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COMPETITION COMMITTEE****Working Party No. 2 on Competition and Regulation****Summary of Discussion of the Roundtable on Competition and Innovation in Land
Transport****28 November 2016**

This document prepared by the OECD Secretariat is a detailed summary of the discussion held during the meeting of the OECD Working Party No. 2 on Competition and Regulation on 28 November 2016.

More documents related to this discussion can be found at www.oecd.org/daf/competition/competition-and-innovation-in-land-transport.htm

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Summary of Discussion

By the Secretariat

1. Introduction

The **Chair** of Working Party No 2 (WP2), Mr. Alberto Heimler, opened the roundtable on competition and innovation in land transport by introducing the speakers and explaining the aims of the roundtable, which was devoted to discussing recent developments in rail and road transport.

The Chair noted that there have been developments regarding both intermodal and intramodal competition in land transportation. As regards intermodal competition, rail has been strongly revitalised with the advent of high-speed services, which provide strong competition to air transport for distances below 1000km. At the same time, bus services are providing cheap alternatives for traditional rail services and, in many countries, to private cars as well. The general picture is that, at least for medium distances, different means of transportation exert competitive pressure on one another. Concerning intramodal competition, the main policy developments have focused on the vertical separation of rail, the liberalisation of air transport, and the deregulation of bus services.

While the main goal of these policy initiatives has been to increase intramodal competition, one of their main consequences has been to increase intermodal competition. As the same time, in many countries there are still unjustified regulatory constraints that restrict intermodal competition. Examples of this are ticketing across different means of transportation and domestic cabotage in road transport. Ultimately, these policy developments will in the future interact with technological innovations such as the automation of transport, including driverless vehicles and platooning.

2. Intermodal Competition

The Chair then introduced the first sub-section of the discussion, on intermodal competition in transport. Many developments have taken place since the Working Party last approached the issue. High-speed services have become widespread, buses have been liberalised, and platforms providing taxi and car-sharing have emerged. At the same time, pricing issues are still a problem, as are regulatory obstacles to the introduction of competition through platforms.

The Chair called on **Professor Marco Ponti** to give a presentation on the roles of the market and governments in the development of transportation systems. Professor Ponti began by noting that transport liberalisation has had a great impact in the adoption of operational improvements. Technological innovations, however, have very often been driven by the military and the state. Furthermore, it is unclear what role competition plays in promoting innovation.

He then moved on to review the three main arguments against liberalisation and in favour of supporting certain modes of transport over others. The first argument focuses on promoting equality of access, and is not very convincing: in practice, such policies end up subsidising those who already have medium to high incomes. The second argument invokes environmental concerns to subsidise rail and electric vehicles. However, there is evidence that taxing vehicles and fuels (“polluter pays”) is a far more efficient and effective tool to address this concern; and, in Europe at least, recent studies indicate that

polluters are already paying for externalities. The third argument revolves around road congestion, but, again, road pricing is much more efficient in dealing with road congestion than attempts to reduce it via subsidies to other modes of transport. Furthermore, technology is moving towards making road pricing easier.

Ultimately, the core of the fight against liberalisation is a result of regulatory capture. While this may be a natural outcome of democratic processes, it is also clear that subsidies are not justified from an economic perspective and reduce competition. A good example of this is the evolution of the rail market, where – due to the fact that the infrastructure is a natural monopoly that allows exerting control over transport services – innovations and competition have not been adopted even though they have been available and on the agenda for over 30 years. In road transport, on the other hand, rapid innovation is occurring, even as it faces a number of regulatory obstacles: for example, while buses are mainly used by low-income people, they're taxed with tolls, gasoline taxes, and so on.

Professor Ponti then finished with some tentative recommendations. First, every market failure is better addressed directly than through subsidies. Thus, one should attempt to implement homogeneous pricing rules for different transportation modes. Secondly, competition policy should be devoted to promoting new entry. This includes not only advancing certain regulatory policies – e.g. regarding road pricing, the adoption of pro-competitive common standards – but also adopting enforcement action to prevent further integration of certain sectors such as rail.

