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Economic equilibrium test for new rail passenger service

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1. Introduction

Pursuant to Article 14, section 1 of the Commission's Implementing Regulation 2018/1795¹, the methodology used by the regulatory body² to perform the test shall be clear, transparent and non-discriminatory and shall be published on its website. The regulatory body will use the methodology after receiving a justified request to evaluate the impact of the new rail passenger service on the economic equilibrium of existing agreement on public service contracts. Pursuant to Article 16 of the Commission's Implementing Regulation the test will be applied, in time for the working timetable starting on 13 December 2020.

The economic equilibrium test³ referred to in the Implementing Regulation is applied according to Article 2 in situations, where a Member State has decided to limit, pursuant to Article 11, section 1, the right of access referred to in Article 10, section 2 of Directive 2012/34/EU⁴ for new rail passenger services between a given place of departure and a given destination, when one or more public service contracts cover the same route or an alternative route, as provided for in Article 2 section (i) of Regulation (EC) No 1370/2007⁵ of the European Parliament and of the Council. Pursuant to Article 11, section 1 of the Railway Market Directive, the section 114, subsection 1 of the Railway Transport Act (1302/2018)⁶ gives a competent authority the right to limit the rail network's access rights with similar conditions. Pursuant to Article 6 of the Implementing Regulation, even if a competent authority has granted exclusive rights to the railway undertaking performing a public service contract, the existence of such rights shall not preclude access being granted to an applicant for the purpose of operating a new rail passenger service, provided that access would not compromise the economic equilibrium of the public service contract in question.

Pursuant to recitals 2 and 3 of the Implementing Regulation, the purpose of the economic equilibrium test is to ensure that the right of access referred to in Article 10, section 2 of the Railway Market Directive is not restricted in regard to the railway infrastructure's new rail passenger services (including high-speed trains), unless it can be shown that this type of service would directly compete with public rail passenger services and would, thus, serve the same customer base and taking a significant portion of public transport service customers. The new rail passenger service might bring new users to the rail passenger service sector and provide net benefits for passengers without compromising the continuation of rail passenger services referred to in the public service contract.

This memorandum describes the processes related to the new rail passenger service's notifications, test requests and communication related to tests, as well as the methodological principles for the economic equilibrium test used by the regulatory body, on the basis of which the regulatory body makes decisions on the right of access to infrastructure. Pursuant to Article 11, section 2 of the Railway Market Directive referred to in Article 11, section 1 of the Implementing Regulation, the regulatory body shall make decisions on the basis of predetermined criteria. According to Article 10, section 2 of the Implementing Regulation, predetermined threshold or specific criteria can be applied, but not strictly or in isolation from other criteria, which will mean that

¹ Hereinafter the Implementing Regulation.

² Hereinafter the regulatory body.

³ Hereinafter the economic equilibrium test.

⁴ Hereinafter the Railway Market Directive. The Directive was implemented nationally in Finland with the enactment of the Rail Transport Act (1302/2018). Specifically, sections 114 and 115 of this Act apply to the economic equilibrium test. Insofar as the Implementing Regulation refers to the Directive, the provisions in question are directly applied to the processes described in this memorandum.

⁵ The Regulation has been amended with Regulation 2016/2338.

⁶ Hereinafter Rail Transport Act.

the application of the test will inevitably include case-specific analysis and the weighing of various criteria. According to Article 14, section 2 and recital 22 of the Implementing Regulation, regulatory bodies also comply with the best international practices and information exchanged with regulatory bodies in other countries and, where necessary, adjust their method over time.

2. Processes for notifications on a new rail passenger service, test requests and economic equilibrium tests

2.1. Notification process

According to Article 4, section 1 of the Implementing Regulation, the entity, who requires rail capacity for the provision of a new rail passenger service, shall notify the competent rail infrastructure manager and regulatory body of its intention to provide a new rail passenger service at least 18 months prior to the enforcement of the schedules related to the service. In this document, the new rail passenger service refers pursuant to Article 3, section 1 of the Implementing Regulation to a rail passenger service designed to be operated as a regular time-tabled service that is either entirely new or that implies a substantial modification of an existing rail passenger service, in particular in terms of increased frequencies of services or increased number of stops, and which is not provided under a public service contract. The notification shall contain the information listed in Article 4, section 2 of the Implementing Regulation in accordance to the provisions laid down in the Article.

After receiving the notification, the regulatory body shall pursuant to Article 4 of the Implementing Regulation publish the standard notification form filled in by the applicant and within a period of ten days notify the entities referred to in the Article in question that it has received the notification.

