



## **Internalisation of External Costs for Transport**

*Response to the European Commission's consultation exercise*

22 January 2008

### **1. General comments**

The European Sea Ports Organisation (ESPO) represents the port authorities, port administrations and port associations of the seaports of the European Union. The organisation acts as the representative body of all seaports in the EU and Norway and has observer members in accession countries and countries neighbouring the EU.

ESPO notes that internalisation of the external costs of all transport modes is assumed to lead to a more efficient transport system based on the 'user pays' and 'polluter pays' principles. Environmental-friendly modes of transport such as short sea shipping and inland navigation would theoretically gain market share with a European policy framework which applies this principle. In addition, it would ensure the proper functioning of the internal market and remove distortions of competition between transport undertakings in Member States.

Pricing is however far from being the only factor which determines the choice of a transport mode. Other, service-related, factors play an equally important – if not more important – role. Higher efficiency and more market-oriented behaviour for instance largely explain why road transport is still much more attractive today than rail transport. The fact that short sea shipping is much more burdened by cumbersome administrative procedures than road transport is another example. Past oil price rises did not cause a perceptible decline in road usage, which proves that trying to manipulate modal change through price structures is not likely to have much impact.

ESPO furthermore believes that the negative side-effects of trying to establish a common pricing policy for all modes of transport and the complications it generates for nodal points such as seaports are likely to offset any potential advantages it might generate. All previous attempts of the Commission to make progress in this field ever since the 1995 Green Paper have ended up in a mixture of economic textbook theories and political horse-trading without any tangible positive result. It is furthermore far from certain that any revenues generated from internalisation of external costs will effectively be used to improve the European freight transport system by upgrading infrastructure networks. The lack of adequate infrastructure is nevertheless one of the principal causes of congestion.

In addition, it seems that the EU has only limited competence to impose a pricing policy in the field where perhaps the most significant external costs are generated, i.e. the use of private cars. Penalising freight transport with a mixture of theoretical and political solutions whilst one of the main sources of congestion and pollution remains unaffected seems therefore hardly effective.

Finally, it may be questioned to what extent external costs such as congestion, represented by the loss of time, are not already borne by users and are therefore already internalised.

For all these reasons ESPO is sceptical about the Commission's aim to blow new life in the internalisation of external costs debate. ESPO has therefore chosen not to respond directly to the internet-based questionnaire of the Commission. Instead, this paper briefly presents some reflections on the internalisation of external costs in seaports. At the same time, it proposes a constructive alternative agenda to reach the Commission's objective of achieving a sustainable European transport system.

## **2. Internalisation of external costs in seaports**

### **2.1. Seaports are intermodal nodal points**

It should first of all be clear that seaports cannot be regarded as a transport mode. A seaport brings together maritime transport and, depending on the particular characteristics of the port involved, a combination of road, rail and inland navigation.

Whereas ports for centuries used to be predominantly seaward-looking, this is no longer true today. Logistics chains are the relevant focus in European port competition. The traditional division of tasks within the logistics chain has become blurred by vertical integration strategies. European ports are therefore increasingly competing within supply chains and have become natural habitats for logistics services. The pre-eminent role of seaports in international distribution offers opportunities for the development of value-added logistics.

The availability of good hinterland connections is therefore vital for the competitive position of a seaport which essentially is an intermodal nodal point and a key link in the logistic chain.

