Annex 4.3.8 : SCENARIO 2A – PKP Power Engineering Vertical, 000 PLN

	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income											
2	Passenger transport income											
3	Other income											
4	TOTAL	0	0	0	0	0	0	0	0	0	0	0
5	Subsidies											
6	Total operational incomes (4+5)	0	0	0	0	0	0	0	0	0	0	0
7	Salary costs	129,443	158,936	154,757	150,578	146,399	142,219	138,040	133,861	129,682	125,503	121,324
8	Fuel and energy costs	3,849	4,549	4,588	4,627	4,666	4,706	4,745	4,784	4,823	4,862	4,901
9	Material costs	29,161	31,399	31,669	31,939	32,209	32,479	32,749	33,020	33,290	33,560	33,830
10	Maintenance costs	10,379	7,971	8,040	8,108	8,177	8,245	8,314	8,382	8,451	8,520	8,588
11	Other operational costs	16,583	17,465	17,615	17,765	17,916	18,066	18,216	18,366	18,517	18,667	18,817
12	Redirected costs	9,068	8,350	6,947	6,609	7,620	7,520	7,427	7,341	7,260	7,190	7,124
13	Total operational costs	198,484	228,670	223,615	219,627	216,987	213,235	209,491	205,754	202,022	198,301	194,584
14	Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15	Operational income excl. depn.	-198,484	-228,670	-223,615	-219,627	-216,987	-213,235	-209,491	-205,754	-202,022	-198,301	-194,584
16	Depreciation	51,086	66,988	71,241	82,102	95,372	109,713	124,673	140,234	155,630	171,107	186,623
17	Operational costs incl. depn.	249,570	295,658	294,857	301,728	312,359	322,948	334,165	345,988	357,652	369,407	381,207
18	Net income	-249,570	-295,658	-294,857	-301,728	-312,359	-322,948	-334,165	-345,988	-357,652	-369,407	-381,207
19	Financial costs			0	3,732	9,945	17,876	26,354	36,192	47,258	61,073	75,479
20	Profit / loss	-249,570	-295,658	-294,857	-305,460	-322,304	-340,824	-360,519	-382,180	-404,910	-430,480	-456,685
21	Redirected to Passenger Sector	151,489	179,464	178,978	185,415	195,638	206,880	218,835	231,983	245,781	261,301	277,208
22	Redirected to Freight Sector	98,081	116,193	115,879	120,046	126,665	133,944	141,684	150,197	159,130	169,179	179,477
23	Profit / loss after redirected costs	0	0	0	0	0	0	0	0	0	0	0

Annex 4.3.9 : SCENARIO 2A – PKP Telecommunication Vertical, 000 PLN

	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income											
2	Passenger transport income											
3	Other income											
4	TOTAL	0	0	0	0	0	0	0	0	0	0	0
5	Subsidies											
6	Total operational incomes (4+5)	0	0	0	0	0	0	0	0	0	0	0
7	Salary costs	136,003	166,990	162,599	158,208	153,817	149,426	145,035	140,644	136,253	131,863	127,472
8	Fuel and energy costs	9,465	11,184	10,945	10,706	10,467	10,228	9,989	9,750	9,511	9,272	9,034
9	Material costs	39,064	42,062	41,163	40,265	39,366	38,467	37,569	36,670	35,772	34,873	33,974
10	Maintenance costs	16,391	12,589	12,320	12,051	11,782	11,513	11,244	10,975	10,706	10,437	10,168
11	Other operational costs	25,431	26,784	26,212	25,640	25,067	24,495	23,923	23,351	22,778	22,206	21,634
12	Redirected costs	9,528	8,773	7,299	6,944	8,006	7,901	7,803	7,713	7,628	7,554	7,485
13	Total operational costs	235,882	268,382	260,538	253,813	248,506	242,031	235,564	229,103	222,649	216,205	209,766
14	Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15	Operational income excl. depn.	-235,882	-268,382	-260,538	-253,813	-248,506	-242,031	-235,564	-229,103	-222,649	-216,205	-209,766
16	Depreciation	48,915	64,140	69,795	75,230	80,664	86,099	96,333	106,567	116,802	127,036	137,271
17	Operational costs incl. depn.	284,797	332,522	330,333	329,043	329,170	328,130	331,897	335,671	339,451	343,242	347,037
18	Net income	-284,797	-332,522	-330,333	-329,043	-329,170	-328,130	-331,897	-335,671	-339,451	-343,242	-347,037
19	Financial costs			0	4,425	7,879	11,887	15,889	22,923	30,591	40,159	50,149
20	Profit / loss	-284,797	-332,522	-330,333	-333,469	-337,050	-340,017	-347,786	-358,594	-370,042	-383,400	-397,186
21	Redirected to Passenger Sector	166,036	193,860	192,584	194,412	196,500	198,230	202,759	209,060	215,735	223,522	231,560
22	Redirected to Freight Sector	118,760	138,662	137,749	139,056	140,550	141,787	145,027	149,534	154,308	159,878	165,627
23	Profit / loss after redirected costs	0	0	0	0	0	0	0	0	0	0	0

Annex 4.3.10 : SCENARIO 2A – PKP Real Estate Vertical, 000 PLN

	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income											
2	Passenger transport income											
3	Other income											
4	TOTAL	0	0	0	0	0	0	0	0	0	0	0
5	Subsidies											
6	Total operational incomes (4+5)	0	0	0	0	0	0	0	0	0	0	0
7	Salary costs	55,957	68,706	66,899	65,093	63,286	61,480	59,673	57,866	56,060	54,253	52,447
8	Fuel and energy costs	23,278	27,506	27,506	27,506	27,506	27,506	27,506	27,506	27,506	27,506	27,506
9	Material costs	18,346	19,754	19,754	19,754	19,754	19,754	19,754	19,754	19,754	19,754	19,754
10	Maintenance costs	43,922	33,733	33,733	33,733	33,733	33,733	33,733	33,733	33,733	33,733	33,733
11	Other operational costs	21,783	22,942	22,942	22,942	22,942	22,942	22,942	22,942	22,942	22,942	22,942
12	Redirected costs	3,920	3,609	3,003	2,857	3,294	3,251	3,211	3,173	3,138	3,108	3,079
13	Total operational costs	167,206	176,250	173,837	171,885	170,515	168,665	166,819	164,975	163,133	161,296	159,461
14	Extraordinary profits and losses					0	0	0	0	0	0	0
15	Operational income excl. depn.	-167,206	-176,250	-173,837	-171,885	-170,515	-168,665	-166,819	-164,975	-163,133	-161,296	-159,461
16	Depreciation	26,891	28,792	28,251	27,718	27,195	26,675	26,158	25,642	25,127	24,614	24,101
17	Operational costs incl. depn.	194,097	205,042	202,088	199,603	197,710	195,341	192,977	190,617	188,260	185,910	183,563
18	Net income	-194,097	-205,042	-202,088	-199,603	-197,710	-195,341	-192,977	-190,617	-188,260	-185,910	-183,563
19	Financial costs			0	154	285	442	602	786	989	1,250	1,520
20	Profit / loss	-194,097	-205,042	-202,088	-199,757	-197,995	-195,783	-193,578	-191,403	-189,250	-187,160	-185,082
21	Redirected to Passenger Sector	119,486	126,224	124,405	122,970	121,886	120,524	119,167	117,828	116,502	115,216	113,937
22	Redirected to Freight Sector	74,611	78,818	77,683	76,787	76,109	75,259	74,412	73,575	72,748	71,944	71,146
23	Profit / loss after redirected cost	0	0	0	0	0	0	0	0	0	0	0

Annex 4.3.11 : SCENARIO 2A – PKP Housing Vertical, 000 PLN

	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income											
2	Passenger transport income											
3	Other income	125,288	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966
4	TOTAL	125,288	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966
5	Subsidies											
6	Total operational incomes (4+5)	125,288	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966	153,966
7	Salary costs	40,524	49,757	48,449	47,140	45,832	44,524	43,215	41,907	40,599	39,290	37,982
8	Fuel and energy costs	80,370	94,966	94,966	94,966	94,966	94,966	94,966	94,966	94,966	94,966	94,966
9	Material costs	9,389	10,110	10,110	10,110	10,110	10,110	10,110	10,110	10,110	10,110	10,110
10	Maintenance costs	28,539	21,919	21,919	21,919	21,919	21,919	21,919	21,919	21,919	21,919	21,919
11	Other operational costs	61,595	64,873	64,873	64,873	64,873	64,873	64,873	64,873	64,873	64,873	64,873
12	Non transportation costs											
13	Total operational costs	220,416	241,625	240,317	239,008	237,700	236,392	235,083	233,775	232,467	231,158	229,850
14	Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15	Operational income excl. depn.	-95,128	-87,659	-86,351	-85,042	-83,734	-82,426	-81,117	-79,809	-78,501	-77,192	-75,884
16	Depreciation	26,314	34,505	34,062	33,199	32,336	31,474	30,611	29,749	28,886	28,023	27,161
17	Operational costs incl. depn.	246,730	276,130	274,378	272,207	270,036	267,865	265,694	263,523	261,353	259,182	257,011
18	Net income	-121,442	-122,164	-120,412	-118,241	-116,070	-113,899	-111,728	-109,557	-107,387	-105,216	-103,045
19	Financial costs			0	361	326	329	331	342	355	381	403
20	Profit / loss	-121,442	-122,164	-120,412	-118,602	-116,396	-114,229	-112,059	-109,899	-107,741	-105,597	-103,448
21	Redirected to Passenger Sector	24,325	24,469	24,119	23,756	23,314	22,880	22,445	22,013	21,581	21,151	20,721
22	Redirected to Freight Sector	18,592	18,702	18,434	18,157	17,819	17,488	17,155	16,825	16,494	16,166	15,837
23	Redirected to Traction	34,126	34,329	33,837	33,328	32,708	32,099	31,490	30,883	30,276	29,674	29,070
24	Redirected to Infra (road)	15,462	15,554	15,331	15,101	14,820	14,544	14,268	13,993	13,718	13,445	13,171
25	Redirected to Infra (non-road)	6,560	6,599	6,504	6,406	6,287	6,170	6,053	5,936	5,820	5,704	5,588
26	Redirected to Automation	6,173	6,210	6,121	6,029	5,917	5,807	5,696	5,587	5,477	5,368	5,259
27	Redirected to Electro-energetic	5,876	5,911	5,826	5,738	5,631	5,527	5,422	5,317	5,213	5,109	5,005
28	Redirected to pass wagons	3,063	3,082	3,037	2,992	2,936	2,881	2,827	2,772	2,718	2,664	2,610
29	Redirected to freight wagons	4,725	4,753	4,685	4,614	4,528	4,444	4,360	4,276	4,192	4,108	4,025
30	Redirected to real estate	2,540	2,555	2,518	2,481	2,434	2,389	2,344	2,299	2,253	2,209	2,164
31	Profit / loss after redirected cost	0	0	0	0	0	0	0	0	0	0	0

Annex 4.3.12 : SCENARIO 2A – PKP Railway Health Service Vertical, 000 PLN

	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income											
2	Passenger transport income											
3	Other income											
4	TOTAL	0	0	0	0	0	0	0	0	0	0	0
5	Subsidies	307,848	392,223	392,223	392,223	0	0	0	0	0	0	0
6	Total operational incomes (4+5)	307,848	392,223	392,223	392,223	0	0	0	0	0	0	0
7	Salary costs	224,307	275,415	268,173	260,931	0	0	0	0	0	0	0
8	Fuel and energy costs	13,828	16,340	16,340	16,340	0	0	0	0	0	0	0
9	Material costs	77,140	83,061	83,061	83,061	0	0	0	0	0	0	0
10	Maintenance costs	8,065	6,194	6,194	6,194	0	0	0	0	0	0	0
11	Other operational costs	20,484	21,574	21,575	21,576	40,000	40,000	40,000	40,000	40,000	40,000	40,000
12	Non transportation costs											
13	Total operational costs	343,824	402,584	395,343	388,102	40,000	40,000	40,000	40,000	40,000	40,000	40,000
14	Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15	Operational income excl. depn.	-35,976	-10,361	-3,120	4,121	-40,000	-40,000	-40,000	-40,000	-40,000	-40,000	-40,000
16	Depreciation	11,163	14,638	15,325	19,861	0	0	0	0	0	0	0
17	Operational costs incl. depn.	354,987	417,222	410,668	407,963	40,000	40,000	40,000	40,000	40,000	40,000	40,000
18	Net income	-47,139	-24,999	-18,445	-15,740	-40,000	-40,000	-40,000	-40,000	-40,000	-40,000	-40,000
19	Financial costs			0	463							
20	Profit / loss	-47,139	-24,999	-18,445	-16,203	-40,000	-40,000	-40,000	-40,000	-40,000	-40,000	-40,000
21	Redirected to Passenger Sector	9,442	5,007	3,695	3,246	8,012	8,012	8,012	8,012	8,012	8,012	8,012
22	Redirected to Freight Sector	7,217	3,827	2,824	2,481	6,124	6,124	6,124	6,124	6,124	6,124	6,124
23	Redirected to Traction	13,247	7,025	5,183	4,553	11,240	11,240	11,240	11,240	11,240	11,240	11,240
24	Redirected to Infra (road)	6,002	3,183	2,348	2,063	5,093	5,093	5,093	5,093	5,093	5,093	5,093
25	Redirected to Infra (non-road)	2,546	1,350	996	875	2,161	2,161	2,161	2,161	2,161	2,161	2,161
26	Redirected to Automation	2,396	1,271	938	824	2,033	2,033	2,033	2,033	2,033	2,033	2,033
27	Redirected to Electro-energetic	2,281	1,210	892	784	1,935	1,935	1,935	1,935	1,935	1,935	1,935
28	Redirected to pass wagons	1,189	631	465	409	1,009	1,009	1,009	1,009	1,009	1,009	1,009
29	Redirected to freight wagons	1,834	973	718	630	1,556	1,556	1,556	1,556	1,556	1,556	1,556
30	Redirected to real estate	986	523	386	339	837	837	837	837	837	837	837
31	Profit / loss after redirected costs	0	0	0	0	0	0	0	0	0	0	0