2.2. Test request process

Pursuant to Article 5, section 1 of the Implementing Regulation, the regulatory body will assess the impact of the new rail passenger service on the economic equilibrium of the public service contract at the request of an entity specified in Article 11, section 2, subsection 1⁷ of the Railway Market Directive, when the request has been completed in the manner provided in the subsection in question within a month of the time the entity has received a notification on a planned new rail passenger service.

In connection with the request, the entity, who submitted the request shall also submit the information listed in Article 7, section 1 of the Implementing Regulation, including, in particular, substantiation that the economic equilibrium of the contract risks being compromised by the new rail passenger service. As part of substantiation, it would be necessary to show proof on how large a net change the new service is estimated to cause to public service passenger numbers, in other words, how large an amount of public service customers it will take or how many completely new passengers it will add. A demand elasticity analysis carried out with objective methods provides a good starting point for such an estimate. Pursuant to Article 8, section 2 of the Implementing Regulation, the entity that has requested an economic equilibrium test, shall substantiate any proposed non-disclosure of commercially sensitive information at the time the information is provided to the regulatory body.

2.3. Economic equilibrium test process

Pursuant to Article 9, section 1 of the Implementing Regulation, the regulatory body can pursuant to Article 7, section 2, within a month of receiving the request, ask the entity that requested an economic equilibrium test for all the necessary additional information, case-specifically, for example, the information specified in the section in

⁷ As it has been amended by Directive 2016/2370.

question. In the same way, Article 9, section 3 contains provisions on how the regulatory body shall within a month of receiving the request, ask the other parties referred to in Article 7, section 2 to submit all necessary additional information. The entities in question shall submit the requested information within a reasonable period of time determined by the regulatory body. In addition to this, the regulatory body can ask for additional information, if it feels it necessary.

Additionally, Article 9 of the Implementing Regulation lays down the following conditions for the submission of information and the processing of a test request, if incomplete or inadequate information has been submitted to the regulatory body:

- In the event that six weeks before the final date for receipt of requests for rail capacity, the information provided to the regulatory body by the test requesting entity is still incomplete, the regulatory body shall perform the economic equilibrium test on the basis of available information. If the regulatory body considers that the information in question is insufficient to perform the test, it shall reject the test request.
- In the event that six weeks before the final date for receipt of requests for rail capacity, the information submitted to the regulatory body by the entity that is applying for the right of access for the provision of a new rail passenger service is still incomplete, the regulatory body shall perform the economic equilibrium test on the basis of available information. If the regulatory body considers that the information provided by the applicant is insufficient to perform the test, it shall adopt a decision resulting in access being denied.
- Where the undertaking performing the public service contract is not the requesting entity, and where six weeks before the final date for receipt of requests for capacity the information provided by this undertaking is still incomplete, the regulatory body shall perform the test on the basis of available information. If, however, the regulatory body considers that the information provided is insufficient to perform the test, it shall adopt a decision resulting in access being granted

According to Article 11, section 1 of the Implementing Regulation, after completing the economic equilibrium test, the regulatory body shall take a decision provided for in Article 11, section 2 of the Railway Market Directive, on the basis of which the right of access to the rail infrastructure shall be granted, modified, granted only under conditions or denied. If, as a result of the test, it is observed that the new rail passenger service will compromise the economic equilibrium of the public service contract, the regulatory body shall pursuant to Article 11, section 2 and recital 18 of the Implementing Regulation, as appropriate, indicate possible changes to the new rail passenger service, which would ensure that the conditions for granting the right of access are met. The regulatory body shall adopt a decision within six weeks from the receipt of all relevant information, and, in any event, before the final date for receipt of requests for. The regulatory body shall inform the infrastructure manager of its decision without delay.

Where a request for the economic equilibrium test is made according to Article 5, section 2 of the Implementing Regulation, in respect of a public service contract, which is in the process of being competitively tendered, the regulatory body may, according to Article 9, section 7, suspend consideration of the proposed application for a new rail passenger service for a maximum period of 12 months from receipt of the applicant's notification of the new rail passenger service or until the tender process has concluded, whichever is the sooner.

3. Information submitted by parties and used in the test

Article 7, section 2 of the Implementing Regulation lists information that the regulatory body can request from a competent authority, the railway undertaking performing a public service contract, an entity applying for right of access to infrastructure for the provision of a new rail passenger service in question, and a rail infrastructure manager. However, the list is not exhaustive, but rather provides examples of the information used in economic equilibrium tests. According to the Article 7, the regulatory body can ask the aforementioned parties for all the information it needs. Gross costs contracts⁸ will likely deviate from the list below on the division of information between the railway undertaking performing a public service contract and the competent authority.

