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INLAND TRANSPORT COMMITTEE

Working Party on Rail Transport

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Item 8 of the provisional agenda

**STUDY OF THE SITUATION OF THE RAILWAYS IN MEMBER COUNTRIES**

Report by the Government of Serbia

1. The Programme of Work of the Inland Transport Committee for 2006-2010 adopted at its sixty-eight session (ECE/TRANS/166/Add.1, Item 2.5) requires the Working Party on Rail Transport to monitor harmonization of requirements concerning international railway transport including rail safety and facilitation of its operations. The present document is submitted for consideration by the Working Party in compliance with that mandate.

- I. DATA ON PAST AND FUTURE DEVELOPMENTS OF RAIL PASSENGER AND GOODS TRAFFIC
  - A. Transport activities in 2006
2. Participation of the passenger and freight transport in overall transport:
  - (a) passenger transport 17%
  - (b) freight transport 83%.

## 3. Participation of the national and international transport in overall transport:

- (a) national transport 28%
- (b) international transport 72%.

## 4. Realization of the transport activities during 2006:

- (a) volume of the passenger transport increased by 17.2%
- (b) volume of the freight transport increased by 12.5%.

Table. 1 Indicators of the realization of the transport activities in 2006,  
with plans for 2007

Indicators	Measure unit	2005. (in millions)	2006. (in millions)	Index (4/3)	2007-plan (in millions)	Index (6/4)
1	2	3	4	5	6	7
Overall transport	PTKM	4.334	5.078	117,2	5.510	108,5
Passengers						
Transported passengers	Nr. of passengers	13,46	14,11	104,9	12,05	85,4
Passenger kilometre	PKM	852	846	99,3	860	101,7
Freight						
Transported goods	Tons	12,57	14,14	112,5	15,28	108,1
Netotons kilometre	NTKM	3.482	4.232	121,5	4.650	109,9

## B. Planned transport activities in 2007

## 5. Participation of the passenger and freight transport in overall transport:

- (a) passenger transport 16%
- (b) freight transport 84%.

## 6. Participation of the national and international transport in overall transport:

- (a) national transport 26%
- (b) international transport 74%.

## 7. Realization of the transport activities during 2007:

- (a) volume of the passenger transport decreased by 14.4%
- (b) volume of the freight transport increased by 8.1%.

## II. NEW DEVELOPMENTS TO BE OBSERVED SUBSEQUENT TO THE REORGANIZATION OF THE RAIL SECTOR WITH SPECIAL ATTENTION TO THE SETTING UP OF NEW RAILWAY COMPANIES

8. PE “Serbian Railways” is 100% owned by the State and the entire property is placed at its disposal for use. In line with the provisions of the Decision establishing the PE “Serbian Railways” and with the aim of preparing for more independent operation in the market of transport services, the sector is organized in two directorates: the Directorate for Infrastructure and the Directorate for Transport, and a special entity represented by joint services (finances, procurement, legal issues etc.). Such organization enables cost allocation by company sections and the creation of internal balance sheets. The restructuring process of PE “Serbian Railways” is still ongoing.

9. Some of the key changes in railway sector have already been implemented, the most significant of which are as follows:

(a) On March 1, 2005, the new Law on Railway - enacted on February 17, 2005<sup>1</sup> - came into force;

(b) On May 17, 2005, the new enterprise - Public Enterprise “Serbian Railways” - was registered with the Business Registers Agency – Business Entities Register;

(c) The Railway Directorate was established, as a regulatory body, commencing its operations in mid 2005;

(d) Pursuant to the Decree on Establishment of PE “Serbian Railways”, the Enterprise will perform its activity in parts, in line with the principles of separation between the activities of public railway infrastructure management and the activities of performing of public transport of passengers and goods and maintenance of railway rolling stock; accordingly the Statute prescribes that the parts should be organized within the Enterprise, namely Infrastructure Directorate and Operations Directorate;<sup>2</sup>

(e) The Enterprise has a member, i.e. an observer status, in UIC, CER and other international railway and financial organizations and institutions;

(f) Pursuant to provisions of the new Law on Railway, a number of by-laws were enacted (among other things, rulebooks on conditions for issuing and contents of safety certificates for railway infrastructure management and for railway operations, effective as of May 17, 2006);

(g) Preparation of the draft Strategy and Policy for Development of Transport Sector in Serbia is under way.

