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Methodology for the economic equilibrium test of public service contracts pursuant to Article 12 of Legislative Decree No. 112/2015 and Article 14 of Commission Implementing Regulation (EU) 2018/1795

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METHODOLOGY

1. Scope and procedure of the economic equilibrium test

- 1.1 This document illustrates the methodology applied by the Transport Regulation Authority (hereinafter: Authority) to perform the economic equilibrium test (hereinafter also: EET) pursuant to Article 12, paragraphs 5 et seq., of Legislative Decree No. 112 of 15 July 2015, by defining the pre-established criteria underlying the relevant decision.
- 1.2 The objective scope of the methodology includes new rail passenger services provided on network infrastructure that is already used by operators holding public service contracts. These encompass both entirely new services on an origin-destination relation and services that substantially change an existing rail passenger service, in particular in terms of variation of frequencies, number of stops or time slots.
- 1.3 The applicant for a new rail passenger service and the entity requesting the economic equilibrium test of the public service contract fall within the subjective scope of application of the methodology, as specified below:
 - a) applicant entity: railway undertaking providing passenger services or undertaking providing rail passenger services on the basis of commercial agreements with railway undertakings, both separately or combined with passenger services of different modes and types (scheduled and non-scheduled), that has notified the Authority and the concerned rail infrastructure manager of its intention to operate a new rail passenger service;
 - b) requesting entity:
 - b.1) any entity that has awarded a public service contract for a rail passenger service on the route of the new rail service or on an alternative route pursuant to Legislative Decree No. 112/2015;
 - b.2) any railway undertaking providing services under a public service contract on the route of the new rail service or on an alternative route;
 - b.3) the manager of the rail infrastructure on which the new rail service is, wholly or partly, planned.
- 1.4 The procedure to notify a new rail passenger service by the applicant entity, to submit the request to implement an EET by the requesting entity and to carry out the EET is governed by Commission Implementing Regulation (EU) 2018/1795 of 20 November 2018 and by Articles 12, 12a and 24 of Legislative Decree No. 112/2015, and, insofar as it is not provided therein, by paragraphs 2 and 3 of the present methodology.

2. General principles for the implementation of the economic equilibrium test

- 2.1 Upon receipt of a request to implement an EET, the Authority shall initiate the relevant procedure to assess whether the new rail passenger service would have a substantial negative impact on the economic equilibrium of the public service contract. This assessment considers the impact of the new service on the profitability of the public service contract of the undertaking providing the public service and/or on the net cost for the competent authority awarding the public service contract. The analysis is carried out by assessing the impact on the public service contract as a whole and for the entire contractual period.

2.2 Taking into account the outcome of the consultations referred to in article 12, paragraph 6, of Legislative Decree No. 112/2015, the Authority carries out its assessments by preliminarily verifying the novelty of the service offered and the eligibility requirements of the request to implement an EET of the new service; in case of positive verification of both, the Authority assesses the actual substitutability between the new service and the services covered by the contract under public service obligations (hereinafter, also PSO), and further evaluates the impact of the new service, including by considering the net benefits arising from its introduction, with particular reference to: net benefits to customers; social and environmental benefits; network effects, not only on the rail network management, but on the transport system as a whole.

3. Procedure for the implementation of the economic equilibrium test and assessment criteria

(i) Assessment of EET admissibility

3.1 Within one month of publication of the notification on the Authority's website, the railway infrastructure manager concerned shall notify to the Authority and the applicant entity the reasoned outcome of the assessment of the general technical and operational consistency of the new service. This is carried out – according to the procedures referred to in the network statement – exclusively with regard to the technical and operational features of the infrastructure concerned, without considering its current and prospective levels of allocated capacity, by indicating any technical changes that are necessary for the notified service to be scheduled into operation.

3.2 Where the characteristics of consistency referred to under 3.1 above are in place, the Authority assesses whether the rail passenger service qualifies as a new service within the meaning of paragraph 1.2, and, if so, evaluates the eligibility of the request to perform the EET.

(ii) Assessment of EET eligibility

3.3 The request to implement the EET shall not be admissible if one of the following conditions is met:

- a) the ratio between traffic revenues and operating costs of the PSO contract, net of the charge paid to the railway infrastructure manager, is below the thresholds as defined according to the applicable legislation;
- b) the PSO contract expires in the period between the entry into force of the relevant working timetable of the new service and the following 12 months; in the case of a service contract that is subject to extension, the deadline coincides with that of the extension if:
 - (i) the extension is provided for in the contract,
 - (ii) was exercised prior to the notification of the new rail service to the Authority and
 - (iii) the Economic and Financial Plan is updated in accordance with the new duration.

In case of ineligibility, the Authority shall reject the request to implement the EET and shall accordingly inform the parties concerned on a reasoned basis.

