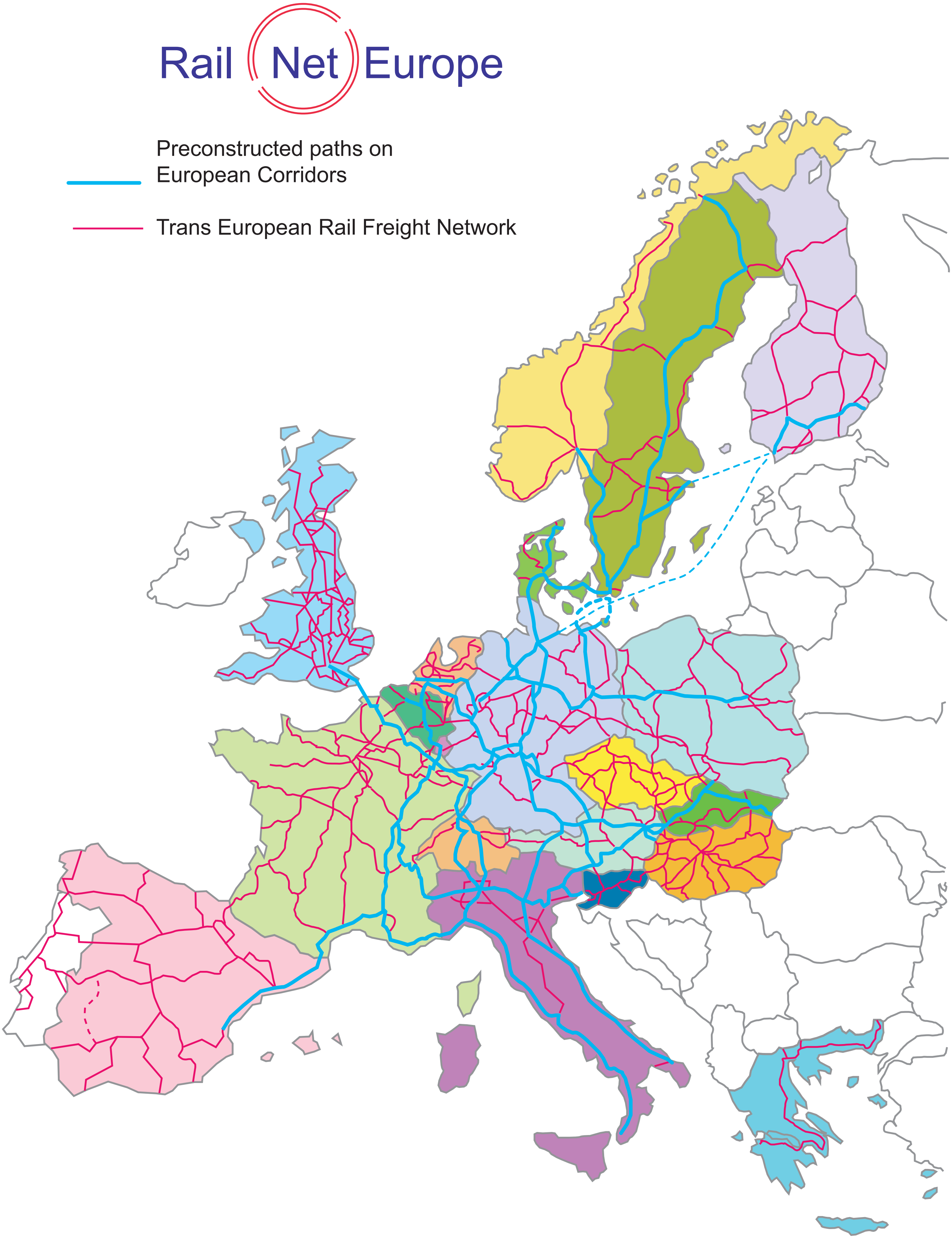
In regard to an example of where Technical Standards for Interoperability (TSIs) could reduce costs arising from the complexities of freight companies working across a number of borders, we would suggest two standards for consideration: The Telematics TSI details the type of performance reporting once the train is running that is required between infrastructure managers and railway undertakings, and the Rolling Stock TSI sets the requirements for rolling stock running in all EU countries.

With regard to Rail freight movement and punctuality; from 1996 to 2004 UK rail freight has grown by a yearly average of 5.0 per cent and by a total of 41 per cent from 19.4 billion gross tonne miles in 1995–96 to 27.2 billion gross tonne miles in 2003–04. Rail's market share has increased from 6 per cent to 11 per cent. Delay minutes for major passenger and freight operators (as reported in the annual return) is as follows: passenger 11,394,367 and freight 2,279,360 network rail delay minutes.

Further to the request for an explanation of the stand-alone safety case for the Channel Tunnel, please note that the Channel Tunnel Safety Case safety case has been developed based upon the specification of the service. The Channel Tunnel Rail Link is unique in the UK, in that it is a high speed, cab signalled, fully "Automatic Train Protected" facility, and therefore requires a different maintenance and operating regime with different standards. The higher speeds mandate that personnel are not allowed near the line and that more inspections are required to maintain the facility. It was agreed that as much of the system was French—French standards would be used; these have, it is worth noting, been proven in France over a 20 year period.

Finally, the Committee asked us whether we had reviewed the proposal for a rail freight route submitted as written evidence by Mr Kelvin Hopkins MP, of the Rail Freight Group. This is a proposal for a significant enhancement to the network and therefore it is currently a matter for the Strategic Rail Authority, and going forward would be a strategic matter that as such would transfer to the Government for consideration.

6 December 2004



Written Evidence

Memorandum by Central Railway

Central Railway has developed a proposal for a 400 mile freight railway system in France and England mainly comprising upgraded existing lines and designed to enable lorries and any continental freight train. The Company has secured letters of support from key institutions in the financial markets for the project as a commercial venture and proposed that public subsidy for it be ruled out, in fact made unlawful.

As its project incorporates many ideas from commercial railways in North America and has been developed with help from SNCF, the Company has given some thought to the contrast between the relatively thriving railfreight businesses across the Atlantic and the difficulties experienced by railfreight in the EU. These largely reflect technical and structural deficiencies in European railways which could only be addressed by considerable new investment, which may be beyond the means of Member States given so many other priorities. However if the private sector is to have any significant financial input then the current EU approach to railfreight liberalisation should be reconsidered.

Comparison of the European and North American Railfreight Industries

The North American rail freight industry comprises six large and many smaller vertically integrated freight railway companies. The railways' share of freight in tonne kilometres has been stable at about 40 per cent compared to around 10 per cent in the EU. Some of the difference is attributable to geographical differences but by no means all.

In North America technical standards, in particular structure gauges (ie the amount of room under overhead structures, bridges, tunnels etc and so the maximum dimensions of rolling stock), axle weights and signalling for maximum train lengths, have developed according to the commercial needs of each rail route and the kind of traffic it runs. The main lines, at least, have been continuously upgraded to handle bigger longer trains. America thus possesses several lines capable of operating the core modern freight rail services—lorry trailers on flat wagons (TOFC), double stack containers and very heavy coal and other bulk traffic, in trains a mile or more in length running at up to 70mph. Europe has none. As a result the EU railfreight industry has far fewer opportunities to attract business from logistics firms.

In Europe technical standards are inadequate (the main problem) and incompatible (another significant problem) as they tend to vary by country rather than by route, which makes "interstate" cross-border railfreight business particularly problematic, and little investment has gone into modernising key freight routes. This is a shame because EU railways' best hope should be competing for longer distance traffic between Member States.

American railway companies are basically free, subject to some regulatory oversight, to allocate capacity on their lines to their traffic or trains from other companies subject to negotiated, commercial rates. But each train operator has an incentive to maximise use of his tracks by other companies' trains because he is (usually) the track owner too. Since they are unsubsidised companies also have an incentive to keep their investment focused on meeting customers' needs (eg raising bridges to make sure hauliers' lorries can actually be carried) and improving operating efficiency.

By the way, American railways, like those in the EU, generally face competition from roads which are free at the point of use, so both systems would benefit from the introduction of (economically more rational) road pricing. But this would not help EU railways that much because their technical deficiencies would remain.

Railway Technical Standards in the EU

The growth area in the freight market is finished and intermediate goods travelling between Member States in lorries. In the case of the UK/continent market, traffic has grown on average at around 6 per cent in volume terms annually since the 1980s compared to 1 per cent to 2 per cent for the UK freight market as a whole. In America this kind of traffic is carried by double stack container and lorry trailer on train rail services, but this is not possible in Europe. To carry a lorry, more sensibly just the semi-trailer, on a train needs a structure gauge between 1 and 2 metres higher than prevailing standards in Western Europe. In central Europe things are a little better as structure gauges are higher and some lorries and semi-trailers can be carried in special, operationally less satisfactory, wagons. Only the Channel Tunnel actually has sufficient clearances to handle lorries properly and as a result it has around a 25 per cent market share of the UK-continent road freight market, compared to the through freight train services which of course cannot carry lorries because of structure gauge problems, with a 3 per cent share.

There are no railway lines in Europe upgraded to carry double stack containers, a basic and growing American railfreight business. Few if any have 30 tonne axle weight limits (standard in the States but in Europe maximum weights are in just above 20 tonnes), and signalling systems generally require short (less than half a mile) train lengths. These marketing and operating handicaps are cumulative and together account for much of the EU railways' lower market share, inefficient use of capacity and resources and financial losses.

It doesn't help that European technical standards are not only (commercially) inappropriate but also inconsistent so that for example standard European freight trains cannot enter the UK, but it is only part of the problem. It would be prohibitively expensive and very wasteful to upgrade all or even many lines to, for example, a one size fits all EU structure gauge standard and the risk that the wrong standard would be chosen would be great.

If the objective is to increase EU railways' share of freight markets then a necessary condition is a basic network of freight priority main lines, perhaps no more than one or two in most Member States, with high structure gauges, priority for freight traffic, signalling for long trains and high axle weights.

Central Railway has demonstrated that such a railway would be technically capable of carrying traffic equivalent to the whole UK-continent lorry market and commercially capable of achieving 40 per cent to 50 per cent market shares in this favoured market for rail-favoured because there is no road across the Channel so every haulier must use rail (in the form currently of Eurotunnel's 30 mile lorry shuttle) or ship transport.