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<sup>1</sup> Official Gazette of the Republic of Serbia No 18/2005, dated 24 February 2005.

<sup>2</sup> For the needs of the Infrastructure Directorate and Operations Directorate, common affairs are performed at the Enterprise level.

10. The new Law on Railway has created an institutional framework for the introduction of a Public Service Obligation (PSO) funding mechanism. The Public Service Obligation is expected to be financed by the Republic – from the Republic budget and the local authorities' budget.

11. The position of the national operator will be defined, i.e. reconciled, depending on the capability of the above operator with respect to market conditions of operation. Therefore, it is necessary to perform, as soon as possible, a technological and financial consolidation of the railway so that the railway could be prepared, upon the State joining the European Union, to compete at the market of railway services. The legal frameworks are expected to bear in mind the current position of the national operator at the railway transport market, and solutions are expected to be accordingly projected in order for the national operator to become capable, as soon as possible, to operate under market conditions of operation.

12. The Ministry of Infrastructure is leading the project of designing an infrastructure access regime for the Rail Sector, which is financed by PPIAF with the assistance of the World Bank. It contains the Network Statement document, as well as the Report on Track Access Charges document that relates to the methodology for determining an infrastructure access charge. The project started in March 2007 and will last for 8 months. The project tasks are the following:

(a) To define a framework for using the infrastructure and define prices, in line with the relevant EU Directives, to promote international transport, competition and private investment;

(b) To draft a Network Statement for PE "Serbian Railways", in line with the EU definitions, including the technical and economic information for beneficiaries in relation to the exploitation of network and which will be largely aligned with the neighbouring countries;

(c) To create an Action Plan for establishing a defined regime of use, as soon as possible, including institutional and organizational modifications together with recommendations, cost estimates and potential implementation in order to strengthen the regime where possible and appropriate.

### III. RESTRUCTURING OF PE "SERBIAN RAILWAYS"

13. When it comes to restructuring of public enterprises, certain necessary aspects of this complex process are usually omitted. In the case of railway companies and, based on the experiences of Western European countries, this process lasted from 5 to 7 years or even longer. The restructuring of PE "Serbian Railways" can be observed in the following manner:

- (a) Legislative framework
- (b) Organizational structure
- (c) Rationalization of unprofitable sections of the network
- (d) Separation of secondary activities
- (e) Reduction in the number of employees
- (f) Relation between the State and railway.

Each of the above-mentioned activities has a certain degree of significance, and positive impacts of restructuring happen only when all activities are followed by certain results.

A. Legislative framework

14. On 24 February 2005, the National Assembly adopted the Railway Law ("Official Gazette of RS", No. 18/2005), which entered into force on 1 March 2005. This law regulates the management of public railway infrastructure and transportation.

15. The Decision establishing the public enterprise for managing the railway infrastructure and transportation ("Official Gazette of RS", No. 78/04 and 19/05) was passed by the Serbian Government on 26 February 2005.

16. The main features of the Railway Law and the Decision establishing the PE "Serbian Railways" are the following:

(a) Creating conditions for free and fair access to public railway infrastructure for all interested carriers;

(b) Operating independent railway companies, implying free pricing;

(c) Dividing the railway system in two parts i.e. one part for managing the railway infrastructure, organizing and regulating the transport and the second part responsible for passenger and freight transport;

(d) Special financing of railway infrastructure manager and carrier from the Republican and local self-government budgets in form of: provision of lacking means for maintenance works of public railway infrastructure, organization and regulation of railway traffic, as well as construction, reconstruction and modernization of railway infrastructure performed by a public enterprise and subsidisation of unprofitable lines in passenger traffic by the Republic of Serbia and local self-government units;

(e) Introducing a Public Service Obligation for certain lines;

(f) Requesting payment for the infrastructure fees for using railway lines, done by carriers;

(g) Establishing a Railway Directorate as a separate organization.

