



FICIL
RAISE THE BAR!



Position Paper No. 11

Foreign Investors' Council in Latvia Position Paper on Transport and Infrastructure Issues

16 September 2021



Executive Summary

The transport sector is one that will face the greatest change as a result of the global shift towards sustainability. The policy-makers' response to these trends, as well as local developments, impact the entire society due to the economic significance of the sector. The Foreign Investors' Council in Latvia (hereinafter - FICIL) appreciates the efforts by the Government, and especially by the Ministry of Transport, to address the existing issues within the sector and to prepare Latvia for the green transition.

As some reforms have already been initiated and others are likely to follow, in this Position Paper FICIL shares its opinions and recommendations for positioning Latvia in such a way that brings the best possible outcome from the upcoming transformation. Firstly, FICIL addresses the reform process as a whole and highlights the room for improvement when it comes to reforming the transport sector. Investors call for transparency and predictability in the reform process that should arise out of open dialogue among all stakeholders and a thorough socio-economic assessment of the proposed solutions. FICIL emphasises that reforms should serve as a means to accomplish the long-term vision and strategy and that reforms themselves should not be viewed as the end-goal.

Secondly, the Position Paper pinpoints the area of green transport, as it will have a vital role in the fulfilment of Latvia's green targets. Since reaching these targets will not be possible without the involvement of investors, it is essential to bring clarity over the country's vision and strategy over the next few decades, in order to reassure investors and society as a whole. FICIL also recommends centralising the policy-making in this area and finding ways to incentivise the changes in consumer habits.

Finally, the Position Paper goes beyond the transport sector, as FICIL puts forward recommendations regarding infrastructure development in general. Here, FICIL calls for reducing the administrative burden put on infrastructure developers, laying down adequate requirements and using a long-term approach in planning and communicating infrastructure development plans.



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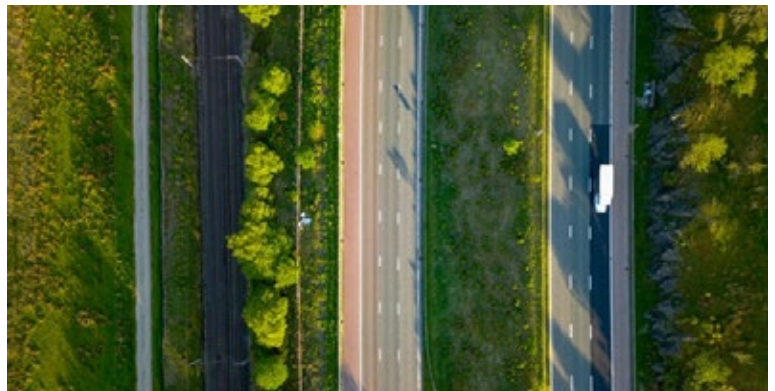
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Recommendations

Approach to reforms in the transport sector

Recognising the significant role that the transport sector plays in the overall economy of Latvia and supporting the need for reforms in this sector, FICIL puts forward the following recommendations with the goal of ensuring that any upcoming reforms truly strengthen Latvia's competitiveness and improve the investment climate in this area:

- ▶ Define a clear long-term strategy in the sector to create alignment, assure focus and support the realisation of the opportunities into devising new business concepts and support the Latvian economy.
- ▶ Clear goals, priorities, measurable activities and regular milestones must be defined to realise the strategy. KPIs must be set on the levels of outcomes, outputs and inputs in order to ensure holistic planning. It is advisable to set annual KPIs to measure progress more frequently on goals that matter the most.
- ▶ Reforms should be carefully thought through and well-considered to fit within the broader national plans and support the long-term national strategy, not the other way around.
- ▶ Stakeholders should be proactively involved from the first stages of a reform elaboration.
- ▶ Socio-economic analysis must be carried out to ensure data-based decision-making that takes into account the potential effects on all involved stakeholders.
- ▶ Integrated governance should be introduced over the definition and fulfilment of goals; involved institutions should have clear responsibilities and mandates to act.
- ▶ Corresponding State support should follow to reach the defined goals.
- ▶ State companies should be run by business professionals (both a board of directors and supervisory council). Recruitment of these professionals must be based on values, competencies and (preferably international) experience.
- ▶
 - Systems must be put in place to limit the political influence into State companies and to guarantee a level playing field and fair competition.
- ▶ Governance processes must be controlled, monitored and enforced. For example, intervention is required if the transport or climate council has not convened for a substantial period of time.