Annex 4.3.13 : SCENARIO 2A – PKP Welfare Vertical, 000 PLN

Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1 Cargo transport income											
2 Passenger transport income											
3 Other income	68,914	69,406	70,076	81,100	89,200	96,000	101,000	105,000	108,000	110,000	112,000
4 TOTAL	68,914	69,406	70,076	81,100	89,200	96,000	101,000	105,000	108,000	110,000	112,000
5 Subsidies											
6 Total operational incomes (4+5)	68,914	69,406	70,076	81,100	89,200	96,000	101,000	105,000	108,000	110,000	112,000
7 Salary costs	32,419	39,806	21,185	23,300	25,200	27,500	28,800	29,950	30,800	31,400	32,028
8 Fuel and energy costs	7,024	8,299	7,000	7,800	8,500	9,300	9,765	10,253	10,560	10,770	10,985
9 Material costs	10,054	10,826	22,000	22,500	24,750	25,614	27,084	27,948	28,693	29,040	29,332
10 Maintenance costs	17,852	13,711	15,722	17,700	19,200	20,929	21,975	22,854	23,541	24,003	24,485
11 Other operational costs	17,791	18,737	5,330	7,700	8,400	9,156	9,613	9,997	10,196	10,400	10,608
12 Non transportation costs	0	0	0	0	0	0	0	0	0	0	0
13 Total operational costs	85,140	91,379	71,237	79,000	86,050	92,499	97,237	101,002	103,790	105,613	107,438
14 Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15 Operational income excl. depn.	-16,226	-21,973	-1,161	2,100	3,150	3,501	3,763	3,998	4,210	4,387	4,562
16 Depreciation	2,622	3,438	3,560	3,713	3,902	4,132	4,394	4,690	5,025	5,402	5,802
17 Operational costs incl. depn.	87,762	94,817	74,797	82,713	89,952	96,631	101,631	105,692	108,815	111,015	113,240
18 Net income	-18,848	-25,411	-4,721	-1,613	-752	-631	-631	-692	-815	-1,015	-1,240
19 Financial costs			0	179	347	567	819	1,129	1,497	1,991	2,550
20 Profit / loss	-18,848	-25,411	-4,721	-1,792	-1,099	-1,198	-1,449	-1,821	-2,311	-3,006	-3,790
21 Redirected to Passenger Sector	3,775	5,090	946	359	220	240	290	365	463	602	759
22 Redirected to Freight Sector	2,885	3,890	723	274	168	183	222	279	354	460	580
23 Redirected to Traction	5,296	7,141	1,327	504	309	337	407	512	650	845	1,065
24 Redirected to Infra (road)	2,400	3,235	601	228	140	152	185	232	294	383	483
25 Redirected to Infra (non-road)	1,018	1,373	255	97	59	65	78	98	125	162	205
26 Redirected to Automation	958	1,292	240	91	56	61	74	93	118	153	193
27 Redirected to Electro-energetic	912	1,229	228	87	53	58	70	88	112	145	183
28 Redirected to pass wagons	475	641	119	45	28	30	37	46	58	76	96
29 Redirected to freight wagons	733	989	184	70	43	47	56	71	90	117	147
30 Redirected to real estate	394	531	99	37	23	25	30	38	48	63	79
31 Profit / loss after redirected cost	0	0	0	0	0	0	0	0	0	0	0

Annex 4.3.14 : SCENARIO 2A – Structural Units subordinated to PKP's Management Board + remaining incomes & costs, 000 PLN

	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income											
2	Passenger transport income											
3	Other income	769,418	951,614	951,614	951,614	951,614	951,614	951,614	951,614	951,614	951,614	951,614
4	TOTAL	769,418	951,614	951,614	951,614	951,614	951,614	951,614	951,614	951,614	951,614	951,614
5	Subsidies				400,000	400,000	400,000	400,000	400,000			
6	Total operational incomes (4+5)	769,418	951,614	951,614	1,351,614	1,351,614	1,351,614	1,351,614	1,351,614	951,614	951,614	951,614
7	Salary costs											
8	Fuel and energy costs											
9	Material costs											
10	Maintenance costs											
11	Other operational costs	855,523	944,814	944,814	944,814	944,814	944,814	944,814	944,814	944,814	944,814	944,814
12	Non transportation costs											
13	Total operational costs	855,523	944,814	944,814	944,814	944,814	944,814	944,814	944,814	944,814	944,814	944,814
14	Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15	Operational income excl. depn.	-86,105	6,800	6,800	406,800	406,800	406,800	406,800	406,800	6,800	6,800	6,800
16	Depreciation	20,128	48,478	43,630	38,782	33,935	29,087	24,239	19,391	14,543	9,696	4,848
17	Operational costs incl. depn.	875,651	993,292	988,444	983,596	978,749	973,901	969,053	964,205	959,357	954,510	949,662
18	Net income	-106,233	-41,678	-36,830	368,018	372,865	377,713	382,561	387,409	-7,743	-2,896	1,952
19	Financial costs	63,905	114,564	163,564	163,564	163,564	163,564	163,564	163,564	163,564	163,564	163,564
20	Profit / loss	-170,138	-156,242	-200,394	204,454	209,301	214,149	218,997	223,845	-171,307	-166,460	-161,612
21	Redirected to Passenger Sector	95,100	87,593	111,444	-107,255	-109,874	-112,492	-115,111	-117,730	95,731	93,113	90,494
22	Redirected to Freight Sector	75,039	68,649	88,950	-97,199	-99,428	-101,657	-103,886	-106,115	75,576	73,347	71,118
23	Profit / loss after redirected costs	0	0	0	0	0	0	0	0	0	0	0

Annex 4.3.15 : SCENARIO 2A – PKP Base Data, 000 PLN

Base Data for Financial projections	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Passenger-km (mln)	26,622	26,558	26,767	26,977	27,186	27,395	27,605	27,814	28,023	28,233	28,442
Net ton-km	69,094	68,308	68,399	68,489	68,580	68,670	68,761	68,851	68,942	69,032	69,123
Passenger revenue increase			0%	0%	0%	0%	0%	0%	0%	0%	0%
Freight revenue increase			0%	0%	0%	0%	0%	0%	0%	0%	0%
Passenger vehicle-km	1,072	1,069	1,056	1,042	1,029	1,015	1,002	988	975	961	948
Freight vehicle-km	1,000	989	990	991	993	994	995	996	998	999	1,000
Staff Numbers	240,792	233,183	227,052	220,920	214,789	208,657	202,526	196,394	190,263	184,131	178,000
Line-km	22,599	22,285	21,809	21,333	20,857	20,381	19,904	19,428	18,952	18,476	18,000
Electrified line-km	11,625	11,625	11,725	11,825	11,925	12,025	12,125	12,225	12,325	12,425	12,525
Passenger gross-ton-1000km	51,570	50,941	51,343	51,744	52,146	52,547	52,949	53,350	53,752	54,153	54,555
Freight gross-ton-1000km	142,398	142,788	142,977	143,167	143,356	143,545	143,734	143,924	144,113	144,302	144,492
Total	193,968	193,729	194,320	194,911	195,501	196,092	196,683	197,274	197,865	198,456	199,046
Passenger train-km	172,654	168,956	166,831	164,706	162,581	160,456	158,331	156,207	154,082	151,957	149,832
Freight train-km	107,828	109,803	109,949	110,094	110,240	110,385	110,531	110,676	110,822	110,968	111,113
Total train-km	280,482	278,759	276,780	274,800	272,821	270,842	268,862	266,883	264,904	262,924	260,945

Annex 4.3.16 : SCENARIO 2A – PKP's 1995 Costs, 000 PLN

Sector / Vertical	Total	Salary costs	Fuel & Energy	Materials	Repairs	Other Operational costs	Operational costs excl. depreciation	Depreciation	Operational costs incl. depreciation
Passenger Sector	666,647	535,889	31,394	19,775	1,871	73,138	662,068	4,578	666,647
Freight Sector	494,298	409,590	23,264	14,847	1,362	42,107	491,170	3,129	494,298
Traction	1,873,913	751,822	632,066	101,270	148,411	131,815	1,765,385	108,528	1,873,913
Passenger Rolling Stock	316,692	67,489	4,788	22,996	120,078	46,850	262,201	54,491	316,692
Freight Rolling Stock	379,625	104,087	3,753	28,254	146,281	10,015	292,389	87,236	379,625
Infrastructure Sector	212,320	144,513	7,936	13,272	4,702	34,842	205,265	7,055	212,320
Social Units	87,764	32,419	7,024	10,054	17,852	17,791	85,140	2,622	87,762
Housing	246,731	40,524	80,370	9,389	28,539	61,595	220,417	26,314	246,731
Railway Health Service	354,988	224,307	13,828	77,140	8,065	20,484	343,825	11,163	354,988
Real Estate	190,177	55,957	23,278	18,346	43,922	21,783	163,286	26,891	190,177
Automatics	275,269	136,003	9,465	39,064	16,391	25,431	226,354	48,915	275,269
Road	1,170,519	340,643	22,206	220,095	64,106	124,221	771,272	399,248	1,170,519
Energetics	240,502	129,443	3,849	29,161	10,379	16,583	189,415	51,086	240,502
Total	6,509,445	2,972,685	863,223	603,663	611,959	626,656	5,678,186	831,259	6,509,445
Other organizational units	301,453								
Total	6,810,898								

Annex 4.3.17 : SCENARIO 2A – PKP's 1996 Costs, 000 PLN

Sector / Vertical	Total	Salary costs	Fuel & Energy	Materials	Repairs	Other Operational costs	Operational costs excl. depreciation	Depreciation	Operational costs incl. depreciation
Passenger Sector	800,849	657,990	37,096	21,293	1,437	77,030	794,846	6,003	800,849
Freight Sector	595,885	502,914	27,489	15,987	1,046	44,347	591,783	4,102	595,885
Traction	2,174,148	923,121	746,861	109,044	113,983	138,829	2,031,839	142,309	2,174,148
Passenger Rolling Stock	326,303	82,866	5,658	24,761	92,223	49,343	254,851	71,452	326,303
Freight Rolling Stock	399,944	127,803	4,435	30,422	112,347	10,548	285,555	114,389	399,944
Infrastructure Sector	250,665	177,439	9,378	14,290	3,611	36,696	241,415	9,250	250,665
Social Units	94,817	39,806	8,299	10,826	13,711	18,737	91,379	3,438	94,817
Housing	276,129	49,757	94,966	10,110	21,919	64,873	241,624	34,505	276,129
Railway Health Service	417,222	275,415	16,340	83,061	6,194	21,574	402,584	14,638	417,222
Real Estate	207,903	68,706	27,506	19,754	33,733	22,942	172,641	35,262	207,903
Automatics	323,750	166,990	11,184	42,062	12,589	26,784	259,610	64,140	323,750
Road	1,385,076	418,258	26,239	236,990	49,235	130,831	861,552	523,524	1,385,076
Energetics	287,308	158,936	4,549	31,399	7,971	17,465	220,321	66,988	287,308
Total	7,540,000	3,650,000	1,020,000	650,000	470,000	660,000	6,450,000	1,090,000	7,540,000

Annex 4.3.18 : SCENARIO 2A – PKP's Investment Schedule, 000 PLN

Item	1997	1998	1999	2000	2001	2002	2003	2004	2005
Infrastructure	625,978	832,000	832,000	832,000	842,000	842,000	842,000	842,000	842,000
Infrastructure - cumulative	625,978	1,457,978	2,289,978	3,121,978	3,963,978	4,805,978	5,647,978	6,489,978	7,331,978
Automation	205,526	200,000	200,000	200,000	320,000	320,000	320,000	320,000	320,000
Automation - cumulative	205,526	405,526	605,526	805,526	1,125,526	1,445,526	1,765,526	2,085,526	2,405,526
Signalling	0	0	0	0	0	0	0	0	0
Signalling - cumulative	0	0	0	0	0	0	0	0	0
Energetic	173,321	338,500	398,750	425,500	441,000	456,000	451,900	453,900	454,900
Energetic - cumulative	173,321	511,821	910,571	1,336,071	1,777,071	2,233,071	2,684,971	3,138,871	3,593,771
Passenger Rolling Stock	25,000	25,000	25,000	25,000	25,000	25,000	25,000	25,000	25,000
Passenger Rolling Stock - cumulative	25,000	50,000	75,000	100,000	125,000	150,000	175,000	200,000	225,000
Freight Rolling Stock	23,067	13,672	85,977	20,509	21,033	92,960	41,688	41,688	12,729
Freight Rolling Stock - cumulative	23,067	36,739	122,716	143,225	164,258	257,218	298,906	340,594	353,323
Traction	1,030,598	1,138,415	1,252,258	1,377,483	1,515,231	1,666,754	1,707,213	1,833,428	2,218,413
Traction - cumulative	1,030,598	2,169,013	3,421,271	4,798,754	6,313,985	7,980,739	9,687,952	11,521,380	13,739,793
Social	8,313	9,560	10,994	12,643	13,907	15,298	16,828	18,511	19,437
Social - cumulative	8,313	17,873	28,867	41,510	55,417	70,715	87,543	106,054	125,491
Housing	16,770	0	0	0	0	0	0	0	0
Housing - cumulative	16,770	16,770	16,770	16,770	16,770	16,770	16,770	16,770	16,770
Health	21,506	60,000	0	0	0	0	0	0	0
Health - cumulative	21,506	81,506	81,506	81,506	81,506	81,506	81,506	81,506	81,506
Real Estate	7,143	7,500	7,860	8,000	8,100	8,150	8,200	8,250	8,300
Real Estate - Cumulative	7,143	14,643	22,503	30,503	38,603	46,753	54,953	63,203	71,503
TOTAL FOR YEAR	2,137,222	2,624,647	2,812,839	2,901,135	3,186,271	3,426,162	3,412,829	3,542,777	3,900,779
TOTAL - CUMULATIVE	2,137,222	4,761,869	7,574,708	10,475,843	13,662,114	17,088,276	20,501,105	24,043,882	27,944,661

Annex 4.4.1 : SCENARIO 1C(i) – PKP Consolidated + Infrastructure +separated units (Macroeconomic view), 000 PLN

