The Voice of European Railways

POSITION PAPER

Consultation - Draft Guidelines on environmental and energy aid for 2014-2020 (EEAG consultation)

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COMMUNITY OF EUROPEAN RAILWAY AND INFRASTRUCTURE COMPANIES - COMMUNAUTÉ EUROPÉENNE DU RAIL ET DES COMPAGNIES D'INFRASTRUCTURE - GEMEINSCHAFT DER EUROPÄISCHEN BAHNEN UND INFRASTRUKTURGESELLSCHAFTEN

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INTRODUCTION

The European Commission has opened on 18 December 2013 a consultation related to *Guidelines on environmental and energy Aid for 2014-2020* (EEAG) aimed to replace the 2008 *Community guidelines on state aid for environmental protection*. The EEAG will define the framework for assessing government aid projects for energy and environment-related issues in the coming years.

CER welcomes this initiative and would like to contribute to this consultation in order to address several concerns and needs for clarifications relating to the content of the draft guidelines.

CER brings together 81 members: railway undertakings and their national associations, infrastructure companies and vehicle leasing companies from the European Union, the Western Balkan countries, Turkey, Norway, and Switzerland. CER members represent about 75% of the rail network length, more than 85% of the rail freight business and over 90% of rail passenger operations in EU, EFTA and EU accession countries.

Railway undertakings are seeking since several years to reduce their CO2 emissions from train operations with the objective of reducing them by 50% by 2030, with the further objective of making railway operations entirely carbon-neutral (CO2-free) by 2050. These are commitments the railway industry has already taken several years ago and is going to achieve ahead of the scheduled timing[1].

SUMMARY OF CER POSITION

CER`s proposal is based on the need to continue with a consistent approach on the State aid support to green energy consumers such as the railway sector. We consider that certain clarifications and/or modifications should be introduced in order to reflect the role that railway transport plays in environmental policy making including the following statements:

- sector-specific provisions for the rail market should remain unaffected;
- simpler compatibility test including more room for Member States on the application of the State aid rules;
- To avoid alternative instruments which are not effective to the rail market;
- Clarification of the scope of the guidelines;
- The need to increase or at least to maintain the current aid intensities.

[1] *"Moving towards Sustainable Mobility: European Rail Sector Strategy 2030 and beyond" (link).*

This position paper is divided into 2 parts:
In the first part, CER has done a general assessment of the planned EEAG and provides some background information on the specificities of the railway market (points a, b and c). The second part focuses on some concrete suggestions aimed at improving the draft EEAG (points d, e, f, g…k).

I. EVALUATION OF THE PLANNED EEAG

a. State Aid policy and Railway market are perfectly aligned

First of all, CER would like to point out that funding of the railway sector is fully compatible with the State aid rules which protect the internal market. As it is enacted in Article 107(3)(c) the Commission may consider compatible with the internal market State aid to facilitate the development of certain economic activities within the European Union, where such aid does not adversely affect trading conditions to an extent contrary to the common interest. Furthermore, according to Art. 93 TFUE State aids shall be compatible with the Treaties if they meet the needs of coordination of transport. This is the current situation of the railway sector: state aids which are granted to the undertakings of the railway sector are vital for the development of this market in Europe. These State aids not only create advantages for the environment, but also do not create any distortion of the market that could affect consumers or any other European policy.
Moreover, this is enhanced if we take into account the compatibility assessment enacted in Point 5 of the EEAG. The measures developed by the undertakings in the rail market increase contribution to the EU environmental and energy objectives without affecting trading conditions or any common interest.

b. Application of the proposed point 5.7 EEAG to railway undertakings will compromise their major role in climate and environmental protection

It is not needed to recall what the role of railway in the European Economy is nor what the policy goals of the EU for its rail policy are. The European state aid policy should reflect the important role that the railway sector plays as a consequence in the European energy policy and environmental protection matters. The application of the provisions of Point 5.7 EEAG of reductions in funding support for electricity from renewable sources to railway undertakings would create a clear harm to the undertakings operating in the rail market. It would make the sector less competitive and therefore less attractive for a modal shift towards rail by the consumers, putting a clear drawback to the achievement of both the European Single Railway Area and of a cleaner and environmentally friendly Europe.

Indeed, rail mobility is in most Members States mainly powered by electricity (53% of the EU rail networks are electrified) with an overall EU promoted effort by Member States to target the electrification of their main rail networks, hence reducing the use of high carbon emission diesel fuel traction. As a result the CO2 emissions of rail transport only amount to 0,4% of the total CO2 emissions of transport. At EU level, the carbon footprint of electric railways (35,15 g/p-km) is also three times lower than the one of road transport (109,41 g/p-km) or air transport (112,08 g/p-km).