B. Organizational structure

17. PE "Serbian Railways" is 100% owned by the State and the entire property is placed at its disposal for use. In line with the provisions of the Decision establishing the PE "Serbian Railways" and with the aim of preparing for more independent operation in the market of transport services, the sector is organized in two directorates: the Directorate for Infrastructure and the Directorate for Transport, and a special entity represented by joint services (finances, procurement, legal issues etc.). Such organization enables cost allocation by company sections and the creation of internal balance sheets. In the next company transformation, the Directorate for Transport shall be divided into the following: transport of goods, passenger transport and maintenance of trains as independent areas of operation with almost all powers in legal transfers (similarly to the holding model in certain EU countries).

18. The above transformation is due in the course of 2008 and will translate into a Law on Transformation of PE "Serbian Railways".

19. The process of restructuring will last from 3 to 5 years, depending on the efficiency in implementation during the first few years, starting from this year. The first two years (2006 and 2007) are intended for adjustment, while the period of 5 years is proposed due to possible unpredicted circumstances.

C. Rationalization of unprofitable lines of the railway network

20. With the aim of more efficient realization of the PE restructuring and with the support of the EBRD, the consulting company Booz Allen & Hamilton was engaged for creating the project "Institutional study". This study provided solutions that were partly implemented in practice. One of the envisaged and implemented solutions is the suspension of traffic on unprofitable lines. Until 2005 i.e. in 2005 and 2006, passenger traffic was suspended along 543.1 km of railway lines (from the aspect of commercial effects). This makes around 14% of the entire length of PE "Serbian Railways" lines. Furthermore, with the aim of service rationalization, 300 official posts were closed, 140 whereof in passenger and 160 in freight traffic.

21. Rationalization of network and services is a precondition for railway operation in compliance with market principles. This implies that income and operation costs have to be taken into account for profitable business. Decision-making was so far based only on the need for transport and profit, while the costs were disregarded. Some of the necessary measures are suspension of passenger and freight traffic on certain lines, closing of unprofitable stations, redirection of transport capacities from unprofitable to profitable lines, as well as provision of transport services, with mandatory funding by the region, city or economic entity at stake.

D. Separation of secondary activities

22. A Memorandum of economic-financial programme of the Government of the Republic of Serbia and the IMF imposed the obligation to transfer the secondary activities to the Government of Serbia by the end of June 2005, as well as to initiate the privatization procedure in the newly-established dependent companies.

23. The Government agreed that the public enterprise "Serbian Railways", as the founder of daughter companies, may transfer to the Republic of Serbia the founder's rights for the 10 following daughter companies:

- (a) Factory of railway vehicles "Zelvoz" ltd. Smederevo;
- (b) Tourist enterprise "KSR Beogradturs" ltd. Belgrade;
- (c) Railway rolling stock and road equipment cleaning and maintenance, "Nega kola i DDD", Ltd, Belgrade;
- (d) Transport equipment factory "Faso" Ltd, Belgrade;
- (e) International and domestic freight forwarding "Fersped" stock company, Belgrade;
- (f) Railway publishing and news enterprise "Zelnid" Ltd, Belgrade;
- (g) Railway catering and tourism enterprise "Zelturist" Ltd, Belgrade;
- (h) Building maintenance enterprise, Ltd. Belgrade;

- (i) Enterprise for fire protection, protection of buildings and assets Ltd. Belgrade;
- (j) Pron Invest ltd. Belgrade.

24. The transfer of founder's rights to the Republic of Serbia has been completed for all 10 daughter companies. Management bodies have been formed (management and executive boards) and establishment acts have been amended in line with the Company Law. All these companies are in the process of preparation for privatization, while prospectuses are already issued for some of them by the Privatisation Agency. The total number of employees in these companies is around 3,822. Further separation of dependant companies will be defined by the Company business policy for 2007 and Business Plan for 2006-2010.

E. Reduction in the number of employees

25. In the past five years, the company has achieved significant results, especially regarding the reduction in the number of employees, which is illustrated by the data on the number of employees on the following dates:

- (a) 31 December 2000 - 32.823;
- (b) 31 December 2004 - 26.211;
- (c) 31 December 2005 - 22.271.

26. During the reduction process, the cooperation with unions was very satisfactory, which enabled favourable realization of the process.

27. The target number of employees at the end of the restructuring process is between 17,000 and 19,000, depending on the following:

- (a) Technical and technology level that the company will realize in the following period;
- (b) Level of introduction of public service obligation by the State or local self-government unit, i.e. level of State determination to subsidize unprofitable transport in passenger traffic.