	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income	4,298,289	5,025,380	5,032,042	5,290,639	5,297,635	5,304,630	5,311,625	5,318,620	5,325,616	5,332,611	5,339,606
2	Passenger transport income	1,069,226	1,221,580	1,231,209	1,464,188	1,475,550	1,486,912	1,498,273	1,509,635	1,520,997	1,532,359	1,543,721
3	Other income	963,620	1,174,986	1,175,656	1,186,680	1,040,814	1,047,614	1,052,614	1,056,614	1,059,614	1,061,614	1,063,614
	Required New Income				33,000	65,000	130,000	195,000	260,000	390,000	520,000	650,000
4	TOTAL	6,331,135	7,421,946	7,438,907	7,974,507	7,878,998	7,969,155	8,057,512	8,144,869	8,296,226	8,446,583	8,596,940
5	Subsidies	1,011,641	963,723	963,723	963,723	571,500	571,500	571,500	571,500	571,500	571,500	571,500
6	Total operational incomes (4+5)	7,342,776	8,385,669	8,402,630	8,938,230	8,450,498	8,540,655	8,629,012	8,716,369	8,867,726	9,018,083	9,168,440
7	Salary costs	2,972,685	3,650,001	3,505,487	3,381,709	3,011,114	2,897,125	2,782,136	2,666,997	2,551,558	2,435,869	2,320,209
8	Fuel and energy costs	863,223	1,020,000	1,019,520	1,021,138	911,351	912,970	914,254	915,560	916,686	917,715	918,748
9	Material costs	603,663	649,999	654,987	649,300	552,193	546,871	542,154	536,832	531,391	525,551	519,657
10	Maintenance costs	611,959	469,999	469,990	469,949	441,316	441,026	440,052	438,911	437,579	436,021	434,484
11	Other operational costs	1,482,178	1,604,813	1,587,888	1,586,739	1,537,471	1,534,708	1,531,645	1,528,510	1,525,189	1,521,874	1,518,563
12	Redirected costs	0	0	0	0	0	0	0	0	0	0	0
13	Total operational costs	6,533,708	7,394,812	7,237,871	7,108,836	6,453,445	6,332,698	6,210,241	6,086,810	5,962,403	5,837,030	5,711,660
14	Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15	Operational income excl. depn.	809,068	990,857	1,164,758	1,829,395	1,997,054	2,207,957	2,418,772	2,629,559	2,905,324	3,181,053	3,456,780
16	Depreciation	851,385	1,132,008	1,191,008	1,260,591	1,313,556	1,415,779	1,531,982	1,662,834	1,778,494	1,902,215	2,048,425
17	Operational costs incl. depn.	7,385,093	8,526,820	8,428,879	8,369,427	7,767,000	7,748,477	7,742,222	7,749,645	7,740,896	7,739,246	7,760,085
18	Net income	-42,317	-141,151	-26,249	568,804	683,498	792,178	886,790	966,725	1,126,830	1,278,838	1,408,356
19	Financial costs	63,905	114,564	163,564	205,472	220,292	239,377	251,774	267,722	284,999	288,638	283,089
20	Profit / loss	-106,222	-255,715	-189,813	363,332	463,206	552,802	635,016	699,003	841,831	990,200	1,125,267
1	Net operating income			-189,813	363,332	463,206	552,802	635,016	699,003	841,831	990,200	1,125,267
2	Depreciation			1,191,008	1,260,591	1,313,556	1,415,779	1,531,982	1,662,834	1,778,494	1,902,215	2,048,425
3	Investment			2,098,946	2,668,182	2,891,555	2,971,022	3,227,644	3,443,546	3,071,546	3,188,499	3,510,701
4	Investment Subsidy			400,000	800,000	800,000	800,000	800,000	800,000	400,000	400,000	400,000
5	Borrowing in year			697,752	244,260	314,794	202,441	260,646	281,709	51,222	-103,916	-62,991
6	Borrowing to date (additional)		700,000	1,397,752	1,642,012	1,956,805	2,159,246	2,419,892	2,701,601	2,752,822	2,648,906	2,585,915
7	Borrowing / Investment - cumul			33.2%	20.7%	16.9%	14.0%	12.6%	11.7%	10.2%	8.3%	7.0%
8												
9	interest rate	6.0%										

Annex 4.4.2 : SCENARIO 1C(i) – PKP Freight Sector(incl. freight, wagons, traction), 000 PLN

Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1 Cargo transport income	4,298,289	5,025,380	5,032,042	5,290,639	5,297,635	5,304,630	5,311,625	5,318,620	5,325,616	5,332,611	5,339,606
2 Passenger transport income	0	0	0	0	0	0	0	0	0	0	0
3 Other income	0	0	0	0	0	0	0	0	0	0	0
4 TOTAL	4,298,289	5,025,380	5,032,042	5,290,639	5,297,635	5,304,630	5,311,625	5,318,620	5,325,616	5,332,611	5,339,606
5 Subsidies	0	0	0	0	0	0	0	0	0	0	0
6 Total operational incomes (4+5)	4,298,289	5,025,380	5,032,042	5,290,639	5,297,635	5,304,630	5,311,625	5,318,620	5,325,616	5,332,611	5,339,606
7 Salary costs	802,706	985,600	951,231	916,861	882,492	848,123	813,753	779,384	745,014	710,645	676,276
8 Fuel and energy costs	491,037	580,218	581,930	583,641	585,353	587,064	588,776	590,488	592,199	593,911	595,622
9 Material costs	82,033	88,330	88,515	88,700	88,885	89,070	89,256	89,441	89,626	89,811	89,996
10 Maintenance costs	204,697	157,212	157,486	157,760	158,034	158,307	158,581	158,855	159,129	159,403	159,676
11 Other operational costs	102,797	108,266	108,501	108,735	108,970	109,205	109,439	109,674	109,908	110,143	110,378
Infrastructure charges					2,779,627	2,777,681	2,776,174	2,774,893	2,765,593	2,756,348	2,747,130
12 Redirected costs	1,005,160	1,377,637	1,364,751	1,357,664	319,796	315,011	311,901	309,251	306,608	303,648	300,350
13 Total operational costs	2,688,430	3,297,263	3,252,414	3,213,362	4,923,157	4,884,462	4,847,880	4,811,985	4,768,078	4,723,908	4,679,428
14 Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15 Operational income excl. depn.	1,609,859	1,728,117	1,779,629	2,077,277	374,477	420,168	463,745	506,635	557,538	608,702	660,178
16 Depreciation	132,087	173,200	191,002	204,954	229,153	252,260	278,737	313,415	345,843	381,327	424,312
17 Operational costs incl. depn.	2,820,517	3,470,463	3,443,416	3,418,316	5,152,310	5,136,723	5,126,617	5,125,400	5,113,920	5,105,236	5,103,740
18 Net income	1,477,772	1,554,917	1,588,626	1,872,323	145,325	167,907	185,008	193,220	211,695	227,375	235,866
19 Financial costs	0	0	0	8,363	9,718	13,102	15,035	17,636	21,030	22,120	21,497
20 Profit / loss	1,477,772	1,554,917	1,588,626	1,863,961	135,607	154,805	169,973	175,584	190,665	205,255	214,369

Annex 4.4.3 : SCENARIO 1C(i) – PKP Passenger Sector (incl. freight, wagons, traction), 000 PLN

	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income	0	0	0	0	0	0	0	0	0	0	0
2	Passenger transport income	1,069,226	1,221,580	1,231,209	1,464,188	1,475,550	1,486,912	1,498,273	1,509,635	1,520,997	1,532,359	1,543,721
3	Other income	0	0	0	0	0	0	0	0	0	0	0
4	TOTAL	1,069,226	1,221,580	1,231,209	1,464,188	1,475,550	1,486,912	1,498,273	1,509,635	1,520,997	1,532,359	1,543,721
5	Subsidies (current)	338,293	571,500	571,500	571,500	571,500	571,500	571,500	571,500	571,500	571,500	571,500
6	From Passenger PSC Fund					3,173,548	3,163,550	3,157,211	3,150,042	3,142,835	3,143,190	3,147,590
7	Total operational incomes (4-6)	1,407,519	1,793,080	1,802,709	2,035,688	5,220,598	5,221,962	5,226,985	5,231,178	5,235,332	5,247,049	5,262,810
8	Salary costs	1,066,171	1,309,094	1,263,444	1,217,794	1,172,144	1,126,494	1,080,844	1,035,193	989,543	943,893	898,243
9	Fuel and energy costs	204,229	241,321	241,389	241,457	241,524	241,592	241,660	241,728	241,796	241,864	241,932
10	Material costs	105,109	113,177	112,803	112,428	112,054	111,679	111,305	110,930	110,556	110,181	109,807
11	Maintenance costs	213,305	163,824	162,860	161,896	160,932	159,968	159,004	158,040	157,076	156,112	155,148
12	Other operational costs	201,129	211,831	212,078	212,325	212,572	212,820	213,067	213,314	213,561	213,809	214,056
13	Infrastructure Charges					2,325,269	2,325,895	2,327,038	2,328,524	2,323,511	2,318,568	2,313,658
14	Redirected costs	1,075,694	1,399,410	1,388,366	1,379,952	448,595	442,208	438,158	434,749	431,349	427,499	423,172
15	Total operational costs	2,865,638	3,438,657	3,380,939	3,325,852	4,673,090	4,620,656	4,571,076	4,522,479	4,467,393	4,411,925	4,356,015
16	Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
17	Operational income excl. depn.	-1,458,119	-1,645,577	-1,578,231	-1,290,164	547,507	601,306	655,908	708,699	767,940	835,124	906,795
18	Depreciation	125,875	165,055	200,209	230,313	269,447	313,438	362,770	417,979	474,757	536,429	613,032
19	Operational costs incl. depn.	2,991,513	3,603,712	3,581,148	3,556,165	4,942,538	4,934,094	4,933,847	4,940,458	4,942,150	4,948,355	4,969,047
20	Net income	-1,583,994	-1,810,632	-1,778,440	-1,520,477	278,060	287,868	293,138	290,719	293,183	298,694	293,763
21	Financial costs	0	0	0	13,152	15,461	19,872	23,095	27,300	32,017	33,749	32,865
22	Profit / loss	-1,583,994	-1,810,632	-1,778,440	-1,533,629	262,599	267,996	270,043	263,419	261,166	264,945	260,899

Annex 4.4.4 : SCENARIO 1C(i) – PKP Infrastructure Sector (road , non-road, electro-energetic), 000 PLN

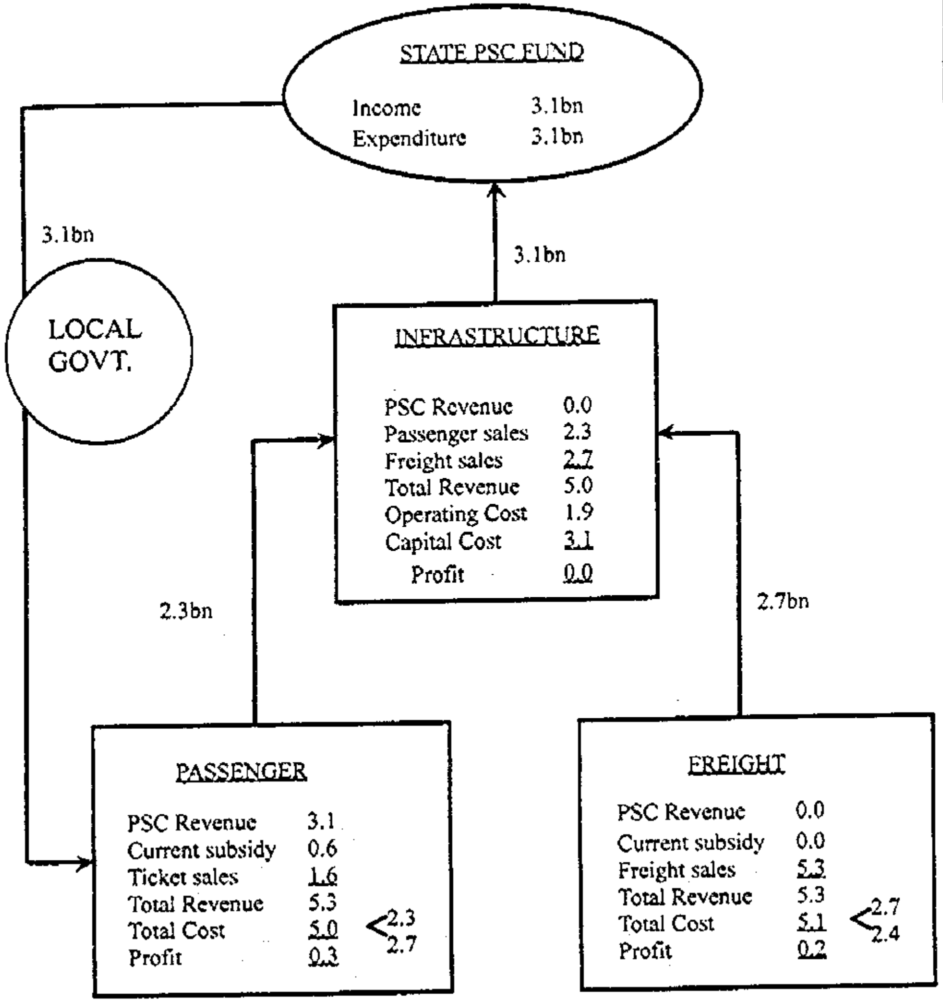
	Year	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
1	Cargo transport income	0	0	0	0	2,779,627	2,777,681	2,776,174	2,774,893	2,765,593	2,756,348	2,747,130
2	Passenger transport income	0	0	0	0	2,325,269	2,325,895	2,327,038	2,328,524	2,323,511	2,318,568	2,313,658
3	Other income	0	0	0	0	0	0	0	0	0	0	0
4	TOTAL	0	0	0	0	5,104,896	5,103,577	5,103,212	5,103,417	5,089,104	5,074,916	5,060,788
5	Subsidies	365,500	0	0	0	0	0	0	0	0	0	0
6	Total operational incomes (4+5)	365,500	0	0	0	5,104,896	5,103,577	5,103,212	5,103,417	5,089,104	5,074,916	5,060,788
7	Salary costs	614,599	754,633	728,318	702,003	675,687	649,372	623,057	596,742	570,427	544,111	517,796
8	Fuel and energy costs	33,992	40,166	39,444	38,722	38,001	37,279	36,557	35,835	35,113	34,391	33,670
9	Material costs	262,527	282,679	277,581	272,482	267,384	262,285	257,187	252,089	246,990	241,892	236,793
10	Maintenance costs	79,187	60,817	59,757	58,696	57,636	56,575	55,515	54,454	53,394	52,333	51,273
11	Other operational costs	175,646	184,992	181,563	178,134	174,705	171,276	167,847	164,418	160,990	157,561	154,132
12	Rdirected costs	43,056	39,644	31,752	27,936	19,673	19,299	18,962	18,654	18,376	18,150	17,949
13	Total operational costs	1,209,008	1,362,931	1,318,414	1,277,974	1,233,085	1,196,087	1,159,125	1,122,192	1,085,289	1,048,439	1,011,613
14	Extraordinary profits and losses	0	0	0	0	0	0	0	0	0	0	0
15	Operational income excl. depn.	-843,508	-1,362,931	-1,318,414	-1,277,974	-1,233,085	-1,196,087	-1,159,125	-1,122,192	-1,085,289	-1,048,439	-1,011,613
16	Depreciation	457,389	599,762	607,743	637,094	671,810	707,490	744,087	781,225	803,815	826,477	849,175
17	Operational costs incl. depn.	1,666,397	1,962,693	1,926,157	1,915,068	1,904,896	1,903,577	1,903,212	1,903,417	1,889,104	1,874,916	1,860,788
18	Net income	-1,300,897	-1,962,693	-1,926,157	-1,915,068	3,200,000	3,200,000	3,200,000	3,200,000	3,200,000	3,200,000	3,200,000
19	Financial costs	0	0	0	15,943	26,452	36,450	42,789	49,958	57,165	56,810	52,410
20	Profit / loss	-1,300,897	-1,962,693	-1,926,157	-1,931,010	3,173,548	3,163,550	3,157,211	3,150,042	3,142,835	3,143,190	3,147,590
21	Redirected to Passenger Sector	620,381	922,962	906,277	909,480	0	0	0	0	0	0	0
22	Redirected to Freight Sector	680,516	1,039,731	1,019,880	1,021,530	0	0	0	0	0	0	0
23	Given to Passenger PSC Fund	0	0	0	0	3,173,548	3,163,550	3,157,211	3,150,042	3,142,835	3,143,190	3,147,590