It is therefore important to keep in mind that promoting rail transport within the EU is intrinsically linked to the price of the electricity. The higher the electricity prices the more difficult modal shift in favour of rail will become. Keeping electricity costs at a sustainable and affordable level is crucial for rail undertakings. If this is not the case, the aims of some major EU policies will not be achieved. Moreover this will put at risk the whole railway sector, triggering higher cost for its end-users, the consumers and to the tax-payers as most of the railway passengers activities are funded by public authorities by setting in place local and regional public transport by public service obligations (PSO) in accordance with European rules.

CER is glad to see that the EEAG proposal does not forget about Europe 2020 strategy[2] which is focus on creating the conditions for smart, sustainable and inclusive growth. Considering that sustainable growth remains a key issue for these guidelines, we consider that the railway sector fulfil all the requirements for switching towards a resource-efficient and low-carbon economy.

Nevertheless, rail is also confronted to many external challenges, already putting at risk its affordability and its potential for greening the European Economy.

First of all, the costs of even maintaining rail infrastructures - not to speak of the costs for developing it – are more and more unsustainable for state budgets, a situation which leads to a constant raise of the costs for accessing rail infrastructure capacity. This situation is unfair both from an environmental and level playing field point of view. Indeed, railway operators already bear higher infrastructure costs and taxes compared to those of their less environment friendly competing modes. For example road transport do not pay infrastructure charges on the whole network as the ecotax/eurovignette has not been generalized so far ; airways are still exempted from the ETS despite the use of kerosene benefitting from tax exemptions.

Beside these risks of rising costs and constraints due to the special pattern of electric consumption for railways, rail transportation is facing numerous other policy issues that need to be addressed:

1. Intra EU-Intermodal competition as explained hereinafter.
2. The constraint of having to send the adequate price message to clients in their intermodal mobility choices is a real challenge for railways. The fact that railways will pass on to clients their tax costs will clearly contribute to favour the use of less environment friendly mobility solutions, creating a real risk of endangering the EU actions for a modal shift towards rail.
3. Railways are facing urgent needs for fresh investment capacities to address main EU structural policy challenges, such as:

[2] *COM(2010) 2020 final of 3.3.2010*

- the need for a long lasting promotion of clean low carbon urban and sub-urban guided transport systems versus the use of individual fossil fuelled vehicles ;
- the ongoing move towards a necessary but costly achievement of a robust EU rail interoperability absolutely necessary for the completion of the EU single rail area, but which will have a financial impact on railways ;
- the need for investing in bottlenecks and missing links on EU corridors and main hubs throughout Europe while the TEN-T funding proposed by the EC have been cut by half in the final text adopted.

The application of the provisions of reductions in funding support for electricity from renewable sources pursuant to Point 5.7 EEAG for the railway sector would lead to a substantial increase of operating costs. This would put all the positives aspects that the railway sector is bringing to the market, consumers and in particular to the environment at risk.

The application of this point would put railway undertaking in a situation where their cost increase and consequently their affordability will restrain. At the end, this could trigger a change in their environmental policy too. Most of the undertakings in the sector are developing these policies taking into account the state aids to the energy that they consume.

Hence the extra cost that the decrease in this support would represent could damage the sector making it to develop different policies in order to achieve a fair level of competition with other modes of transport. There is therefore a clear risk to see railways stopping their electrification policies and also doing less to make use of renewable energy. Compared to those other forms of transport, the railway sector is by far the largest user of renewable energy, and it is also the one capable of increasing this figure at the higher rate. Combined, these factors mean that trains are the transport sector's most important contributors to the renewable energy changeover.

Furthermore energy prices for railways are already very high in the EU compared with competitors from other transport modes and the railway undertakings have no real cost-pass through abilities given that, for some of its services, prices are regulated and in addition, the company faces competition from other modes of transports exempted from paying the costs of greenhouse gas emissions. Hence, there is a need for having an ad hoc approach towards rail in establishing the European Energy State aid policy. For these reasons CER request the European Commission to avoid bringing additional costs for the EU railway sector that are not shared by other global competitors, thus further undermining its global competitiveness.

c. EU policies for the development of the single EU rail area call for financial relief of railway undertakings

Overall, it can be said that the question of the suitable guidelines to tackle these railway issues is not essential as long as compatibility assessments and criteria are cross examined between all the relevant EU policy objectives and stakeholders in a consistent and cohesive approach. The integrated objective being that the EU policies for the development of the single EU rail area are also supported through the state aid policy.