EU Liberalisation and Private Investment in Modernised Freight Lines

It would be open to EU Member States to develop freight priority main lines with taxpayer funds—or guarantees which amount to the same thing—and offer modern railfreight products on a subsidised basis. In this scenario the current EU approach to liberalisation would not be particularly damaging or indeed relevant.

However if such lines are ever to be developed it seems likely that much, at least, of the money would have to come from the private sector. In this context the current EU emphasis on separating track and train operation, and on depriving infrastructure owners of the ability to allocate capacity and negotiate commercial access rates freely, would need to be revised at least as applied to proposals with big infrastructure costs.

The core assumptions underlying EU proposals for rail freight liberalisation, and indeed in railway establishment, seem to be as follows:

> "European railways are basically fit for the purpose of developing commercially effective freight products with little investment in infrastructure. The need is therefore for competitive operation and marketing of existing rail freight services."

This prevailing wisdom has been accompanied by continuing decline in railfreight market shares and needs to be questioned. If, as we believe, EU railways are fundamentally not fit for purpose, in commercial freight terms, but require heavy investment in upgrading key routes before they can make much impact then the (dis)incentives facing potential investors in railway infrastructure become of key importance to any successful liberalisation.

Clearly the financial markets will not pay for railway infrastructure investment proposals under an EU regulatory system which prevents the infrastructure owning company from also controlling trains. The trains are the revenue generating element, which the investors will insist are managed and controlled by them. Similarly investors cannot take the risk that regulators grant competing third parties cheap access to the assets built with their money, thus undermining projected revenues.

We would welcome moves by the EU to make special regulatory provision for proposals most of whose costs are investment in rail infrastructure rather than train, allowing investors to develop modern vertically integrated freight railways, for which Eurotunnel offers something of an example, and which can freely dispose of excess capacity to other rail users on commercial terms.

August 2004

Memorandum by Deutsche Bahn AG

1. *What are the current barriers to entry in the international rail freight market?*

1.1 General

Several acts of European legislation will lead to a gradual opening up of the entire European rail freight market. Since 15 March 2003 railway undertakings have access to the "Trans European Rail Freight Network". As of 1 January 2006 the entire international European rail freight market will be opened to competition, including domestic services as of 1 January 2007. Despite the progressive liberalisation, the international rail freight market in Europe today is still characterised by a varying degree of market opening and by a range of national differences in technical and safety related legislation.[1] The diversity of existing national regimes, with often non-transparent procedural rules, can cause considerable difficulties for the development of viable business models for international rail freight services. Granting access rights alone is not sufficient to successfully liberalise the European rail freight market. The following aspects will remain market entry barriers, until the ongoing harmonisation process[2] becomes effective in practice.

1.2 Approval of Rolling Stock

Railway undertakings seeking access to the infrastructure of another Member State need to have their rolling stock approved by the national certification body. The approval prodecure is subject to national law. In practice the approval of rolling stock (homologation) is the most time-consuming and high-cost barrier for new providers of rail transport services. In some countries there are documented and legally codified network statements and open access provisions for freight transport, which cannot be used by external railway undertakings owing to the prolonged, non-transparent and expensive processes for the approval of rolling stock. The level of technical details and prerequisites vary from country to country. In some countries seemingly banal things, such as an outside mirror, or the colour of locomotives, can delay or complicate the approval process. In other countries a locomotive has to have two fully equipped driver positions, as there always have to be two drivers on board. The duration of an approval procedure varies and can stretch up to over 1.5 years in some countries. In addition the range of fees charged for the approval lies between 50.000 Euro and in some cases over 1 million Euro. It should also be mentioned, that in some Member States the national railway undertaking is itself the testing body, or it co-operates closely with the competent national authority.[3]

1.3 Safety Certificates

Railway undertakings seeking access to the infrastructure of another Member State must hold a safety certificate. The certification is subject to national rail safety legislation. The recently adopted Rail Safety Directive 2004/49/EC provides for a transparent, harmonised and non-discriminatory process of issuing the safety certification. It also narrows down the competence of Member States to introduce new national rail safety legislation. Before the Directive becomes practically effective (transposition by 2006), the certification procedure remains subject to varying national rail safety provisions. In the current state, the safety certification procedure leaves room for arbitrary discrimination and disguised restriction of international rail freight. The objective in the long run must be, to create *one* set of European rules for rail safety, uniformly applied in all the Member States and leading to full mutual recognition of safety certificates.

1.4 Certification of Train Drivers

Train drivers must hold a certification for the network, on which the rail service is carried out. The process of issuing the certficate and the standards for vocational training, physical and psychological aptitudes to be met by an applicant, are again fully subject to varying national provisions. A Directive[4] for train driver certification, recently proposed by the European Commission, will harmonise the issuing process and together with the relevant Technical Specification for Interoperability set common standards for the training of train drivers in cross-border rail services as of 2010. In the transition period the certification of train drivers remains a potential market entry barrier.

[1] For further details, see the study "Rail Liberalisation Index 2004" by IBM Business Consulting Services and Prof Christian Kirchner, which is available for download at: http.//www.europa.eu.int/comm/transport/rail/research/studies_en.htm

[2] Directives 2001/12/13/14/16/EC and 2004/49/50/EC and Regulation No 881/2004.

[3] See page 33–35 of the aforesaid IBM-Study.

[4] COM (2004) 142 final.

1.5 Framework Conditions for Intermodal Competition

Finally, the current situation of the international rail freight market cannot be properly appreciated unless its legal framework is seen in context with those of competing transport modes. Firstly, rail's fiercest competitor, road transport, is still not under any obligation for users to incur the costs of their infrastructure utilisation while Directive 2001/14/EC is obliging the Member States to apply the "user pays" principle to rail infrastructure. Secondly, by not making the internalisation of external costs mandatory for all transport infrastructure users, the European transport legislation is depriving the rail mode of the opportunity to benefit from its advantages in term of safety and environmental friendliness.

2. *To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?*

Several Member States failed to notify the transposition of the "First Railway Package" to the European Commission until 15 March 2003. The lack of uniform implementation delays the creation of an integrated European railway market. It has to be underlined though, that the formal implementation alone does not automatically remove market entry barriers. In some Member States the Directives of the "First Railway Package" are not yet formally transposed, but the market for rail freight is nonetheless fully liberalised. New market entrants do not face legal or bureaucratic market entry barriers. On the contrary it can be observed, that other Member States, although having formally transposed European legislation, maintain the national administrative *"status quo"* in the areas outlined above. Apart from formally implementing European legislation, a key factor for removing market entry barriers is the willingness of the national administrative bodies and stakeholders involved, to facilitate transparent, timely, cost-efficient and market-friendly procedures.

To overcome historically grown market entry barriers, originated by different technical standards, different safety philosophies and different political views on liberalisation and competition of rail freight in general, European legislation not only needs to be formally implemented, but first and foremost to be filled with life in practical application.

3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

The new European Railway Agency, which will be fully operational as of 2006, will play a decisive role in the future enforcement of European interoperability and safety provisions. With the Agency, the European Union will not only dispose of a means to further develop Technical Specifications of Interoperability, Common Safety Methods and all the other necessary tools to complete the harmonisation of rail systems, but also of a surveillance body, to ensure and enforce the relevant legislation. It is of the utmost importance, that the work of the Agency, adequately taking into account the expertise of the rail industry, will be supported both by the Member States and the European Union. A well equipped Agency, both financially and in terms of expert staff, can provide the most effective form of ensuring the enforcement of the legislation, which aims at the gradual removal of the market entry barriers outlined above.

Further action by the European Union, in the shape of individual decisions against Member States can and will be necessary, if Member States fail to fulfil either the conditions of European law itself or specific requests of the Agency.

The national regulatory bodies (as introduced by Directive 2001/14/EC) need to be provided with the necessary resources to be more effective in the enforcement of the respective European legislation. In a number of Member States this does not appear to be the case.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

The existing European legal framework, most notably the "First and the Second Railway Package" as well as elements of the recently proposed "Third Railway Package", is sufficient to combine the liberalisation of international rail freight by granting access rights with the need to harmonise the different technical standards. Further purely railway related legislation is not needed at this stage. With regard to the fierce intermodal competition the rail freight market would benefit significantly, if the overall competitive situation of rail freight towards road transport would be improved by creating a level playing field. For this, fair infrastructure charging rules for all transport modes would be an important element.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

With regard to the development of the international rail freight market, the Commission's proposal for a Regulation on compensation in cases of non-compliance with contractual quality requirements for rail freight services[5] is to be seen as a serious threat to the competitiveness of the rail sector. Under this Regulation, the rail freight market would be subject to a number of legal obligations that would lead to considerable extra costs. However, since there are no comparable obligations foreseen for competing transport modes, the Regulation would mean a dangerous setback for rail's initiatives for more competitiveness. Therefore, in the interest of growth of international rail freight, the United Kingdom Government should reject the Commission's proposal.

August 2004

Memorandum by Environmental Freight Services Ltd (EFS)

Introduction

1. EFS is an intermodal Company established in 1998 and operates over 600 containers/swap bodies and flat rack units. The investment in the Company has been £3.5 million to date.

2. EFS trades primarily between the UK and Italy with up to 90 per cent of our traffic utilising the Channel Tunnel. Railheads at Hams Hall (Birmingham) and Daventry are used in the UK.

3. The Company with its curtain-sided swapbody units was very badly affected by the ingress of asylum seekers into our units and the credibility of our service with damage being caused to our customers' cargoes has made life difficult for us.

4. EFS has currently an annual turnover of approx £7 million and in volume terms is the largest intermodal Operator using the Channel Tunnel. We believe that should we cease trading that the main UK/Italy rail service will close down.

1. *What are the current barriers to entry in the international rail freight market?*

1.1 Transporting freight by rail is not, when compared with transportation by road, cost or time effective, for the following reasons:

1.2 The cost of using track, tunnel and wagons is far higher than the use of roads and ferries, as there is more competition in the ferry market, both in routes and operators. The efficiency this provides leads to greater journey time effectiveness.