The regulatory body can request the following from a competent authority:

- relevant traffic, demand and revenue forecasts, including forecast methodology;
- in the case of public service contracts completed with no call for tenders, the methodology and data used to calculate the net financial effect pursuant to Article 6, section 1 of Regulation (EC) No 1370/2007 and the Annex to that Regulation.

The regulatory body can require the following from the railway undertaking performing a public service contract:

- copy of the public service contract;
- the undertaking's business plan for the route covered by the public service contract or an alternative route
- relevant traffic, demand and revenue forecasts, including forecast methodology;
- information on revenues and profit margins gained by the undertaking on the route covered by the public service contract or an alternative route;
- timetable information for the services, including departure times, intermediate stops, arrival times and connections;
- estimated elasticities of the services (for example, price elasticity, elasticity with respect to quality characteristics of the services);
- cost of capital and operating costs for services provided under the public service contract, as well as estimates on variations in costs and demand induced by the new rail passenger service.

The regulatory body can ask the applicant to submit information on its plans concerning the operation of the new rail passenger service, for example:

- business plan;
- forecast on passenger traffic and revenues, including forecast methodology;
- pricing strategies;
- ticketing arrangements;
- rolling stock specifications;
- marketing strategy.

The regulatory body can request the following from the infrastructure manager:

⁸ A gross costs contract refers to a contract between a competent authority and an operator that operates a purchased transport contract, where the party ordering the transport carries the risk for ticket income.

- information regarding the relevant lines or sections, in order to ensure that the new rail passenger service can be run on the infrastructure concerned;
- estimates on potential performance and resilience impacts of the proposed new rail passenger service;
- assessment of impacts on capacity use;
- plans for developing infrastructure as regards routes covered by the proposed new rail passenger service, including an indication of the time when any such plans will be implemented;
- information on relevant framework agreements concluded or under discussion.

The regulatory body analyses the information sent, especially assessing the enclosed calculations and methodology in order to guarantee their reliability taking into consideration the information submitted by various entities in its entirety. Examples of materials that can be taken into account in the analysis include the demand elasticity analyses with objective methods conducted by either the parties or commissioned from external research institutes, with which an attempt has been made to predict the impact of the new service on the ticket costs and demand for the routes specified in the public service contract and, on the other hand, traffic volumes in their entirety. If the regulatory body believes that the analyses submitted to it are inadequate or unreliable, it may be forced as part of the economic equilibrium test to commission a supplementing demand elasticity analysis from an external expert organization. The manner, in which costs will be charged from the test request submitting entity, is detailed in Chapter 4.8.

4. Assessment criteria for economic equilibrium

4.1. General basis

4.1.1. Requirements laid down in the Implementing Regulation

Pursuant to Article 10, section 1 of the Implementing Regulation, the regulatory body shall assess whether the economic equilibrium of a public service contract would be compromised by the proposed new rail passenger service. Economic equilibrium shall be considered as compromised, where the new rail passenger service would have a substantial negative impact on at least one of the following elements:

- the profitability of services that the railway undertaking operates under the public service contract in question;
- the net cost for the competent authority awarding the public service contract in question.

In accordance with Article 10, section 4 of the Implementing Regulation, when assessing the aforementioned factors, the regulatory body shall assess the contractual arrangements in place between the competent authority and the railway undertaking performing a public service contract, including any mechanisms for sharing risks and the compensation paid to the railway undertaking. Naturally, the risk-sharing mechanisms in accordance with the contract will determine how the impacts of the new rail passenger service will be divided between the competent authority and the railway undertaking performing a public service contract.

Furthermore, Article 10, section 2 of the Implementing Regulation provides that the test shall analyze the contract as a whole, over its entire duration, which will mean that analysis cannot be limited to any individual service provided by the contract and the economic equilibrium cannot be considered compromised due to impacts on an individual service.

Article 10, section 3 of the Implementing Regulation lists the factors that shall, at the very least, be taken into consideration in the examination of impacts on the railway undertaking performing a public service contract and the competent authority, as a result of the market impacts of the proposed new rail passenger service:

- variation in costs incurred and revenues obtained by the railway undertaking performing the public service contract;
- financial effects generated within the network under public service contract by the proposed new rail passenger service, such as new passengers;
- possible competitive responses by the railway undertaking performing the public service contract;
- impact on relevant investments by railway undertakings, or by competent authorities;
- the value of any existing exclusive rights.

4.1.2. *Basis for the test prepared by the regulatory body*

It shall be noted that the factors listed above are partly overlapping and affect one another, as, for example, the impacts on the network covered the contract can cause changes to the expenses and profits of the railway undertaking performing a public service contract, as well as to the competitive responses of the same undertaking. When examining the factors, it shall furthermore be taken into account that the pre-determined awarding threshold criteria provided in Article 10, section 2 can be used, but not strictly or in isolation from other criteria.