The Chair thanked Professor Ponti, and asked **Ms Susanna Metsalampi** to present the new Finnish transport code, which attempts to address some of the issues mentioned by Professor Ponti. Ms Metsalampi explained that Finland is engaged in a total renovation of its transport market legislation. This renovation is driven by the need to make sure that legislation does not prevent digitalisation, automation and innovation, while also creating a system which is customer-centric.

In this context, Finland decided to move from mode-specific regulation towards regulating the transport system as a whole: this includes not only infrastructure and the different transportation modes, but also data. Thus, Finland is creating a system that deals not only with traditional providers of transportation, but also with operators who create and combine new services, e.g. creating transport chains and offering different kinds of solutions for end users. The focus is thus on “mobility as a service”, on eliminating modal silos, and on opening the doors for the development of new, innovative transport services.

Consumers must be able to have access to ticketing options, payment systems and interfaces that are open to third party service providers. Finland considers that, to promote competition, the most important element is making essential data on services available to all operators. This will allow customers to compare and combine offers, while also allowing new service providers to develop better services for end-users. A second focus is on reducing bureaucracy, by simplifying and eliminating licensing procedures, while simultaneously adopting one set of rules for everyone. A last important element of the reform is to ensure that rules are technology neutral.

The **Chair** thanked Ms Metsalampi. He then addressed France, where the competition authority has advocated for the elimination of restrictions on cabotage and on the provision of bus services in certain circumstances. He asked about the reasons behind the identification of these circumstances in the competition authority's recommendations.

France explained how it pursued a sectoral study of bus services in 2014, which led to a number of recommendations, including on cabotage. A 100 km limit was adopted by the

legislator, but this was lower than the limit recommended by the Authority. Regarding the development of an economic balance test for the creation of bus lines, this reflects the sectoral regulator's concern about the sustainability of existing services. France also referred to a study of the impact of these changes conducted by the sectoral regulator, which showed that these changes have led to increased services and to the creation of new jobs.

The **Chair** then asked France about the rules for the authorisation of certain Uber services – and in particular about the distinct legal treatment of taxis and of other services provided by private vehicles. **France** answered that the authorisation of different types of Uber services follows the national law on transport services provided by private vehicles.

At this point the Chair turned towards Spain, where car sharing services have begun to operate. **Spain** is working actively to address the accelerated innovation and increased transparency in the transport market. A successful example of this is Car to Go, a platform that leases electrical vehicles cars in Madrid through a mobile app. The competition authority has also been working on these innovative markets, starting with a study on platforms and the sharing economy in 2013. While there have been some protests against platforms such as Uber and Cabify, there are really no barriers to entry in this market, even if some cities have tried to impose administrative fines on new entrants for failure to obtain the required licenses. The competition authority is also working with the administration to try to improve existing regulations applicable to transportation services.

At this point, the Chair opened the floor to all speakers. **Argentina** asked whether other agencies found advocacy to be as crucial as pursuing antitrust cases, particularly given the role of infrastructure. **Finland** explained that the competition authorities had been quite active on this front and played an important role in how the Finnish legislator opened the taxi market. **Professor Ponti** reiterated his previous points that externalities should be addressed directly, and that existing regulatory and subsidy systems distorted intermodal competition. **Finland** was asked whether its efforts to increase transparency may not create possibilities for collusion on prices and softening price competition, and whether it had adopted any mechanism to prevent this outcome. It replied that information on pricing was already made available to the public, and that its focus was on making it machine processable in an open interface where such information would be available to all and any who want to use it. Nonetheless, transportation providers were anxious about having to reveal their business secrets or business patterns through these open interfaces, so Finland limited access to information so as not to disclose business secrets.

3. Different Transport Modes

At this point, the **Chair** moved the discussion along to focus on the various different modes of land transport.

3.1. Introduction

This section began with a presentation by **Steve Perkins** from the International Transport Forum, a sister organisation of the OECD. The focus of his presentation was to analyse the circumstances where barring entry might bring welfare benefits, and compare that to situations where barriers to entry simply create rents.