Green transport

The EU Green Deal and its targets are already an important factor in setting the agenda for green development in Latvia and we can reasonably expect that it will remain so over the next decades. As green transport is one of the key directions in the global challenge to reduce greenhouse gas emissions, it will shape not only the future of the transport sector but also of the Latvian economy as a whole. This trend can come either as a burden and limit the competitiveness of Latvia, or it can be used as an opportunity to make clear and proactive decisions to prepare the business environment and put Latvia in an advantageous position. Therefore, FICIL lays down the following recommendations in the green transport area:

- ▶ Centralise decision-making and governance over the definition and fulfilment of targets regarding green transport.
- ▶ Define a unified and balanced approach to laws and regulations by precisely defining the requirements for road transport (both private and commercial transport).
- ▶ Educate consumers on the benefits and necessity of switching to environmentally friendly private transport.
- ▶ Provide long-term support (and / or economic incentives) for the purchase of zero-emission road transport for private individuals.
- ▶ Incorporate more targeted measures in the tax policy for businesses to promote low and zero-emission transport.
- ▶ Set movement restrictions for high CO₂ emitting vehicles.
- ▶ Ensure technological flexibility, neutrality and fair competition among alternative low- or zero-emission solutions.
- ▶ By using economic incentives, encourage entrepreneurs to choose cooperation partners that use low-emission or zero-emission fleets for providing services (delivery of goods, passenger transportation).
- ▶ Provide support for the development of alternative filling / charging infrastructures, ensuring technological neutrality and primarily supporting the development of zero-emission technologies.
- ▶ Ensure fair competition in the field of electric car charging by reviewing the financing sources and/or business model for the charging network installed by the Road Traffic Safety Directorate (CSDD).