The impact on revenues collected from the public transport service is formed from the impact of the total turnover of services minus corresponding change in costs. Thus, the key factors that are examined in the economic equilibrium test are the impacts of the new rail passenger service on the user numbers and costs of the services provided on the basis of the contract, the capacity of the railway undertaking performing a services to adapt costs to the new situation, as well as an estimate on whether the impact of these factors on the operating profit of the services provided under this contract will be significant. The assessment of the impact of these corresponding factors with regard to a competent authority can also be necessary, depending on the conditions provided in the public service contract. However, with regard to the competent authority, the scaling of necessary public support is often more important than the profits issue.

The regulatory body will inspect the following case-specifically: 1. the profitability of services provided by a railway undertaking performing the public service contract in question, including public subsidies, 2. the net costs incurred by competent authority as a result of the contract in question, and 3. the profitability of public transport services in their entirety, taking into account the combined effect on both. The methods for sharing the risks determined in the contract between a railway undertaking performing a public service contract and a competent authority, and the compensation paid to the railway undertaking, will determine which of these factors the regulatory body will emphasize in each situation.

4.2. **Impact of new rail passenger service on demand for public transport services**

4.2.1. *General*

An economic equilibrium test shall be able to determine the impacts that the proposed new rail passenger service would have on the demand for services provided on the basis of the public service contract, especially, its impact on passenger numbers for public rail passenger service and the price charged for the service. The premise should thus be to examine whether the new rail passenger service would compete

significantly for the same customers. For this purpose, it shall be possible to determine the characteristics of demand for the public transport service, which would make it possible to examine whether the demand for the new rail passenger service could in some part be overlapping with the demand for the public transport service.

If demand for the new service does not overlap notably with demand for the public transport service, it will also not have a significant negative impact on the profitability of the public transport service. It might even have a positive impact on the profitability of the public transport service, if the new service brought new connecting passengers to the public transport service. If it is observed that demand for the service is not in great part overlapping, economic equilibrium cannot be considered compromised. Determining the characteristics for a public transport service will provide an advantageous starting point for testing, whether economic equilibrium is compromised.

On the other hand, if the new passenger transport would compete for the same customers to a great extent, it will possibly have a marked negative impact on the profitability of public transport services. However, economic equilibrium cannot be considered compromised solely because the demand for the new rail passenger service is overlapping with demand for public transport services. A further analysis on whether the impact on economic equilibrium would be significant is needed in addition to the test. However, it is clear that an operator, who very obviously serves the same customer base, would likely lead to the public transport service losing some of its customers to the new operator, and market prices would experience a downturn. The impact on the profitability of the public transport service might be reimbursed, if the new rail passenger service added new passengers in need of connecting transport to the public rail passenger service.

Exogenous or, in other words, external factors (for example, the general economic situation, changes in consumer behavior when acquiring transport services) may impact the price and demand balance between the new rail passenger service and the public transport service during a long contract period. However, predicting external impacts for an entire contract period, which could be numerous years, can prove too uncertain an approach for producing estimates. This conclusion is emphasized by the fact that these factors likely only have a significant impact on the demand between the two railway services in a very limited amount of cases.

4.2.2. *Checking the overlapping of demand*

The rail passenger service provided on the basis of the public service contract can often also compete with other forms of transport, such as bus transport services, airlines and private cars. Competition law uses a definition of a relevant market, especially, for studying the operator's market power. However, because the purpose of the economic equilibrium test is to only compare the proposed new rail passenger service with the public rail passenger service and not to examine the market power of any operator, it is not necessary to determine the market in such broad context. When conducting an economic equilibrium test, it is enough to examine, whether the new rail passenger service would compete for the same customers with public transport services, in other words, would demand for this service overlap with demand for public rail passenger services. Because there is naturally no existing material on the market impacts of the proposed service before the service enters the market, a comprehensive quantitative analysis based on historical data is not possible.

The key characteristics of public transport services include the operated routes with their departure and destination stations, the stations along the routes, travel schedules, travel times and the pricing of the service. In the first phase, the regulatory body will compare these to those of the proposed new rail passenger service, taking into account the assumed characteristics of public transport demands, in order to determine, whether demand for the new rail passenger service overlaps with it. Also,

according to Article 2 of the Implementing Regulation, it is inevitable that when operators' demand is overlapping, the proposed rail passenger service would operate at least partly on the same or an alternate route with the public transport service. The most fundamental feature of demand for the public transport service is its elasticity with regard to different quality characteristics, for example, how ready the service's customers are to travel the same route at different times of day, and how great an impact the time spent travelling in relation to travel times with other transport services will have on demand for the service. The dependency of demand on the service's details is in practice what determines the overlapping of demand.