The presentation began with a summary of competition policy's general objectives with regards to entry barriers. While the main focus of competition policy is on removing such

barriers, for natural monopolies the goal is instead to regulate in order to produce outcomes that are as close to the result of a competitive market as possible. Evidence shows that structural approaches to creating competition, either in or for the market, have proved more successful than behavioural approaches. However, regulation in this area requires a lot of expertise, and its success is dependent on the capacity of the regulator and its independence to do its job.

At this point, he provided two examples of situations where welfare would likely be undermined if there were no barriers to entry. The first example concerned Mexican freight railways, where the government owns the infrastructure but leases it to vertically-integrated train operators which look after the track and run trains through a series of exclusive concessions. A second example concerned the United Kingdom, which adopts a similar approach to passenger rail franchises. The exclusivity of a large part of the networks preserves the incentive to invest, but most of the markets are subject to some form of competition. In Mexico, while regulators are theoretically able to intervene to set prices as and when necessary, they have never developed the capacity for effective intervention. The granting of access rights across the system was considered, but that would have removed a large part of the incentive to invest and would have complicated the operation of the rail services greatly: the reliability and quality of the services would quite rapidly be undermined and the outcome would probably be that the State would have to step in to fund the infrastructure, or at least to a large proportion in the way that it does across Europe. In the United Kingdom, while there is little structural geographic competition – which otherwise exists in Mexico – this is compensated by periodic competitive tendering for exclusive franchises. At the same time, the United Kingdom has a fairly well resourced rail and road regulatory office which regulates on the basis of a series of quite transparent considerations provided by law and supported by the periodic public release of reports.

He then moved on to look at another typical entry barrier, cabotage laws. These are frequently used to provide protection for national carriers by requiring a company to have a domestically registered ship and crew in order to be able to carry freight within ports of a country. Such restrictions exist not only for domestic shipping, but also for trucking, rail, and, to a lesser extent, aviation. In the European Union, despite the single market there are still significant restrictions to open and free cabotage in truck freight and bus services. Cabotage rules create inefficiency and rents that can be very difficult to overcome. The OECD and the International Transport Forum run a system of truck licenses which are used to try and ease this system, and other international bodies are trying to implement similar mechanisms in other areas of the globe.

Addressing road services, Stephen Perkins mentioned that taxis markets were traditionally closed to entry by means of exclusive concessions granted to serve a specific area. However, with the current IT developments, most rationales for restricting entry – such as maintaining safety, security and the quality of service – are being eroded and substituted by traceability and brand reputation mechanics provided by new mobility services. Regarding freight, truck automation is on the horizon, starting with platooning of vehicles. While platooning and freight automation have the potential to bring about very large welfare improvements, such developments will be resisted not only by intermodal competitors but also within the industry by small operators. Reasons will be presented to restrict entry, and it will fall to regulators whether such reasons are good or bad.

3.2. Rail Services

Following this presentation, the **Chair** addressed rail services. He began by noticing that it has been 30 years since deregulation and vertical separation in rail were first implemented as a means to promote competition for and in the market. Yet, not many countries have pursued these policies successfully. The Chair wondered this was because structural separation was ill conceived, or because competition and rail don't go well together.

He then introduced **Libor Lochman** of the Community of European Rail infrastructure companies. Libor Lochman started by pointing out that rail is the most energy efficient land transport mode. Yet, rail's market share vis-a-vis other transportation modes has remained stable over the last 30 years even as environmental concerns have increased.

He then pointed out that a crucial condition for the success of rail is the appropriate financing of the infrastructure – where there is investment in infrastructure, rail's market share is either stable or growing. As a result, financing – and, not surprisingly, prices – are much more important for the success of rail than whether infrastructure and rail transportation services are integrated or not. Further, while the focus has been for decades on intra-modal competition, intermodal competition has been relatively and unjustifiably ignored. Greater attention should be devoting to charging policies across transport modes, including relative charges, the internalisation of external costs, and fiscal policies.