Annex 4.4.5 : SCENARIO 1C(i) – PKP's Infrastructure Access Charges, 000 PLN

	1999	2000	2001	2002	2003	2004	2005
Value of Infrastructure	32,000,000	33,467,675	34,959,425	36,474,125	38,002,325	39,166,835	40,333,145
Return on Investment (%	10	10	9	9	8	8	8
Required return	3,200,000	3,200,000	3,200,000	3,200,000	3,200,000	3,200,000	3,200,000
Freight Charges							
55.4% of required return	1,772,800	1,772,800	1,772,800	1,772,800	1,772,800	1,772,800	1,772,800
Costs (excl. financing)	1,006,827	1,004,881	1,003,374	1,002,093	992,793	983,548	974,330
Total	2,779,627	2,777,681	2,776,174	2,774,893	2,765,593	2,756,348	2,747,130
Passenger Charges							
44.6% of required return	1,427,200	1,427,200	1,427,200	1,427,200	1,427,200	1,427,200	1,427,200
Costs (excl. financing)	898,069	898,695	899,838	901,324	896,311	891,368	886,458
Total	2,325,269	2,325,895	2,327,038	2,328,524	2,323,511	2,318,568	2,313,658

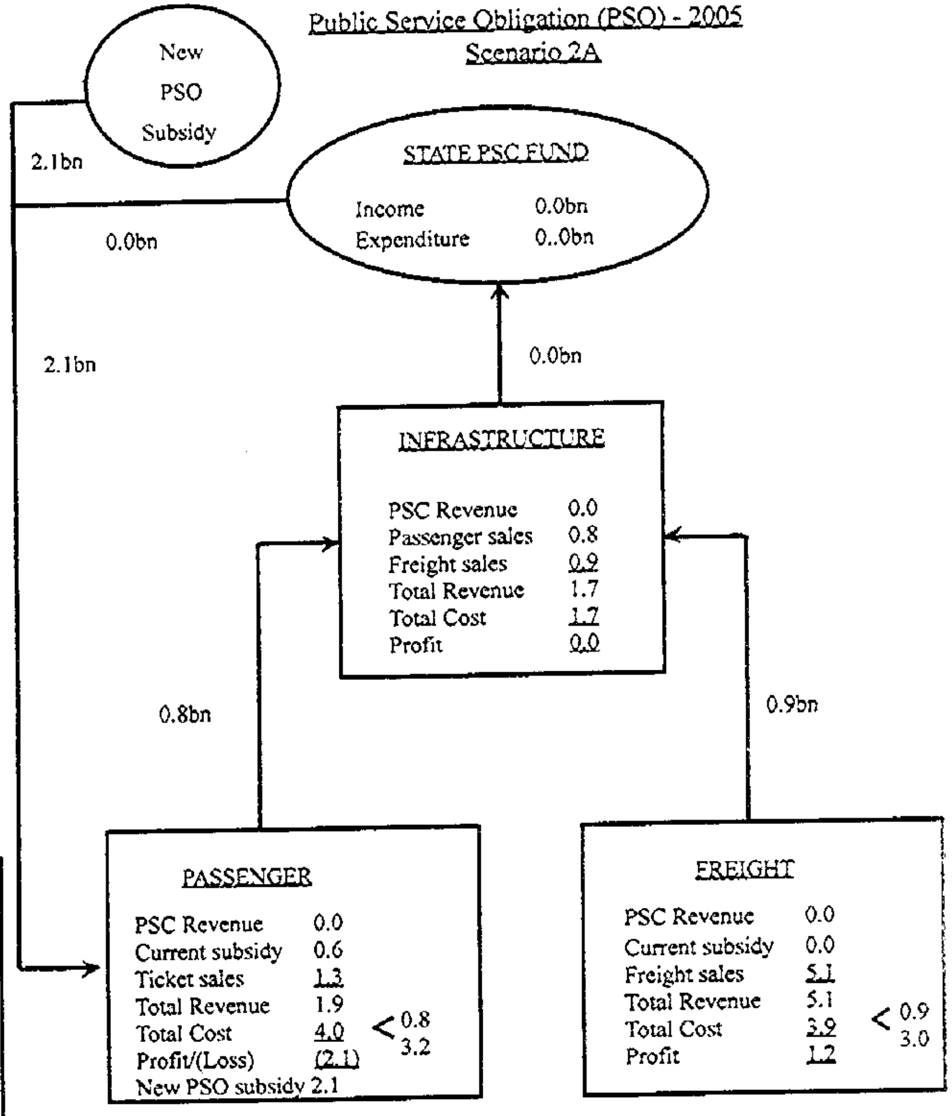
Annex 4.5.1 : SCENARIO 1C(i)

Public Service Contract (PSC) - 2005
Scenario 1C(i)



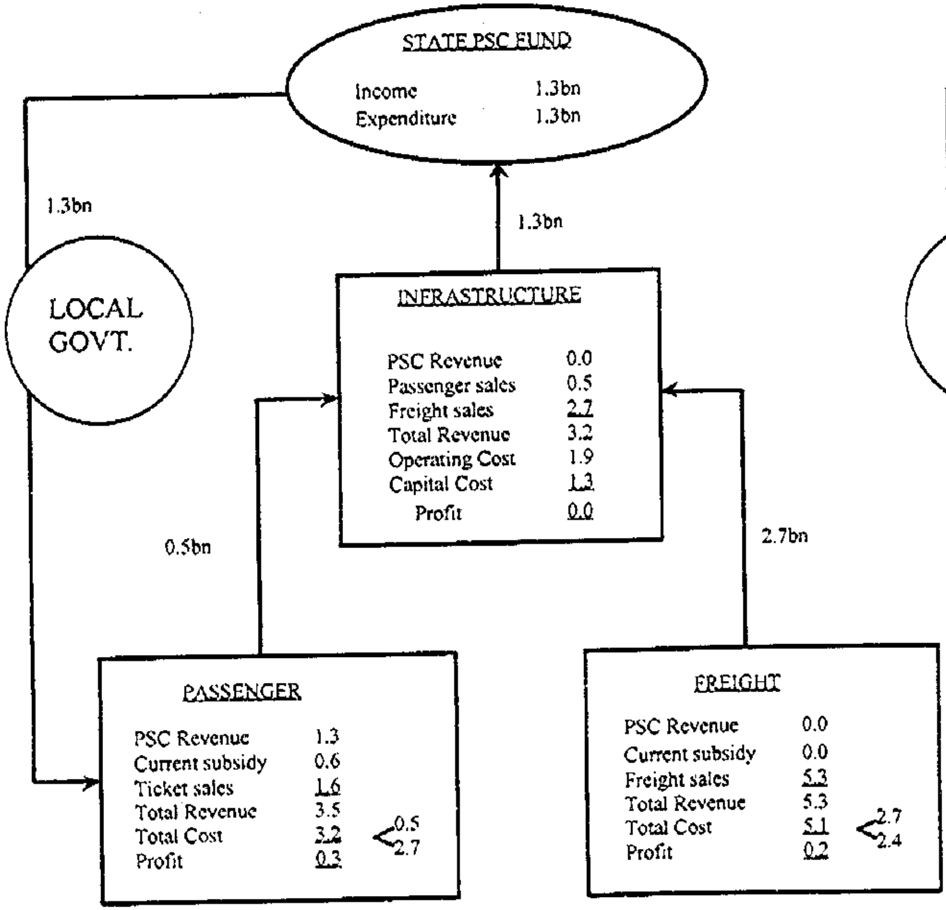
Annex 4.5.2 : SCENARIO 2A

Public Service Obligation (PSO) - 2005
Scenario 2A



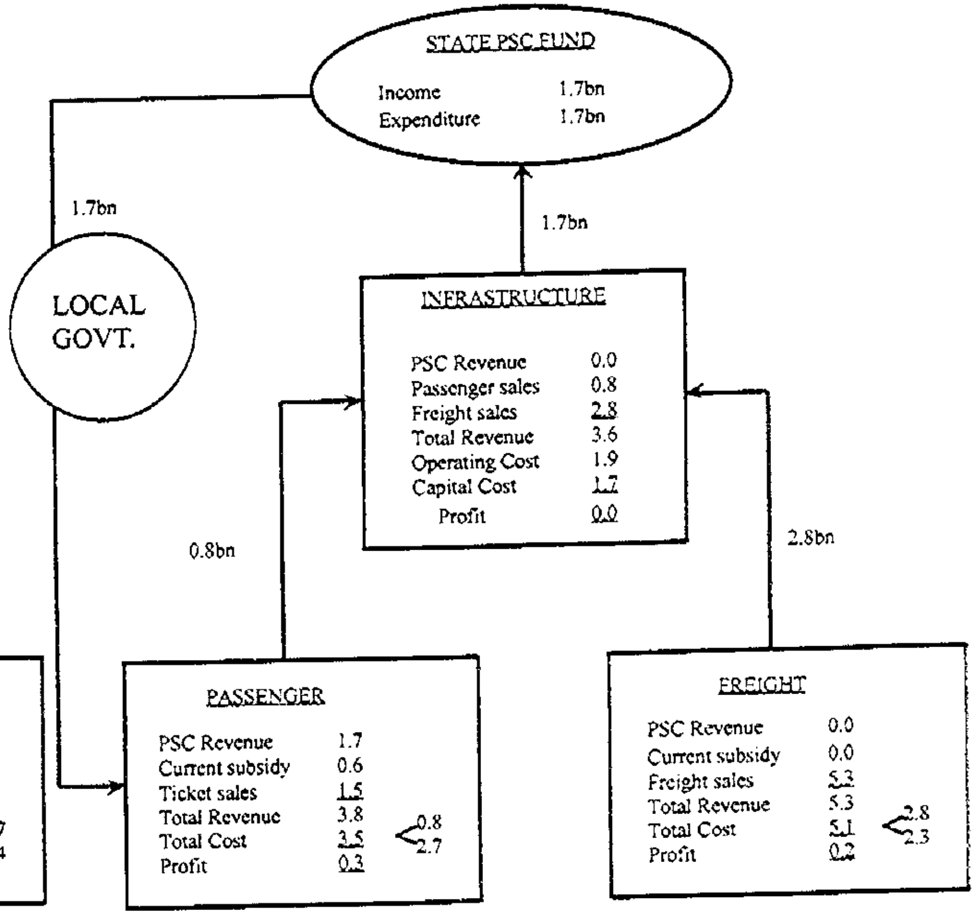
Annex 4.5.3 : SCENARIO 1C(ii)

Public Service Contract (PSC) - 2005
Scenario 1C(ii)



Annex 4.5.4 : SCENARIO 1C(iii)

Public Service Contract (PSC) - 2005
Scenario 1C(iii)



Annex 4.6 :Calculation process for PKP accounts

1 Scenario 2

Conventions:

- Refer to sheets by numbers (1-19)
- Refer to Polish spreadsheet as "Obrachunek kosztow 1995" or OK95

1.1 Base data for financial projections (see Annex 4.3.17)

Figures for 1995 and 1996 are actual values unless otherwise stated.