### **2.2. Port costs versus total transport costs**

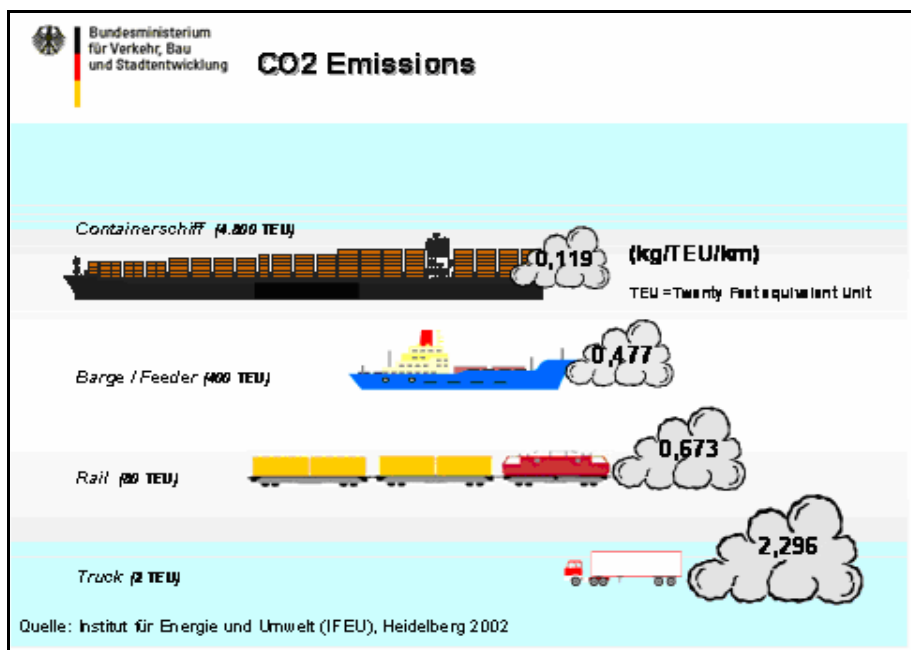
A second important fact is that port call costs, which mainly consist of cargo-handling charges as well as harbour dues, charges for technical-nautical and ancillary services and – in some countries – fairway dues and light dues, only represent a minor element of total transport chain costs. A typical transport journey involving maritime transport usually is most expensive on the hinterland side.

The same applies to external costs as will be explained in the next section.

### **2.3. External costs generated by shipping and port activities**

When considering an intermodal transport journey which includes a maritime leg, the external costs of hinterland transport modes are higher than those generated by maritime transport and the port activities themselves.

As far as maritime transport is concerned, external costs related to noise and accidents are limited or not relevant as the Commission confirms in the background document to its consultation. External costs related to air pollution and climate change are relevant. As illustrated below, for each kilometre a ton of goods is transported, shipping is however by far the most energy-efficient (CO<sub>2</sub> emissions) mode of transport.



External costs related to congestion of shipping essentially occur in ports, i.e. waiting times before locks or berths. Other external costs generated in ports are hardly caused by port operations themselves, but by land-based transport modes such as road transport. Especially congestion and air pollution are relevant in this context. The latter also applies to emissions from industrial installations located in port areas.

#### 2.4. Adverse effects of internalising external costs in ports

Although the external costs generated by shipping and port activities themselves may be limited<sup>1</sup>, internalising them in port call costs through a theoretical common charging system first of all risks to make ports and shipping more expensive. This would be contrary to the Commission's policy of promoting maritime transport as an environmental-friendly mode. Policy-makers moreover seem to view ports as easy points to implement charging systems for costs which are not directly generated by port or port-related activities.

By having more expensive ports in Europe, shipping traffic in regions such as the Mediterranean, Black Sea and Baltic Sea, will further shift to ports in neighbouring countries which today already distort competition with EU ports through lower wages, more flexible State aid rules, tax exemptions and less stringent environmental requirements. Moving cargo to new hubs in neighbouring countries will not only undermine the competitive position of EU ports but will make freight transport subject to even less environmental requirements which is not in the interest of overall sustainability.

It should furthermore be acknowledged that port charges are in most cases subject to negotiation. To regulate charges by means of a common charging system on internalisation of external costs, which is likely to be an incoherent mixture of theoretical and political objectives, would be a return to times of government tariff regulation, which, in most ports which had or still have the

<sup>1</sup> As confirmed by the European Environment Agency: Transport and environment : on the way to a new common transport policy : TERM 2006 : indicators tracking transport and environment in the European Union, p.28.

experience, has led to more bureaucracy, higher port call costs and less efficient use of port infrastructure.

Finally, for any common system on port charging to work it would have to harmonise the financial structure of port authorities. Given the wide variety of systems that exist in Europe in this respect, it is very much doubted whether such harmonisation can be achieved or would be useful.

The above does not mean that ports cannot apply market-based instruments to stimulate environment friendly behaviour. Instruments such as differential charging could for instance be used in the field of ship emissions where some examples already exist. Port authorities can also include specific conditions in concession agreements to ensure that terminal operators ensure optimal land-use, achieve modal shift objectives and use low-emission port equipment.