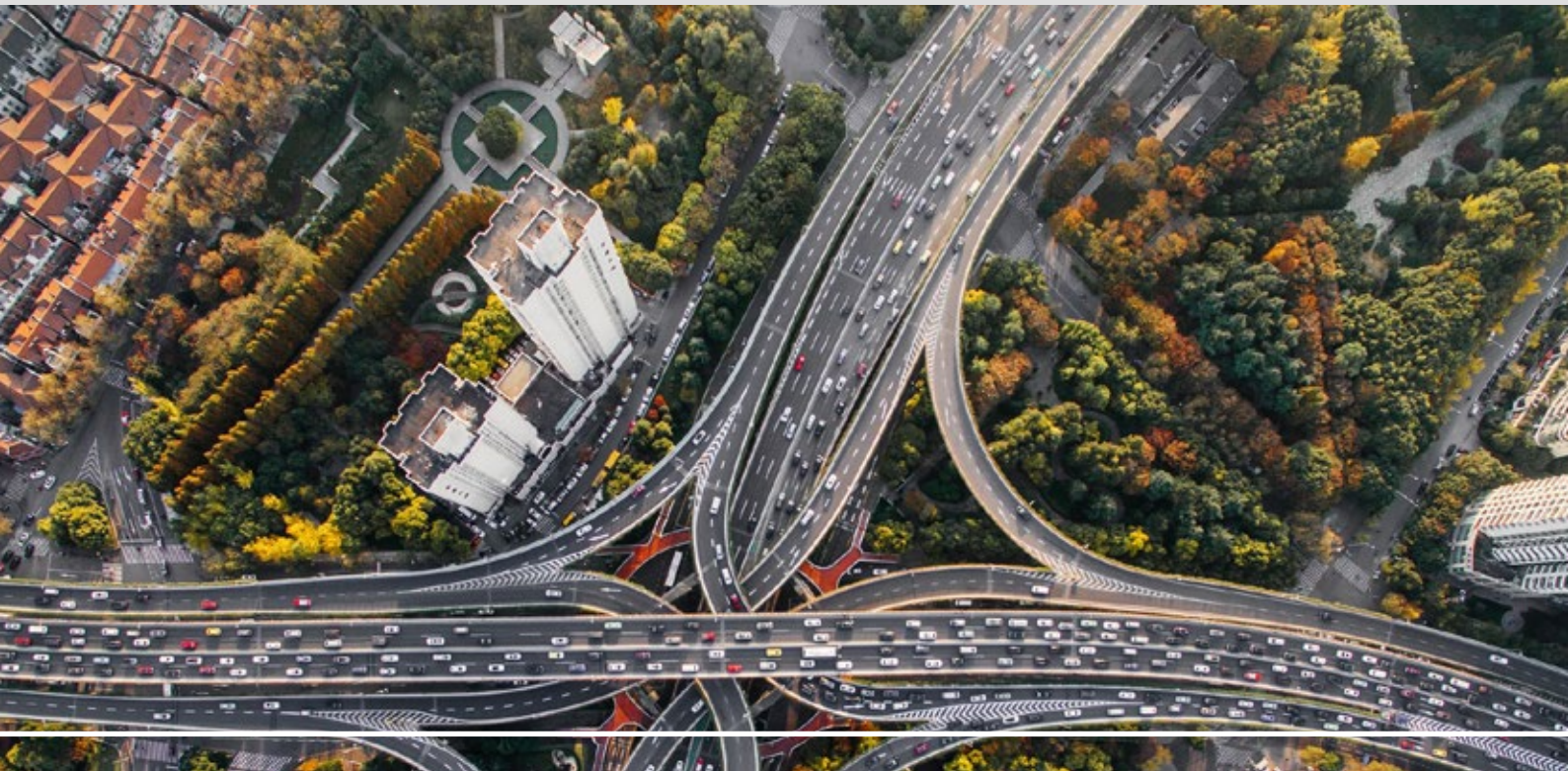
Infrastructure development

Modern infrastructure is not only a key element in establishing an attractive investment environment, but also crucial in increasing the well-being of the entire society by providing access to enhanced services. As

a result, the administrative process and regulatory requirements should create an adequate framework that bolsters the development of the infrastructure and prevents burdens on the infrastructure developers.

This is especially pertinent considering the green and digital transformation that Latvia will go through over the foreseeable future. FICIL recommends the following:

- ▶ Ensure the shortest possible deadlines for the coordination of infrastructure development projects in all subordinate institutions of ministries / municipalities by setting these projects as a priority.
- ▶ Ensure a fair balance between private property rights and the benefits for the entire society associated with a better infrastructure; consider a Rights of Way regulation.
- ▶ Match the requirements for investors towards mandatory infrastructure development with the real situation in a specific micro-market.
- ▶ Maintain consistent long-term planning and development of the infrastructure.
- ▶ Assist Latvian municipalities (starting from those with the highest population) in ultra-low emission zone implementation to improve the air quality in core areas.



Rationale for recommendations

Approach to reforms in the transport sector

Changes are happening more frequently and more rapidly, especially in the transport sector, which is impacted by the geopolitical situation and the energy transition. As all changes come with challenges, they also offer opportunities. A clear (long-term) strategy is essential to create alignment, assure focus and support the realisation of these opportunities into winning new business concepts and support the Latvian economy.

To realise the strategy, plans need to be put in place with clear (end) goals. As part of these plans, policies most probably need to be changed, laws amended or reforms initiated. Changes in that regard are a necessity to cope with the continuously changing market environment. However, changes should be carefully thought through and well considered to fit within the bigger plans and support the long-term strategy, not the other way around.

Taking the process of the port reform as an example, it is evident that it receives substantial opposition as there is a lack of clarity and gaps in communication with stakeholders and the society. FICIL believes that such reforms should follow a long-term strategy with clear end goals for the ports in the future.

