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1. Status report on rail privatisation

Reaching a dead end

Four Federal Ministries (Economic, Home Office, Consumer Protection and Justice) have expressed serious constitutional and legal accounting concerns about the draft bill for the partial privatisation of DB AG, submitted on March 13, 2007 by the Federal Transport Ministry. 'Expressing concerns' means 'won't work'. The two BDI appraisals¹, also come to the same conclusion²: (1) Should the DB Group be allowed to enter the assets of the railway infrastructure into its balance sheet, then according to German and international accounting law, this is only possible if the state refrains from influencing transport policy. (2) If it does this, it will be breaching its constitutional responsibility as guarantor of the German railway infrastructure (Art. 87e GG).

The parliamentary experts' hearing on the question of the constitutionality of the draft bill took place on May 23. The conclusion they came to was: (a) The submitted draft bill is not in line with the German Constitution. The state must retain its scope for influencing the business policy of the infrastructure company. It would lose any scope for influencing policy or it would be unacceptably difficult if the state had to consider the interests of private shareholders. (b) The planned investment by private third parties in the equity capital of the *integrated* Deutsche Bahn would have the consequence that if the state were later to take back the infrastructure, it would then have to pay the Deutsche Bahn a

¹ Brief summary of the appraisal by Prof. Möllers and Prof. Schäfer:
<http://www.privatbahnen.com/pdf/BDI-Gutachten-kurz-26-04-07.pdf>

² BDI memo with the results of the appraisal:

<http://www.privatbahnen.com/pdf/BDI+Kurzzusammenfassung+Gutachten+Moellers+Schaefer.pdf>

value equalisation on top: The state would then be paying for something it had previously financed for decades, more than €130 billion in the last ten years alone. However, if the state were to take over full ownership of the infrastructure before external third parties invested in the rail group then this would cost the state nothing, because as the sole owner it has all the assets of DB AG at its disposal.

2. Where do we go from here? Is the ownership model under discussion again?

The FDP parliamentary group in the Bundestag has submitted a brilliant summary of the status of the legislation procedure including a legal and political assessment.³ At the end of the paper it is noted that the Bundestag's resolution from November 24 does not say that the DB AG must be the economic owner of the railway infrastructure. Accordingly, the solution to the problem might be to grant the DB group extensive rights of use (but not economic ownership). Extensive rights of use for the infrastructure can be shown on the balance sheet. In this case, the "railway infrastructure" which is a state-financed asset would then be in the hands of the state, but not in the hands of the IPO candidate. But in the cold light of day, this would be an *ownership model*.⁴ An arrangement could look like this:

- Ownership of the entire infrastructure: state
- A Licence Agreement between the government and the DB Netz AG (!), in which all the parties' rights and obligations are stipulated (comparable with Licence Agreement in UK)
- Management Contract between government/DB AG: DB AG temporarily administers the former DB Netz AG, e.g. for 5 years, unilateral extension option for the government.
- Defining goals (5-year plan), annual, independent examination of goals achieved
- 5/10-year plan for the socially compatible separation of the infrastructure manager (formerly DB Netz AG) from the DB Group.
- Complete transparency of the infrastructure manager immediately
- During the period of the Management Contract, track access and track charges are to be managed by a neutral office.

3. The Competition Report 2007 (1) A tiger never changes its stripes

Due to its exclusive dispatching authority about all knowledge of track use, the state railway is in the unique position in Germany of being able to quantify German rail transport. Neither the Federal Railway Authority (EBA), nor the Federal Statistical Office, nor the Federal Freight Transportation Office, nor the Federal Network Agency (BNetzA) are able to do this. Of course, there is a healthy amount of mistrust in this situation regarding the figures, even though developments in 2006 were very pleasing for the sector. However, if one asked the Federal Statistical Office about the market share of non-DB rail operators, one is given the (correct) answer that the DB has told the

³ http://www.privatbahnen.com/pdf/070511+FDP+BtFraktion_AK_Verkehr__Bewertung+d+GesEntwurfs.pdf

⁴ However, an IPO for the entire group *without* the railway infrastructure wouldn't work: Too much debt, too few assets, loss of the big spender (the state), who would be constitutionally (Art. 87e GG) obligated to rescue the Deutsche Bahn encase it encounters any serious economic problems.

authorities that it is possible to ascertain DB's market share from these figures; the publishing of DB market data, however, is solely a matter for the DB and not the Federal Statistical Office. - Once again, the DB purports to be a body with subjective rights just because over 10 years ago the state awarded its railway the 'AG' sticker: another reason to separate the infrastructure from the rail group and, as a state instrument of general interest, make it completely transparent. The Federal Network Agency should have the next competition report compiled by an independent third party which is allowed full access to DB AG numerical data.