1.3 Since the demise of Combined Transport Services, there is practically only one aggregator left in the market and the costs are not competitive. Also, in the UK, the infrastructure for operating an intermodal service is not readily available; there are only a number of small terminals that do not allow parking and storage of intermodal bodies, and the operation of the road/rail transport from these depots is limited.

1.4 What is required is a large, dedicated hub/terminal, which will act in the same context as a port; it will assemble freight for onward transmission to all destinations on the continent, using a reciprocal hub such as the facility that has just been constructed using European grant money near Lille, France. It will also have the ability to store swap bodies and intermodal equipment at competitive prices, and could be used by haulage contractors as an operating centre. In addition, the entry of all those who wish to involve themselves in the rail network must be facilitated. The following are the barriers that they have to overcome:

(a) Inflexibility of the European Rail Network compared with the options for road transport.

(b) A long time-scale in establishing a rail service in order to agree rail pathways. A minimum of 12 months has been quoted to EFS (Environmental Freight Services Ltd).

(c) For users such as EFS who rely heavily on the Channel Tunnel, there is the additional burden of the inflexibility of the French Railways and their Trade Unions.

(d) There are considerable cost impediments in the need to hire/purchase rail wagons and to hire rail traction to operate a five times weekly service between the UK and Italy in an uncertain trade environment. Some financial support should be made available for an agreed start up period.

[5] COM (2004) 144 final.

(e) Rail does not have a good reputation for reliability with freight users, and the damage done to customers' cargoes by asylum seekers has created a lack of credibility in rail services coming to the UK. This image must change.

2. *To what extent are these barriers a result of a failure fully to implement existing EU directives in all Member States?*

(a) Not enough funding has been made available in the UK to equip a terminal to act as a hub in the centre of England for the dedicated use of international freight, which would therefore utilise the full potential of the Channel Tunnel.

(b) The failure of the established train operators to embrace and welcome companies to set up in competition is another factor; SNCF are making it difficult for outside companies to set up in competition, and the French Government, who have a financial interest in SNCF, are in breach of the open access rules for the EU. Thus we have not seen any new entrants through the Channel Tunnel.

3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU directives?*

3.1 More encouragement must be provided by the EU to ensure that Member States achieve the undoubted benefits offered by this mode of transport. The opportunities that are open to the Member States—to cut environmental pollution and take from the roads of Europe a large number of heavy freight trucks—are enormous. All governments must be encouraged to work together to extract these benefits on behalf of the community.

3.2 Incentives must be given to encourage more competition for railfreight transport. This must be done by enforcing EU Directives. For example, the industry is actually contracting in the UK, with the aggregator, Combined Transport Ltd going into receivership last year.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

4.1 With the lack of success of introducing further competition into the marketplace it should be made more commercially attractive for new operators to enter, because clearly the existing legislation is largely ineffective.

5. *What action should the United Kingdom government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

5.1 The Government should positively commit itself to the idea and principles of rail transport.

5.2 There can be no doubt that increased transportation of freight by rail would significantly reduce road congestion and carbon dioxide emissions. The commitment should come in the form of positive help for the industry:

(a) The building of a hub in the centre of England to exploit the potential that rail freight has to offer.

(b) In the past rail had an advantage over road by virtue of a 3 tonne weight advantage. This was significant in attracting freight to rail but no longer applies. Measures could be implemented such as tax rebates on fuel for the movement of goods to/from Rail Terminals.

(c) To make rail work, it must be more cost efficient than it currently is. This is illustrated by the fact that when the Channel Tunnel was originally opened, 6 million tonnes of freight was predicted, with a ceiling of 9 million tonnes. However, it peaked at 3 million tonnes, and due to the removal of the weight advantage and the impact of asylum seekers and irregular rail services, it is currently down to 1.7 million tonnes and is predicted to go lower.

(d) The Government should advertise and exploit the environmentally friendly image of rail freight.

August 2004

Memorandum by Eurotunnel

1. This evidence is submitted by Eurotunnel and is written from the perspective of Channel Tunnel railfreight services.

2. We have identified a number of barriers to growth and have taken steps to overcome them. The provision of traction by SNCF has proved to be problematical and so we have obtained a licence and safety certificate to operate our own locomotives with our own drivers in France. The following comments are based on our experiences and knowledge of the market.

3. Eurotunnel has the concession to maintain the Channel Tunnel and associated infrastructure and to operate shuttle trains between the two terminals for the carriage of road vehicles until 2084. In addition to the shuttle operation and under the terms of the Railway Usage Contract (RUC), Eurotunnel is required to allocate up to 50 per cent of the capacity of the Channel Tunnel to passenger trains operated by Eurostar and freight services provided by English, Welsh and Scottish Ltd (EWS) in collaboration with SNCF, the state-owned French train company.

4. As part of the RUC, Eurotunnel is afforded revenue protection by the Minimum Usage Clause (MUC). This guarantees to Eurotunnel a minimum level of revenue when traffic levels achieved by Eurostar and the freight operators, EWS/SNCF are below a certain threshold. The MUC has actually applied since the Tunnel opened in June 1994. However it will cease altogether at the end of November 2006.

5. Furthermore, EWS, who pay no tolls to Eurotunnel at present, will be required to pay these tolls from 1 May 2005. Without compensatory support this requirement is most unlikely to lead to any traffic increases during the period leading to November 2006. It is, therefore, very much in Eurotunnel's interest to try to encourage a very significant increase in the volume of railfreight.

6. After an encouraging start, when services through the Channel Tunnel first commenced in 1994, railfreight volumes have been disappointing. Traffic levels rose to a peak of 3.1 million tonnes in 1998 but dropped almost to extinction in 2000–01 as a consequence of the problems with incursions by illegal immigrants. Business has recovered, reaching 1.8 million tonnes in 2003, but is likely to be no more than around 2 million tonnes this year (with a fairly high proportion of this being bulk traffic such as steel that represents lower toll revenues to Eurotunnel). This represents less than 3 per cent of the cross-Channel unitised freight market. Capacity exists on the UK network between Folkestone and London for 35 freight trains each way per day but currently only around seven are operated each way per day. The Channel Tunnel itself has capacity for significantly more traffic than this.

What are the current barriers to entry in the international rail freight market?

7. The freight train paths on the railway network between the Tunnel and London are allocated to EWS. A new entrant would need to bid for additional paths on this busy network or persuade EWS to relinquish the requisite path/s, if necessary invoking the power of the regulator. This process would be complex and time consuming.

8. Traction through the Tunnel can only be provided by two types of specialised locomotive—those used by Eurotunnel for shuttle services, which are fully committed and class 92 locomotives. The latter are owned by SNCF and EWS (by virtue of the sale of the former British Rail freight services to EWS), with a further seven stored, out of use, by European Passenger Services. Any new operator of cross-Channel services has therefore, to obtain traction from a company that is likely to be a competitor.

9. Long lead times are required to book paths on national networks and obtaining access is time-consuming and costly. Competitors from the road haulage industry simply join the highway network at a time of their choice with no requirement to book paths or to reserve slots to cater for out of course operations.

10. Cargoes are increasingly more bulky and less heavy leading to the use of larger rail wagons and containers. The 9ft 6in high container, for example, is rapidly becoming the norm for both deep-sea and intra-EU movements. Unfortunately, the UK's railway network loading gauge—ie the size of train that can be operated, as dictated by bridges, tunnels and other structures—is significantly more restrictive than that of the railways of mainland Europe. Rather than differentiate traffics destined for the UK or invest in special rolling stock compatible with our network, consignors tend to take the easier option of sending their cargoes by road, where such inconsistencies do not exist. It is important that the enhancement of the two main routes between the Channel Tunnel and London is moved higher on the list of priorities for the Government's rail infrastructure investment programme. It is also vital that freight trains are able to operate into London on the Channel Tunnel Rail Link (CTRL) once this is completed in 2007.

11. The UK Government provides financial support in the form of grants for both capital investment and revenue support to companies involved with railfreight. The Company Neutral Revenue Support grant (CNRS), introduced in April this year, is paid to those who take the revenue risk on the operation of intermodal freight trains. This grant is not available for Channel Tunnel trains. However, the grant is available to support traffic flows via competing ferry services and ports.

12. In France SNCF, the state-owned train operating company, is supported by subsidy provided directly by the government. Such support is not available to new entrants, thereby rather stifling competition, which may explain the marked absence of companies taking advantage of the opportunity to gain access to the French railway network. Other Member States provide aid for existing, state-owned, operators in a variety of ways at are not available to new, privately-owned entrants.

13. Uniformity of access charging mechanisms is only apparent. The revised process operated by RFF, the infrastructure provider in France, is such that it favours large volume train operators (ie SNCF) on key routes where competition is likely and discriminates against the interests of potential new service providers.

Interoperability

14. I have already touched on the question of gauge but there are other problems that inhibit the growth of international railfreight services. There is no standard international signalling system so locomotives to be used on international journeys have to be compatible with more than one type and drivers need to be familiar with the systems used in different countries. There are several differing electrical supply systems resulting in the need to change locomotives at borders or to construct expensive and complex multi-voltage machines. Even small things like documentation and the type of tail lamps used have yet to be standardised. Work is proceeding on achieving a much greater degree of interoperability but it is painfully slow.

15. The certification of locomotives is an area that needs to be addressed. The class 66 diesel locomotive, manufactured by General Motors in the USA, is a reliable, go anywhere, useful piece of equipment operated very successfully in the UK, Belgium, Sweden, Holland and Germany. However, the certification authority in France—SNCF—deems it to be inappropriate for operation there so we have been forced to order expensive, multi-voltage electric locomotives for our proposed freight train service through France. It is worth noting that we decided to choose locomotives built by the French company Alsthom because it was considered that certification would be easier since SNCF have the same machines and would take the lead on the licensing process for France and Germany.

Terminals

16. Where is an increasing shortage of rail-served terminal capacity in the UK and this is especially acute in London and the south east where between a third and a half of all imports are consumed. There is little point in increasing the volume of freight moved by rail if it is not possible to load or unload it efficiently and at a reasonable cost. There are various proposals for new terminals backed by developers but the planning process is a barrier to progress. The need for the capacity is recognised by all parties concerned, including Government, but the process is very slow and incurs significant cost for the applicant. It would be of great assistance if the Government were to support, actively, proposed developments that would facilitate modal shift and to take steps to speed the planning process up without bypassing democratic rights.