28. Labour restructuring and productivity increase – The Enterprise plans to reduce the staff numbers to 21,000 by the end of 2006, i.e. to 19,400 by the end of 2007; further labour restructuring will be implemented, among other things, in line with the document Activity plan for reduction of non-profitable services whereof implementation is under way, i.e. in line with the implementation of this document which will commence by the end of 2007; in the 2000-2005 period, ZS have increased the productivity by 82%. At the same time, it is necessary to achieve the following productivity target values (RTKM per employee), which should be not less than: 180,000 in 2006, 210,000 in 2007, 240,000 in 2008 and 270,000 in 2009 fiscal year, but the Enterprise will endeavour to achieve these target values even earlier.

F. Relation between the State and the railway company

29. Pursuant to the Law on State-owned assets, the State presently owns all assets that are placed at the disposal of PE "Serbian Railways". Current activities are State-subsidized with

around EUR 100 million. Nominal amount of the subsidies has decreased from CSD 10 billion in 2002 to CSD 8 billion in 2006.

30. The infrastructure is intended to be State-funded and the transport, as a commercial activity, should not be subsidized.

31. According to the solutions from the Decision establishing the PE "Serbian Railways", it is necessary to draft a Plan of financial consolidation and implement it before the liberal solutions set out in the law come into force, as they envisage equal access under equal terms to domestic and foreign carriers. This primarily implies the regulation of the status of foreign debts amounting to more than €600 million. The deadline for realizing this activity depends on the State's capacity and readiness of several ministries to invest great efforts in its realization.

32. Financial consolidation is necessary in order to enable PE "Serbian Railways" for market operation. The experiences of European railway companies showed that most of them had certain benefits during the restructuring process, mostly in view of resolving debt issues. This will facilitate the operation in terms of investment and indebtedness in the capital market.

33. The introduction of Public Service Obligation for certain lines by the State or local self-government units is one of the novelties in the Railway Law which ought to be enforced as early as in 2007 or 2008 at the latest. This practically means that the carriers will be obliged to conduct transport on certain unprofitable lines that the State nevertheless deems important for railway transport, but it will at the same time subsidize such transport up to the full cost of transport. The system of fees for using the infrastructure will also become operational in the years to come. The infrastructure management (a part of PE Serbian Railways) will collect the fees for access to and using the infrastructure to all carriers interested in using the railway infrastructure and fulfilling the legally prescribed conditions.

#### 1. Conclusion

34. Certain aspects of restructuring (reduction in the number of employees, legislative framework) are more advanced than others (organization structure, relationship between the State and the railway company etc.), but we may nevertheless say that it will take another 3-5 years for restructuring of this company, depending on the difficulties that will arise.

35. The key problems that hinder the restructuring process at the moment are: insufficient cost coverage by own incomes, insufficient budget subsidization for investment in infrastructure maintenance, insufficient preparedness of all management structures for necessary reforms, high international credit obligations, the lack of proper traction and trailing stock, poor infrastructure causing slow rides on numerous lines.

36. The restructuring process was so far supported by the union of the PE Serbian Railways who contributed to the process by participating in the activities of working groups.

#### 2. Accounting Framework

37. For the first time, the Enterprise's 2004 Financial Statements were prepared in compliance with the International Accounting Standards (IAS).



38. A fact of particular importance is that, at the beginning of 2006, ZS have adopted a new Rulebook on Accounting and Accounting Policies thus defining the bases for setting-up the management accounting at the Enterprise level and the new evaluation of property, plant and equipment will further alleviate the implementation of IAS during the preparation of Financial Statements.