Upcoming newsletters will successively deal with the figures and backgrounds. Here are the most infuriating points: The competition report very adeptly suggests that the allocation of tracks by DB Netz AG works seamlessly and without conflict. Only six disputed decisions were sent to the regulator for examination. - Not taken into account is the fact that the slots and routes of *annual tracks* are often discussed and disputed for months and that a private rail freight operator is not able to prove that it is discriminated by DB Netz AG for the benefit of DB Transport divisions. Before a disputed track decision is submitted to the Federal Network Agency, a formal conflict-resolution procedure is undertaken and each rail operator considers very carefully if he really wants to go through with it. Railways must transport not argue. On the other side, the cooperation between DB Railion and DB Netz is so close that there are even Railion representatives sitting in DB Netz's regional control centres influencing daily despatching. A dispute over tracks makes absolutely no sense for almost 900,000 *occasional tracks*.⁵ Here, the private rail operators are largely at the mercy of the goodwill of DB Netz AG's dispatchers⁶. Occasional transport, however, is just one of the main focuses of activity for private freight rail operators.

4. The DB Netz AG's Incentive Scheme

The opposite of goal-oriented

In Newsletter 2/06 (section 3: Remuneration Principles/Tracks), Network Private Rail criticised the DB Netz AG's incentive scheme as part of its rail network conditions of use⁷. The incentive scheme shall penalise poor performance of the players (ROs and RIC)⁸. Its aim is to create an incentive to reduce interferences and to increase the efficiency of the rail network.⁹ Since the new train schedule came into force (December 2006) delays caused by an RO will be balanced with delays caused by the RIC. One delay minutes is penalised by 10 cents *only*, for exercise purposes.¹⁰ A survey conducted by Network Private Rail found that the DB Netz AG attributed 20 times more delay minute to private rail operators than it did to itself¹¹. This turns the facts upside down and leads to the conclusion that the German rail network is in excellent condition. On the contrary: it is no secret that there are significant defects in the infrastructure. Nevertheless, and this is hard to understand: routes with temporary speed restrictions

⁵ Short-term track orders according to § 14, II of EIBV. According to this, a track offer must be made to an applicant 'immediately', but no later than in five working days. http://www.gesetze-im-internet.de/eibv_2005/___14.html

⁶ In our newsletter, the institutional deficits of the German railway system are discussed. But this has nothing to do with the fact that there are numerous DB employees which are extremely cooperative and helpful and implement their services in terms of the law, i.e. neutrally and not discriminating. The problems we are discussing and commenting on here should never vilify 'the' employees of the DB Group. On the contrary: without the many helpers at DB, new entrants would be in an even more difficult position.

⁷ http://www.netzwerk-privatbahnen.de/pdf/Infobrief2_06.pdf

⁸ ROs = Rail Operators; RIC = Rail Infrastructure Company

⁹ http://www.gesetze-im-internet.de/eibv_2005/___21.html

¹⁰ In the UK delay minutes cost 15 times as much.

¹¹ <http://www.privatbahnen.com/pdf/070402+Folien+NeztwPrivBahnen+zum+Anreizsystem.ppt#267.1>,

and track repair works are excluded from the incentive scheme. Therefore Network Private Rail asks, where is the incentive for infrastructure manager, if typical network defects are not penalised? if the infrastructure manager closes down tracks in both directions instead of just one track? if a repair takes 1 week instead of 2 nights? if it repairs in single shift only due to a lack of personnel or planning errors? if heavy machinery is incorrectly deployed? All this has no consequences for the infrastructure manager. Above all, the rail operators must transfer penalties for delays to DB Netz AG!

In the current incentive scheme, users of the railway infrastructure are the bad guys, at least as long as they don't belong to the DB Group¹². It looks as though preventing delays is of little importance to rail freight operators. That is wrong: no rail freight operator voluntarily causes delays. They are usually contractually obligated to their contractors to be punctual. In addition, longer travelling times cause massive reductions in profit.

5. The DB Netz AG's Incentive Scheme

A bad joke?

