

SOME SPECIFIC OBSTACLES TO FUNDING & IMPLEMENTING OF TRANS-EUROPEAN TRANSPORT PROJECTS

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1 INTRODUCTION

Most major rail and road infrastructure projects are characterised by a lengthy construction period, large up-front costs, a long payback period, high uncertainties, and, at best, thin profitability, which renders financing of such projects through the private sector by no means an easy task.

The Trans European Network (TEN) projects involve several different administrative, legislative and political landscapes, and are often much larger. These exacerbate the problems and render the task of financing TEN projects through either the private sector or private-public sectors partnership arrangements substantially more difficult. Indeed, the trans-national character of the TEN projects leads to a number of complications which potentially could act as a structural barrier to their development.

These problems arise from the national parties involved in the project having different interests, divergences between the costs and benefits of the project to the Union as a whole and the costs and benefits to individual participants, the profitability of a specific link of the network being dependent on another link of the network being built, substantial differences in the project evaluation methodologies used across the Community, and the absence of a mechanism for redistributing costs and benefits between the participants.

Successful and cost effective promotion and implementation of the TEN projects calls for the development of appropriate policies to address these problems; in particular:

- developing a common set of project evaluation criteria and procedure which would be approved and used by all the individual Member States for project evaluation and selection;
- developing a mechanism for redistributing costs and benefits, including an appropriate compensatory machinery, which would require the beneficiaries to make certain contributions towards the new sections or to compensate the parties in the case of anticipated losses; and
- developing an appropriate institutional arrangement to promote, evaluating, and implementing such projects.

2 PROBLEMS WITH FINANCING TEN PROJECTS

2.1 Multiplicity of Institutional and Legal Frameworks

TEN projects involve several administrative, legislative and political landscapes. This renders the task of initiating and promoting such projects doubly difficult, and has a direct impact on the private sector's perception of the risks and uncertainties. In the long run these problems will reduce as EU integration proceeds. However, in the short and medium term many of these problems will persist and will act as an obstacle to implementing the TEN projects.

When it comes to developing a financing package for a typical TEN project, the number of unknown factors are numerous: the different administrative, technical and other frameworks governing all modes of transport, signing of treaties, voting and amendment of laws, issuing of decrees and national or European directives, the likely extent of delays in implementation, time lost in the to-and-fro between institutions, etc. As a result, 10 years is the normal period of time between a project being drawn up and its being put into effect.

On the financial front, the taxation question is of paramount importance in particular for cross-border projects. It is not only the absence of fiscal harmonisation, but also the fact that the concession-holders have to pay tax on their profits in their country of origin and not in the country in which the activity is carried out, i.e. on the basis of the nationality principle and not the territorial principle, which further skews the system of management for the new infrastructure.

2.2 Promoting the Project

Another problem in promoting a typical TEN project, for which the profits are often spread thinly, is that it is difficult for a participant, be it the private or public sector, to promote and administer the project. Since promoting the project will weaken its negotiating position with the other participants involved.

2.3 Scope for Gaming

Further problems in promoting and developing typical TEN projects arise because often there is considerable scope for complicated gaming possibilities, which, in principle, could delay the development of such projects. For example, the last link in a network may be particularly profitable having the greater advantage of the existing or untapped traffic demand. Therefore, each Member State might wait for the other to make the first move, delaying the development of the network.

2.4 Conflicts of Interest

The network will have to be built section by section. In some cases this might not coincide with the national interest or with the particular interests of the individual Member States concerned which would prefer priority to be given to accelerating construction of the projects which are more profitable from their own point of view.

2.5 Network Effects

The profitability of a specific link of the network may depend on another link being built up. Without a well established mechanism for transferring certain costs and benefits between the operators of the sections in the existing network and those of the new sections, there is a risk of holding back network development.

2.6 Evaluation Methodology

Development of the network, including the redistribution mechanism, requires the use of a common evaluation methodology, which would evaluate the economic benefits of the project from the Community's viewpoint. This is particularly important for defining and drawing up the action programme. However, the evaluation methodology varies significantly across the Community countries. In particular, the Community countries have different rules for valuing private and public costs and benefits, and the Internal Rate of Returns (IRR) used for project selection varies widely across the Community, ranging from 3% to 8%.

The differences of approach to investment appraisal arise from various considerations, including:

- 1) differences in political philosophy, notably in policies towards public ownership, central planning and competition between modes;
- 2) the nature of stakeholder and interest groups whose interests would have to be taken into account;
- 3) differences in methods of analysis which have, to some extent, developed independently in different countries.

For instance, in the UK a general principle of competition is asserted by the requirement that road and rail evaluations should use the same discount rate (8%), but the detailed evaluation methods diverge considerably, particularly in the treatment of user benefits. In Germany surface transport is evaluated within a common framework with a broad range of common criteria for all modes. In the Netherlands the evaluation framework is goal oriented, i.e. projects are evaluated in terms of their contribution to the specified goals (e.g. accessibility, environment, etc.). In practice, this requires restraint on the road transport mode, and promotion of rail.