### 3. Future Organization

39. PE “Serbian Railways” will be reorganized with the aim of providing the clear market orientation in the future. The organizational structure, i.e. organizational form, will be further adjusted to the real needs, possibilities and positive experiences of international railway administrations, and will depend on the legal framework in force. As necessary, this will be presented and explained in the following plans. The ZS organization with the two organizational units, i.e. directorates, is envisaged for the transition period (during which the financial consolidation will be performed as one of the basic conditions for setting up the target organizational form), i.e. by 31 December 2009, when the Enterprise’s possible organizational form (holding) is to be set-up, but upon fulfilling the preconditions specified herein. This organizational form may be set-up even earlier, if the conditions are fulfilled, and this will be concretized in the following planning documents. Not later than 31 July 2008, the Government of the Republic of Serbia shall submit to the National Assembly of RS a draft Enabling Act which will include the target organizational form and structure in accordance with the plan; whereas not later than 2009 all preparatory actions will be undertaken to split the part for operations in three organizational parts. Depending on the legal frameworks in force, the implementation of the procedure of transforming from the current into the target organizational form of the Enterprise will be possible perhaps only through enactment of act by the Government of the Republic of Serbia, and the legal procedure of this process will be explained in more detail in the future planning documents.

40. During the transition period the Enterprise will implement the most significant activities from the field of restructuring. However, it will continue to operate as an integrated enterprise within the process of decentralization, delegating a share of responsibilities to the newly created directorates for operations and infrastructure. Thus, the Enterprise will gradually become independent in terms of business operation. The transition period will enable the ZS and the Government of RS to implement a number of measures required to create conditions for a long-term target organization.

41. After the transition period, i.e. upon fulfilling the required preconditions (financial consolidation, implementation of PSO funding mechanism, introduction of the infrastructure access charge, National Assembly of RS adopting the Enabling Act, and/or enactment of the act by the Government of RS which will define the target organizational form, i.e. the Enterprise structure), the Enterprise might migrate to the target organizational form structured into 4 or 5 separate organizational parts. This form will be determined by relevant decisions of the Founder and depend on the technical and technological, as well as economic capacities of particular parts of the current Enterprise in respect of independent functioning.

42. The target organization of PE “Serbian Railways” is expected to need approximately 19,000 employees.

4. Initiative for establishment of Combi union

43. In the course of 2005/2006, the Sector for Railways and intermodal transportation established contacts with the members of the International Union of Combined Road-Rail Transport - UIRR, with the aim of obtaining their recommendations for establishing a Combi union in Serbia. As a follow-up, the PE "Serbian Railways" established a working group which had the task of analysing the need and the model for "Serbiacombi". After the working group submitted its report on the need for establishment of "Serbiacombi", PE "Serbian Railways" continued with its activity for establishment of "Serbiacombi". These efforts will result in the Republic of Serbia obtaining, in a short period of time, a combined transport operator, which would be a partner to other European combi units and which would, beside its commercial role, be a powerful promoter of further development of combined transport.

IV. INVESTMENTS IN RAIL INFRASTRUCTURE AND RAILWAY ROLLING STOCK.

44. The possible sources of finance for the investment projects are the following:

- (a) EIB, EBRD and World Bank loans, loans from EU member countries and from other creditors;
- (b) donations and other grant funds for financing of projects having regional importance;
- (c) earmarked funds of the Republic of Serbia – capital subsidy;
- (d) funds from the National Investment Plan;
- (e) resources from industries, as well those from the local authorities, interested in the use of the railway infrastructure and rolling stock;
- (f) other sources.

45. PE "Serbian Railways" 2006-2010 Investment Plan envisages the total investment in the region of CSD 231 billion, out of which approx. CSD 22 billion or approximately 10% relate to programmes for infrastructure and for operations for which the sources of finance have been determined. The investments planned for other development projects, for which the sources of finance are yet to be identified, amount to approx. CSD 209 billion, out of which approx. CSD 64 billion for infrastructure projects, approximately CSD 42 billion for transport projects and approx. CSD 3 billion for the projects related to modernization and procurement of other facilities.

46. Possible sources of finance, among other things, could also be the grants from the European Union funds for development of railway capacities that will enable a faster integration in uniform European transport system. ZS expect that the EU will invest the grant funds in upgrading of railway corridors, Corridor X in particular, as well as in the rolling stock, and also in other lines, before enabling open access to infrastructure, since Serbian railway can not participate on equal footing in the forthcoming liberalization of the European railway market. This would enable the ZS to speed up the already commenced gradual application of particular

major EU norms and documents, i.e. particular provisions of the directives governing the field of railway traffic.

