IRF Preliminary comment

EU "Infrastructure Charging" – current fallacies and a constructive approach

Barcelona, 12 November 2002

The International Road Federation (IRF)

The International Road Federation is a non-governmental, not-for-profit organization with in over 70 countries worldwide from both public and private sectors. It was established in 1948.

Mission

The IRF's mission is to encourage and promote development and maintenance of better and safer roads and road networks. It helps put in place technological solutions and management practices that provide maximum economic and social returns from national road investment. The IRF believes that rationally planned, efficiently managed and well-maintained road networks offer high levels of user safety and have a significant impact on sustainable economic growth, prosperity, social well-being and human development.

Authorship

This position paper has been coordinated and written by IRF Geneva's Director of Programmes and membership, Ansgar Kauf, taking into account the guidelines agreed upon by IRF board members. The paper has been published and presented on the occasion of DG TREN's 2nd annual conference on Energy and Transport, Barcelona, 11th – 13th November 2002, where the European Commission's draft directive on "infrastructure charging", i.e. pricing for all infrastructure modes including transport, has been debated.

IRF preliminary Comment on EU "Infrastructure Charging" – current fallacies and a constructive approach

1) Introduction – context of EU transport policy
2) Comment on EU new framework directive "infrastructure charging"

1) Introduction – EU transport policy

Ten years after the collapse of the Soviet-Union, the European Commission has conceived a transport policy which recalls the times of central planning, state enterprise and non market-related price fixing. Despite the transport choice of the majority of citizen-users, the Commission has other ideas about which transport mode to choose (although 80 – 90% of inland traffic for passengers and goods are on road).

The IRF already made critical appraisal of the EC White paper on transport policy in 2001. Although EU officials are well aware of the challenges facing the transport sector (congestion, safety, environmental concerns and so on) their proposed policies are largely inadequate to provide a solution to the most pressing problems. A particular concern should be to relieve the already congested road networks from the future growth of at least 38 % in goods and passenger traffic between now and 2010. In fact, major rail projects proposed as an alternative to road will only be implemented *after* 2010, and measures intended to shift traffic, in the meantime, from road to rail are unlikely to have the desired effect; many experts point out that EU policies are more likely to aggravate the situation.

As a first major action announced in the White Paper, Brussels is trying to impose artificial infrastructure charges that will lead not only to economic distortions, but will also mainly increase costs for road users. This is the essence of the ***plans*** *revealed so far in the* ***proposed framework directive on "infrastructure charging"[1].*** Without any viable transport alternatives being offered, socio-economic fall-out from the proposed measures is likely to be considerable

- impeding social mobility, one of the major achievements of EU citizenship and democratic freedom;
- cutting the competitive edge of Europe's private sector on the global economic front.
- losing efficiency through state intervention in terms of road pricing and modal split, the likely result being the generalization of tolls levied by state authorities and designed to cross-subsidize rail investments under the illusion of promoting a shift from road to rail.

However, if the Commission's policies fail to meet the challenges of future transport growth till 2010, congestion in particular, its "escape strategy" of decoupling transport growth from economic growth will prove unrealistic, mainly because measures proposed are ones that focus on symptoms (congestion, emissions, noise) and not causes (structures of industry and economy generating excess transport demand; structures of cities that generate commuters' traffic and cause urban congestion).

In fact, the IRF perceives roads within a global transport sector approach. We also want to revitalize rail, as it has its role to play and should contribute to relieving already congested road networks. But this can only be achieved by using real incentives and not cross subsidies, this means: managing road & rail as a business with a customer focus

[1] For a short summary of the planned directive, see beginning of next page. Relevant publications of the European Commission (DG TREN) are: the Green Paper "Towards Fair and Efficient Pricing in Europe" of 1995; the White Paper "Fair Payment for Infrastructure Use" of 1998; the White Paper "European transport policy for 2010: time to decide" of 2001; the presentation "European transport infrastructure charging policy" of September 2002

2) Comment on EU new framework directive "infrastructure charging"

Why doesn't the European Commission (EC) say straight out that billions of euros of taxpayers' money will be needed to pay for financially unsustainable rail projects? The projects have, in any case, been approved, but member state Ministers of Transport already know that their budgets will not stretch to funding them. In reality, the EC is reluctant to come clean on the true objectives of its infrastructure charging policies and has little idea of how many extra billions the approved rail projects will swallow up.

The opportunity to fund through cross-subsidy is at the heart of the new proposed framework directive for infrastructure charging. It means to create "a new infrastructure-charging system and a common methodology for setting charging levels, offset by the removal of existing taxes, and allowing cross-financing", prohibited under the current directive (1999/62/EC). The official aim is to internalise all transport costs, including negative externalities, into infrastructure charges. But the real purpose is to finance a few mammoth rail projects across the Alps and the Pyrenees, which are neither financially viable nor economically justified. The IRF is concerned that cross-subsidies from road to rail once made legally possible, will become a common practice, even for other purposes, an irresistible temptation for cash strapped governments.

The IRF postulates that road revenues more than cover external costs, that EC methodology is, in any case, flawed, and that transport pricing should be based on normal business practice.

