Institutional and regulatory framework

Contents

Reform of institutional and regulatory frameworks will help improve the future of the industry - should be guided by international experience

- Institutional and regulatory framework – changes are key to improving management focus, efficiency and transparency
- Changes in institutional structures needed to refocus railway management away from government to customers and markets
- Efficiency improvements needed to:
  - Ensure railways can compete with other modes of transport
  - Reduce the burden on governments facing increasing demands on resources
- Transparency to ensure better decision making - based on fuller information
- International benchmarking provides useful lessons on:
  - Frameworks adopted in different countries
  - Impact of different frameworks

International experience - general

- There is no single best solution:
    - Institutional framework should reflect each country's conditions – market, historical, cultural, legal
    - Most useful lessons arise from countries with similar conditions
- Reform is complex and must be carefully planned:
    - Most rail sector reforms take years, and never stop as markets change, e.g. Germany and Russia adopted 3 stage plans over 10 years; still evolving
    - Important to consult with key stakeholders - major customers, potential investors, rail workers and unions – this will ensure plans are sound and minimise implementation problems
- Need to adapt plan if results differ from expectations or markets change
- Key challenge is to change the culture in both the railway enterprise and government

International experience - governance

- Most countries have separated policy making from railway management; those who have not yet done so (e.g., India) are considering how to do it
- Railways are usually run by state owned companies - this reduces excessive government interference in marketing, operations, staffing, expenditure etc.
- Management is made accountable for meeting government policy objectives
- Boards of companies often include several independent directors, sometimes as chairman
- Boards meet regularly and follow defined corporate governance standards
- Boards scrutinise and approve plans produced by management

These governance arrangements allow railways to be run as commercial entities within framework set by government

International experience - structure

- Most comparators have established a line of business structure:
  - Infrastructure
  - Passenger
  - Freight
  - Non-core activities
- Each business has separate accounts and its own P&L and balance sheet
- Operating units are sometimes established as separate subsidiaries or independent companies; they may compete with other operators
- Infrastructure – the natural monopoly part of most railways – usually remains state owned – sometimes operated as a business, sometimes as an agency
- Notable exception is the Americas where mainly vertically integrated freight railways are privately managed

Line of business structure more effective when there are both freight and passenger services – it allows for but does not require multiple operators

Options for rail industry structure

		Examples	Comments
Vertical integration	Single system	Many	Traditional
	Separate freight & passenger sectors, & possibly parts thereof. May privatize.	Latin American concessions	Freight/pass may have separate infrastructure
Partial separation	Main sector: vertically integrated, possibly private. Other sector: Gov't owns assets above rail. Can concession operations.	Freight in US, passenger in Japan	Gives main sector control of infrastructure.
Vertical separation	Infrastructure & traction in public sector, freight wagons competitive and may be wholly/partly private	Russia, Kazakhstan	Key objective: private investment in wagons
	Infrastructure in public sector, transport competitive and fully or partly private	Parts of European Union	Key objective: competition through open access

Economic regulation – depends on industry structure

- Where there are multiple operators over same infrastructure:
    - Need to regulate access to infrastructure – either through concession contracts or through independent regulation
    - Need to agree methodology for determining charges to use infrastructure
- But, where there is enough competition - from road, water, other rail operators - no need to regulate final tariffs to customers
- For subsidised passenger services, minimum service requirements and some prices often stipulated in concession contracts – not subject to independent regulation

Regulation should be replaced by competition, wherever possible. Regulatory arrangements should evolve over time in response to needs, as new operators enter the market, or consider doing so

International experience: concessioning

- Concessions are contracts between a government owner and private parties to provide services
- Concessioning is becoming increasingly common as a means to introduce competition and private investment
- Many countries have introduced concessioning for rail passenger services, particularly for commuting:
  - European Union – e.g. UK, Germany, Sweden, Romania
  - CIS countries e.g. Russia, Kazakhstan
- Concessioning is used in most Latin American countries, especially in rail freight
- India has also let 12 concessions for rail container transport
- Often need to make legal reforms before the concessioning process starts – this helps attract private sector investment, including foreign investment

Some problems have arisen due to unforeseen events - but concessioning has increased investment, transparency and efficiency

Independent regulator may not be required – can rely on commercial arrangements, at least initially

Rely on commercial arrangements

- Many issues can be dealt with through commercial arrangements
  - Between state and operators on concessions
  - Or between rail companies on access to infrastructure
- Some countries may lack funds and skilled personnel to set up independent regulator
- Competition and contract law should limit anti-competitive behaviour
- Regulatory bodies find ways of making work for themselves

Establish independent regulator

- Without independent regulator, Government may intervene in conflicts, politicising decisions
- Private sector may be more willing to invest if there is independent regulator to:
  - Ensure fair access to infrastructure for multiple operators
  - Define common methodology for determining charges to use infrastructure
  - Arbitrate on concession contracts in case of breach of contract

Summary

	Russia & Kazakhstan	India	China	European Union	Mexico	United States	Japan
Governance	State owned company	Ministry/ Board	State owned company	State owned companies	Private companies	Private companies	Private companies
Dominant structure	Infrastructure and traction vertically integrated. Wagons (private) separate.	Vertically integrated	Vertically integrated	Vertically separated, often in holding company	Vertically integrated	Vertically integrated	Vertically integrated
Concessions	Some for passenger services	For rail container freight	None	Many for passenger services	Freight and passenger	Mandated and commercial access rights	None
Economic regulator	Multi-sector regulator	No external regulator	Multi-sector regulator	Independent body	Regulatory Agency for Rail Transport	Surface Transportation Board	Ministry
What does it regulate?	Some tariffs, customer and infrastructure		Services and tariffs	Infrastructure access rights and tariffs	Infrastructure access rights and tariffs if competition ineffective	Excess railway pricing and access (light touch)	Tariffs

International experience: Cross border arrangements

- Cross border movements often suffer major delays and costs
- Traditionally, train brought to marshalling yard in Country A, and locomotive (with crew) from Country B crosses border and hauls it to Country B
- In the European Union, creation of single market (customs union) means:
  - Customs and document inspections not needed
  - Freight and passenger trains and crew increasingly operate across borders
  - But cross border traffic often constrained by differences in technical standards
- Freight in North America:
  - Documents exchanged electronically between railways irrespective of borders
  - Selective customs and document inspections at US/Mexico border, less intensive at US/Canada border
- International agreements on tariffs needed
- Reliable and reasonably priced access of trains to infrastructure in bordering countries avoids wasteful investment in duplicate track

CAREC railways: institutional issues

- **Corporatisaton**: Whether and how should a national rail company be established?
  - **Governance:** what governance arrangements should be put in place?
  - **Staff**: Where to place redundant staff?
  - **Accounting**: How to handle debts? How to change accounting practices and standards?
- **Competition:** Whether to allow multiple operators and competition on the track and in what sectors?
- **Private sector:** Whether and how to go about attracting private investment?
- **Concessioning:** Whether to introduce concessioning and in what sectors?
- **Economic regulation:** What to regulate? Whether to set up independent regulator or regulate through concession contracts and commercial arrangements?
- **Speed and phasing of reform:** How quickly is it possible to complete reforms?
- **Law:** What legal changes are needed and when?

CAREC railways: key questions

- How to separate policy making from railway management?
- How should railways be regulated?
    - Independent regulation OR
    - Commercial agreements
- What legal changes are needed, if any?