The entity, who has applied for right of access to provide the new passenger rail service, shall be prepared to submit to the regulatory body its business plan including calculations and substantiation to clarify, how many customers the new service is expected to draw, what are the assumed benefits that the new service will bring to consumers, as well as how large a share of its customer base it expects to gain from the public transport service's customers, and how much new rail passenger service would generate entirely new demand as a proportion of its total demand. An entity considering entering the market as a new operator has by default evaluated their positioning in relation to the public transport service, so it should, as a rule, have this type of information prepared at the time it submits the notification on a new service. Similarly, a competent authority and/or a rail company undertaking performing a public services contract shall submit to the regulatory body the same information at least on the net change to the public transport service's demand for evaluation as part of its substantiation for why a new service would compromise the economic equilibrium of the public service contract. At the same time, these operators are required to submit information on possible competitive responses and the estimated elasticity of their services. For more information about elasticities, please see Chapters 3 and 4.2.3.

On the basis of submitted information, the regulatory body evaluates whether further studies are needed. The best premise for the justification submitted by the parties is the comprehensive analysis on the reaction of public transport service demand, which would be implemented with a demand elasticity analysis and a related questionnaire. The primary objective would be to determine, what share of all customers of public rail passenger service will begin to use the new service instead, whether the new service will bring new customers to the public transport service, and to what extent the new service will gain completely new customers.

4.2.3. *Demand elasticity analysis*

In order to determine possible changes in user numbers and ticket prices of public rail passenger service during the launch of new service, the regulatory body can, where necessary, to the extent that it has not received an adequate amount of objective and reliable information from entities, commission a demand elasticity analysis from an appropriate research institute or another party suited for this purpose. The entity requesting the analysis will be responsible for covering the costs of the test in question, starting from the time when these costs were included in the Ministry of Transport and Communications Decree on chargeable transport services.

When the impact area of the new service overlaps even partly with the rail passenger service impact area of public service contract, the test is targeted at the assumed area of joint impact. The target area in question can be a region, an area formed by certain municipalities, the municipalities and cities that surround a part of the rail network, or a larger area.

One way to carry out the analysis would be as a questionnaire using different methods, in which case, the sampling will be specified so that it represents the population of the target area. Depending on the interview area the size of the sampling may vary. Quotas can be allocated to the sampling so that the population is equally represented and, on the other hand, an adequate number of interviewees from different

user groups take part. Questions can be targeted to different passenger groups in different ways, but, for example, those who do not use the service shall assess whether their use of services will change with the introduction of the new service.

In a study, from a comprehensive and representative sample of public passenger service customers and other customers it can be asked, for example, about price range, in which they would be ready to change over to using the new service either partially or completely. As part of the questionnaire, it is possible to determine the movement of customers also with help of data on new service prices. The examination of results can, where necessary, be carried out in a more in-depth manner using analyzing methods, if it is essential to acquire additional information on the impact of various factors on demand.

4.2.4. *Example analysis*

Below there are described examples of situations, in which despite partially same routes, the demand for operators is at least somewhat different. This could happen, if the new rail passenger service served for the most part a customer base different from that of the services under the public contract, due to their significant differences in routes and other service details important for demand. This memorandum only includes a few example cases; the actual analysis will be carried out taking into account the characteristics of each situation.

For example, a possible situation would be one, in which the proposed new rail passenger service used partly the same route as the public transport service at a certain time of the day, but it would have departure and destination stations not included in the rail network specified in public service contract, and, with regard to the overlapping portions of the route, the new service would not be a viable option for passengers due to other differences in the services. In such a situation, the new rail passenger service could even bring to the route customers, who would use the public transport service as a connecting form of transport.

In Finland, a situation such as this could actualize, for example, when a local rail service is provided in the Helsinki metropolitan area according to a public service contract during the day, while the proposed new rail passenger service would travel between Helsinki and Northern Finland during the night including some stops at stations in the Helsinki metropolitan area. The proposed rail passenger service would travel partly on the same route going through the Helsinki metropolitan area, so the conditions for an economic equilibrium test laid down in Article 2 of the Implementing Regulation would be met. However, it is unlikely that the economic equilibrium of the contract would be compromised, as it is very doubtful that the customers of local commuter trains would begin to use the long-distance rail passenger service. A large share of passenger traffic in the Helsinki metropolitan area is made up of commuters, for whom the sparse departure and arrival times of the long-distance services would not be better than the local train timetables. In a reversed situation, a long-distance rail passenger service were provided on the basis of a public service contract, and a new competitive rail passenger service was proposed for the Helsinki metropolitan area. It would be obvious that the new service would not compete for the same customers as the public transport service.