17. The complexity and cost of entering the railfreight market are very high, particularly when compared with the simple procedures involved in establishing road haulage businesses. One needs to have a significant sum of spare cash and a great deal of time and patience if contemplating entry to the railfreight industry.

18. Road haulage operators on international (in general long-distance primary distribution operations) operate on very slim margins, as low as two per cent or less. It is generally acknowledged that there is a degree of illegal operation/disregard of drivers' hours regulations and so on. Rail, with high fixed costs and the requirement to adhere strictly to regulations, has great difficulty in competing with such operators.

To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?

19. There would certainly seem to be a degree of feet dragging when it comes to implementation. Based on our experience, obtaining a licence to operate in France under open access rules has not been an easy process. Some Member States seem to have paid lip service to the requirement to split infrastructure from operations as fully as they should. New entrants are therefore required to negotiate access, shunting, breakdown rescue facilities and energy availability with their competitors.

20. There is no common Safety Certificate, each country having a different approach. A train making a comparatively short journey from southern Belgium to the south east of England, for example, would require three separate certificates, all different. The road haulage competitor, on the other hand has one operating licence. In France the "judge and jury" overseeing the grant of such certificates is SNCF whose objectivity could be questioned. Why not have a common framework document granted by an independent body?

Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?

21. It would appear, from our experience, that pressure needs to be brought to bear by the Commission on to Member States in order to speed up the enforcement of Directives. Powers are available but are not fully used.

Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?

22. There is sufficient legislation in place, in the form for example, of the three Directives in the first railway package: the primary aim now must be to accelerate the rate of implementation.

What action should the UK Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international railfreight as a result of this policy?

23. In general the points highlighted above do not apply in the UK. The process of obtaining access to the network for newcomers is certainly complex and fairly expensive but not insurmountable—as witnessed by the fact that there are currently four thriving freight operating companies with two more likely to join the industry soon. Furthermore, the primary railfreight operator in the UK, a privately-owned undertaking, is not able to abuse their position. The real barrier is in continental Europe. France is a particular problem, exacerbated by its key position as a transit state for all Channel Tunnel traffic and much port-related cargo. The United Kingdom Government should use its powers and influence to persuade the EU to take appropriate steps to remove the many barriers to development. A significant proportion of the UK's modal shift aspirations could be achieved by the greater use of rail for traffic between the UK and mainland Europe: it is thus very much in the UK's interest that restrictive practices should be removed as soon as possible.

27 August 2004

Memorandum by GB Railfreight Ltd

Introduction to GB Railfreight

1. GB Railfreight (GBRf) was formed in 2000 as a wholly owned subsidiary of GB Railways, which owned the franchise Anglia Railways and an open access passenger operator, Hull Trains. GBRf was the first third party operator to be formed post privatisation and received no public funding at its inception. From the first it was planned as a commercial enterprise and has operated in this way, with a minimal amount of track access grants for specific intermodal flows, ever since. Now in its fourth year of operations, it continues to grow on a year by year basis and has been profitable from the beginning.

2. In 2003, GB Railways was purchased by First Group, one of the UK's largest operators of public transport. The new Greater Anglia franchise (previously managed by GB Railways) was won by National Express, but Hull Trains and GB Railfreight continue to operate within the First Rail Division, alongside sister passenger franchises such as First Great Western, Trans-Pennine Express, First North Western, Hull Trains and now Scotrail.

3. Since its inception, GB Railfreight has shown steady growth, concentrating predominantly on trainload business on key UK routes. Our prime focus has been on delivering high levels of customer service at competitive prices—something at which we believe we have been successful. This success has enabled us to continue to develop the business from a standing start in 2000, to a business turning over approximately £20 million this year.

4. The open access regime that came with UK rail privatisation was absolutely vital in enabling our company to enter the rail freight market and we believe that as a direct result of increased competition, customer service from all rail freight operators has improved significantly and prices to users have reduced. Whatever problems the railways in the UK have had, rail freight has continued to grow and to offer its customers a real alternative to road transport.

5. At an early stage of GBRf's development it was believed that a major opportunity existed to bring competition into the market for international services and considerable effort was put, at that time, into trying to develop a service. However this did not come to fruition and efforts to break into that market were abandoned.

Liberalisation

6. In spite of the efforts that have been made by the Commission to liberalise networks, it has taken almost a decade for some Member States to set out a framework for open access. In particular, France, our only adjacent international network, has been particularly tardy and it has been difficult to justify spending any time in developing international services faced with a lack of clarity of view from the other side of the Channel. Now that RFF (French infrastructure manager) has published its Network Statement its formal position is at least clearer in principle. This delay has certainly contributed to concerns that open access operators may not be welcome on the French network and that there may be considerable obstacles put in their way.

Barriers to Entry

7. From our perspective, the international freight market remains an interesting one in principle, however there are a considerable number of barriers to entry:

8. *Channel Tunnel charges*

There are two main aspects to the Channel Tunnel charges:

8.1 The actual level of charges to a new user which are higher than comparative ferry charges, making through rail uncompetitive with road and ferry.

8.2 The current subsidy that EWS has received through its agreement with Government at privatisation, and which has meant that Channel Tunnel access charges have been paid by British Railways Board since the privatisation of Railfreight Distribution. No such arrangement exists for other operators and therefore renders them at a competitive disadvantage with EWS.

9. *Technical capabilities*

9.1 Locomotives:

GBRf's existing fleet does not have type approval in France and Italy and seeking such approval would be costly and has no guarantee of success. In other countries where the Class 66 is approved, GBRf's locomotives would require modification to enable operations in mainland Europe. This would add cost and require additional approval processes in each country.

An alternative approach would be the purchase of new locomotives for international use, however, as we would be in competition with railway undertakings which are able to procure locomotives with public sector finance, we would be commercially disadvantaged.

9.2 Wagons:

These are less of a problem for us as a relatively large fleet already exists for use for through Tunnel services and is generally available for hire.

10. *Safety regimes*

10.1 These still vary from country to country and will therefore require additional submissions for safety approval to the relevant bodies in each country.

11. *Access charges*

11.1 The charging regimes vary from country to country and it is difficult to establish whether they are equitable and competitive in an open access regime.

12. *Access to sidings, marshalling yards and terminals*

12.1 In many cases these are "owned" by the incumbent national operator which may restrict access to new entrants.

13. *Competition*

13.1 In many Member States the existing national operator remains in place as the incumbent. In almost all cases, these operators continue to receive subsidy from the taxpayer and can make investment decisions without the need to produce a robust business case. This could restrict competition and render open access ineffective.

14. *Performance and service levels*

14.1 UK rail freight customers have come to expect higher levels of customer service since open access has matured in this country. This has been brought about in part by the introduction of competition but also by the introduction of performance regimes in track access contracts. Few infrastructure managers other than Network Rail are willing to offer such regimes at present, making it difficult to guarantee transit times and service levels.

Working in Partnership—Mitigating the Barriers?

15. A variation on true open access is that of partnership working where a number of private operators work together to provide rail haulage along a line of route. On this model it is likely that each haulier would operate nationally, although in some cases a haulier might operate through two countries. In principle this model is no different from the classic model operated by the State Railways, however, the hope is that new entrants will be more customer focused and able to provide better service levels than those experienced in the past. In this model however, the various partners would still experience the barriers to entry described above, although perhaps to a lesser extent for each party as risks incurred would be confined to their area of operation.

Commercial Viability and Investment

16. Each of these barriers is significant and would require substantial time and money to progress to a point where open access operations could be commenced. The distances involved in international services are significant and should lend themselves to cost-effective and competitive rail freight services, nevertheless, there is no evidence to date which demonstrates that such services are an economic proposition for a private haulier such as GBRf. Given such uncertainty, the investment necessary to break into this market and overcome the hurdles described above, is probably better spent in continuing to develop services in the UK domestic market.

A Competitive Market?

17. Furthermore, even if we were convinced of the economic viability of proposed international services, we would be concerned about the competitive position of the existing national operators which continue to be publicly funded and which would therefore be in a position to price down the market in order to maintain the traffic.

18. Privatisation in the UK, while not being an unqualified success, nevertheless liberated the market for rail freight. All UK rail freight operators are now real commercial endeavours with shareholders who require a certain rate of return. The results of this open market can clearly be seen and has resulted in modal shift brought about by more competitive pricing and improved service levels across all operators.

19. In mainland Europe, however, although some private operators have emerged during the last decade, very few of them are genuine commercial third party hauliers. Several are partially owned by local or regional authorities, some are owned by a group of private companies who have come together to form what is effectively a shared in-house haulier. With the incumbent state railway still in place (unlike the UK post privatisation) it is likely to remain difficult for the small private operators to grow.

Implementation of EU Directives and the Need for New Legislation

20. The key, therefore, to the improvement of rail freight services is the introduction of real commercial competition by open access. We believe that the existing EU Directives are already in place to achieve this, but that they are enforced to a greater or lesser extent in different Member States. Without the will of Member States to implement true liberalisation, the markets will not open up and true competition will never exist.

21. Although change is proving difficult, it is important that the EU resists the temptation to introduce measures to try to improve the position in the short-term. The proposal for a regulation for mandatory freight quality contracts in the Third Railway Package is precisely that—a short-term attempt to resolve a major issue which would be better dealt with by implementing the existing legislation.

22. In many cases, access to freight specific infrastructure continues to be controlled by the incumbent railway undertaking (see 12.1 above). We believe that legislation should be introduced to regulate access to such facilities.

Actions for the UK Government

23. The UK Government, therefore, should:

- continue to press for enforcement of the First and Second Railway Package whilst at the same time addressing the issue of Channel Tunnel charges; and
- lobby for the regulation of access to freight specific infrastructure.

Summary

24. GB Railfreight and its parent company First Group continue to view the international rail freight market as an important commercial opportunity, however we remain to be convinced that, in the current situation where true liberalisation has not yet taken place in many Member States and in the face of significant barriers to entry, it is the best place to focus our investment and management effort.

25. We do not believe that further legislation is required to enable open access, with the exception of the regulation of access to freight specific infrastructure, but that renewed action to ensure enforcement of the existing Directives should be undertaken. If that were the case there would be no need for further legislation, which in any event is likely to become over-prescriptive and simply paper over the cracks rather than get to the root of the problem.