As the results of a reform affect a wide range of stakeholders, their involvement in the process of the reform is essential to understand and provide a broad overview of all possible consequences, as well as to optimise the positive effects and minimise the negative ones. Secondly, pro-active involvement of the different stakeholders smoothens the process, ensures an ongoing dialogue and increases ownership. FICIL strongly believes that, in any reforms, companies, NGOs and other stakeholders should be consulted from the outset, in order to successfully reach the desired outcome.

Any reforms should strengthen Latvia's competitiveness and should be aligned with the vision of industry leaders. For example, the railway industry will require subsidies and the Ministry of Transport should work closely with the industry to support business transition and attract foreign investments, in order to boost and develop this crucial industry. In the port sector, the real competitive advantages of Latvia's ports need to be identified, and answers provided regarding how a reform can capitalise on them, and perhaps develop even better business synergies.

When considering a reform, a single sector cannot be viewed in isolation. A reform must take into account all interlinked sectors, for example, ports, railways, logistics and exporting industries. As future opportunities are the ones that attract new business and investors, a simple SWOT analysis would be a beneficial starting point for any reform.

A reform is by definition a major change that affects multiple stakeholders. The effects can often be both positive and negative, depending on the particular stakeholder. It is, therefore, vital to make a thorough assessment of the reform to ensure it is the most sensible and responsible decision to make. Ex ante economic assessments should be carried out to see if any intervention is needed at all, as well as to assess the potential costs and benefits (the so-called socio-economic analysis or CBA) of the reform to be implemented. The options always need to be compared with the "as is" situation.

Since wider-scale reforms have a potential effect on a large number of parties, it is of pivotal importance to pay due attention to the availability and collation of quality data so that the decisions can be data-driven as much as reasonably possible. Additionally, reforms need to be viewed in a larger policy context, which should look beyond the direct costs and benefits, as well as estimate the potential impact on the wider ecosystem, such as related economic domains, national development planning and competitiveness, and other reforms being undertaken (i.e. digital and green reforms as announced by the European Commission). Such reasoning not only allows well-informed decisions to be made, but also provides certainty and predictability to investors, as well as making it easier to communicate the decisions to the society.

Carrying out a socio-economic assessment also serves the purpose of increasing the credibility of a reform, as well as ensuring the buy-in of the stakeholders. Investments in the transport sector are typically evaluated over a very long term, even up to 50 years. A socio-economic assessment carried out properly serves as a basis for inclusive and holistic discussions of reforms – as opposed to serving as a tool for the procurer of the assessment to serve his or her needs. Therefore, it is also important to make the assessment available to as many varied stakeholders as possible. A high-quality assessment is a win-win situation for all involved stakeholders.

Setting out locally adapted general rules for undertaking socio-economic assessments can be a great learning experience and qualification improvement in the society over the medium to longer term. Latvia needs to build the public sector competence of undertaking socio-economic assessments, perhaps in a single organisational unit under the Cross-Sectoral Coordination Centre.

Furthermore, a strong governance model is vital to ensure that the interests of the common good are upheld and cemented for the future. In that sense, a trustworthy governance model reduces uncertainties and risks, as well as supporting and stimulating international investors to make long-term commitments and investments in Latvia.