The proposed new rail passenger service could also operate in its entirety along the same route, but with fewer stops at stations along the way than the transport service offered under the public service contract. This would facilitate fast travel times between the fewer stations. Such a rail passenger service could bring new customers to existing public contract services. Conversely, the new rail passenger service might operate on the same route with the public transport service, but stop at more frequent stations. In that way it could acquire new customers from bus transport and private motoring. In these situations, the result of the analysis depends on what share of the customer base for the new service is made up of new customers and to what extent they would also increase demand for the public transport service.

In the case of the last examples, it is appropriate to determine the impact of rail passenger services on demand for transport services provided on the basis of public service contracts, using, for example, demand elasticity as mentioned above.

4.2.5. *Impact of the new service's scope on the economic equilibrium of the public transport service*

If it is noted that the proposed new rail passenger service would likely compete for the same customers with the public transport service, it should be determined whether this would have a substantial impact on the economic equilibrium of the public service contract. The impact of the new service is assessed for the service covered by the entire contract, i.e. the size of the rail passenger service planned by the applicant is an important assessment criterion. If the applicant's maximum capacity (number of seats multiplied by number of departures) is very small in comparison to the comprehensiveness of the public service contract, the impact of the proposed new rail passenger service on the economic equilibrium of the contract cannot be considered substantial. In such a case, the impact on the profitability of transport services provided on the basis of the contract, or the net costs of a competent authority, could likely be minimal, even in the extreme case that the user numbers for the proposed new rail passenger service came directly from the customer base of services provided by public contract. Secondly, the same assessment can be conducted on the basis of user number estimates submitted by the applicant. In these situations, where the scope of the new service is small in relation to the public transport service contract, the determination of economic equilibrium can in many cases likely be completed without an actual analysis on the division of demand between the new service and the public transport service.

4.2.6. *Evaluation of the impact originating from overlapping demand*

The questionnaire on public transport service demand, mentioned in connection with the determination of overlapping, can be used for determining how large a share of public transport service customers would shift to the new service at the specified price level. A rough estimate on the change to turnover of services provided under public service contracts could be determined in the following manner

*current price * the number of tickets lost to the new service*

if it is assumed that public transport service ticket prices will not change. On the other hand, this estimate could also include an estimate on turnover, which is caused by a drop in public transport prices in response to competition, and, as a result, the rise in demand for the public transport service:

*change in price * elasticity of demand in relation to the price.*

As part of its analysis, the regulatory body could take into account for the bases of determining price changes and price related demand elasticity analyses, the estimates and predictions completed by the railway undertaking performing public contract service and/or the competent authority, as well as the entity, who proposed the new rail passenger service.

In principle, it is possible that the regulatory body may have to assess two or more applications for new rail passenger services that, at least in part, would compete for the same customers as the public transport service, but as separate entities would not compromise the contract's economic equilibrium. However, their joint impact would have a substantial effect on the economic equilibrium of the contract. Pursuant to Article 10, section 6 of the Implementing Regulation, the regulatory body can make a different decision on each application it receives, depending on their separate impacts on the economic equilibrium of the contract, their competitive impacts, the net

benefits and network impacts for consumers and their combined impact on the economic equilibrium of the contract.

When discussing the capacity of the rail passenger service planned by an applicant, it should be taken into consideration that the economic equilibrium test and the following decisions apply to the information specified in Article 4, section 2 of the Implementing Regulation. Pursuant to Article 3 of the Implementing Regulation, notable changes to an existing service, especially to the frequency of departures or a change to the number of stations, where the service stops, meets the definition of a new passenger service, meaning notification shall be submitted on these changes as provided in Article 4. According to recital 7 of the Implementing Regulation, changes to the pricing of a service should not be considered substantial, unless these changes conflict with a business plan submitted with a previously conducted economic equilibrium test and common market behavior. The method for determining what type of change is considered substantial in its entirety with regard to the existing service will be left up to the discretion of the regulatory body.

4.3. Adjustment of costs

In addition to taking into account the impacts that the proposed new passenger service would have on the user numbers for services provided on the basis of public service contracts, and, thus, on the turnover of the railway undertaking performing a service and/or further, based on contract details, on the net costs of the competent authority, one shall also take into consideration the possibility of the railway undertaking performing the public service contract and the competent authority to adapt their expenses to the reorganization of their operations. On the basis of the information it has received, the regulatory body will assess the possibility of operators to adjust their expenses.