26. In any agreement with Eurotunnel, the UK Government should ensure that rail freight charges are competitive with those of Eurotunnel's freight shuttle services and ferry charges and that they are available on an equal basis to all rail freight operators.

GB Railfreight

31 August 2004

Memorandum by Kelvin Hopkins MP, The Rail Freight Group

Introduction

1. We are grateful for this opportunity to present our scheme to your Committee for consideration. We represent a group which has for some months been seeking to promote what we currently call The Rail Freight Route, a dedicated freight rail line linking the major industrial areas of Britain with the Channel Tunnel with gauge capacity to permit the transportation of full-scale roll-on roll-off road haulage trailers between terminals in the industrial centres of Britain and the continent of Europe. A more detailed description of the scheme accompanies this paper in the form of a presentation (*not printed*).

2. We have looked at the Terms of Reference of your inquiry and our submission relates primarily to the last specific question in your Call For Evidence. Rail freight is very much more substantial on the continent of Europe than in Britain and growing. New large guage rail freight routes are being constructed to the east and south of Europe and it will not be long before these routes are all easily accessible from the continental end of the Channel Tunnel. Our Rail Freight Route is intended to provide vital links to the British end of the Tunnel.

3. This will open up the prospect of direct dedicated rail freight services right through from Scotland to the industrial heart of Germany, France and Italy and on into eastern Europe. I believe that if our scheme, or one very like it, is not built Britain will be severely disadvantaged economically as a peripheral if still major component of the European economy.

Who We Are

4. The three of us represent a larger group of people drawn from the railway and freight industries. Tim Brown is a railway engineer of over 30 years experience. Ken Russell with his father John Russell runs Russell Transport, Scotland's largest freight haulage company, with several hundred road trailers and much rail borne freight traffic. Kelvin Hopkins is the Labour Member of Parliament for Luton North with a long-standing interest in railways in general and rail freight in particular. He was at one time a TUC and UNISON policy researcher covering transport.

Comparisons with Central Railway

5. The Rail Freight Route proposal has similarities with the Central Railway scheme but also has substantial differences in a number of respects. The Rail Freight Route would be constructed on a combination of old railway track bed, unused or under-utilised rail routes and alongside other existing rail routes. It would require the construction of only a minimal amount of new railway route and would be substantially cheaper than the proposal by Central Railway. Central Railway's proposal, admirable in many ways, was sadly rejected by the Government earlier this year. Our scheme would not only be much cheaper but would also be practicable and easily built, with phased construction beginning with a terminal on the Thames Estuary.

Phased Construction

6. The stages of construction would be broadly as follows. The first phase would be the construction of a terminal on the north side of the Thames Estuary linked directly into the new Channel Tunnel Rail Link (CTRL) route to the Channel Tunnel. This would be simple and inexpensive and mean that road haulage trailers could be carried from there through the Channel Tunnel very soon after the opening of CTRL.

7. The next phase would be a link across north London using a very precise route already identified, maximising use of existing track bed and old routes and requiring only one relatively short linking section at a particular point. A second terminal would be located to the north west of London, adjacent to, or within easy reach of several motorways.

8. The line would then make use of the old Great Central route travelling northwards to terminals in the Midlands. The route would then proceed further north to another terminal in south Yorkshire, pass through the Woodhead Tunnel to a south Lancashire terminal adjacent to motorways, and finally reach northwards making again use of older track routes including the Settle-Carlisle line right through to Glasgow.

Thames Crossing

9. A final link in the route would be a new Thames Estuary crossing which would be necessary to cope with the increase volume of traffic as each terminal travelling north became operational.

Domestic Freight Lines

10. The Scheme would provide for domestic freight traffic between the terminals in Britain, as well as direct services right through to Europe, linking up with the expanding rail freight network on the Continent. Other branches, to Wales and the west, to the north-east etc could also be added to the spinal route as required.

Link with Europe

11. The Scheme would provide guaranteed and reliable delivery of road freight trailers (as well as containers) between the major centres of economic activity in Britain and the continent, and contribute substantially to reducing the disadvantages of Britain's peripherality to the core European economy. It would of course take substantial volumes of freight traffic off Britain's roads with very considerable environmental benefits.

A Carefully Planned Route

12. Our engineering colleagues have already identified the precise route and we believe there are no significant technical difficulties in construction. A major difference with the Central Railway route is that it would avoid the need to construct substantial lengths of new route in the south-east. Central Railway proposed a western circular route to get round London which would have been expensive and posed significant political difficulties.

Other Presentations

13. In July we hosted a presentation at the House of Commons to a range of senior representatives from the freight and railways industries. The scheme was generally praised for its conception but there was a general view that it could only go ahead with the backing and financial involvement of Government.

14. We have had a number of other discussions about our scheme including meetings with freight representatives from Eurotunnel and with one of the major banks and its ROSCO (Rail Operating Stock Company) subsidiary. Most recently we have sought a meeting with the Mayor of London, following the recent publication of his report on rail freight in London.

15. We remain convinced that our scheme is practicable, financially viable, and above all would provide essential links between Britain's major economic centres and the European economy. Its environmental benefits will also be obvious.

Channel Tunnel and CTRL

16. We have emphasised that our scheme would transform the economics of the Channel Tunnel which has been in almost continuous financial difficulty. CTRL too is unlikely to be financially viable without substantially increased traffic. Putting large volumes of freight traffic onto CTRL at an early stage and utilising spare capacity, especially at night, would also contribute greatly towards CTRL's economic viability.

Conclusion

17. We submit our scheme to you as a contribution to your own debate on rail freight. We would be especially pleased if a positive reference to our proposals could be made in your final report. We are convinced that our scheme is right for Britain and right for Europe and an opportunity which the country cannot afford to miss. We are not especially concerned whether the scheme is built by the private or public sectors, or a combination of the two. We believe, however, that it should be built and the support of Your Lordships' Committee would be a very significant and important step in the necessary political process to seeing the Rail Freight Route become a reality.

Kelvin Hopkins MP
Tim Brown
Ken Russell

November 2004

Memorandum by Kühne and Nagel Management AG

1. Rail Freight Transport in Europe

- Insufficient political framework conditions for building a competitive European rail freight transport system;
- lack of rail-specific regulations for the liberalised European rail freight transport;
- competitive disadvantages due to unequal route cost burdens between the different modes of transport to the detriment of rail are being dismantled insufficiently and too slowly;
- no sufficient allocation of the environmental impact cost burden to the modes of transport that cause them;
- no transparent cost distribution between freight and passenger transport for the rail infrastructure; and
- competitive disadvantages through technical, technological and commercial boundaries on the EU single market.

Conclusion

The harmonisation of the competitive conditions for the European land modes of transport and the development of internationally valid framework conditions for European rail freight transport have to become priority tasks for EU politics.

2. Rail Infrastructure

- Higher speeds and integration of passenger transport cycles reduce the availability of the main lines for freight transport. Separate freight lines are usually not available.

  The possible line loads (axle loads) often do not suffice for an economic capacity use of the railcars.
- Freely accessible transhipment equipment and facilities or haulage terminals with sidings are more or less non-existent due to the insufficient connecting services of the rail. Thus, there is a severely limited range of offers for the rail mode of transport and individual railcars transport.

— In intermodal transport, an acceleration of the transhipment has to be achieved, above all, requiring a sufficient number of transhipment terminals and the help of new technologies.

Dwindling interest in the construction and maintenance of private sidings due to the more favourable alternative of the road. State and European subsidies are missing or are only available to a limited extent or are only offered sporadically and with a high bureaucratic threshold (eg Marco Polo).

— Failed use of deployment and procurement policy of national railways often leads to bottlenecks in the provision of locomotives for freight transport. This issue is even aggravated by the priority of passenger traffic along shared routes.

Conclusion

Politics should identify investment and promotional focuses to create high-performance rail freight routes with high axle loads. An increase of the private investment readiness is called for as regards haulage terminals, private sidings and transhipment facilities of intermodal transport, for instance, with the help of subsidy incentives.

3. System Access

— Developing competition will lead to innovation, improvement in performance and cost reduction in European rail freight transport.

— Making available the "rail" mode of transport has to be neutral for all potential users. The provision and maintenance has to be in the public interest of the respective states in guaranteeing transport safety and equal conditions of competition, in line with the provision of roads.

— The rail systems have to be opened in all countries more or less at the same time, as otherwise equal conditions of competition cannot be guaranteed for the rail transport operators.

— Given free access to the rail systems, all other operational and transport conditions also have to permit free competition for private rail transport operators.

Conclusion

The opening of the rail systems has to be conducted observing the same rules of access and comparable route pricing and needs to be understood as a European solution.

4. International Rail Freight Transport

— The technical/infrastructural differences (especially power systems, Gabarits, gauges, length of the overtake tracks, automatic signalling) of the various countries are hampering the development of cross-border rail offers in Europe.

— The collaboration of various rail service providers in cross-border rail freight transport has negative consequences in designing commercial offers. For instance there are the following problems:

  — separate pricing by each railway company with new calculated freight cost degression;

  — strongly differentiated and often non-transparent ancillary cost regulations;

  — charging minimum prices for short distances; and

  — different opinions on designing agreements (contract life, scale of discounts, terms of payment).

— National differences in the technological implementation of the transport service (axle loads, permissible train length and weight) often prevent the provision of an efficient rail alternative.

— The conditions for the border passage between the European countries have to be designed as to prove neutral for all interested rail transport operators. Existing agreements of the national railway companies on simplified border passage (eg take-over on the basis of trust) have to be applicable also to other interested rail transport operators observing safety standards.

Conclusion

The EU needs to initiate a programme for the harmonisation of technical and technological standards in rail freight transport in Europe as soon as possible.

5. European Rules

- The majority of the European rules on rail freight transport in the public, commercial, technical and technological areas require reform. The reforms already initiated need to be accelerated.
- Equal conditions in competition for the private cars as compared to the rail owned cars have to be guaranteed.

Conclusion

The initiated reforms of the rules have to be accelerated under the auspices of EU/UIC.