Road revenues cover more than cover external costs.

Any tortuous and pseudo-scientific argument is welcomed by the EC to justify cross-subsidy. The official line is "the road does not pay for its true costs", or at least not the external costs. This ignores the fact that, since the 1980s, EU governments are siphoning off over two-thirds of all road-related taxes into the general budget, instead of investing them in urgently-needed road maintenance, safety features and other measures (e.g. against congestion). The IRF estimates user charges in the EU raise revenues of some EUR 260 billion, about the same as the GDP of Belgium (just under EUR 268 billion).

A recent study[2] by the French Ministry of Transport reveals that, on the national motorway network, fuel tax revenues roughly cover the authorities' estimates of external costs, including wear and tear (EUR 2,895 million). Add on toll revenues (EUR 1,420), and road user payments far exceed external costs. These official, somewhat inflated figures are, in themselves, questionable: e.g. congestion might be viewed as the result of a failed transport policy rather than an external cost.

Does rail pay its true costs? Not in view of the huge subsidies – between 30 and 80%, plus investments in networks - paid to operators. Yet the EC has already expressed reserves about internalising rail's environmental costs if this were to jeopardise its market position.

The "external cost" argument ignores, moreover, the road's significant external or indirect benefits; for instance, gains in efficiency and productivity by road transport result in a net positive contribution to GDP. More interestingly, in June 2001 the Swiss Parliament rejected the principle of internalising external costs (the so-called "Bundi Initiative") after a study[3] showed that the external benefits of road transport, expressed in monetary terms, were roughly three times higher than its external costs. After a comprehensive analysis of economic and transport data from 1980 to 1995, the study found that, in 1995 alone, the external costs of road transport

[2] Study attached as annex1
[3] Executive summary of the study attached as annex 2

amounted to 7 billion Swiss francs (CHF), while the external benefits totalled CHF 27 billion, a net gain in external benefit of CHF 20 billion, or 7-8% of GDP. This might come as a surprise to EU officials, Switzerland being considered a model for European transport policy.

Flawed methodology

The official methodology in the Commission draft directive, Social Marginal Cost Pricing (SMCP) has been largely discredited by experts as outdated and unrealistic. It is

1) inadequate as a means of establishing prices that reflect the true costs incurred by the various transport modes;
2) incompatible with Public Private Partnerships / private financing, which it would discourage;
3) not an efficient tool for influencing traffic flow, i.e. the EC's stated aim of shifting traffic from road to rail; and
4) can encourage practices with perverse results; operators may deliberately allow roads to deteriorate as a means of leveraging infrastructure charges.

"Fair and efficient pricing": price and manage transport like a business

In its *dirigiste* approach, the Commission has overlooked three fundamental principles of transport economics:

1) **"sustainability"** does not mean that only environmental, safety and other norms are respected, but that transport projects are ***financially self-sustaining***. Who pays the bill in times of budget shortfalls and compliance with Maastricht criteria? To a large extent, it is the road user who already finances other government expenditures through fuel and vehicle taxes, over 2/3 of the revenues of which are not affected for roads at all. Moreover, sustainability means to maintain transport infrastructure as an asset. Therefore, accounting which is already in place for rail networks, should also be introduced for all road networks.
2) **cross-subsidies provide wrong incentives.** They encourage inefficiencies (management, allocation of resources and so on) and produce economic distortions. In principle, the IRF has always been opposed to the practice of subsidizing economically unjustified roads from profitable road projects as for example in France (motorway concessionaires) and Japan, unless it is justified by macroeconomic reasons and road network development.[4]
3) **Who should fix the price: technocrats or the market?**
   Although governments have to keep an eye on transport charges, in setting price caps that protect the users against excessive pricing, two key principles should be applied. Prices should be based on cost recovery for transport infrastructure investment, including measures to be implemented for combating externalities. Moreover, prices should be "fixed" by the market, in the interplay between user and operator.

Conclusion:

External costs should not be levied artificially to transport charges without combating externalities. They should be included in project and vehicle costs as measures necessary for meeting environmental, safety and other standards. All transport modes should, moreover, be financially self-sustaining and efficient in providing quality services to the user. The only realistic method of setting infrastructure charges is to price and manage all modes like a business.

---

[4] In 2001 due to a forceful request by EU Competition Commissioner M. Monti, the French government halted the practice of cross-subsidy in its motorway sector, criticizing it as unfair competition, and initiating the privatization of public concessionaires. In that case, why should cross-subsidizing rail by profitable toll roads be considered fair? It will only encourage the creation of white elephant projects. Instead, viable toll road concessions should be offered to the private sector, providing higher value for money (service to road users in exchange for the toll they pay). They should be part of an overall road masterplan with non-tolled and tolled segments, public and private participation.

Annexes

1) ***Study by the French Ministry of Transport*** **on social marginal costs compared to fuel tax revenues (for the national motorway network);**

2) ***Herbert Baum, Judith Kurte:*** **Estimation of the economic benefits of road transport in Switzerland, Cologne 2000 (Executive Summary of the study)**