Increased intramodal competition, however, should also be incentivised. An essential step in this direction is the harmonisation of the infrastructure's technical parameters and of the parameters for the authorisation of the railway equipment – steps which must be adopted at the international level.

Lastly, he reacted to the use of the word “subsidies” previously in the discussion. He considered that the word is misleading, since the issue is that it is the responsibility of governments to decide whether to invest in relevant infrastructures across all transport modes, and whether there should be a contract signed with a provider of the transportation services to operate that infrastructure – which will naturally include payments to compensate the losses made out of the operation – or whether the market should be completely open.

The Chair then called on **Sweden**, which rail transport system has gradually been transformed from a government monopoly to comprising competitive markets in all regions and submarkets. Sweden started opening its rail market in the early and mid-1990's, and fully opened it up in 2012. Rail freight cargo was fully competitive from 1996, and, while the incumbent was dominant for the first 10 years, today Sweden has 10 to 12 companies operating in this market and the incumbent's market share has decreased to around 50%. In these developments, Sweden benefitted from a good national and international market for rolling stock in freight.

Regarding passenger transport, competition for the market was introduced in the early 90s. While it started slowly, nowadays all markets in Sweden benefit from competition. The public transport authority established a joint rolling stock company, so that bidders could buy or rent all the rolling stock they required for engaging in public tendered railway traffic. Even though the incumbent still has a large market share, this will be probably go down to somewhere near 60% by 2017.

At this point the Chair called on **Russia**. Russia explained that the first plans to reform the railway sector appeared in the 1990s. In 2001, a structural reform program for railway

transport was adopted, following which the Ministry of Railways was abolished and an open joint stock company, Russian Railways, was created. Following these reforms, Russia now has more than 400 operators, 1 700 owners of freight wagons, and more than 170 private locomotives are owned by private companies.

Ensuring non-discriminatory access to the infrastructure is the greatest challenge in this sector. In order to ensure this, tariffs are regulated by FAS taking into account three components of freight costs: carriages, infrastructure and locomotives. The ultimate goal in this sector, which has been adopted by Russia's government, is the full development of competition in the Russian market by 2030.

3.3. Buses

The discussion then moved on to buses. The **Chair** noted that he would like to combine the discussion of bus and rail because, in recent years, bus services have become an alternative not only to private car and taxi services, but to rail services as well. Furthermore, the price of bus services have declined, in some cases quite markedly, at the same time as the network of available bus services expanded substantially.

He then gave the floor to **André Schwämmlein**, the CEO of Flixbus, which is a technology and mobility platform that provides services for a network of bus companies. The company is four years old and is a child of deregulation of the bus market in Europe. At the moment, Flixbus works with 250 mid-sized privately owned bus companies. They have created a network which profits from scale and size, and offers customers an attractive unified offering across Europe.

Flixbus competes across all modes of transportation – including car-sharing services and passenger rail. This includes high speed rail, even if competition is on price rather than speed since Flixbus targets mainly price sensitive customers. While initially Flixbus may have disrupted train services, the result was that train operators reacted competitively to the challenge by starting to offer Wi-Fi and other services, by extending their networks and by lowering their prices. Further, Flixbus' data indicates that they have increased the market, providing transportation services to people who would otherwise have been priced out.

André Schwämmlein then explained the importance of deregulation for a company like Flixbus. Fundamentally, if the market is deregulated they are able to enter it. Nonetheless, even in deregulated markets there are very long authorisation processes – usually taking three to six months. This same amount of time is usually required if one wants to change the bus schedule, even if by as little as 5 minutes. Yet another issue is the number of players benefiting from State support which are active in private markets.

The Chair then gave the word to the **United States**, where bus services have been a traditional means of transportation for many years, but where their usage has increased in recent years. Megabus entered the US market in 2006 and since then a number of smartphone applications providing parking, booking and tracking services have made the service more consumer friendly. A lot of these services have resulted from foreign entry. There has also been an entrepreneurial response to demand, with vans and private cars competing in underserved areas against subsidised busses, and with several cities experimenting with partnerships with Uber or Lift to subsidise rides in underserved areas or to provide access for citizens to get from their homes to rail stations.