6. Car Equipment/Transport Vessels on Rail

- The European rolling stock and the management systems are often outdated.
- Due to a lack of financial means of the national railway companies, as well as a growing sense of insecurity among the private car companies, innovation and investments have been curbed over the past years.
- There are still deficits in the area of load securing, satellite-controlled monitoring of the position as well as in the horizontal as well as a vertical suspension of the car superstructures.
- The rules of public railways in using private cars leads to an inequality (empty run prices, too low freight discounts, operating conditions).
- The insecurities in the future treatment of railcars (eg minor loss settlement/catalogue damage) leads to a general restraint in the replacement or additional investments in rolling stock.

Conclusion

The EU and UIC are called upon to establish equality in competition for private and public railcars. Furthermore, the international terms for the use of railcars need to be laid down bindingly for the future. This is an essential prerequisite for investment into modern transport vessels/car equipment.

7. Block Train Operation

- Step by step strong competition is developing for all block train services by the involvement of private operators. This is leading to a change in the previous price and service structure for block trains and individual cars/car groups.
- Apart from the block trains for a single type of freight from siding to siding, more and more importance is attached to the joint formation of mixed block trains (possibly with intermodal transport) by forwarding companies, operators and railway companies.

Conclusion

Block train operation remains the most competitive offer of rail freight transport. The subsidy options from block train revenue for individual car services will cease to exist. The competitiveness of rail transport companies means less flexibility in the reloading and causes more empty runs.

8. Individual Car/Car Group Operation

- The transport possibilities for individual cars will dwindle over the years to come. The reasons are:
  - Closure of branch lines and private sidings due to declining economy and lack of alternative transport options on rail (eg loading at third-party facilities or change to intermodal means of transport);
  - car use dependent on the rail transport operator;

— lacking or insufficient networks for comprehensive collection and distribution services for individual cars/car group services;
— insufficient car material (capacity, load securing appropriate for the respective type of freight as well as modality of the cars);
— a lack of products appropriate for the market; and
— a lack of cross-subsidy possibilities from profitable block train business for national railways.

The opportunities for individual railcars lie in the concentrated feeding of consignments to consolidation terminals nearby and their addition there to intermodal transport and other car groups.

Conclusion

The IBS members are striving for cooperation among the European railways in expanding individual car and car group services. Setting up high-performance nodes for forming and dissolving Block trains with a maximum coverage in Europe will be of the greatest significance for the future role of rail freight transport.

9. Intermodal Transport

— Intermodal transport in complete trains via central intermodal terminals represents the greatest potential for the entry of private rail transport companies.
— The merging of the production systems of intermodal and conventional car freight systems has to be guaranteed besides intermodal freight transport in block trains throughout Europe.
— With more and more closures of sidings and access points to the rail system, the setting up of alternative transhipment points for intermodal transport, transhipping the freight or equipment with mobile gear is growing in importance. The merging with the individual car transports has to be guaranteed.
— The number of companies involved in the service chain of intermodal transport has to be reduced in the interest of a competitive system offer.
— The economy of intermodal transport may be improved through growing pan-European standards (cars, equipment, transhipment facilities).

Conclusion

Intermodal transport displays long-term growth potential despite the problems outlined. Insofar as equal conditions of competition cannot be established *vis-à-vis* road transport, public subsidies have to be continued and also granted in future.

10. Situation of the European Rail Forwarders

The position of the European rail forwarders as a director especially of international rail freight transport is required for the following reasons:

— setting up customer-oriented transport solutions across the modes of transport, including the rail system;
— creating forwarding nodes for mixed block train services in the industrial as well as consumer product areas in all European countries;
— short-term offers in European door-to-door transport in merging the system strengths of rail transport companies and railway forwarders;
— improving the services during and after rail transport;
— drawing up alternative concepts in case of planned closures of branch lines and access points to the rail system; and
— including modern information and settling systems.

Conclusion

The rail forwarders operating throughout Europe are prepared to bundle the individual car services economically and to conduct a shift from road to rail transport by investing in merging points/transhipment facilities as well a cooperating with competitive-minded rail transport companies.

Memorandum by Rail Freight Group

Introduction

1. The Rail Freight Group is the representative body of the UK rail freight industry. Its objective is to grow the volume of freight carried by rail both in the UK and to and from it. RFG is also a member of the European Rail Freight Customer Platform, which we understand is also submitting evidence, as are a number of RFG members.

2. This response concentrates on issues related to UK origin or destination rail freight, although many of the comments are likely to be applicable Europe-wide.

History

3. Freight has been carried across the Channel by rail in train ferries for many years. The last ferry between Dover and Dunkerque stopped operating in the 1990s when the Channel Tunnel opened. Traffic volumes on the ferry varied, but about 1.5 million tonnes per annum were carried by ferry in the last years of that service.

Cross-Channel Rail Freight

4. The forecast volumes of freight through the Channel Tunnel was forecast to be between 6 and 8 million tonnes per annum at opening in 1994, rising to over 10 million tonnes a few years later. In fact, traffic only reached 3 million tonnes per annum, then reduced to below 1 million tonnes at the time of the problem with illegal immigrants, and is now running at about 2 million tonnes per annum. This gives a share of the addressable market of about 2.5 per cent compared with over 11 per cent for domestic UK rail freight. The market share of rail freight in France, in spite of the poor service quality, is nearly 15 per cent.

5. However, in the UK, rail freight volumes have risen by 50 per cent since privatisation, with the market share up from around 8 per cent to 11 per cent. In France, volumes of freight carried has declined along with market share, with SNCF expecting to lose further volumes in 2004–05 as a result of implementing the rationalisation plans that have been developed in response to its worsening financial position

6. The above figures demonstrate the poor showing of cross-Channel rail freight. If it were as easy and competitive as domestic rail freight, one would expect the market share of cross-Channel rail freight to be about 15 per cent as achieved in France, ie 12 to 15 million tonnes per annum. The fact that the market share is only 2.5 per cent indicates some serious problems.

7. Put another way, on the basis of current evidence, there is no reason why 15 million tonnes a year of rail freight should not be carried through the Channel Tunnel, ten times the existing volume. It is against this background that we seek to provide answers to the questions posed by the Committee.

The Channel Tunnel Arrangements for Freight

8. Before answering the Committee's questions, it is necessary to explain briefly the current arrangements relating to freight through the Channel Tunnel.

9. At the time of financing of the Channel Tunnel in the mid 1980s, an agreement was signed (the Usage Contract) between BR/SNCF (the Railways) and Eurotunnel which gave the former 50 per cent of the capacity of the Tunnel for some 50 years in return for payment of charges for its use, which were set for that period. In addition, minimum usage payments (called Minimum Usage Charges or MUC) were to be made by the Railways to Eurotunnel for the period up to November 2006. On the basis of BRB's allocation of charges, it is likely that rail freight's share of these payments amounts to around £50 million per annum. The Railways are obliged to pay Minimum Usage Charges until a combination of Eurostar passenger and rail freight traffic volumes reach a certain level, so far unattained and, on present trends, unlikely to be reached by November 2006.

10. These MUC payments have generally been seen as an important back-door Government guarantee to Eurotunnel to assist in its financing in the light of the likely concerns of investors and lenders, since legislation effectively prevented Eurotunnel receiving direct Government funding of any form.

11. When the UK Government sold Rail Freight Distribution to EWS Railway, it retained the obligation to pay the MUC for the UK half of the Channel Tunnel until May 2005. There thus remains an 18 month period where EWS will be liable for a minimum charge of about £25 million per annum if it runs any trains; if it ceases to operate services, then the UK Government retains the obligation to pay the MUC until November 2006. The UK Government is also entitled to repurchase EWS's key Channel Tunnel assets (Class 92 locomotives and freight depots) for use by a substitute publicly-owned freight operator; should this be required to meet the Railways' obligations under the Usage Contract.

12. More recently, Eurotunnel announced its intention to apply for licences to operate freight trains through the Tunnel and across both the UK and France to other countries. It stated that this would be achieved through Eurotunnel using part of its 50 per cent of Tunnel capacity, rather than the capacity owned by the Railways. Separately Eurotunnel, as an infrastructure manager, recently published a Network Statement, as required by the first EU Rail Infrastructure Package. The Statement provides prices for third party operators (including Eurotunnel's own subsidiary), wishing to run freight trains using tunnel capacity allocated to Eurotunnel and also gives technical, operational and safety information. It remains to be seen whether any independent operator will be willing to bear the high market entry costs involved.

RESPONDING TO THE COMMITTEE'S QUESTIONS

What are the current barriers to entry in the international rail freight market?

13. Before a train operator can provide services for rail freight on any part of the European rail network, it must have an operating licence and a safety licence, it must procure or arrange the use of suitably-approved traction and wagons, recruit or hire drivers with the necessary skills and qualifications and have negotiated access rights on the network concerned.

14. For international traffic, the operator must achieve the above for each part of the European network on which he wishes to operate; there is generally one railway network per Member State and, in this respect, Eurotunnel is a separate infrastructure manager with separate rules.

15. Additionally, a new operator may also have to negotiate separate arrangements for crossing frontiers, such as between Germany and Poland where, until recently, frontier control regulations prevented any operator except the national rail operators from hauling trains across this frontier. In general, frontier control and associated customs procedures are still orientated to the needs of national railways rather than new entrants.

16. Track access charges vary between Member States but there are examples of charging structures which disadvantage new or small entrants, such as when a large lump sum is payable for access to the network, plus a small charge for kilometres used. Clearly, with the same lump sum charged to all operators, the need for a small operator to spread this over a small number of service kilometres places him at a severe disadvantage compared with the larger national rail operator. Any such "volume incentives" should therefore be strictly limited to prevent their use as barriers to entry, and justified economically on a case-by-case basis.

17. Finally, obtaining access rights to a train path can be difficult where the infrastructure manager (IM), who usually allocates capacity, is owned by the same body as the national train operator. There are many instances where the IM has failed to keep confidential the applications of independent operators, resulting in the national operator being able to block access for its competitor or to take pre-emptive marketing action.

To what extent are these barriers a result of a failure to fully implement existing EU Directives in all Member States?

18. Most of the barriers to entry and operational constraints outlined above are clearly the result of inadequate or incomplete implementation of the open access Directives. If they had been fully implemented in the spirit and detail intended, then most of these problems would disappear.