3.4 In case of eligibility of the request, the Authority shall verify the substitutability of the service.

(iii) Assessment of substitutability

3.5 The Authority shall assess whether there is effective substitutability between the new service and the services covered by the PSO contract. This assessment is carried out by verifying the substitutability

on the demand side, by considering: scope of the service, origin/destination relations served, ability of the new service to produce new demand for travel, existing liberalised rail services operated by the operator of PSO rail services, travel times, timetables and time slots, daily and weekly frequencies, number and proximity of stops, number of connections, level of theoretic capacity of the supply, level of available fares and tickets by type of user.

- 3.6 The criteria referred to under 3.5 above are applied to verify the substitutability also where the new service qualifies as being “of high value”, and therefore such to justify the presumption of characteristics of non-substitutability with PSO services. A new service shall be understood as being of high value if the following characteristics are in place, even separately:
- a) integration in a commercial package (including a single ticket or travel pass) of several transport modes and types (scheduled and non-scheduled) and different services;
 - b) high technical and/or commercial quality standards offered to users, that are related to: level of comfort, on-board services, customer service, conditions for reimbursement, higher commercial speed, reduced travel times.
- 3.7 Where no sufficient degree of substitutability is observed, the Authority shall conclude the EET and grant access to the new service, by informing the parties concerned about the findings of its assessments. Otherwise, it shall assess the net financial impact on the public service contract and the existence of any other advantages and benefits associated with the introduction of the new service.
- (iv) Assessment of the net financial impact on the public service contract and of the existence of positive effects arising from the introduction of the new rail passenger service*
- 3.8 The Authority shall assess the degree of negative impact on the public service contract based on: revenues from the services provided by the railway undertaking under the public service contract; net cost for the awarding entity.
- 3.9 For this purpose, the Authority shall assess the net financial impact, considering the public service contract as a whole, based on the following criteria:
- a) level of traffic that is estimated to be diverted from the PSO contract due to the new service;
 - b) risk matrix of the public service contract;
 - c) deviation between total revenues as provided for in the economic and financial plan of the undertaking performing the public service contract and the estimated revenues following the entry into operation of the new service;
 - d) actual degree of efficiency improvement of the services and achievement of Key Performance Indicators that are determined according to the criteria and principles set out in the Authority’s decision No. 120/2018 of 29 November 2018, if they are provided for in the public service contract. Otherwise, the efficiency parameters that are determined by the methodology set out in Annex 1 of the above-mentioned decision shall be applied to the operating costs of the PSO services;
 - e) other variations in the costs and revenues of the manager of PSO rail services, resulting from any changes in level of production of the service, turnover of personnel and investment plan for rolling stock, as well as any competitive responses and changes in other investments provided for the public service contract;
 - f) network effects concerning the impact on the services covered by the public service contract, arising from the introduction of the new service, also in respect of any application of integrated ticketing, including multimodal, that facilitates the use of the connections between services

operated by different operators, and relating to the increased frequencies on a given origin/destination relation that are determined by the new service.

3.10 The Authority shall assess the existence of positive effects arising from the introduction of the new rail service in relation to:

a) net benefits for customers:

- direct benefits for users of the new rail service (in terms of technical and commercial quality, reduced overcrowding, use of integrated and differentiated fares, shorter travel time, more choice in terms of timetables);
- indirect benefits for users of rail services other than the new rail service (in terms of performance and quality);
- other effects, due to positive externalities, such as reduced road congestion, accidents and polluting emissions depending on the share of demand diverted from private mobility, with positive effects in terms of improved collective mobility on the territory concerned;

b) impact of the new rail service on timetable planning, service performance and quality, by considering:

- new origin/destination relations generated by the new service or due to the correlation between new and existing services, including any interference of the new service with the existing timetable grid;
- improvement of travel times and frequencies in the relations served by the new service.

3.11 Upon conclusion of the assessment, the Authority shall inform the interested parties of the findings and reasons for its decision, specifying, in particular, the degree of negative impact on the public service contract and the net benefits arising from the introduction of the new service. By this decision, the Authority may either grant access, including with modifications, or refuse it.

3.12 By its decision referred to under 3.11 above, the Authority may, in particular, indicate any changes to the new service that would ensure compliance with the conditions governing eligibility for access, including any information requirements to monitor the impact determined by the new service; it may make recommendations to the awarding entity concerning other changes that would ensure compliance with the conditions governing eligibility for access, in particular in the light of the analyses of the net benefits for customers arising from the new rail passenger service, including the application of any compensation rights.

3.13 The Authority's decision shall specify the conditions under which interested parties may request a review of the decision within one month of its notification. The powers referred to in Chapter IV-a of Law No. 241 of 7 August 1990, and in Article 37 of Legislative Decree No. 112/2015, shall remain unaffected, in particular if the new service has been later significantly modified compared to the characteristics that were analysed by the Authority or if there is a substantial difference between the actual and estimated impact of the new service on the public service contract.

4. Final provisions

4.1 24 months after the publication of this methodology on its website, the Authority shall assess whether an update is needed based on the results of the initial application.