ESPO however strongly believes that the use of such market-based instruments should be left to the discretion of individual port authorities. Their value added and concrete content very much depends on local circumstances and cannot be generally imposed, let alone imposed through a common system which would apply to all transport modes.

An important obstacle for voluntary dues differentiation highlighted in a 2005 NERA study<sup>2</sup> is that port dues may not be high enough to provide sufficient incentives, even with substantial differentiation. Moreover, some dues are not everywhere under the direct control of the port authority but are charged by third-party contractors. Interfering in these port due mechanisms seems to be very complicated without having a huge impact. The study further also indicates that ports are increasingly operating in a deregulated and competitive market and raising charges for some ships, while lowering for others, may not be commercially feasible. Moreover, dues frequently are specially negotiated on a bilateral basis. As explained above, ESPO underlines the importance of maintaining this negotiation freedom where applicable.

### **3. Alternative measures to reach a sustainable transport system**

As outlined in the general comments above, ESPO is sceptical about the introduction of a common system of internalisation of external costs. The effects it would generate for ports and shipping may be contrary to the overall objective of creating a sustainable transport system in Europe.

Taking also into account that the effect of pricing policy will be limited anyway and risks becoming subject of a very complex and time-consuming theoretical and political debate, ESPO believes that the Commission would better concentrate its time and resources on the alternative measures highlighted below which would contribute in a much more effective way to sustainability of transport in Europe.

These measures are not new but are already part of the Commission's transport and maritime policy framework as laid down in the series of communications and working documents that were published in October 2007. Making further progress on them should therefore be less complex than entering into the potential minefield of internalising external costs.

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<sup>2</sup> NERA – Economic instruments for reducing ship emissions in the European Union – 26 September 2005, p. vi

The detailed point of view of ESPO on the issues below can be found in the more elaborate responses it has published on the Commission's ports policy communication, freight logistics package and maritime policy 'Blue Paper'<sup>3</sup>.

### 3.1. Sustainable provision of infrastructure

The most important priority is the sustainable provision of adequate transport infrastructure in Europe. This is most certainly the case for seaports which are responsible for almost all of Europe's external trade and nearly half of its internal trade.

As a result of strong growth on the arterial container trade routes in recent years, and in order to anticipate on future volume increases, many shipping lines have embarked upon ambitious expansion plans to upgrade the capacity of their ship fleets. Whereas shipping lines clearly prepared themselves to handle the expected increase in container volumes in the short term, the development of additional capacity to meet this demand in European ports is seriously lagging behind. The growing mismatch between the demand for shipping services and the supply of port capacity and adequate hinterland connections leads to increasing port congestion and as such the integrity of the entire supply chain is affected.

The Commission can stimulate the resolving of infrastructural bottlenecks through its general transport policy as well as existing regional development, cohesion fund and TEN-T programmes. The 2010 mid-term review of the latter should be used to generate more resources for hinterland connections to ports. These funds should be allocated on the basis of objective cost-benefit criteria and there should be no discrimination among ports on the basis of perceived traffic imbalances.

ESPO is very conscious that infrastructure impacts on the environment and that scarce land is claimed by multiple interests, including nature conservation and urban development. Harmonising environmental and economic values has proved to be a difficult learning exercise for many ports and other infrastructure managers resulting often in conflict situations. European seaports have however made considerable progress in achieving high environmental standards and improving environmental management and have over the years succeeded in developing constructive agreements with NGOs and local stakeholders leading to win-win situations for nature, citizens and ports.

Nevertheless, legal uncertainties with regard to the application of nature conservation legislation continue to cause substantial delays for many projects. It is generally recognised that these delays are, to a large extent, caused by ambiguities in the applicable EU legal framework. The European Commission can therefore facilitate the sustainable development of infrastructure by creating more clarity about its own legal framework.

This is why ESPO has welcomed the Commission's initiative to produce guidelines on the application of Community environment legislation to port development. Such guidelines should ensure recognition of pre-existing EU and international legal regimes for waterway and port-related activities, introduce good governance principles on prior consultation with port authorities before designation of sites under environmental Directives and clarify outstanding interpretation problems with the present legal framework. ESPO is contributing to the development of these guidelines and hopes they can be completed in 2008 as originally intended by the Commission.

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<sup>3</sup> These documents are all available from the ESPO website: [www.espo.be](http://www.espo.be)

ESPO has further invited the Commission to consider, in addition to guidelines, measures which would reinforce the legal status of port development projects and simplify existing legislation.