Table 1 - Sources and Assumptions for Base Data

Base Data	Value Source	Assumptions
Passenger-km (million)	JICA team (2005)	Linear change between 1996 and 2005
Net ton-km	JICA team (2005)	Linear change between 1996 and 2005
Passenger vehicle-km	JICA team (1995 and 2005)	Linear change between 1996 and 2005
Freight vehicle-km	Index of 1000 in 1995	Correlation between Net ton-km and Freight Vehicle-km
Staff numbers	PKP (2005)	Linear change between 1996 and 2005
Line-km (Total)	PKP/JICA (2005)	Linear change between 1996 and 2005
Electrified line-km	Actual 1996 figure	Increase at 100km per annum
Passenger gross-ton-1000km	Actual 1996 figure	Proportional to Passenger-km
Freight gross-ton-1000km	Actual 1996 figure	Proportional to Net ton-km
Total gross-ton-1000km	Sum of Passenger and Freight gross-ton-1000km	N/A
Passenger train-km	Actual 1996 figure	Passenger vehicle-km
Freight train-km	Actual 1996 figure	Freight gross-ton-1000km
Total train-km	Sum of Passenger and Freight train-km	N/A

1.2 PKP's 1995 costs (see Annex 4.3.18)

The allocation of 1995 costs by sector/vertical and by cost category was especially prepared for the JICA team by the PKP in Jaharanka.
The starting point was the division of 6.5bn PLN of 1995 costs into 13 categories. It should be noted that the following vertical's costs have not been separately identified;

- Retirement Pension
- Computerized Data Processing
- Training
- Procurement
- Railway Security Service
- Structural Units Subordinated to the Management Board of the PKP

Passenger Sector, **Freight Sector** and **Traction** costs refer directly to the costs of those sectors.

The JICA team requested the **Passenger Rolling Stock** and **Freight Rolling Stock** costs be separately identified so that the rolling stock could be incorporated into either the **Passenger Sector/Freight Sector** or the **Traction Sector**.

Infrastructure Sector here refers to non-road infrastructure costs.

Social Units, **Housing**, **Railway Health Service** (Railway Health-Care Service), **Real Estate** (Real Estates), **Automatics** (Power Engineering) and **Energetics** (Telecommunication) refer to the costs associated with these verticals.

Other Organizational units includes CNTK, CIK, CBRZ, PKL, POLRES, CBK, FERPOL and printing houses in Poznan, Krakow and Warsaw.

1.3 PKP's 1996 costs (see Annex 4.3.19)

The PKP has not yet analyzed the 1996 costs by sector and vertical. Thus the JICA team has provisionally allocated costs which can be changed once the "actual" numbers are received from the PKP.

The following criteria were used for the 1996 cost allocation:

1. The **Total** is based on the totals for 1995.
2. The allocation by cost category is based on the 1996 cost profile. (e.g. in 1996, staff costs are a higher percentage of total costs).
3. The allocation by sector/vertical is based on the 1995 percentage allocations.

1.4 Investment Schedule (see Annex 4.3.20)

This sheet charts the proposed investment in the various sectors and verticals, and attributers to each a percentage depreciation rate. This data is used in calculating both the financial costs associated with borrowing and the depreciation allocated to each sector and vertical.

1.5 Sheets 2 to 16

1.5.1 General Methodology

The explanation for the derivation of these sheets is given below:

a) All the cost figures are drawn from Sheet 19: "PKP's 1996 costs" and are presented assuming zero inflation.
b) The drivers can be found on Sheet 17: "Base data for financial projections".
c) Numbers in brackets refer to the Annex 4.3 sheet numbers e.g. 4.3.13.
d) Italic words refer to base values on Sheet (17).
e) Values for 1995 and 1996 are actual, after which they are projected on the basis of the stated assumptions.

Table 2: General Methodology

Category	Relating to...		Assumptions and Notes
Cargo transport income	Freight Sector (3)		Proportional to *Net ton-km*
Passenger transport income	Passenger Sector (2)		Proportional to *Passenger-km*
Other income	Housing Vertical(13)		Constant at 1996 value
	Health Vertical(15)		
	Social Vertical(16)		
Subsidies	Passenger Sector (2)		Constant at 1996 value
	Infrastructure Sector (5)		Subsidy ends in 1995
	Health Vertical (14)		Constant at 1996 value until 1998
Salary Costs	Sheets (2) to (15)		Proportional to *Staff Numbers* which vary equally across sectors from year to year
Fuel and Energy Costs, Material Costs, Maintenance Costs and Other Operational Costs	Passenger Sector (2)	Energy, Material and Maintenance	Proportional to *Passenger vehicle-km*
		Other Operational Costs	Proportional to *Passenger km*
	Freight Sector (3)	Energy, Material and Maintenance	Proportional to *Freight vehicle-km*
		Other Operational Costs	Proportional to *Net ton-km*
	Traction Sector (4)		Proportional to *Total-gross-ton-1000km*
	Infrastructure Sector (5)		Proportional to *Line-km*
	Telecommunications Vertical (8)		Proportional to *Line-km*

	Power Engineering Vertical (9)		Proportional to *Electrified line-km*
	Passenger Rolling Stock (10)		Proportional to *Passenger vehicle-km*
	Freight Rolling Stock (11)		Proportional to *Freight vehicle-km*
	Real Estate Vertical (12)		Constant at 1996 value
	Housing Vertical (13)		Constant at 1996 value
	Health Vertical (14)	Energy, Material and Maintenance	Constant at 1996 value until 1998
		Other Operational Costs	Constant at 1996 value until 1998 1999-2005 fixed at 40,000.
	Social Vertical (15)		Constant at 1996 value
	Other Structural Units Vertical (16)	Energy, Material and Maintenance	Not separated
		Other Operational Costs	Constant at 1996 value
Redirected Costs	Sheets (2) to (12)		See explanation below
Total Operational Costs	Sheets (2) to (16)		Sum of the above 6 costs
Operational Income excluding Depreciation	Sheets (2) to (16)		(Total operational income) - (Total operational costs)
Depreciation	Sheets (2) to (16)		Calculated at 1996 rate with a reduction for fully depreciated assets, and the addition of depreciation on new investment (20)
Operational Costs including Depreciation	Sheets (2) to (16)		(Total operational costs) + (Depreciation)
Net Income	Sheets (2) to (16)		(Total operational income)-(Operational costs including Depreciation)
Financial Costs	Sheets (2) to (16)		See explanation in section 1.6.2
Profit/Loss	Sheets (2) to (16)		(Net income) - (Financial costs)

1.5.2 Redirected Costs

Where percentages appear, these are taken from the document "Obrachunek kosztow 1995". (OK95)

Table 3: Redirected Costs

Sector / Vertical		Redirected to...		Assumptions / Notes
Traction Sector (4)		Passenger Sector	Fuel and Energy Costs	Proportional to Passenger/Total gross-ton-1000km
			All other costs	Proportional to Passenger/Total Train-km
		Freight Sector	Fuel and Energy Costs	Proportional to Freight/Total gross-ton-1000km
			All other costs	Proportional to Freight/Total Train-km
		Passenger Sector	**Freight Sector**	
Infrastructure Sector (5)		44.6%	55.4%	Percentage from OK95
Telecommunications Sector (8)		58.3%	41.7%	Percentage from OK95
Power Engineering Sector (9)		60.7%	39.3%	Percentage from OK95
Passenger Rolling Stock Sector (10)		100%	-	Percentage from OK95
Freight Rolling Stock Sector (11)		-	100%	Percentage from OK95
Real Estate Vertical(12)		61.56%	38.44%	Percentage from OK95
Housing Vertical (13)		Sheets (2) to (12)		On basis of 1996 Salary costs. The use of these services is proportional to the number of employees in each Sector/Vertical, which is proportional to the Salary Cost category
Health Vertical (14)				
Social Vertical (15)				
Other Structural Units Vertical (16)	POLRES and PKL	100%	-	Percentage from OK95.
	The rest	54.02%	45.98%	Percentage from OK95.

1.6 Sheet 1

1.6.1 PKP Consolidated

The upper part of this sheet contains the consolidated results of the15 sheets that follow.

1.6.2 Financial costs associated with borrowing

The lower part of this sheet serves to calculate the financial costs associated with borrowing.

These are allocated to the following years' financial costs and can be found in the individual sectors and verticals, which are then consolidated in the "financial costs" entry in the consolidated table (1).

2 Scenario 1

2.1 How Scenario 1 differs from scenario 2

a) The accounting of the government subsidy

Option 1: included in the infrastructure investment.

Option 2: included in the P&L.

b) The value of the government subsidy for infrastructure investment

Option 1: Between 1998 and 2002 this is increased by 400m/year and is also accounted for in infrastructure investment.

Option 2: This is received as a subsidy for the Restructuring Agency.

c) Staff numbers

Option 1: These are reduced to 160,000 by 2005 . The reduction is quicker from 1999.

Option 2: Reduced to 178,000.

d) Infrastructure charges

Option 1: Charges to gain return on capital employed (ROCE).

Option 2: Cost allocation only.

e) Income

Option 1: Freight income increased by 5% due to abolishing subsidy on coal tariffs and price increases.

Passenger income increased by 18% due to reduction of benefits and price increases

"Required New Income" estimated for new ventures.

5. PROPOSALS FOR EXECUTING THE SELECTED SCENANIO

In this chapter, concrete recommendations to materialize the selected scenario in chap. 4 (Scenario 1) are proposed.

5.1 MANAGEMENT FORM

5.1.1 Infrastructure Sector

The infrastructure sector is separated from PKP and transformed into an independent SOE, and subsequently to a JSC and finally a listed company. The income derived from the ultimate sale of the SOE is contributed to the PSC fund through the MOT. The degree of privatization can differ depending on the goverment's policy toward public infrastructure. For example, 51% of the shares may be retained by the MOT.

Main effects of Scenario 1 on the infrastructure sector are as follows:

1) Separate SOI is responsible for research and development, construction and maintenance of railway infrastructure, and has the option to leave as it is, maintain, lease, sell or dispose of surplus assets such as closed lines.
2) The SOI announces its capacity, and serves its facilities to the selected operators.
3) The SOI charges full cost for access charge to operators.
4) Before privatization, capital cost portion of access charge collected is contributed to government (the PSC Fund) as an interest expense for the long-term government debt. After privatization, capital cost (fair return) is paid to private lenders/investors in the form of interest expense/dividends
5) The privatized infrastructure JSC can raise private money for infrastructure investment easily, on the condition that a fixed return on loan / investment is guaranteed by law.

5.1.2 Holding Company (HC)

The organization of PKP is streamlined by separation, integration, closure and sale (direct privatization) etc. of field-work units for maintenance, pillars (see 5.2.1) and medium and small-sized railway-related businesses etc. Afterward, these streamlined 8 JSC of Inter-city passenger company etc (see 4.3.3 (4)) are 100% owned by a holding company (HC). Both commuter and local line companies will serve under contract with local goverment, so accounting responsibility of both companies will be substantially separated from PKP.

HC sells and/or lists 8 subsidiaries, but preserves its supremacy. HC itself lists and 85% of the income from its sale are paid to the National Treasury. The function of HC will change, as the subsidiaries grow or the economic situation changes. The main functions of HC are as follows:

1) Objective of HC is to make the whole group's business efficient, not to control the market.
2) In principle, the authority to execute individual business is delegated to each subsidiary. HC plans a united strategy for the whole group and coordinates the subsidiaries, responding swiftly to economic trends.
3) HC receives periodic business information from subsidiaries, to help it in its advisory and coordinating roles.
4) HC develops new businesses by establishing, merging and purchasing other companies, or by selling and closing businesses at opportune times.
5) HC raises money on advantageous terms. It provides effective investment in and loans to subsidiaries by intensive management of the whole group's financial affairs.
6) HC manages the group's common administrative tasks such as legal matters, accounting, data processing, research & development, human resource development etc. collectively in order to streamline organization, make those tasks efficient and reduce overhead costs.
7) HC holds personnel records and reshuffles staff among the subsidiaries. It contributes to employment stabilization of whole group, and staff are given the opportunity to realize their full potential, thus raising morale.

5.2 PRIVATIZATION PHASES AND EFFECT OF PRIVATIZATION

5.2.1 Privatization Phases (see 4.3.3, Fig. 4.3.2)

Privatization phases are shown in 4.3.3 and Fig. 4.3.2, and some additional explanation on 2 items of 2nd phase (1999~2000) is given here.

(1) Extend and privatize the railway-related business (RRB) pillar

1) RRB pillar (formerly the real estate pillar) is merged with 3 other divisions (welfare, railway security service, structural units), and actively extends businesses.
2) Welfare pillar has some sanatoriums, and these can be upgraded or rebuilt as resort hotels for external customers.
3) Railway security services can be contracted out to private security companies, and dissolved. Alternatively, the pillar could turn itself into a consultancy business, retrain its staff and seek external orders.

4) Structural units pillar has the train tickets reservation unit (POLRES), cable-cars unit, printing unit etc. These businesses can form the mainstays of the future RRB. Preparing a business plan is indispensable to start the new RRB. It is recommended that, after disposing of any of the current undesirable businesses, the newly formed RRB division is separated into individual companies, the appropriate staff are transferred and given authority to manage the firm, together with responsibility for the results. When self-sufficiency of some businesses is in sight, such businesses should be actively privatized.

(2) Reorganize other pillars (housing, pension, health-care service, training, procurement)

1) 170 thousand houses for employees cause a deficit of about 122 million PLN annually. 90% of the houses are not yet registered with local government offices, and these cannot be sold. Even if they are sold, the proceeds are contributed to the Social Fund, and are not received by PKP. It is proposed that management of such houses should be transferred to self-governing resident associations, with caretaking/maintenance obligations being charged to each association. The authority to dispose of houses would also be given to the associations. Each association would be responsible for financing itself. As a result, management expenses would be forced to be economized, and, the housing pillar would be excluded from PKP's account.
2) The mass of clerical work regarding retirement pensions should be computerized, or consigned to outside companies and the pension pillar should be dissolved.
3) The health-care service pillar consists of 84 hospitals and clinics. Such a public service is not suitable for a PKP that wants to privatize. So, these should be amalgamated, sold, donated to the local government or closed except for small clinics annexed to workplaces.
4) Training and procurement pillars should be divided and merged into other appropriate sectors, or transferred to the future holding company as common services for the whole group in order to intensify and make the function efficient.
5) As a result, the current pillar organization of PKP would be reduced to 3 pillars; namely, RRB, computerized data processing and telecommunications. All pillars will be specialized in promising businesses related to PKP's railway business. Each pillar would separate its component businesses and encourage privatization of individual firms.