Green transport

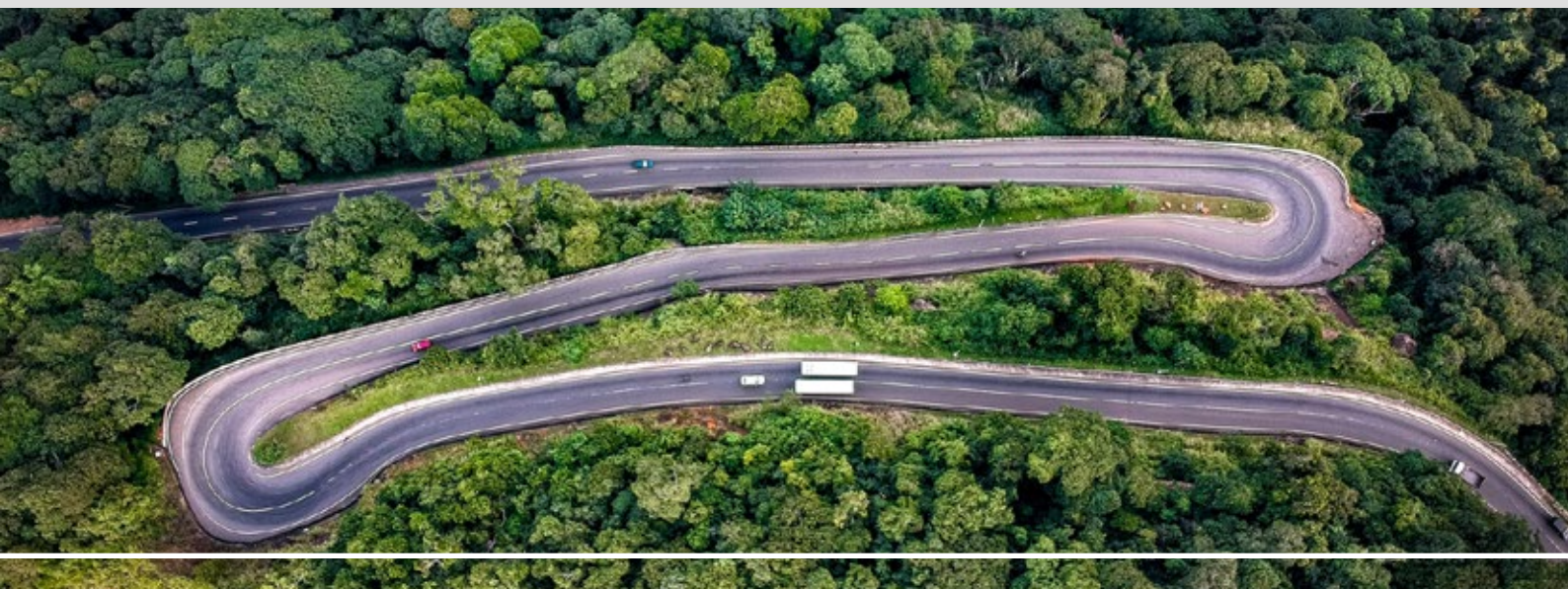
The transport sector creates 31% of all CO₂ emissions in Latvia¹. Inevitably, green transport should be viewed as a tool to reach the climate goals. For this, a clear long-term vision is required, in order to outline and communicate the country's plan in reaching these goals. As the green transport policy consists of many complex factors (for example, environmental issues, energy sources, tax incentives, economic incentives, infrastructure development, etc.), policy-making in this field is fragmented and involves multiple ministries, such as the Ministry of Transport, Ministry of Environment Protection and Regional Development, Ministry of Finance and Ministry of Economics. This leads to fragmented priorities and unclear accountability over

¹ Source: Auto Asociācija

the end result. A more centralised governance model that oversees the entire green transport policy, instead of just a single aspect of it, would be beneficial in developing a sustainable long-term vision and strategy in reaching the green goals.

Undoubtedly, companies and investors will play a significant role in Latvia's green development through infrastructure development, product offerings, market trend determination, communication with the society and other means. At the same time, it is also crucial that throughout this transformation, the investment environment remains favourable, so that the competitiveness of Latvia does not suffer. Green investment projects typically span over the long-term, even up to 20 years and beyond. Clarity about the country's long-term direction is required because investors are not ready to invest in these long-term projects without clear decisions and visions from the public sector. In turn, this delays Latvia's path to reaching the green goals and negatively affects the country's ability to attract investment.

At the same time, FICIL also calls for technological flexibility in Latvia's green transport plans. We appreciate that the Transport Development Guidelines for 2021-2027 include development and maintenance of the infrastructure for various alternative fuel technologies. FICIL strongly believes that, in order to ensure fair competition, the same flexibility should be exhibited in Latvia's plans regarding the investment of funds allocated through the Resilience and Recovery Facility



(RRF). Any decisions favouring a particular technology should be based on independent research regarding the best solutions specifically for Latvia – electricity, hydrogen, biogas or other.