19. However, it may be helpful to examine a few nearby examples of where they have and have not been implemented. France has implemented them in full but, unfortunately, is still setting up the necessary structures to approve safety applications; it is of concern that SNCF is still involved in providing technical advice on the safety cases of its prospective competitors. There is also a wider problem for the EU's vision of

truly international competition, since it appears that the regulations introduced in France have been drafted in such a way as to make it virtually impossible for non-French operators to receive approval.

20. There are a number of examples of applications for equipment not manufactured in France being turned down. Approval of GM-manufactured class 66 freight locomotives is proving a time-consuming process, in comparison to experience in Germany, Belgium and the Netherlands. Since almost all existing locomotives approved to operate in France are owned by SNCF who will not sell or lease even the oldest ones to a potential competitor, new entrants are forced into expensive new orders from a French manufacturer. Several non-French operators have sought to operate trains even a few kilometres into France, including Arcelor (SNCF's largest customer) and EDF and have been rebuffed.

21. Neither Germany nor the UK has implemented the Directives but, conversely, in these Member States there is already open access for freight. In Germany, there are issues of confidentiality between the IM, DB Netz, and the national train operator DB Cargo/Railion and other operators; there are many restrictive practices concerning fuel suppy and traction current, access to ports and terminals, and the regulator is not seen by the smaller operators as sufficiently independent.

22. In the UK, by comparison, there has been an increasing amount of competition for domestic traffic since privatisation, a situation that has contributed to better service quality and more competitive prices, and a consequent growth in rail freight. This happened before the implementation of the open access Directives in the EU's First Rail Infrastructure Package. However, there is still no such competition for rail freight through the Channel Tunnel, which is a critical link in the Trans-European Rail Freight Network. The implementation of these Directives and their full application to international rail freight, in terms both of encouraging competition between rail freight operators and of establishing access charges that are competitive with other modes of cross-channel traffic, is urgent and essential.

23. We conclude that in the UK, France, Germany and other Member States, the full implementation of the Directives and/or their implementation in a positive manner to encourage competition to achieve better service quality and more competitive prices is not being pursued with the necessary vigour. We consider that this is generally for reasons of perceived national interest which is much to the detriment of European rail freight generally.

Is further action needed at EU or Member State national level to ensure enforcement of EU Directives?

24. The failures described above are, in our view, so serious that urgent action is required both at EU and Member State level to ensure consistent, uniform and urgent implementation both of the Directives, of the subsidiary structure needed to enable them to function. At EU level, this must include investigations of competition issues by the competition directorate.

Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?

25. We believe that the most important action is to ensure common, consistent implementation of the existing Directives. However, one issue remains unresolved, that of allowing companies or customers that do not hold operating licences but that wish to use rail freight (technically known as "authorised applicants") to be able to reserve capacity on the network. This is important for companies planning a commercial rail freight service who wish to test its overall feasibility viability before seeking bids from train operators for traction. Similar issues apply to ports and developers who seek to fund railway connections or other infrastructure to expand railway capacity or capability; there is no mechanism for reserving wider network capacity for the trains that such new infrastructure is intended for.

26. The position is particularly absurd where those railway works form part of a planning condition intended to encourage an increase in the number of freight trains operating on the network. The lack of such mechanisms is damaging to the long run success of rail freight as it directly affects the proper use of the town planning system to encourage the development of cargo generators adjacent with and connected to the railway network. Indeed, in the UK it can render useless sensibly framed conditions defined by the Secretary of State.

27. Authorised applicants are already permitted to reserve capacity on the British rail system and similar rights were proposed by the European Commission previously. However, the proposal was rejected by the EP or Council of Ministers under pressure from national rail operators. Rail freight customers continue to press for this change; it would encourage the market and competition to develop and there is absolutely no reason for continuing to reject this idea.

What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?

28. Confidence in cross-Channel rail freight is probably at an all-time low, with increasing concern as to whether rail freight services will continue after May 2005 when EWS becomes responsible for paying the UK part of the minimum usage charge. Without early confirmation of service continuity, there is a risk that current users will soon begin to switch traffic to other modes and freight routes as a precautionary measure. Further uncertainty concerns the future of Eurotunnel itself, and whether, when the UK Government publishes regulations to implement the open access Directives, these will take precedence over the Usage Contract between BRB/SNCF and Eurotunnel. Opinions differ on this.

29. We point out again that currently traffic is running at perhaps 10 per cent of what one might expect given normal market conditions. These involve the same long-term confidence building measures outlined in the UK Government's White Paper but, in addition to competition above rail, charges must be competitive with the shuttle or ferries and a reasonable variety of suitable equipment.

30. The ability to accept continental gauge rail freight would also help the market develop. Such equipment is much more easily available than some kinds of special UK equipment. This could initially be achieved by allowing some flows of such traffic to use the Channel Tunnel Rail Link (CTRL), with terminals in the East London area. However, it is also important for the Government to affirm its commitment to a strategy of enhancing the loading gauge of the UK's conventional-speed rail network to the Channel Tunnel and the Port of Dover for lower-speed, heavier freight flows.

31. Government must ensure both access and competitive pricing for using CTRL, which, although nominally in the private sector, is in effect financially guaranteed by the Government through long-term usage agreements. It must also encourage the sensible application of safety rules covering both the equipment and operations both through the Tunnel and on the CTRL.

32. Finally, in the competitive European freight market, rail freight already is forced to pay much higher rates to use the Tunnel, a situation which both governments and the European Commission must address in the implementation of the open access Directives. This unfair competition is exacerbated by the increasing operation of road transport in the UK using low duty continental fuel, often carried in very large tanks on five axle articulated lorries where extra large tanks are located in place of the sixth axle. Such five axle units are not legal at gross vehicle weights of 44 tonnes (needed to carry typical international payloads). Effective enforcement appears to be hindered by a lack of alignment between the interests of VOSA (The Vehicle and Operator Services Agency) and individual ports which compete with each other, and by the agency's concerns not to discriminate against foreign hauliers.

33. We understand that the resulting rates charged per mile may be as much as one third lower than legally operating UK lorries. This, on top of the Channel Tunnel rail freight issues described above, will make it even more difficult for rail services to compete.

34. It appears that, because of technical problems, the introduction of the distance tax for lorries is some years away. In the mean time, the Government could take action through the VOSA to prevent such illegal operation of lorries in the UK. So far, it has failed to do so, to the severe detriment, both to rail freight and the UK road haulage industry.

August 2004

Memorandum by Réseau ferré de France

1. *What are the current barriers to entry in the international rail freight market?*

Among the various barriers to entry, one can underline the following ones, as far as infrastructure managers are concerned:

— the approval process in licensing railways is sometimes cumbersome and expensive. Part of this situation reflects a learning process which is just starting. It is most likely that under the pressure of market opening, the process will gradually improve in the coming years.

— Information on access may also be poor and not reliable.

— Self-interested national behaviours remain dominant within the industry when it comes to moving toward harmonised systems or processes (international timetable, harmonisation of access contracts, . . .). In addition, Members States or regulatory bodies, who have a key role to play in establishing national rules, too often disregard international constraints and harmonisation process.

2. *To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?*

Now that existing EU Directives are being implemented in most Member States, legal barriers are becoming less stringent. The development of rail freight market opening is now mainly hindered by concrete and operational obstacles.

To tackle any failure in the implementation of the Directives and to ensure an effective application of the law, it is necessary to have regulatory bodies entrusted with the needed power and competence. As we see it from the continent, it is already the case in the United Kingdom.

3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

The best way to go forward is to strictly follow the essence of the EU Directives, ensuring an effective division of the key functions of infrastructure management. This requirement has already been addressed in the United Kingdom. Our belief is based on the fact that separation brings (i) efficiency because it allows each company to concentrate on its core activity (ii) transparency as we set out our "wares" in a manner that is clear and obvious to all users, (iii) neutrality as we do not operate trains in competition with existing or potential users of our tracks—indeed, we encourage the arrival of properly accredited newcomers. All this provides for the conditions under which competition can bring its new dynamism to the market.

The arguments for separation and integration show that either arrangement is possible but it is our belief that, if one looks for the furtherance of efficiency, transparency, neutrality and competition, as the EC does, separation provides the best setting for this.

Some railways have claimed that the costs of separation would be astronomical. This is not well tested and tried evidence. Whilst any reorganisation costs money, it is undertaken in order to gain the resulting benefits, which lead to a better safety, economic, commercial and technical outcome.

In a system largely based on public finance, separation makes the need for state investment more visible.

Separation secures the transition from a series of autonomous national railways to the provision of a homogenous European rail area, on which national train operating companies and third party companies can operate in full and open competition. Without it, such a vision is scarcely imaginable. It provides the basis for the true internationalisation of rail services in Europe, and offers clearer division of responsibilities, these leading to greater productivity and increased quality of service.

We believe this allows the use of the "supply chain in railway business" concept; according to which each party accepts his tasks and responsibilities *vis-à-vis* the end-customer. This is more in line with regular business relationships, versus the cloudier customer relationships of the integrated systems.

Whilst the separation of infrastructure management from operations can facilitate competition, the ensuing productivity and efficiency gains must not be jeopardised by too much concentration within the relevant railway market. The Commission should use its present powers to regulate such a risk.

4. *Is further European legislation necessary to make the policy of introducing competition into international freight effective?*

One challenge for the Commission and Member States is to provide the necessary prerequisites for a borderless and competitive European transport system. A European railway market must entail harmonised rules of various kinds in order to contribute to borderless rail services, free of national restraints and practices. Some examples of the need for harmonisation and co-ordination are decisions on international capacity allocation, track access agreements, policies on safety matters, technical standards and norms, processes for approval for rolling stock and certification of personnel, traffic control rules, train control system and a competitive supply of infrastructure services.

Maybe more than any additional European legislation, it is necessary to ensure that the complex regulations-that-exist-at (COTIF [Convention concerning international Carriage by Rail] regulations, national and EU regulations) are reworked into a comprehensive package establishing clearly what is in the EU domain and what is left to subsidiarity. The European Rail Agency should play a central role in this matter.

The existing rail network should be used in such a way that all visible and invisible border obstacles be removed where this makes economical sense. Apart from the technical and operational interoperability described in the interoperability Directives, there are also other obstacles, eg different customs regulations for incumbents and new entrants and different gauges which must be considered.