One could describe the incentive scheme as a bad joke if it wasn't for the penalties against private rail freight operators which, at only 10 cents per delay minute, would reach several thousand euros per month. In order to counteract the numerous unjustified penalties imposed by DB Netz AG, private rail operators have to employ additional personnel to make the (impossible) attempt to clarify circumstances to which it has no access. Many rail competitors have since given up checking hundreds of individual delay announcements each day in detail. But that is certainly dangerous as the state railway is merciless in calling in its debts. The fact that only employees of the DB Netz AG allocate delayed minutes on routes and in the regionally control centre, must be described as scandalous¹³. Those, who expected these employees are at least obligated to neutrality, are again mistaken: DB Netz AG's service regulations to train dispatchers contain the stipulation of averting unjustified payment demands for DB Netz AG¹⁴.

These are all the typical characteristics of a monopoly. They make it easier to answer the question as to whether it would be recommended to make the German rail network completely user neutral. It is also an illusion to believe that one could compensate for the absence of institutional separation with a strong regulation. The railway is not telecom or energy. Rail transport plays on the minds of thousands of people and on thousands of railway kilometres. This business, however, is not about bits and bytes or about kw/h x cents which can be managed and controlled virtually. Railway can not. Even at telecom and certainly in the energy sector one can monitor how problematic effective regulation is.

6. Image advertising by the state railway

At the expense of the general public?

Advertising by the DB AG is currently increasing inversely to its chances of floating on the stock exchange as an integrated group. For weeks, adverts have appeared in

¹² To date, no complaints about the incentive scheme have been submitted to the Regulator by DB Railion or DB Regio.

¹³ But the OVG Münster (13 B 2592/06, Resolution from March 26, 2007) sees that differently: *A train dispatcher (of DB Netz AG) has a good overview of operational workflows, has the corresponding experience and, therefore, appears particularly suitable for allocating the causes of delays.*

¹⁴ <http://www.privatbahnen.com/pdf/061200+DBN+an+FdI+wg+Abrechng+v+VerspaetungsMin.pdf>

Germany's large daily newspapers and magazines, sometimes with whole-page photographs, extolling the inner virtues of this state logistics company¹⁵. The costs of which may have reached double-digit millions. As welcome as such campaigns may be for the print media, they are dangerous: The DB AG has sometimes even avenged critical reporting by withdrawing their advertising. No comment is made here as to whether the DB is right to boast about its billion-euro spending or whether it is the German tax payer who has financed these investments. For private rail freight operators who are forced to give the state railway around 40-50% of revenues in the form of remunerations, the important question is whether they are also being forced to pay for DB's image advertising for its IPO. One may be interested to know how deep the Federal Network Agency will dive into DB AG's cost accounting, as part of their track charge regulation. According to today's given tools (legal basis, personnel, budget and the state's political will), it doesn't look good.

7. And finally

Bravery medal for the German Federal Court of Auditors

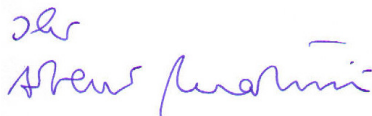
In newsletter 1/07, section 6, we reported on the draft of a report by the German Federal Court of Auditors (BRH) on the maintenance of the Federal rail network. The official report is now available¹⁶. On page 5, it also mentions the Federal Transport Ministry's attempted excuse that the Ministry cannot demand *any particular infrastructure quality* from DB and, anyway, the *German Stock Corporation Act* limits the state's influence on the business policy of DB AG. About which the BRH made the following statement:

The Federal Ministry has obviously misjudged its guarantee obligation in accordance with article 87e, paragraph 4 GG. According to which the state must take account of the collective good in extending and retaining the rail network. The Federal Ministry cannot defy this constitutional obligation by referring to the fact that ordinary legal and company law regulations restrict the possibilities of influencing the DB AG. Rather it must ensure that DB sufficiently fulfils its obligations in accordance with the law (Federal Railway Extension Act).

Until the next newsletter

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http://www.privatbahnen.com/index.php?option=com_content&task=view&id=51&Itemid=99



(Arthur-Iren Martini)

The English version of our last Newsletterth ==> http://www.netzwerk-privatbahnen.de/pdf/Newsletter1_07.pdf

¹⁵ "Each year the DB AG invests billions in Germany as a location", "No economic miracle without a transport miracle"

¹⁶ BRH Report dated May 9, 2007

<http://www.privatbahnen.com/pdf/070509+BRH+Bericht+zur+Instandhaltung+d+BSchienenwege.pdf>