The influence of stakeholder works in complex ways. A major issue in this respect is how far transport policy should aim at regional development. For instance, in Belgium evaluations have to take into account the equality of the two regions as recipients of development funds. In France regional authorities also act as providers of finance for projects which benefit their regions.

With respect to evaluation methodology, the discount rate employed in evaluating projects varies widely across the Community. France, Italy and the UK use a discount rate (DR) of 8%. Spain and Greece use a lower rate of 6%. Ireland employs a DR of 5%, while Germany evaluates transport projects at a DR of 3%¹. Also, there are

significant differences in the treatment of user and non-user benefits. No country claims to include all socio-economic impacts in their monetarized cost-benefit framework, though the range of items included varies. The formal German evaluation framework carries out a consistent set of evaluations in real 'user benefits' terms; but, benefits to newly generated user are not included. In the UK and the Netherlands *international* user benefits are excluded from published evaluations. A similar approach is adopted in Belgium for national funding purposes; but, such benefits are considered as relevant for international funding purposes.

There are a wide range of other disparities in undertaking impact assessment. For instance, the definition of value of time is not always completely consistent. Sometimes the disutility element of time may be valued separately, or by an unexplained modal preference function. Theoretical problems arise in treatment of uncaptured user benefits. Many countries are reluctant to give different values to the same benefit to different citizen², and therefore use 'equity' values for benefits to all. For instance, the German approach adopts 'equity' user values of time, while SNCF uses behavioural values for user benefits in its own evaluations. The bases of 'equity' values are also not always comparable, particularly as countries differ in their conventions on break-down of non-work journeys³.

3 REDISTRIBUTION MECHANISM

The transnational character of TEN projects, combined with possibilities of conflict of interest between the national participants, and the potential differences between the costs and benefits of the project to the Community as a whole and its costs and benefits to an individual participant, point to the need to establish a mechanism for redistributing costs and benefits, in conjunction with an appropriate compensatory machinery. Such a mechanism, for instance, would require the beneficiaries to make certain contributions towards the new sections, or to compensate the parties in the case of anticipated losses. A major challenge in developing such a mechanism is the development of methods for attributing to each section the network effects it is expected to generate

4 ALTERNATIVE APPROACHES TO PROMOTING & FUNDING THE TEN PROJECTS

4.1 Project Specific Agreements Between Member States

To date the development of TEN projects has largely relied upon the ad hoc arrangements between Member States which have formed the basis for developing international transport systems. For instance, such arrangements have formed the basis for the Eurotunnel and Oresund projects. The role of the Commission in such a framework is to encourage proper network evaluations of projects by the Member States concerned; and generally to act as a facilitator or possibly an arbiter in the case of failure to agree on issues such as the sequencing of project construction and the distribution of the financing burden.

4.2 International Service Agreements

An alternative approach would be to adopt the traditional system of international service agreements, with certain modifications to make it suitable to the network requirements. For instance, each country would finance its own infrastructure and supply the rolling stock in proportion to the time spent on its territory, with revenues being shared between the parties through a network agreement. Private participation in the project, including financing, would be promoted within each country through the national promoter with the assistance of the EU to harmonise the process.

4.3 Trans-European Agency

A third approach, which is favoured by the Commission as the solution to the problems arising from transnationality of the TEN projects, would be to establish a community/transnational agency which would evaluate projects from the Community's view and determine how any required public sector financial support for the project should be distributed between the Member States concerned.

The function of such an agency could include:

- provision of the necessary impetus for network development;
- the establishment of redistribution methodologies for the network effects;
- the coordination of Community contributions towards completing the network projects; and
- the seeking out and refining of new financing instruments.

The agency might also be given other functions such as providing technical assistance to promoters.

In support of this option, it could be argued that, compared to other possible "solutions", such an agency would benefit from economies of scale and scope in carrying out these activities. On the other hand, however, it could be argued that such an agency would simply create a further layer of bureaucracy, since in practice, Member States would be unwilling to cede influence on "strategic" decisions regarding network development to any supranational agency. Also the agency could only function on the basis of agreed evaluation criteria, and rules for distributing benefits and financing costs. Yet if agreement could be secured on these issues, a major obstacle to using existing frameworks and institutions would be removed, and the incremental benefit of establishing a new agency significantly reduced.

REFERENCES

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2. European Commission, Directorate General for Transport (October 1994), Financing of the Trans-European Road Network, *Transport Infrastructure Committee, Motorway Working Group*.
3. European Commission (June 1993), High Level Group for High Speed Rail Network, Background Document on Financing the European High-Speed Train Network, *European Commission, Director General for Transport, Finance Sub-Group*
- 4 Ian Jones, Hadi Zamani, Rebecca Reehal (1995), Financing Models for New Transport Infrastructure, a Report for DGVII of the EU, *National Economic Research Associates, the UK*.

NOTES

1. In Germany , use of low discount rate and capital rationing gives bias to long term projects.
2. Which would mean giving greater weight to benefits of the rich.
3. For example, does shopping count as leisure?