### 3.2. Implementation of the 'co-modality' concept

Whilst ESPO supports the idea of generating a modal shift to more environmental-friendly transport modes and recognises that port authorities can play an active role in this process, it must be underlined - as indicated above - that seaports need all modes of transport to function optimally within the supply chain.

The full potential of short sea shipping has not yet been reached mainly because of existing logistical and administrative bottlenecks which make this mode of transport more time consuming when compared with road transport. These bottlenecks need to be solved urgently. Given developments in distribution structures, it should however be acknowledged that road haulage is likely to remain a dominant mode on shorter distances. Rail and barge have increasing importance on high-volume trunk lines.

ESPO therefore prefers the 'co-modality' concept presented by the mid-term review of the European Commission's Transport Policy White Paper instead of a theoretical modal shift concept based on internalisation of external costs. ESPO reads 'co-modality' as ensuring that all modes of transport are as efficient and environmental-friendly as possible. This will be explained further in the following sections.

### 3.3. Efficient service levels in all transport modes

Service-related factors play a determining role in the attractiveness of one mode over another. The Commission should therefore continue to focus on enhancing efficiency levels of the more environmental-friendly transport modes.

The NAIADES action programme for inland navigation should for instance be fully implemented and the European legislative packages to modernise and liberalise railway transport should be actively enforced and correctly implemented by all Member States. In particular, the participation of new entrants in the management and exploitation of railway infrastructure should be encouraged and facilitated. In addition, all remaining operational bottlenecks related to inland navigation and railway transport should be resolved as quickly as possible. In this respect, ESPO particularly welcomes the Commission's recent proposal to develop a freight-oriented rail network.

As intermodal connecting points, the efficiency of seaports relies very much on the efficiency of services provided both in the hinterland and the maritime foreland. This efficiency is furthermore influenced by the fact that seaports are favoured locations for the provision of border controls including safety of ships, security, customs, public health and environmental quality; many of these controls are unique to the maritime sector. This is why ESPO very much welcomes the initiative of the Commission to create a European Maritime Transport Space without Barriers. This will simplify administrative procedures for intra-EU maritime transport and create a true internal market for shipping, bringing it on a more equal footing with land-based transport modes.

### 3.4. Source-based measures to combat pollution

A port area is characterised by the fact that several transport modes and industry come together in a relatively small geographical location. As explained above, port authorities can contribute to

reduction of pollution in the port area under their jurisdiction. This however has its limits. Port authorities can for instance not ask transport operators which are in compliance with European legislation to reduce their emissions more. This applies both to surface and maritime transport modes.

ESPO therefore believes that source control measures such as the Euro VI and V emission standards for vehicles and the use of low-sulphur fuel in ships are the most effective way forward. ESPO is pleased that the political agreement reached on the proposal for a Directive on Ambient Air Quality has recognised the importance of such source control measures but strongly recommends that European policy-makers give much higher priority to the development of these measures in the context of the co-modality concept.

#### **4. Conclusion**

Internalisation of the external costs of all transport modes could in theory lead to a more efficient transport system. Pricing is however far from being the only factor which determines the choice of a transport mode. Other, service-related, factors play an equally important – if not more important – role. The negative side-effects of trying to establish a common pricing policy for all modes of transport and the complications it generates for nodal points such as seaports are likely to offset any potential advantages it might generate.

ESPO is therefore sceptical about the Commission's intention to blow new life in the internalisation of external costs debate.

ESPO believes that the Commission would better concentrate its time and resources on alternative measures which would contribute in a much more effective way to sustainability of transport in Europe. These include the sustainable provision of infrastructure and the implementation of the 'co-modality' concept. The latter implies achieving efficient service levels in all transport modes and applying source-based measures to combat pollution.

The Commission has already developed policy instruments in all of these fields and would therefore be able to make much more progress than with a common pricing policy of which the effect will be limited anyway and risks becoming subject of a very complex and time-consuming theoretical and political debate.

*Since 1993, ESPO represents the port authorities, port associations and port administrations of the seaports of the European Union. The mission of the organisation is to influence public policy in the EU to achieve a safe, efficient and environmentally sustainable European port sector operating as a key element of a transport industry where free and undistorted market conditions prevail as far as practical.*

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