Whilst we believe that technical interoperability can improve cross-border operations, there are benefits to be gained from slick operations at borders for freight trains (as practised now for passenger trains) that can improve services whilst waiting for the development and implementation of the interoperability requirements.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

As a national infrastructure manager, we lack detailed information on the international rail freight market in the UK to make any appropriate recommendation.

Memorandum by Swiss federal railways SBB

Preamble

Since 1999, SBB has been a vertically integrated joint-stock company, owned by the Confederation; its assets, budget and accounting are separate from the state. Foreign rail freight companies as part of international groupings have access rights, also for combined transport pursuant to Directive 91/440/EEC, which Switzerland has undertaken to implement by way of the surface transport agreement with the EU.[6] Under national Swiss law, a Railway Undertaking can be given network access options. Such companies would then have open access for freight transport in the national market.

Switzerland's rail freight sector is one of the most dynamic markets of its kind in Europe.[7] Although Switzerland has not yet implemented the first Railway Package, it offers non-discriminatory and objective network access conditions in the freight transport sector.

Rail transport productivity depends mainly on efficient management of locomotives, freights cars and crews. The difficulties for cargo companies resides in the fact that responsibility for resource management is only partially in their hands, most of it still being in those of the infrastructure companies. That is precisely why the world's most productive rail freight companies, those in the United States, are organised as integrated companies that can, by their nature, participate in infrastructure-related decisions.

SBB are convinced that total unambiguous responsibility for complex railway systems, a responsibility assumed by the primary user, is the deciding factor for the quality of services provided. The example of Switzerland and SBB shows that such a situation (vertically integrated enterprise) has no adverse effect on the principle of non-discriminatory access to the network. The causes slowing down competition are on another level, in practice all the countries establish an always more pervading bureaucracy. The problems of the separation between infrastructure and transport lie in the potential losses of efficiency which result from the elimination or weakening synergy effects between the infra-structure and transport services. The requirements of European legislations can be met with the organisational structure of the incumbent and with accounting separation. The goal, however, is always to ensure non-discriminatory network access without the loss of synergy effect.

We do not know if Brussels is aware of the fact that although the "invisible hand of the market" settles some problems, the key to radical improvement in the quality along the major corridors lies above all in collaboration between the infrastructure companies involved (production and train path planning, operations management, infrastructure planning, extension and financing).

What are the Current Barriers to Entry in the International Rail Freight Market?

In general, we can say that many countries in practice (even if the legislation envisages it) do not allow a non-discriminatory access to the market, due to complex licensing and approval processes (rolling stock approval or delays in issuing safety certificates are typical examples of market access barriers). The differences of speed in implementing the European legislation, which are considerable from one country to another, lead also to distortions in competition. It also should be considered that in many cases, the structural changes in reality incorporate existing institutions under a different name. The fact of having officially implemented the first Railway Package is not always a guarantee of better market access conditions. The regulatory bodies are frequently out of resources and unable to fulfil their new functions of monitoring and regulation. Some

[6] Switzerland is not a member of the EU and does not participate in the European Economic Area. In 2001, Switzerland signed seven Bilateral Agreements with the EU. In the Land Transport Agreement, the EU expressly recognises both Switzerland's aim of transferring heavy goods transport through the Alps from road to rail, and the Heavy Vehicles Fee as a means of achieving this goal. The adoption of the European legislation is discussed within a joint committee which meets twice per year. The adoption of the first Railway Package is currently under discussion.

[7] IBM Rail Liberalisation Index 2004.

countries have also a bad information policy in regard to the network access modalities or have divided the powers amongst various institutions.

Liberalisation is a slow process and was implemented only a short time ago. It is too early for assessing on the effects of market opening (partly due to the poor data situation) who will for sure not be realised everywhere in Europe in an immediate future.

Regulation Rail Freight Quality

The published proposal for a regulation on Rail Freight Quality[8] is concerned with the setting up of a mandatory system of penalties for rail freight services. It includes provisions on liability, penalty and monitoring schemes. We are strongly opposed to such an initiative, which discriminates rail compared to other transport modes that rail competes against. This regulation would simply overburden the rail system administratively and financially, to the extent of actually deterring some existing and potential customers from using the rail mode. In the British case, experience already shows that compensation systems imposed by law do not improve quality, nor safety, much to the contrary. This intervention of the public authorities into normal business life is difficult to understand one year after the liberalisation of the rail freight market. Furthermore, the existing international legal framework,[9] already imposes rules on the railways which are twice as strict as those applicable in the road sector.

Walter Moser
Head of International Affairs

Daniel Trolliet
International Affairs

19 July 2004

Memorandum by Union of Industrial and Employers Confederations of Europe (UNICE)

1. *What are the current barriers to entry in the international rail freight market?*

— Absence of an independent referee to prevent dominant operators enjoying unfair advantages. This applies particularly in those countries where both the track and dominant operator are state-controlled. Track access and charges may be disproportionately burdensome for newer and smaller operators. Together these represent a barrier to effective planning by potential new entrants.

— Requirements in terms of operating licence and safety. They may appear to apply disproportionately to potential new entrants to the market, thus reinforcing the dominance of the incumbent operator. The requirements also differ between countries.

— Uncertainty as to when a "level playing field" will become a reality.

— Operational requirements (on such matters as speed, axle-weight and length) determined primarily by passenger train considerations. On some lines the requirements may appear inappropriate or excessive. Compliance (eg, purchase of new locomotives or shorter train lengths) may be expensive.

2. *To what extent are these barriers a result of a failure fully to implement existing EU Directives in all Member States?*

— Failure to implement in full the open access Directives is a major contributory factor.

— Lack of effective independent regulation is a serious barrier in some EU countries where the organisation controlling the track appears to operate in concert with the dominant, state-owned operator.

— Subsidies for the dominant incumbent operator.

3. *Is further action needed at a European Union or Member State national level to ensure enforcement of EU Directives?*

Action is required at EU and Member State levels to ensure full implementation of the existing open access Directives, specifically:

— Separation between provision of infrastructure and operation of trains;

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8 COM(2004)144, Third Railway Package.

9 CIM (Convention Internationale Marchandises), applicable in 41 countries.

- Independent regulation; and
- The European Commission's DG Competition focusing on the situation on Europe's rail network and in particular on the issue of organisations controlling the track operating in concert with the dominant, state-owned operators.

4. *Is further European legislation necessary to make the policy of introducing competition into international rail freight effective?*

- No. Effective implementation of existing legislation (1st, 2nd and the proposed 3rd rail packages) is what is required.

5. *What action should the United Kingdom Government consider to ensure that the United Kingdom takes full advantage of the potential growth of international rail freight as a result of this policy?*

- Committing itself to early investment in projects necessary to continue the recent expansion of rail freight. A good example is gauge enhancement of the line between Southampton and the West Midlands, enabling carriage of the 9ft 6in "high cube" boxes which are becoming the standard for the container industry. There is a need for capacity improvements on lines serving ports, more and longer passing loops on congested lines, together with a strategic network of facilities for road/rail inter-modal exchanges.
- Giving an indication that it understands and plans to address the present capacity constraints on the network, together with those likely to emerge in the medium and longer terms (eg from road user charging). More capacity is needed for freight trains connecting the Channel Tunnel and the UK's regions.
- Investigating the reasons for the present—often prohibitive—cost of connecting factories and warehouses to the rail network, with a view to driving it down.
- Ending the present damaging hiatus caused by the suspension since January 2003 of freight facilities grants in England. These enable the construction of facilities for the transfer of freight between rail and road and in the past have levered in substantial private capital. The grants continue to apply in Scotland and Wales.

Focusing on early resolution of issues surrounding the future of the Channel Tunnel, in order to increase business confidence and ensure competitive charges for potential users of the tunnel.

16 September 2004

Supplementary written evidence from Lord Berkeley OBE, European Rail Freight Customers Platform

Following my oral evidence last week, I promised to give the Committee further information about Eurotunnel. I now enclose a copy of our RFG Response to Eurotunnel's Network Statement dated February 2004 (*not printed*). Although this was written some time ago, very little has moved on since then and I hope that it will shed some light on this difficult subject.

In response to the Committee's question about what the UK Government should do, we suggested that it starts near to home, and complies rather more effectively with its statutory duty to promote rail freight through the Channel Tunnel. So far, this has resulted in just one tenth of the potential traffic using the Tunnel.

The volume of freight through the Channel Tunnel was forecast to be between 6 and 8 million tonnes per annum at opening in 1994, rising to over 10 million tonnes a few years later. In fact, traffic only reached 3 million tonnes per annum, then reduced to below 1 million tonnes at the time of the problem with illegal immigrants, and is now running at about 2 million tonnes per annum. This gives a share of the addressable market of about 2.5 per cent compared with over 11 per cent for domestic UK rail freight. The market share of rail freight in France, in spite of the poor service quality, is nearly 15 per cent.

However, in the UK, rail freight volumes have risen by 50 per cent since privatisation, with the market share up from around 8 per cent to 11 per cent. In France, volumes of freight carried has declined along with market share, with SNCF expecting to lose further volumes in 2004/05 as a result of implementing the rationalisation plans that have been developed in response to its worsening financial position.

The above figures demonstrate the poor showing of cross-Channel rail freight. If it were as easy and competitive as domestic rail freight, one would expect the market share of cross-Channel rail freight to be about 15 per cent as achieved in France, ie, 12 to 15 million tonnes per annum. The fact that the market share is only 2.5 per cent indicates some serious problems.

Put another way, on the basis of current evidence, there is no reason why 15 million tonnes a year of rail freight should not be carried through the Channel Tunnel, *ten times* the existing volume.

Finally, I enclose a cutting from the French railway magazine "La Vie du Rail" 13 October 2004 (*not printed*) which gives some interesting comments about the opposition within Germany and Deusche Bahn to the open access Directives. It is a matter of concern that both Germany and France do not seem to be embracing open access and fair competition above rail in the manner which they signed up to in approving these Directives.

Tony Berkeley
Chairman

October 2004

Printed in the United Kingdom by The Stationery Office Limited
3/2005 992244 19585

ISBN 0-104-00626-9
9 780104 006269