The railway aid guidelines set rules, that railway undertakings could be exempted from funding support for electricity from renewable sources. If the Commission should consider the provisions in point 5.7 EEAG to be primarily applicable to railway undertakings, the EEAG should be adapted taking into consideration the overall importance of the railway sector concerning climate and environmental protection.

The competition impact of the aid scheme and the need for a sound funding of clean energies should always be taken into account. To this end, and regarding railways, the Commission should ensure that benefit of state aid compatibility to railway undertakings related to funding of renewable energies are fairly allocated in the Member States for the sake of a level playing field regarding competition between railway undertakings.

II. CER SUGGESTIONS

Taking into consideration the important role that the railway sector plays in the environmental policy, CER would like to propose the following points to be clarified or amended in the EEAG.

d. Point 5.7 EEAG - sector-specific provisions for railway sector

Point 5.7 in the EEAG should explicitly state that, regarding aid in the form of reductions in funding support for electricity from renewable sources, the Community guidelines on state aid for railway undertakings (2008/C184/07; "Railway guidelines") will remain unaffected and as sector-specific provisions take precedence over the sector-neutral provisions in the EEAG.

This rule stipulates the conditions for aid in the form of reductions in funding support for electricity from renewable sources. At the same time, motivated by environmental and transport considerations, the Railway guidelines consider aid for railway undertakings with the objective of “coordination of transport” to be compatible. According to Point 98 of the Railway guidelines, this aid comprises the following: *"aid for reducing external costs, designed to encourage a modal shift to rail because it generates lower external costs than other modes such as road transport."* Railway undertakings could therefore be exempt from funding support for electricity from renewable sources. This has been confirmed by decisions of the European Commission[3]. The EEAG should accordingly clarify that the sector-specific Railway guidelines will remain unaffected and as sector specific provisions take precedence over the sector-neutral provisions in the EEAG.

The sector-specific provisions of the Railway guidelines are necessary as well as being justified. Exempting railway undertakings follows different objectives than exempting other undertakings with high energy consumption.

Moreover the characteristics of the railway sector perfectly match the guiding principles of the European state aid policy as reflected in Recital 181 EEAG. A reduction of the possible aids to the

[3] *See the European Commission's decision of 8 April 2011 (SA.31348 and SA.32614 - UK) stating that the complete exemption of electricity used in electric rail transport from a climate change levy in the UK is compatible with the internal market by virtue of Article 93 TFEU.*

aforementioned sector would contravene this rule since without the support of the Member States the undertakings will be in a difficult competitive situation against other transport modes as said above. The <u>rail market is directly affected by the funding of renewal energy support in order to avoid the use of carbon and to promote a modal shift to this environmental friendly mode of transport.</u>

Furthermore, Point 5.7 EEAG is designed to avoid that undertakings in the manufacturing sector, particularly affected by the funding of renewable energy support, are put in a difficult competitive situation. The provision aims at preventing competitive distortions resulting from individual countries' national energy levies and the ensuing costs for undertakings. The provision's intention is to create a level playing field for the manufacturing sector's energy intensive undertakings and ensure public acceptance for the ambitious renewable energy support measures.

In contrast, the aim of Point 6 of the Railway guidelines focuses on providing aid to railway undertakings for fundamental environmental protection reasons. Railway transport is the mode with the lowest external costs. Aid to railway undertakings strengthens their position in intermodal competition and therefore supports a modal shift to rail, an environmentally friendly transition. This means:

- It is worth supporting the railway sector simply because such aid contributes to the implementation of environmental policy objectives. This support not only aims at reducing company costs in order to safeguard their competitiveness. Moreover, it is above all a method of achieving environmental policy objectives, namely reduction of CO2 emissions through a modal shift from road to rail (see the above-mentioned information on the railway sector's reduction of CO2 emissions). The Railway guidelines create a special standard to meet the special characteristics of aid for railway undertakings.
- From a legal point of view, this compatibility is founded on the transport-specific provision in Article 93 TFEU: it declares compatible aid to coordinate transport, and this comprises funding for reducing external costs.

These sector-specific provisions would be contravened if railway undertakings were subject to the provisions for aid in the form of reductions in funding support for electricity from renewable sources according to the planned EEAG. This would be contrary to the rationale of Article 93 TFEU. Also it would fail to reflect the environmentally beneficial aspects of railway transport.

Applying only the provisions of Point 5.7 EEAG to reducing railway undertakings' energy levy costs would also contravene Article 15, Section 1, Part e) of EU Directive 2003/96, which states that Member States can exempt energy products and electricity from taxation or introduce reductions if they are used as a source of power for trains, trams, metros and trolley buses involved in passenger and freight transport. This environmentally motivated exemption for public transport would be undermined if the exceptionally strict exemption conditions pursuant to the abovementioned point were to apply to energy levies, in contrast to energy taxes.