5.2.2 Effects of Privatization

(1) Qualitative effects

1) Conditions for fair competition will be arranged in the railway industry by the institutional separation of infrastructure from PKP. This is the most advanced model of EU directives, and it will assist Poland in joining the EU early.
2) The infrastructure sector can be privatized by charging full costs for access to operators. It can be modernized and soon catch up to other EU countries' technical level.
3) Privatization of PKP will improve the standard of railway service, mobilise human resources and materials, and make the Polish economy more efficient. It will also contribute to controlling pollution.
4) SIF will secure the financial interests of staff, and heighten morale for early privatization and cooperation with management.
5) The PSC fund will advance services contracted with the local governments by giving grants for loss-making commuter & local lines to the local governments, and will accelerate the abolition of lines of less social importance by strict assessment and disclosure of its process to the public.
6) Active privatization and extension of RRB will develop staff capacity, increase employment opportunities, and promote the market economy.

(2) Quantitative effects

The infrastructure sector can be self-financing and privatized by charging for access at full costs (5,061 million PLN for 2005). The passenger sector, as well as the freight sector, will become a profitable entity by being granted the capital cost (3,148out of 5,061 million PLN for 2005) via the PSC fund. As a result, all railway sectors can be independent profitable industries, and moreover, it is important to note that this balance can be achieved without additional government subsidy except 2 billion PLN for investment.

Access charges envisaged under Scenario 1 are considerably lower than that of the UK's railways as indicated in Table 5.2.1, and PKP will be able to compete on the EU open access market. Rather, access charges should be raised in line with the EU's standard charges in order to allow for infrastructure modernization as soon as possible.

Regarding Access Charge/Sales in Table 5.2.1, the fares of PKP are about at only 20% and 30% of UK and German railways respectively, so the ratio (AC/Sales) of PKP should be substantially lower than that of those countries (ref. 3.3.2, Table 3.3.3, the fare is one per passenger-km adjusted by purchasing power parities). The access charge of German railways is not made public, and the figure is only estimated.

Table 5.2.1 Comparison of Access Charge (AC)

	PKP (2005)	UK railway (95/96)	German railway (1994)
1. AC (Passenger)	2,314mPLN	£2,003m	NA
2. AC (Freight)	2,747mPLN	£158m	NA
3. Total AC Income	5,061mPLN	£2,161m	DM8,000m
4. Railway Sales	8,597mPLN	NA	DM23,753m
5. Railway length (km)	18,000km	16,564km	41,256km
6. Passenger-km	28,442mP-km	28,656mP-km	61,333mP-km
7. Freight ton-km	69,123mT-km	12,992mT-km	70,554mT-km
3/4. AC/Sales (%)	**58.9%**	**76~203%**	**33.7%**
3/5. AC/thou km	**281.17PLN($78.8)**	**£130.46($213.9)**	**DM193.91($106.5)**
1/6. AC(P)/thouP-km	**81.35PLN($22.8)**	**£69.90($114.6)**	**NA**
2/7. AC(F)/thouT-km	**39.74PLN($11.1)**	**£12.16($19.9)**	**NA**

Note; AC of German railway is not made public (estimated), m: million,
1US$ = 3.57PLN = 0.61£ = 1.82 DM (Jan.1988)

(3) Concerning costs of privatization

Many types of costs are needed during privatization process such as below. It is a very important subject but very complicated and changeable. So, further detailed study should be done continuously. Revenues which are earned through privatization usually exceed costs in almost every case. Therefore when the costs amount is estimated, the revenues amount should be estimated at the same time.

1) Responsibility of government
  a. Enactment of PKP reform law and regulation for separation and privatization. (administrative cost)
  b. Determination of assets, liabilities and capital of newly established entities through separation and privatization. (administrative cost)
  c. Selection of promoters and top management of new entities. (administrative cost)
  d. Government subsidy
    1 Subsidy for modernization of railway facilities. (2 billion PLN, see 5.7.3)
    2 Abolition cost of low density lines (90 million PLN, see 5.4.6)
    3 Buy out cost
2) Responsibility of PKP
  a. Determination of assets, and division of assets and staff into new entities. (ordinary operating cost)

b. Arrangement of facilities for new entities. (ordinary operating cost)

c. Staff training and placement activities for privatization.

Some taxes, and registration costs of land and newly established affiliated companies etc. could be reduced or exempted by legislation.

5.3 SEPARATION AND DISPOSAL OF ASSETS

Only the private sector can generate the high rates of investment and savings necessary to sustain the high rate of economic growth which is needed to close the gap with the rest of Europe – World Bank Resident Mission in Poland, June 1997.

It has been well known for some time that in a market economy, small specialized units can be better managed – Janusz RENDA, Head of Silesian Rail Labour Union.

Privatize first; restructure later. It is privatization that has been instrumental in bringing about restructuring – World Bank Study [1]

5.3.1 Desirable Separations and their Methodology

(1) Goals for the Separation and Disposal of assets

The basic objectives (primary and secondary) for the separation and disposal of assets are:

1) To make the PKP smaller so that it is easier to privatize (primary)

The PKP is the 4th largest company in Central Europe (by revenues). The current PKP is probably too big to privatize as a whole as its net assets (even excluding much property) is $8 bn (same as the market capitalization i.e. the value of all the shares of the Warsaw Stock Exchange). This is one major reason for separation of assets i.e. to create manageable, salable units from oversized units.

2) To lead to improvements in efficiency, effectiveness and profitability (primary)

The efficiency, effectiveness and profitability of the PKP could conceivably be improved if the management were to concentrate on the core activities rather than on the range of activities currently being undertaken. Thus by the separation and disposal

[1] Privatisation and Restructuring in Central and Eastern Europe, World Bank Technical Paper No. 368 – based on the analysis of financial and operating data for more than 6,000 industrial companies in seven countries (Bulgaria, Czech Republic, Hungary, Poland, Romania, Slovakia and Slovenia).

of assets, the management could focus more on railway activities.

3) To reduce subsidies (secondary)
The separation and disposal of assets could in some cases lead to increased profitability and thus reduce the necessity for state subsidies. This is because the PKP subsidizes the Railway Health Service, the maintenance of staff apartments etc. If such activities were to be separated and disposed of, the PKP's losses would decrease and the necessity for state subsidies would decrease.

4) To make costs more transparent i.e. so that it is more clear as to the real losses on the activities to be subsidized (secondary)
The separation of assets would also permit the financial performance of individual activities to be better monitored. Thus, for example, separating Warsaw agglomeration railway transport into a separate company would make the exact extent to which this is being subsidized to be known. Similarly, separating the property into a separate company and charging rent for use of any property would allow better performance measurement of the of the property assets as well as the property users.

5) To bring in new investments i.e. from non- government financial sources (secondary)
The separation of assets could lead to new investments that might not otherwise be possible. The World Bank or private investors may want to invest in a infrastructure company that is allowed a Return On Capital Employed (ROCE) but separated from loss-making operating companies. Similarly investors may be willing to lend to separated rolling stock companies that have profitable contracts to provide rolling stock to operating companies.

6) To improve the quality of services (secondary)
Separation and / or disposal could also lead to improvements in quality of services and better maintenance of existing assets. It is well known that private property is better cared for than public property and that owner-cum-managers provide a better quality of service.

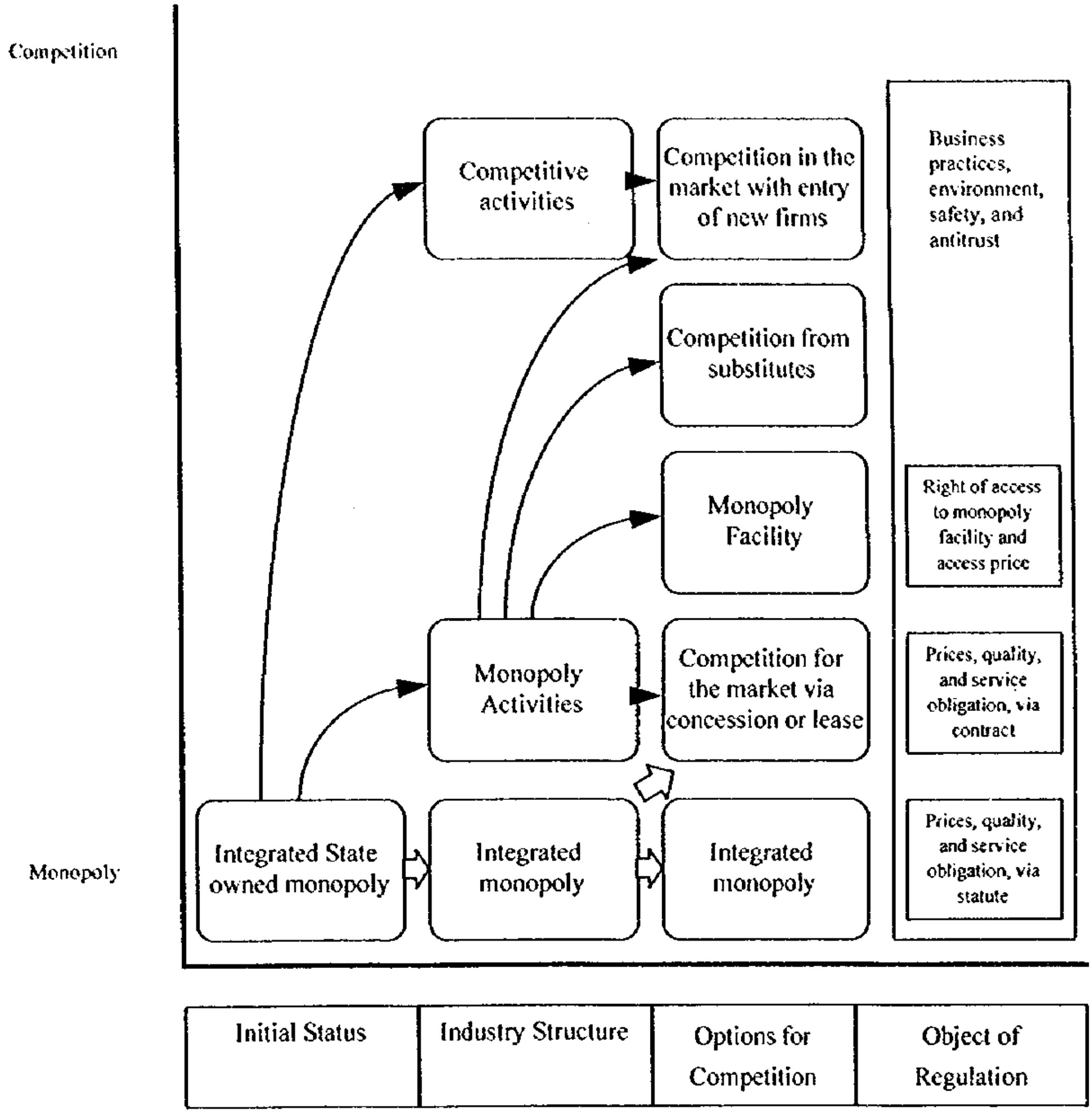
7) To reduce the influence of the unions (secondary)
The separation and disposals of assets etc. can lead to reduced staff influence. As one large unit, the staff of the PKP can better resist change and are more able dictate government and public policy. Thus the separation and disposal of assets and units (including staff) can lead to less power - both for the staff that are separated out and for those who remain. Alternately, we could also say that one of the ways of reducing

staff influence (thus making privatization easier) is to first separate and dispose of assets (see also the section on the Staff Investment Fund below).

8) To increase the options for competition and private sector involvement (primary)Separation and disposal can lead to increased competition and increased private sector involvement. An example of this was in the PKP itself where the heavy maintenance was separated and disposed of into several new companies. Now these companies not only compete against each other but also against the private sector (e.g. Pafawag of Wroclaw) and other State Owned Enterprises (e.g. Cegielski of Poznan) who also tender for the work.

The following chart shows how separation and disposal of assets increases the options for competition and private sector involvement.

Separation and disposal of assets increases the options for competition and private sector involvement



→ with the separation and disposal of assets

⇨ without the separation and disposal of assets

Source : World Bank, World Development Report 1994, Infrastructure for Development

In choosing the methods to be applied, the following criteria must also be kept in mind :

- Does the chosen method maximize receipts /revenues ?
- Is the asset marketable / salable ?
- Can the asset exist independently ?
- Can the process of separating and disposal of assets be properly controlled ?
- How quickly can separations & disposals / privatization be implemented ? [2]

(2) Definitions of separations and disposals

For the purpose of this study, two definitions of separations can be made :

1) internal separation

A separation whereby the asset stays within the PKP but becomes the property of a different sector / section / division etc.

2) external separation

A separation whereby the asset becomes the property of another State Owned Enterprise reporting to the MTME or the Ministry of Finance. This is a separation out of the PKP but the asset remains the property of the State.

A disposal can be defined as when rights over an asset of the PKP or of the Polish people is given away to private persons or companies, with or without consideration (e.g. cash receipts).

(3) Lessons from the separations and disposals in the PKP from 1991 to 1995

Prior to the current restructuring program of the PKP, assets were internally separated and subsequently disposed of for no consideration i.e. no money was received (see chapter 3.1.4). Actually the staff concerned only agreed to this separation and disposal of assets because valuable properties (stadiums, schools, cinemas etc.) were given as well. Thus not only were these assets disposed of for no consideration but additional valuable property was given away, that was subsequently sold by the newly independent companies.

We have been informed that the method of disposal was actually illegal i.e. not strictly executed according to Polish laws, and thus cannot be repeated. Although the exact methodology used to separate and dispose of the assets cannot be repeated, something

[2] "The method of privatization is less important than the speed" - Privatisation and Restructuring in Central and Eastern Europe, World Bank Technical Paper No. 368

something similar can be attempted.

The 70 companies that were separated had their own internal accounting in the way, for example, each locomotive depot has its own internal accounting system now. (In fact, there are still over 500 such cost-Centers, each with its own accounting office, many of which can be easily separated and disposed of).

Then effects of the separation and disposal were :

- A reduction in PKP's staff numbers of 65,000
- The disposed of companies are free to work for clients other than the PKP
- Only 2 small companies employing less than 500 people have closed down. The rest have adapted and are somehow managing.
- Some competition has been introduced. Not only the divested companies but other companies (e.g. Pafawag of Wroclaw and Cegielski of Poznan) also tender for the work previously carried out by the disposed of companies.

The conclusions that can be derived from these past experiences is that :

- disposals can be made if the price is right
- the (old) management has been able to keep the companies from closing down.