The ability of the entities to implement any cost savings, such as those arising from the non-replacement of rolling stock reaching the end of its useful life, or staff, whose contract ends, are examples of methods to be considered for adjusting expenses. The average annual write-offs of rolling stock and the possibility of selling or renting extra rolling stock to other parties can be seen at the starting point. However, the resale market for rolling stock can be limited, especially due to Finland's track gauge. If a railway undertaking performing public service contract rents rolling stock from a separate rolling stock undertaking, the railway undertaking's possibility to terminate the equipment lease with regard to extra rolling stock will be assessed.

4.4. Value of exclusive rights

Article 10, section 3 of the Implementing Regulation lists the value of possible exclusive rights as one of the factors used for assessing economic equilibrium. However, according to Article 6, exclusive rights cannot prevent access rights being awarded to the new rail passenger service applicant, if the access right will in no way compromise the economic equilibrium of the public service contract in question. Pursuant to Article 3, section 6 of the Implementing Regulation, exclusive rights refer to the right as defined in Article 2 (f) of Regulation (EC) No 1370/2007 entitling a public service operator to operate certain public rail passenger services on a particular route or network or in a particular area, to the exclusion of any other such operator. Pursuant to Article 2 (a) of Regulation 1370/2007, public passenger transport means passenger services⁹ of general economic interest, provided to the public on a non-discriminatory and continuous basis. Pursuant to Article 6 of the Implementing Regulation, the regulatory body shall take the value of these exclusive rights into account appropriately, when conducting economic equilibrium tests.

⁹ Services of general economic interest (SGEI).

Exclusive rights are used for giving public passenger transport operators the possibility to strengthen their pricing power on the routes, for which the exclusive rights have been awarded. They can thus, for their own part, reduce the need for the payment of public support for performing a public service obligation. The value of exclusive rights is thus equal to the profitability deficit incurred by a railway undertaking, due to the performance of a public service obligation, which would have to be covered with increases to public support, if the operator were not awarded exclusive rights.

The value of exclusive rights will be taken into account in connection with the economic equilibrium test carried out by the regulatory body in the following manner: the economic impact of the new rail passenger service offered on the route, for which exclusive rights have been awarded, on the public transport service will be included in the public service contract's economic equilibrium calculation. In this case, the economic equilibrium test would ensure that the entry of a new passenger service that is similar enough and substantial enough in scope, would be restrained from entering the market on the same route, for which the public passenger service has been awarded exclusive rights. In this case, the new service would compromise the economic equilibrium of the contract that provides the exclusive rights in question. However, it is also possible, in this connection, to take into account the regulatory body's possibility for proposing changes to the new service, as specified in Article 11, section 2.

4.5. Evaluation of significant impact

Because the new rail passenger service will inevitably have impacts on public transport services that in part serve the same customer base, it shall be possible to define the size of the impacts that will be considered substantial. The values given by the rail undertaking performing a public service contract and a competent authority can be used as the starting point for determining the substantiality: the cost and turnover calculations provided in business plans and public service contracts, and, especially, the variances of costs, turnover and passenger numbers, as well as the annual variances that have already taken place during the contract's implementation period. The assessments on the impacts of the new passenger service on expenses and turnover that are within these frequency variations, which are considered normal by the relevant parties, cannot be considered substantial.

Impacts on a railway undertaking performing a public service contract also cannot be considered substantial, if the undertaking's profit for the provision of overall services over the contract's entire period of validity is reasonable. When the contract in question is public service acquisition pursuant to Article 5, sections 2, 4, 5 or 6 of Regulation (EC) No 1370/2007, with no tendering, a reasonable profit¹⁰ requirement, mentioned in Regulation's Annex, is applied to it pursuant to Article 6, section 1 of the Regulation. In this case, a reasonable profit will act as the maximum limit for profit for the services provided on the basis of the contract by the railway undertaking. Thus, as the new service impacts the public transport service and affects the railway undertaking, the profitability of the railway undertaking falls below a reasonable profit, although the impact of the new service was not substantial. Thus, a reasonable profit cannot act as the minimum profit a railway undertaking shall achieve in the assessment of economic equilibrium. Additionally, the application of a reasonable profit is challenging in situations, where an undertaking uses rented rolling stock.

The assessment of what is a substantial impact is carried out case-specifically taking all factors into account, and an individual criteria or percentage that is independent of other factors is not significant. In most cases, an impact that is sufficient for prohibiting the entry of the new service to the market, i.e. a substantial impact, will

¹⁰ A rate of return on capital that is normal for the sector in a given Member State and that takes account of the risk, or absence of risk, incurred by the public service operator by virtue of public authority intervention.

likely settle at a level, where the lower limiter is a negative profit by the railway undertaking just below a net profit of zero for the entire contract period, and the upper limit is a profit level just below a profit, which the railway undertaking has verifiably set as its minimum profit and which is at the level of a reasonable profit, when using its own rolling stock and at the level of a comparable level, when using rented rolling stock. However, in this context, this type of profit level does not need to be determined in detail in accordance with the standards of reasonable profit. The limit for substantial impact is in any case lower than the profit level in question.