## **A. EIB and EBRD loans**

### 1. EIB 1

47. The realization of EIB-1 credit is finalized, credit amounting €70 million for reconstruction of railway infrastructure and particularly the critical sections of Corridor 10 and its branches. (sections: Dimitrovgrad–State border, Kusadak–Velika Plana, Slovac–Valjevo, Resnik–Lazarevac, Cortanovci–Petrovaradin, enlargement of tunnels and reconstruction of bridges between Nis and Dimitrovgrad, as well as works on track plants in the Dimitrovgrad station. **Impact:** EIB-1, beside its regular impact, had a significant impact after the finalized reconstruction of 6 tunnels and 19 bridges on Nis-Dimitrovgrad line (Corridor 10) ensuring track gauge in line with UIC-C standard i.e. enabling the transport of all types of intermodal transport units along Corridor 10. The above-mentioned reconstruction was also a precondition for future railway electrification.

### 2. EBRD-1

48. The credit of the European Bank for Reconstruction and Development (EBRD-1) amounting €57 million is intended for purchase and reconstruction of rolling stock, provision of mechanization for line maintenance and for social programme. **Impact:** EBRD-1, improved situation, significant synergy with the Government's social programme for reduction of employees in the Serbian railways of 11,832 in the period from 31.12.2000 to 31.12.2006.

### 3. EIB-2

49. Within the new EIB-2 credit amounting €80 million signed on 8 December 2006, the following sections should be reconstructed and modernized: Batajnica-Stara Pazova-Golubinci (Belgrade-Sid line), Jovac (Gilje)-Cuprija (Belgrade-Nis line), Cele Kula-Stanicenje (Nis-Dimitrovgrad line).

(a) Belgrade - Sid line: €22 million Reconstruction and modernization of the railway line for speed of 160km/h, section between Batajnica and Golubinci station, from km 21 to km 45. Works include section from Batajnica station to Nova Pazova station overhauling works on the one part of left track and whole right track of the double-track line, reconstruction of the existing interlocking system and OCL at the distance between stations. Nova Pazova station - reconstruction of tracks and connecting tracks, construction of station platforms, including subway, station square reconstruction, reconstruction of the existing interlocking system and OCL according to new track design. Stara Pazova station reconstruction of tracks and connecting tracks, construction of station platforms, including subway completion, reconstruction of the existing interlocking system and OCL according to new track design. Section from Stara Pazova station to Golubinci station - completion of works on construction of the right track (substructure and permanent way), procurement and installation of equipment for OCL, signalling, interlocking and telecommunication systems.

(b) Belgrade - Niš line: €28 million Modernization works will be reconstruction i.e. construction of the new Jovac – Čuprija double-track section, 7.2 km long, due to bad condition of single-track bridge over the Velika Morava River.

(c) Nis-Dimitrovgrad line: €30 million Modernization works will be rehabilitation works on the 59.0 km long Čele Kula – Staničenje railway line section, from 5 km to 64 km. Works include: urgent works on the substructure (correction of railway alignment layout elements in about 40% curves, rehabilitation of weak spots in the road bed, placing of sub-base on the railway line sections with earth road bed, placing of blinding course in rock cuts and cut-and-fills, drainage of road bad and station areas, rehabilitation of culverts, gauge extension on particular line sections in rock cuts, protection of slopes, regulation of watercourse and hydro engineering works, all other works required for improvement of road bed stability and bearing capacity). Reconstruction of stations: extension of arrival and departure station tracks in order to enable usable length of 635 m for trains with 120 axles, enabling one relief track, usable length of 750 m in Ostrovica station. Urgent works on the permanent way: complete replacement of permanent way structure on the open track and station tracks with new rails on concrete sleepers with flexible fastening set and new points, rail welding to make continuous welded rail

#### 4. EBRD-2

50. Within the new EBRD-2 credit amounting € 60million, signed on 14 July 2006, up to 1,100 freight carriages should be purchased and the under floor wheel lathe.

#### 5. EBRD-3

51. Negotiation is ongoing. Proposal for this loan is purchasing of new passenger electrical motor trains.

#### 6. Spanish credit

52. The Republic of Serbia i.e. PE “Serbian Railways” was granted the credit from the Kingdom of Spain at the amount of €32 million for purchase of rolling stock. The credit will be used for obtaining 10 new diesel trains, reconstruction and modernization of at least 20 passenger cars for internal transport, repair and modernization of minimum 10 sleeping cars for international transport.

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