What remains unknown is how the (disposed of) companies would have performed if the disposals had been better organized and accompanied by management changes e.g. sale to strategic investors etc.

Although there have been some negative effects of these separations, the lessons learnt are summarized below:

1) These companies had their own internal accounting in the way, for example, each of the current 450 odd WORGs and organizational units have their own internal accounting system now. Thus many of the existing WORGs and can be easily separated and disposed of. Thus units to be separated must have their own separate accounting.

2) The separated units now compete against each other for contracts from both the PKP and other clients. It is believed that the costs to the PKP of services provided by these units have decreased. Thus it is better to separate into several companies where possible rather than into a new monopoly so as to increase competition.

3) The exact costs for specific services provided by the separated units is known

because tendering is required. Cost allocation problems are also reduced. Thus any services / activities for which the exact costings are required should be separated.

4) The separated companies owned their assets and thus were able sell these assets to raise money. If for example one of the 8 mechanized road works departments is separated from the PKP with a US$80m track laying machine, this department would have the right to sell this asset. If the same mechanized road works department were to be separated without the track-laying machine, then there would be no right to sell this machine. Thus valuable assets should not be given but only leased to separated units.

5) The management of the separated companies is more or less the same as before the separation from the PKP. In general, no 'new blood' has been introduced, the companies have not developed new products or services and haven't found new customers. Thus consideration should be given to introducing new management before / at the time of separation.

6) The separated companies knew their costs but had no idea as to their income before their separation. This is because these units were cost-centers and were not converted into profit-centers before being separated from the PKP. Thus as an intermediary step, cost-centers should be converted into profit-centers before being separated. Profit-center managers would then be able to take action to balance their finances before separation.

In addition, during discussions with WORGs and Organizational Unit managers (who would like to be separated from the PKP) another important lesson has been identified. This is that the PKP should maintain some interest in the units to be separated i.e. the PKP should retain some shares in the companies to be separated. Thus the separated and remaining parts while being independent enough to pursue their own best interests, would also have a benefit in each others well-being.

(4) The PKP Law (1995) on the separation and disposal of assets

The separation and disposal of assets should ideally conform to the existing laws and not require the introduction of new laws as new laws can take up to four years to implement. The PKP Law (1995) allows the separation and disposal of assets by the PKP and also the separation and disposal of assets by the MTME.

1) Separation and disposal of assets by the PKP

The PKP Law (1995) states :

a) The PKP may contribute organized portions of assets of the PKP or other assets considered as fixed assets to the PKP, for lease by other entities for a set period of time.
b) Existing provisions for State Owned Enterprises shall be applicable with respect to the sale of fixed assets or organized portion of assets of the PKP.
c) In economically and socially justified cases, the PKP may transfer ownership of its redundant assets for free. Approval from the MTME is required in the case of Lines of National Importance.
d) The PKP may create business entities.
e) The Council of the PKP must approve any disposal by the PKP the value of which exceeds the amount stated in the by-laws.
f) The Management Board of the PKP must approve any disposal by the PKP the value of which exceeds the amount stated in the by-laws. The mutual action of two Board members is sufficient.

To summarize, the PKP can do whatever it wishes with its assets (except for the Lines of National Importance where government approval is required).

2) Separation and disposal of assets by the MTME

The PKP Law (1995) states :

a) By December 31, 1998, the MTME may separate from the PKP organization units or "organized portion of assets"[3] to form new State Owned Enterprises or to use these assets as contribution to companies.
b) By December 31, 1998, the MTME may lease assets of the PKP applying provisions on privatization of State Owned Enterprises previously exercised by the Ministry of Privatization.

To summarize, legally the government can separate from the PKP an "organized portion of its assets". In reality, this will be resisted and made a matter for the courts to decide. Since the introduction of the law, the MTME has not exercised this right. The MTME should exercise this right in order to separate and dispose of assets as in the recommendations below.

(5) Recommendation to the PKP - Immediate creation of a Restructuring Agency subsidiary

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[3] See articles 2 and 44 of the PKP Law (1995)

A draft law has been presented to the parliament asking for funds to finance a Restructuring Agency (RA) to be responsible for

- Narrow gauge lines
- Disused normal lines
- Housing properties
- 15,880 employees

The rationale for the creation of such a RA is not clear. During the first stage of restructuring, the PKP was able to liquidate 88% of marshalling and 50% of maneuvering yards, 22% of gate crossing points, 3,624 km of unprofitable lines, 30% of rolling stock and technical base enterprises, 13% of electric and 35% of combustion rolling stock and 17% of passenger and 30% of freight rolling stock (see chapter 2.3.2). Thus it is not clear as to why a RA (internal or external to the PKP) is suddenly required for further reductions. The PKP argument has not convinced the Ministries of Finance and of Labor. We expect that this RA would be loss making and that there are no assets that could or should be sold to assist in the financing of this RA.

- It is recommended that the PKP set up one or more units in-house for the sepaaration and disposal of individual classes of assets e.g. sales of surplus tracks and scrapping old rolling stock (see 5.3.3).that would have the same assets and liabilities as the proposed RA as soon as possible (e.g. 1st of January 1998). We see no good reason to wait for a RA to be created (by means of a new law) before the tasks of such a RA begins. Such activities can and should begin immediately.

(6) Recommendation to the MTME – To use its powers under the existing PKP law before the 31st of December 1998 deadline.

To date the MTME has not employed it powers to separate any organized portion of assets from the PKP. Unless this power is exercised, the MTME will not get practice in dealing with the PKP's response. The reason why the MTME must take the initiative is that the PKP of its own accord has no plans to sub-contract / spin-off functions that clearly can be carried out by independent sub-contractors. The PKP is too much vertically and horizontally integrated for the good of railway transportation in Poland.

The most often quoted reason for PKP's resistance to the separation of useful / valuable assets is that they (the PKP) have paid for everything and so no-one else should have the use of these assets, especially competitors. In response it must be made clear that all the assets of the PKP belong to the State. In addition, if the PKP's reasoning is carried forward to its logical conclusion, the proceeds of privatization will not belong to the State but will belong to the PKP.

The MTME can take the initiative for the separation of:

- Infrastructure (into a new SOE)
- Traction and Back-up (into 32 separated companies)
- All land and buildings (excluding tracks and structures)
- Etc.

(7) PKP's future program for the separation and disposal of assets

The future program of the PKP is outlined in chapter 3.1. In relation to the separation and disposal of assets, the PKP have created 2 new departments i.e. the Real Estate Directorate and the Bureau of Joint Stock Companies (Department "KBS").

1) Separation and disposal of assets using the Real Estate Directorate

A Real Estate Directorate has been set up with a Director and staff to manage the Real Estate of the PKP.

The PKP views its land and buildings as falling into 3 categories i.e.

- Category I (PKP owned). In this category, evidence that the property is owned by the PKP exists.
- Category II (State owned). In this category, evidence that the property is owned by the State exists.
- Category III (Unknown and / or disputed). In this category, evidence that the property is owned by the PKP or the State has been lost or the ownership is disputed.

Until 1994, the PKP included all 3 of the above categories of land and buildings in its Balance Sheet. For 1995, only category I is included. As a result, 97 % of the land (included in the 1994 Balance Sheet) has been excluded from the 1995 Balance Sheet.

It is planned that the non-PKP tenants will pay a market price for the rental of any property (in categories I, II and III) to the PKP. PKP tenants (i.e. the PKP and related companies / organizations) will be charged the maintenance / cleaning costs only i.e. no rent will be charged.

The current philosophy is that charging rent to PKP tenants would tend to make them unprofitable or if already unprofitable, look more unprofitable. For example, in the case of POLRES (a PKP travel reservations service) there is a possibility that the staff costs less possible rents receivable from another tenant may be less than current losses. To put it another way, it may be cheaper to pay the staff to stay at home and do nothing and rent out the shops currently occupied by POLRES[4]. This policy of charging for only maintenance costs will also be applied to the freight and passenger sectors etc. after their separation.

The consequences include :

- Non-inclusion of significant real estate will detrimental to the current owners (Polish people) in that this undervalues the real estate portfolio.
- Not charging market rents to PKP clients will, for example, mean the total infrastructure costs will be lower. Thus there will be an under-recovery of costs not only from the passenger and freight sectors but also from any foreign / non-PKP operators.

There is the danger that real estate will be disposed of at less than market value or will simply become "lost" i.e. as no documents exist as to the ownership. Any property where possession is transferred cannot be subsequently recovered easily. An additional danger is that this Directorate will dispose of real estate and that the proceeds will be used to cover operating losses, thus eroding the capital base.

2) Separation and disposal using the Bureau of Joint Stock Companies (KBS)

The Bureau of Joint Stock Companies (Department"KBS") is a new department within the PKP whose purpose is to manage companies separated from the PKP and to establish new companies using the assets of the PKP. It is envisaged that the spun-off companies will develop new businesses as well as provide services to the PKP and to PKP's customers.

The PKP's 4 new sectors (i.e. infrastructure, passenger, freight and traction & maintenance) are also likely to become separate stock companies. Prior to this, the 4 sectors will decide on establishing new companies (e.g. subsidiaries etc.). This function will also be supported by the KBS.

The philosophy here is that a lot of PKP property is not being used. Property (including land, hotels, restaurants etc.) will be used as investment in kind into joint

[4] POLRES has no income from selling PKP tickets unlike normal travel agents

ventures and other companies.

The department KBS will thus be engaged in separating and disposing of PKP assets i.e. in cases where the PKP will be losing a portion of ownership rights or control. Thus department KBS will effectively be involved in privatization as well.

From the point of privatization, KBS is not the owner of any assets. Ownership will rest with the sectors or other subsidiaries. KBS will however be in-charge of managing the PKP's shareholding and also representing PKP's interests on the Board of Directors where appropriate.

(8) Effect of the lack of debts on the separation and disposal of assets

The PKP has little long-term liability because shareholders funds account for 96.5% of total assets. In this sense the PKP's Balance Sheet may be one of the strongest in the world [5]. The lack of debts increases the attractiveness of the PKP (as a whole or in part) to prospective investors in the privatized company (or companies). This is because there is no need to get rid of any debt when separating the assets. This attractiveness will be lost if the PKP or any part of it incurs debts before separation / disposal. The lack of debt also means that a greater range of methods can be considered for the separation and disposal of the assets of the PKP.

The starting point (base line) for the PKP is probably better than any other railway pre-privatization. It may thus be wise for the PKP to remain essentially without debt during the period pre-privatization. If this is the case, both direct and indirect, partial and complete privatization would be possible.

The situation of the PKP (i.e. no debt) is different from that of the old Japan National Railway (i.e. huge debts). Thus the Settlement Agency concept required for the separation and disposal of debts and property may not be required in Poland (unlike Japan).

(9) Problems for the separation and disposal of assets

The separation and disposal of assets is problematic (for reasons both from within and

[55] Annex I/2 of the EU White Paper "A Strategy for Revitalising the Community's Railways" shows the EU average debt in 1994 was 54% (highest 89% and lowest 14%) of total assets

from outside the PKP) and is discussed below.

1) The PKP Law obliges the PKP to maintain a non-rail asset like the Railway Health Service. For this purpose the PKP receives both maintenance and investment subsidies from the State. Thus the PKP cannot dispose of the Railway Health Service.

2) Housing units must by law be disposed of at the market price with vacant possession i.e. at the price that can be achieved if there is no tenant. However these housing units are occupied for an indefinite period with low rents. The market values of the housing units can be small (e.g. 10,000 PLN) compared to the legally required selling price (e.g. 50,000 PLN).

3) Social units have been funded by both the PKP and its Social Fund. Thus since ownership can be disputed, it will be problematic to separate / dispose of Social Whilst in fact owned by the PKP, the "moral" owners are probably employees via the Social Fund.

4) The financial performance of the units that can be separated from the PKP is unknown. This is because although the PKP has over 500 cost-centers, the incomes of these cost-centers are unknown. Thus (for example) all the costs incurred by the locomotive garage at Kielce is known but this unit has no income nor a business plan. Thus although separated, with its own office for accounting purposes, because this locomotive garage has no income, it cannot be so easily disposed of.

5) One of the most important problems is that employees have worked in a planned economy for over 50 years. Under such a system the PKP provided not only employment, but also housing, subsidized food, nurseries, schools, hospitals, recreational facilities including seaside resorts etc. The staff will resist giving up these benefits.

(10) Concepts for the separation and disposal of assets

Based on the extensive experience of Japan and the World Bank, the JICA team recommends the that the following concepts are followed :

The above recommended concepts are discussed below :

Concept / *Explanation*	Merits	Demerits
(1) To separate the PKP's assets into small units. The PKP's many functions could be separated and disposed of to other companies.	· Management could be more focused if they have fewer tasks · Small units are more easily disposed of	· Services provided by the private sector can be more expensive than doing the tasks in-house (i.e. by the PKP)
(2) To use existing structures (organizational and accounting) to separate assets. Current structures can be used separate and dispose assets of the PKP	· Easier, faster as current budgets etc. is known · Contracts can be easily be put into place where income is unknown · Further re-structuring will not be required	· The current structure may not be the best way of dividing the PKP
(3) To separate and dispose in a way that introduces competition. Separating the PKP into 4 sectors (as is currently planned) might only create 4 new inefficient monopolies i.e. not introduce competition.	· Privatization without introducing competition leads to few benefits · Competition increases efficiency	· Competition will lead to lower employment · Possible closures of uneconomic units
(4) To separate in a manner so that costs incurred only for a single client should be known. Any costs only incurred for a single client e.g. a single factory or for defense only can be identified by separating assets appropriately	· May lead to lower costs · Fairer allocation of costs	· Costs may increase for certain clients · The hidden subsidy e.g. to certain factories will become known
(5) To charge market rents for the use of separated assets. to both PKP and non-PKP companies for the use of PKP and Government land and buildings. Currently the PKP does not, and has no plans to, charge market rents to PKP companies.	· If users of property are charged market rents, assets will provide a return on capital. These users can then pass on the costs. · If the true costs of operating companies etc. is known, subsidies can be better targeted.	· The costs to operators, infrastructure, subsidiary companies etc. will be increased thus making some e.g. POLRES even more unprofitable · The PKP may not want the true subsidy to areas such as POLRES to be known.
(6) To separate and dispose in a way so that new management is brought into the railways. If, for example, a private company wins the tender to provide maintenance from the Locomotive Garage at Kielce, they (the private company) will install a new management team consisting of both PKP and non-PKP staff.	· More 'commercial managers can be responsible for carrying out some of the activities currently being carried out by the current management who are basically (government) 'bureaucrats in business' (a World Bank term).	· Some of the current management may not be needed if the provision of certain services is contracted out.