Due to its content alone, the provision of Point 5.7 EEAG cannot be applied to railway undertakings. It merely comprises undertakings in the manufacturing sector, not service providers such as railway undertakings. Recital 184 of the planned EEAG makes explicit mention of an increase in "production costs". These can hardly include the costs entailed in providing railway transport services. Furthermore, this recital also makes explicit mention of "intensity of trade". However, railway undertakings are service providers and are not involved in trade in any form.

e. Clarification of the application of the guidelines

In consequence of the above, CER also considers that recital 12 EEAG should be clarified since it is important to have a concrete interpretation of the application of this rule. The application or not of sectorial rules represents a key point for a sector as Railway.

f. Recital 14 (b) EEAG

CER is pleased of the approach of the Commission in this article. We consider appropriate that these guidelines would not be applied to the financing of environmental protection measures relating to railway infrastructure, and therefore we suggest to the Commission to keep this rule.

g. Alternative policy instruments

Point 5.1.3.1 EEAG enacts certain measures to be implemented as an alternative instruments to achieve environmental and energy objectives. CER could not agree that instruments such as eco-labels or the diffusion of environmentally friendly technologies could be applied to the rail market. We should point out that the railway undertakings are just consumers of energy without any power to decide about these measures. We agreed that those measures may be effective for operator which control de energy supply but not for simple consumers as in the railway sector.

h. Appropriateness among different aid instruments

Point 5.1.3.2 EEAG goes beyond what is reasonable to request to the Member States. CER considers that imposing the obligation to justify the application of one aid instead of another would not be applicable and therefore will attempt against the principle followed by the State aid modernisation. The effectiveness of this type of aids is proven and if the Commission imposed the justification of the aid and the burden of the proof to the Member States, the system would not be effective since an in deep test should be performed.

i. Alternatively: Simpler compatibility test with more room for member states

If the Commission considers the provisions of Point 5.7 EEAG to be also applicable to railway undertakings a sound state aid approach towards rail in the EEAG should aim at strengthening low carbon transport services providers while sending a strong signal to national policy makers that the apportionment of the funding of renewable electricity to a given sector has to be related to its long term overall contribution to the achievement of EU main environmental policy objectives and targets, including within the common transport policy. This would also be perfectly in line with the article 15.1 (e) of the Directive 2003/96/EC. In that context, compatibility criteria should also take into account the capacity of a given sector to stand a significant raise of its tax burden in the context of a tough intermodal competition and the overall contribution of a sector and its development to a low carbon economy. Of course the "polluter pays" principle has to apply as a prima facie approach. However there is also a need for a global assessment of this principle on the apportionment of an energy consumer which should be related, based on scientific evidence, to overall negative external costs created by this consumer compared to those of their competing transport modes. Otherwise, state aid policy would contradict not only EU transport policy but also competition policy if such an approach would favour competing transport modes generating more external costs with lower internalisation ratios.

The consultation is not the prefect instrument to go into an in-depth economic analysis of the right level of compatible state aid a sector could be entitled to. However, the need for legal certainty and financial predictability for EU undertakings should certainly push for more detailed provisions. Surely the current renewal of the guidelines could be the occasion to further analyse this issue concerning sectors such as rail, for example through admissible level of compatible state aid that should be set at national level. This level could be set on the basis of EU parameters such as the length, the quality and the level of interoperability of power supply for trains in each national network, the implementation of a phasing out program for diesel fuelled traction, the comparison with negative external costs of competing modes, the capacity of other less environment friendly industries to contribute to the funding of renewable electricity in line with EU objectives.

Finally CER agrees with a part of Recital 179 EEAG, we consider that a simpler test of compatibility should be applied, essentially related to sectors' or undertakings' ability to pass on the additional costs, without loss of market share in the EU. In addition, the Commission should leave some room to the Member States as regards the minimum percentage of national environmental tax to be paid by the aid beneficiary. The EEAG fix it at 20% without any possibility of reductions, while the current Community Guidelines on State aid for environmental protection allow a lower rate in case of limited distortion of competition. The Commission must keep this room for manoeuvre in order to enhance the competitiveness of industries and modes of transports which are already energy consumers with low costs externalities and promoting sustainable products or services. This is a minimum as long as aviation is *de jure and de facto* exempted from ETS and from the taxation of kerosene, which is likely to be the case during the existence of the proposed EEAG.

j. Need to increase the aid intensities (Annex 1 EEAG)

The aid intensities given in Annex 1 EEAG should be increased above the levels of the Environmental protection guidelines currently in force. At the very least, these intensities should be retained. More attractive incentives should be established to encourage voluntary environmental protection measures.