The conditions during a public rail passenger service contract period may change from what was originally planned. The determination of economic equilibrium only takes into account the impact of the new service and does not give an opinion as such on the economic result of the public transport service contract nor the risks to development of business.

Additionally, the assessment criteria should to some extent be neutral with regard to how risk-sharing is implemented in the contract. Thus, when risk-sharing in a contract targets the risk at the competent authority, an effort can be made to determine the scale of the substantial impact, for example, by first simulating the situation, in which the impact is targeted at the railway undertaking. After this, the economic conditions that apply to the competent authority could be assessed separately. After all, this issue often concerns scaling the public support.

4.6. Other impacts of the new passenger rail service and decision on right of access to infrastructure

Pursuant to recitals 8 and 16 and Article 10, section 5 of the Implementing Regulation, in addition to determining the economic equilibrium of a public service contract, the regulatory body shall assess the following impacts of the new rail passenger service:

- the net benefits to consumers in the short and medium term;
- the impact on the performance and quality of railway services;
- the impact on timetable planning for railway services.

If it is found that the new rail passenger service will compromise the economic equilibrium, but it is also determined that the new passenger service would result in substantial benefits to consumers, Article 11, section 2 (b) states that the regulatory body can give recommendations to competent authorities on changes other than those that would impact the new rail passenger service, which would make it possible to award right of access.

The regulatory body often only has the estimate provided by the rail infrastructure manager, when assessing the impact to the performance and timetable planning of railway services. Specialized rail capacity and possible priority criteria (for example, the synergic passenger transport entirety) should also be taken into consideration.

The impacts on the consumers' net benefits and the railways services' performance, quality and scheduling are additional factors that could be taken into consideration, when making decisions, in addition to the results of the economic equilibrium test. These do not as such directly impact the economic equilibrium test, but they can potentially either weaken or strengthen the weight of economic equilibrium related impact in decisions concerning right of access to railway infrastructure.

The additional criteria means that it is not appropriate to allow an operator that would substantially weaken the performance of railway services to enter the market, for example, due to overloading of capacity. On the other hand, the economic equilibrium test also examines the possibility to adjust the scope of a service provided under a public service contract, which could free up capacity. Finally, the rail infrastructure manager will be left with the option of examining the matter also at the capacity

allocation stage. It is possible that the new rail passenger service would reduce passenger numbers on the routes covered by public service contracts or on alternative routes. This could potentially happen, if the entry of the new rail passenger service to the market resulted in a situation, where a section of the rail network covered by the contract exceeded its maximum capacity in a way that had notable negative impacts on the rail network's performance capacity, for example, in the form of travel times.

The net benefits gained by consumers are a factor, on the basis of which primarily a recommendation is given to a competent authority, and they are not included in the economic equilibrium test. The net benefits noted in international assessments are, for example, a lower price, more frequent traffic and faster travel times. When net benefits are substantial, they can be taken into consideration as a factor, mainly, when setting the limit, at which point the impact on economic equilibrium could be considered so substantial that it will lead to denying the new service entering the market.

4.7. Capacity of the regulatory body to propose changes to the new rail passenger service

Pursuant to Article 11, section 2 (a) of the Implementing Regulation, the regulatory body shall, as appropriate, indicate possible changes to the proposed new rail passenger service, if there is any indication that economic equilibrium will otherwise be compromised. The section gives examples of such possible changes including modification of frequencies, paths, intermediate stops or schedule. This is an example-like list of conditions, which the regulatory body can set for approving right of access applications, and it should not be interpreted as being exhaustive.

In a situation, in which the new rail passenger service demand overlaps with the public transport service demand and the economic equilibrium of the contract is considered compromised, the regulatory body could permit the new rail passenger service on the condition that the operator gives up some of the stops overlapping with the public transport service.

4.8. Payment for conducting an economic equilibrium test

The regulatory body will charge the entity that requests an economic equilibrium test a fee for conducting the test. The amount of the fee is listed in the Ministry of Transport and Communications Decree on chargeable transport services, and is based on the time used for the processing of the case in question and the regulatory body's hourly charge. Additionally, the costs of a possible study acquired from external expert organizations (for example, a demand elasticity study) shall be charged from the entity that requested the test, from the time that these costs have been included in the Ministry of Transport and Communications Decree on chargeable transport services.