Finland was asked by the Chair to comment on an alleged cartel by competing bus companies that precluded access to central ticketing and parcel facilities. This cartel consisted of a company owned by the Finnish bus and coach association, which had a nationwide network of bus stations, timetable information and ticket systems. The cartel prevented competing bus companies from accessing travel and postal services which, in certain roads, were essential to be able to run a profitable business. While the case is still pending, the Finnish Competition Consumer Authority has proposed that a fine of EUR 38 million should be imposed.

Turkey then described how it has 100 bus operators and a competitive market. Regarding long distance services, there have been a number of cartels which were influenced by a number of factors. First, the existence of unstable demand, with peaks during the holiday season, creates excess capacity that may facilitate cartel behaviour, especially during the low-demand periods. Secondly, bus operators must have offices in terminals, which leads to great transparency. This is aggravated by legislation that sets minimum tariffs for bus companies depending on the distance, and regulates the allocation of bus times and seats to bus operators. Lastly, the owner of a terminal may be also an operator in another, connected market, which may further limit competition.

Mexico then asked two questions. First, it noted that Stephen Perkins had said that entry barriers are acceptable to maintain incentives for investment and contain the need for State subsidies. What is the threshold, however, to determine whether the barriers are acceptable? Secondly, it asked André Schwämmlein to describe the type of deregulation necessary to make Flixbus' business model possible.

Stephen Perkins answered that identifying the threshold at which barriers to entry are no longer acceptable is the big question in this matter, and its answer requires a lot of work from regulators. It is important to note, however, that solutions adopted in one country may not translate into others. For example, Sweden's liberalisation of the rail sector has worked better than in other places because in Sweden the state pays for 90% of the infrastructure, leaving only marginal cost to be paid by operators. The same approach would likely not work as well in countries with other set ups. So there is not an off-the-shelf answer to Mexico's question.

André Schwämmlein identified two main regulatory obstacles to entrants like Flixbus. First, this can occur if a potential competitor – usually railways – is protected. A good example of this is rules allowing routes not to be open because they are sufficiently served, which meant that companies would ultimately be discussing the meaning of “sufficient”. This rule has been abolished in a number of countries, which has led to the flourishing of competition. The second obstacle is state concessions that restrict long-distance offers to routes between two cities. Having the state decide what the offering should be always creates inefficiencies, since it excludes the possibility of network that serves small cities and other niche locations being created.

At this point **Germany** intervened to explain that Flixbus' business model has led to a wave of mergers in the market which were not subject to merger notification despite Flixbus being based in Germany. The prevailing business models seems to be akin to Flixbus', according to which a tech company responsible for the organisation of the network and ticket sales subcontracts mid-sized companies that are the owners of the busses and carry on the business risk. Unlike what seems to be the Finnish approach, the German authorities still consider that, even if other modes of transport exert competitive pressure, the product market should be the market for long distance busses, since its customers are typically price sensitive but not time sensitive. The main entry barriers

seem to be the duration of license procedures with our different regional States. The German authorities are watching the market closely, and are very impressed by its fast development – the market has grown from 80 routes before liberalisation to 350 at present.

Turkey then also asked a question about whether Flixbus had to deal with operators with market power on bus terminals or other upstream markets. **André Schwämmlein** answered that, while in some cases a station operator is also a competitor, this situation includes not only bus stations but also rail operators. Nonetheless, they have not yet faced unfair or anticompetitive behaviours regarding terminals.

3.4. Taxis and Private Vehicles

At this point, the **Chair** moved the conversation along towards taxis, and called on Denmark to comment on its working group for taxi services. **Denmark** described how, after the competition authority having advocated for deregulation of taxi services for more than 15 years without any success, the new government's program includes the deregulation of taxi services.

Singapore explained that it applies a price cap on apps providing booking services for private hire vehicles. On the other hand, the booking fee charged by regular taxi services is not regulated. The reasoning behind this is that, if the app providers are given the flexibility to charge a higher booking fee, then regular taxi companies would charge the corresponding or higher booking fees and therefore drive up the fee for regular taxi.