The Environmental protection guidelines currently in place provide for an aid intensity of 50% for large enterprises if these undertakings go beyond what is required by Community standards or increase the level of protection in the absence of such standards. Even the current maximum rate is only of limited use for tackling the market's failure to invest money in environmental protection. As a rule, these investments at large undertakings entail substantial additional costs. This spending puts extra strain on company resources, and the undertakings have very little (at best) or no additional revenue which counterbalances this spending.

Annex 1 EEAG now contains the proposal to reduce aid for large undertakings that go beyond what is required by Community standards or that improve the level of environmental protection in the absence of such standards: the reduced maximum aid intensity is 35%. This change ignores the higher costs of investing in environmental protection that goes beyond current legal requirements - investments which were not actually obligatory for undertakings.

Such a low level of aid would effectively eliminate undertakings' motivation to voluntarily implement environmental protection measures. However, these voluntary improvements in environmental protection are of particular importance for society as a whole, as they generate a substantially higher level of acceptance for environmental protection measures than government-imposed restrictions and obligations. Voluntary environmental protection measures also foster people's ability to identify with environmental policy objectives and sustainability targets. More than state-issued mandatory measures, they encourage other undertakings to follow suit with their own efforts.

Moreover CER considers that this reduction of the maximum aid intensity is contrary to the proportionality principle enacted in Point 3 (e) EEAG. As we have explained above, this reduction would eliminate the incentives to develop policies which are directly enjoyed by consumers and the society. The maximum aid intensity of 35% could not be considered as a minimum to promote objectives and sustainability targets on environmental policy.

The planned reduction in aid intensities for undertakings that go beyond Community standards or improve environmental protection in the absence of such standards would also contradict the EU's environmental policy objectives as outlined in Article 191, Section 1 TFEU, which states that the aims of the Union's environmental policies are preserving and protecting the environment, in addition to improving its quality and protecting human health. Without aid that covers at least half of total costs, economic constraints will, in all likelihood, prevent undertakings from implementing voluntary environmental protection measures.

The incentive effect envisioned by Point 5.1.4 EEAG would normally require at least half of the costs of environmental protection measures to be covered by aid. At lower aid intensities, it is virtually impossible to motivate any company to implement such measures. As a rule, these measures do not generate additional revenue or reduce costs. Merely enhancing the company's reputation as being a green firm or one with sustainable business practices cannot serve as adequate motivation without the availability of aid that covers at least half of costs.

Higher aid intensities would, furthermore, be proportionate. There is no risk that higher aid intensities could result in a distortion of competition. A large number of aid measures available to undertakings that go beyond Community standards or improve environmental protection in the absence of such standards do not have any effect on competition. Often, it is not the undertakings themselves that benefit from environmental aid - instead, it is society as a whole.

k. Increase of the notification thresholds

The notification thresholds for investment aid in Point 2 EEAG for individual notifications should be raised or abandoned entirely. At the least, it should not generally be necessary to carry out detailed assessments for such aid measures. Instead the notification for assessment could be replaced by a reporting obligation of purely informational purposes.

At present, Member States are required to notify individual aid to the European Commission if investment aid exceeds the aid amount of EUR 7.5 million. This also applies if the aid is part of an approved aid scheme. The current draft of the EEAG retains the EUR 7.5 million thresholds in point 19.

This contradicts the European Commission's objectives for State Aid modernisation, which outlines the European Commission's intention to focus on enforcing cases with the biggest impact on the internal market[4].

Of themselves, environmental protection measures have virtually no influence on competition between undertakings, and there is simply no way that environmental protection measures with a volume of merely EUR 7.5 million can be considered to have a significant impact on the internal market.

In practice, EU Member States refrain from notifying individual aid granted on the basis of a notified aid scheme: the corresponding assessment process would generate an enormous workload for undertakings and Member States alike, hence effectively capping aid at EUR 7.5 million as a result.

This would result in aid intensities far below the figures permitted by Annex 1 EEAG in cases where the investment volume is actually several times this level. In such situation, undertakings would either limit or avoid investments in projects that benefit the environment. In other words, undertakings' green measures would be blocked by paperwork and purely administrative formalities.

Major undertakings are at a double disadvantage: not only are they unable to benefit from aid designed for small and medium-sized businesses, but they normally have to invest larger sums of money. This unhelpful situation does nothing to further environmental protection objectives.

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[4] *See Point 2.2. of the Commission's communication on EU State Aid Modernisation of 8 May 2012, COM(2012) 209 final.*

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