Out of all transport sector emissions, road transport accounts for 83.5%². Therefore, while all modes of transportation should be considered when discussing the reduction of emissions through the development of green transport, the primary focus should be on road transport. Latvia has the smallest number of cars in the EU per 100 inhabitants³. Public transport is an important element in urban and intercity traffic, but is not always sufficiently competitive with private transport. As the well-being of the population, both locally and globally, increases, the demand for convenient and fast means of transportation will continue to grow. Therefore, it is necessary to set timely and strict guidelines for the development of green road transport and to slow down the boost of high-emission vehicles in Latvia.

While defining a clear vision and specific goals is the first step of a comprehensive green transport policy, it is equally important to lay down a specific plan for the achievement of these goals. Facilitating the change of consumer habits, as well as incentivising company investments into the infrastructure, such as charging stations and filling stations for alternative fuels, requires financial support and other tools from the State that correspond to the established goals. Economic or other incentives are crucial to speed up the transition to green transport, as currently consumers are inclined to prefer traditional vehicles due to financial considerations and a superior infrastructure.

Infrastructure development

Regardless of the industry, infrastructure development plays a significant role in the improvement of services and enhancing access to those services. When developing the infrastructure, investors would like to see a seamless and rational administrative process, in order to ensure that their investments are applied efficiently. In some cases, investors feel that there is an inadequate administrative burden that interferes with their plans for new investments and/or with their attempts to protect their previous investments.

FICIL calls for rational and well considered requirements towards the infrastructure developers. As an example, investors feel that the requirement for each fuel station to ensure an electric charging station is unjustified. Instead, FICIL believes that such requirements should

have thorough consideration that is based on multiple criteria, instead of a single overarching factor. This is especially the case, considering that there is a network of State-subsidised charging stations operated by CSDD, which the private operators would not be able to compete against, if the stations are located close to each other.

Additionally, the protection of investments already made into the infrastructure and respecting the legitimate expectations of investors is a prerequisite to attracting additional investments. In certain contexts, investors face unreasonable obstacles when it comes to maintaining, repairing or rebuilding infrastructure objects that are placed in territories owned by third parties. Here, the operators face high access costs or inadequate requests by property managers.

FICIL encourages the government to consider the introduction of a Rights of Way⁴ type of regulation in these contexts. For example, the availability of high-speed networks, both cable and wireless, including 4G and 5G, is a key element of swift digital transformation and a sustainable information society, equally affecting the development of all industries and raising Latvia's economic competitiveness as a whole. Easing and equalising current norms and regulations to achieve a transparent, speedy, cost effective and competition conducive framework of the building and deployment of a new infrastructure and the reconstruction of the existing infrastructure (cables, towers, base-stations, antennas), both in private and public areas/facilities, as well as predictable and fair maintenance costs of these networks (lease payments towards landlords, access conditions), are essential to boost network speed and coverage and sound competition between various network operators. A Rights of Way regulation should be considered as an instrument already in place to facilitate the coverage and density of high-speed networks.

Finally, FICIL also calls for a consistent long-term approach in the planning and development of infrastructure. As already discussed in the previous sections, investors would like to see a long-term vision and strategy from the public sector before they are ready to invest in long-term projects. Ensuring a clear development plan would improve the image of Latvia as an attractive place for investment. Looking at the transport sector and infrastructure, investors call for a long-term plan (at least for the next 20 years) with clear mid-term (up to 5 years) steps to be taken. Investors also believe that sustainable long-term development in Riga requires immediate actions regarding the Park & Ride infrastructure.

² Source: Auto Asociācija

³ <https://www.acea.auto/figure/motorisation-rates-in-the-eu-by-country-and-vehicle-type/>

⁴ A right of way is an easement granted by the property owner that gives the rights to travel over the land and the provision by the property owner of reasonable use of the property to others, as long as it is not inconsistent with the use and enjoyment of the land by the owner.



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FICIL is a non-governmental organisation that unites 38 largest foreign capital companies from various industries, 10 foreign chambers of commerce in Latvia, French Foreign Trade Advisers and Stockholm School of Economics in Riga. The goal of FICIL is to improve Latvia's business environment and overall competitiveness in attracting foreign investment, using the experience and knowledge of its members to provide recommendations to Government and state institutions.

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