Brazil explained how it received a complaint from the Taxi Association, and was thus obliged to open a case against Uber. The case was still ongoing, and it would be assessed under standard competition rules.

3.5. Trucking and freight

Following this short discussion, the **Chair** started the section on trucking and freight. He began by pointing out that, for many years, the big discussion in trucking was on how to promote intermodal services where goods would travel by rail over long distances while trucks would only provide pick-up and delivery services. The process would have required the creation of a common interface between rolling stock and trucks, and the development of reliable rail-freight services between cities. The Chair stated that he was unaware of any developments on this front, and that, in the meantime, technological developments were taking over.

The Chair then invited **Dirk-Jan de Bruijn**, from the Dutch Minister of Infrastructure, to present on work being pursued on platooning. Platooning occurs when trucks slip-stream very close one another. This is made possible by a combination of different automation technologies, combined with radar, camera and GPS technologies. The trucks communicate by wireless vehicle-to-vehicle, which reduces their individual response time to almost zero and allows them to drive close together safely. Truck platooning has many advantages. Platoons take up less space and don't overtake. This optimises road mobility and minimises traffic jams. Driving so close together also decreases the air drag, resulting in less fuel consumption and fewer CO₂ emissions. Given technological developments, platooning may also lead to substantive improvements in road safety.

Dirk-Jan de Bruijn provided the background for the truck platooning challenge which was organised under the umbrella of the EU Dutch presidency. The challenge saw platoons of

trucks of six large lorry producers in Europe traverse Europe on public roads. A video was displayed providing an overview of the challenge. The first platooning pilots and experiments were successful and look promising. However, in addition to technological developments, Dirk-Jan de Bruijn emphasised that international legislation which regulates factors such as the permitted degree of autonomy and allowable driving time will need to be amended. The logistics and operational aspects of road freight will also need to be properly regulated, as it seems that a platooning service provider will be responsible for certification and for acting as the central traffic co-ordinator for the truck platoons. In due course this will allow other trucks to join the platoon on the fly.

The **Chair** commented on how certain reasons advanced to invest on truck platooning, namely to minimise the impact of the high number of trucks that travel empty at any given time, are related to concerns about cabotage. He then mentioned that in Spain there is currently a project to improve the rail/road interface by promoting substantial investment in logistics.

Spain stated that its market for freight transport in rail was opened to competition in 2005. Nonetheless, the entrants were not particularly successful. The competition authority pursued a study which identified a number of problems, including: a very large market share by the incumbent, and an infrastructure operator that provided quasi-exclusive services at terminals; both the incumbent and the infrastructure operator being dependent on the same government ministry; a lack of logistic facilities for road and marine transport; inadequate access to rail at airports; and inefficient and costly last mile transportation to ports. This study contained recommendations to address these problems, some of which have been implemented and led to an increase in freight transport. Spain also expressed interest in promoting competition in trucking.

India intervened to describe how it attempted to increase competition in the taxi market. The competition authority intervened mainly by issuing recommendations, but it did investigate one particular case which revealed that incentives were being provided to private drivers to compete in the regular taxi drivers. The government is as a result considering imposing a cap on pricing. India then asked whether other jurisdictions had a similar problem.

The **Chair** explained that some countries have banned platforms, while others have allowed them. Others still have attempted to regulate platforms as taxi services and introduced requirements for drivers. He incentivised India to engage directly with a number of delegations who had experience on the topic.

Professor Ponti then intervened to express his view that, while everyone supports greening, it is more effective to deal with the issue directly by applying the “polluter pays” principle than by trying to foment modal change.

4. Conclusion

The **Chair** then concluded the session. He emphasised that the delegates had witnessed many technological and demand-driven developments, both in intermodal and intramodal competition. He also pointed out that competition advocacy efforts are important, as the benefits of intermodal competition are very much dependent on the degree of competition which is allowed to exist between different transportation modes. Lastly, the Chair thanked the experts, which provided substantial value-added to the discussion, the delegations that submitted a contribution to the discussion, and the secretariat for its background paper.