(7) To create profit-centers (from cost-centers) prior to separation and disposal of assets. If the cost-centers in the PKP e.g. the Geodesy Section (DOG) Warszawa 'charges' (at market rates) for the provision of its services to it clients (elsewhere in the PKP), then its efficiency will be known.	· Sections for whom incomes and costs are available can be more readily privatized · the real benefits of having a section within the PKP will be known · can decide if a service should be carried out in-house or contracted out	· It can be a costly and time consuming to convert cost-centers into profit-centers · It can be difficult to negotiate the 'charges' or 'transfer prices' for the services to be provided
(8) To separate and dispose in a way that eliminates cross-subsidies. Separations should be made so that any cross-subsidy is eliminated or can be clearly identified	· The true costs of a service will be more transparent · The subsidy required will be transparent	· greater subsidy will be required for unprofitable activities.

(11) Options for the separation and disposal of assets

Based on the experience in Japan and elsewhere, the JICA Team suggests the following options for the separation and disposal of assets :

The above options are discussed below :

Option / *Explanation*	**Merits**	**Demerits**
(1) To prepare a list (and value) all PKP, government and disputed (both leased and owned) property assets. All of the railway property is not being accounted for / listed in any capital ledger.	· The deeds to a property (document showing ownership) cannot be easily lost or misplaced	· The current management of the PKP do not want to keep a record of and maintain valuations for all PKP, government and disputed railway property
(2) To separate all land and buildings into a property company. The land and buildings of the PKP, the government and of disputed ownership can be separated and entrusted to one organization..	· Consolidation will make it easier to control investment and development activity · Easier to ensure that property is not sold cheaply · Can prevent property sales to cover operating losses	· The values of the infrastructure, passenger, freight companies will be reduced as they will have no property
(3) To use external professionals to manage the property portfolio. The current management may not be the best persons to manage the investment and development potential of PKP's properties (including the governments and disputed property).	· Property investment and development is best left to property professionals · Independent professionals can charge market rents to the PKP and PKP related organizations (e.g. POLRES, OBET etc.).	· Property portfolio management costs will be higher.

(4) To make business plans for each profit-center. Currently there are only cost-centers and so there are no suitable business plan.	· Areas with business plans can be more easily separated and disposed of e.g. to strategic investors. · Easier for potential buyers to audit the assets.	· The cost / time required to prepare business plans.
(5) To set up 'management contracts' between profit-centers and the MTME. A Management Contract between a SOE (State Owned Enterprise) and the government will require performance measures of the SOE. The PKP can be treated as one SOE or there can be many SOE's in the PKP e.g. a Locomotive Garage.	· Clear targets can be set for the managers of SOEs · Will make it easier to separate and dispose of assets	· The government cannot interfere in the running of the SOE as long as the SOE meets its targets.
(6) To separate (infrastructure) maintenance from Infrastructure and dispose into many companies Maintenance of infrastructure can be sub-contracted to other companies. (In Japan, the Shinkansen track maintenance by private companies is more efficient and cheaper than that of Japan National Railways where this was carried out in-house).	· Costs can be reduced if the maintenance contract is well negotiated. · Separates costs into smaller units · Each maintenance center can become a separate company · Competition will be introduced	· Costs can increase if the maintenance contract is poorly negotiated · Many contracts will have to be negotiated
(7) To separate the rolling stock out of the PKP and dispose into many rolling stock companies.	· Easier to get financing · Introduces competition · Reduces entry costs for new operators · Possible tax benefits	· Operating companies costs will increase as lease charges will be higher than current depreciation charges
(8) To separate infrastructure, passenger, freight etc. out of the PKP. The PKP has no intention to allow any other party entry into undertaking railway activities.	· Separated divisions can have armßs length negotiations with the PKP · Greater independence to follow own interests	· Possibility of disputes between the divisions · Can be coordination problems
(9) To separate passenger operations into several companies. The PKP intends to set up only 1 passenger operating company.	· Management can better respond to local needs · Easier to know the costs of services requiring subsidy	· Likely to be timetabling problems
(10) To separate freight operations into several companies. PKP plans to have only one freight company.	· The true costs of separated freight services e.g. coal will be known	· No benefits from economies of scale enjoyed by a single freight company.
(11)To separate infrastructure used by a single client. Any infrastructure used for a single client only e.g. a single factory only or for defense only need not be maintained by the main infrastructure company	· Lower maintenance costs · Fairer allocation of infrastructure costs	· Costs may increase for some clients · Hidden subsidy to certain factories etc. will be known · Some clients will have to manage own maintenance
(12) To separate related business from railway operations. Related business has separate managers.	· The management can be transferred to specialists · Avoids cross-subsidies	· The PKP will lose the benefit of any profits from related businesses.

(12) Role of the Polish Government in the separation and disposal of assets

Option / *Explanation*	Merits	Demerits
To have the MTME in-charge of the separation and disposal of assets. The separation and disposal of assets can be carried out by the MTME. In Japan, the Ministry was responsible for this.	· MTME is more likely than the PKP to want separations / disposals · Can monitor the privatization process from outside of PKP	· MTME may have no experience · MTME may be weak relative to the PKP
Publicize PKP's problems creating public awareness for the separation and disposal of assets. In Japan, the JNR was too strong until public awareness reached the level where government action was necessary	· Can obtain public support and thus pressurize the PKP · Politicians may no longer be able to put off privatization	· Possible public opposition to privatization · Politicizes the issue
To conduct a complete audit of PKP's controls, systems and procedures. The auditing function and environment is weak in Poland.	· The 'management letter' provided by the auditor is critical in protecting the interests of shareholders.	· A thorough study of controls, systems and procedures is expensive to prepare and check each year.
To set up an arbitration panel to deal with disputed separations Disputes can arise when property is separated into another PKP unit or out of the PKP	· Will speed up the separation process	· May not be needed if no land & buildings i.e. the only valuable assets are to be given away (all occupants are treated as tenants)

(13) Methods to dispose of assets

The preferred method of disposal will have an impact on the separation and disposal of assets. The assets to be separated will have to be made attractive for potential buyers. For disposals, a market of potential buyers will have to be created. The World Bank distinguishes the following tradeoffs among privatization routes for large firms :

Tradeoffs among privatization routes for large firms

	Objective				
	Better Corporate Rule	Speed and feasibility	Better access to capital and skills	More government revenue	Greater fairness
Method					
Auction (Tender)	+	+	+	+	-
Public Offering	-	-	-	+	+
Sale to strategic investors	+	-	+	+	-
Management – employee buyout	-	+	-	-	-
Equal access voucher scheme	?	+	?	-	+
Spontaneous privatization	?	?	-	-	-

Source : World Bank, Human Development Report 1996, From Plan to Market, modified by the JICA team

The above tables and other methods are discussed below :

Option / *Explanation*	Merits	Demerits
Auction (tender) An open, contestable, and competitive bidding process.	· Quick to implement, most effective and direct · Requires the minimum of management attention · Management will change	· Does not always maximize the value realized from the sale
Public Offering of Stock This may be the only viable domestic source of private capital.	· May be the only option for a company with high asset value · May be the best way to maximize revenue	· This method is slower · Restructuring must be completed first · Future earnings must have a probability of growth. · A well developed capital market is needed
Sale to Pre-qualified Strategic Investors A third party qualifies potential investors, enters into dialogue, develops an offering memorandum. Following due diligence, qualified bidders are invited to prepare bids.	· Normally brings in new capital and new management	· The mechanism is subject to abuse · Appropriate for smaller enterprises only
Concessioning under Contract A concessionaire uses public assets in return for a profit share and a commitment to maintain the assets under its custody and make additions and improvements as stipulated in the concession contract.	· Can contract out the operation of unprofitable services (concessionaires to bid on a minimum subsidy) · Entry cost is low as the ownership of railway assets is not transferred	· Is revocable i.e. this is a threat for the concessionaire
Franchising under Contract Franchises are different from concessions in that no capital commitments for assets is required	· Simple as a basic fee is decided for specified services	· Will not lead to new investment
Leasing and Operating This is especially appropriate for small railway companies.	· Substantially lowers the entry costs · Track and structures are financed by third parties	· Track and structures have to be financed by third parties
Sale of Operating Rights In this case, a track authority gives operating rights over the network.	· Suited to Polish conditions	· Issues are complex and only limited experience exists

5.3.2 Recommendations for organization units and "organized portions of assets"

(i.e. to be separated ad disposed if by the PKP)

(1) Desirable methods for separation / privatization

Chapter 2.5.2 has outlined the various methods of privatization that have been employed in Poland. For the separation / privatization of the units that can be separated

/ privatized from the PKP, the following methods are recommended (in order of merit) :

- Direct privatization by leasing to employees
- Direct privatization by leasing to a strategic investor

Leasing of assets is recommended for the following reasons :

- Employees are unlikely to have enough money to buy assets (e.g. all the assets of a locomotive depot or rolling stock leasing company)
- Avoids the problem of asset allocation (e.g. if 8 track-laying companies are to be created from the current 8 WORG's doing this task and there are only 3 modern satellite controlled track-laying machines, no allocation needs to be made)
- In case the new company becomes insolvent / goes bankrupt, the assets will not be lost to the separated company's creditors

It is relevant to note that the Ministry can waive 2 of the conditions for creating employee owned companies to lease assets i.e.

- The maximum number of employees is limited to 500 (artificial companies of 500 persons can be created from larger units or WORGS)
- Other persons must have 20% of such a company

A typical share-holding scenario for a company created by employees to lease assets from the PKP could have the following structure :

		Shares per person	Share price	Total	%
Employees shareholding	500 employees	4 shares each	10 PLN per share	20,000PLN	80
Friends / relatives	500 persons	1 share each	10 PLN per share	5,000 PLN	20

Thus it may be necessary for employees to contribute only 50 PLN each in order to start a company that can lease PKP assets in order to earn income from the PKP and from other sources.

(2) Analysis and recommendations

The following analysis is based on

- the PKP's proposed organizational structure (see chapter 2.3)
- the goals for desirable separation in 5.3.1 (1)
- the lessons from the previous separations and disposals in 5.3.1 (3)

- the lessons from the previous separations and disposals in 5.3.1 (3)
- the PKP law 5.3.1 (4)
- Polish privatization laws (see chapter 2.5.2)

1) Real Estates Vertical

Real Estate is discussed first because land and buildings are the only valuable assets of the PKP and they have alternative uses.

A Real Estates Vertical (REV) was set up from the 1st of July 1997, headquartered in Gdansk. This vertical is staffed by persons previously working in the 20 Buildings Sections which have been consolidated into 16 new Real Estate offices. It is expected that 800 people in total will be employed in this vertical.

The REV will be responsible for all land and buildings except for those used for

- the Traction and Back-up Sector
- the Social Vertical
- the Railway Health Service
- rail & structures in the Infrastructure Sector.

The REV will thus undertake the maintenance of all properties used by the Passenger Sector, Freight Sector, Infrastructure Sector and the other Verticals. The costs incurred by the REV will be passed onto the Sectors and Verticals. In the case of non-PKP tenants, "market rents" will be charged.

The REV will also undertake all the activities of a normal property company like property investment / development.

The difficulties that will arise from this approach are

- There will be no pressure (incentive) to rationalize on the use of PKP land and buildings by the PKP tenants. This is because the only cost of using more property than is needed (by any sector / vertical) will be the extra maintenance costs. Also there will be no incentive to move out of city center properties the functions that could be carried out in less central properties thus releasing space that could contribute large rent receipts.
- The REV will be staffed by specialists only in buildings' repairs and lacking other skills required to properly manage a huge property portfolio like Asset Management (exploitation), Agency (determining rental values), Investment

(valuation of properties, purchases and sales), Developments (of offices, shops, shopping centers, housing), Architects etc. While many of these skills can be bought-in (sub-contracted), the lack of management skills (asset management) will not be resolved.

The above two difficulties can be solved by

- Charging "market rents" to all users (including PKP tenants)
- Sub-contracting the responsibility for Asset Management to a specialist firm (Chartered Surveyors)

The various options for executing the above are (in order of preference):

- Separate all land and buildings into a new State Owned Enterprise
- Separate all land and buildings into the Infrastructure Company
- Keep land and buildings in the PKP e.g. as a subsidiary of the Related Businesses Division

The effect of charging "market rents" to PKP tenants will be :

Freight Sector	• profits reduced • P&L will show true picture	• can be used to subsidize the Passenger Sector
Passenger Sector	• losses increased • P&L will show true picture	• rent paid can be returned by increasing subsidy
Infrastructure SOE	• profits reduced • increased charges to clients	• transfer from one SOE to another SOE only

Thus the net effect will be to

- extract money from the Freight Sector that can be used toward the required passenger subsidy
- new income due to increased charges to foreign / non-PKP operators

2) Welfare (Social units) Vertical

This new vertical was established on the 1st of July 1998, headquartered in Gdansk. The headquarters will have 23 staff who will be in-charge of 8 regional offices employing 170 staff.

Top Management
(23 staff)

↓

Regional Offices
(8 offices, 170 staff)

↓

Holiday resorts	48 units
Canteens	45 units
Hotels	7 units
Bars	8 units
Culture Houses	10 units
(total 1500 staff excluding seasonal workers)	

The underlying financial situation of the Welfare Vertical is not too bad. The results / forecast received from the new management (2nd column) shows :

Welfare Vertical's forecast P&L

YEAR	Profit / Loss (PLN 000)	Adjusted P&L
1995	-18,850	-18,848
1996	-15,996	-25,411
1997	-3,261	-4,721
1998	0	-1,777
1999	150	-1,087
2000	201	-1,195
2001	298	-1,461
2002	395	-1,857
2003	499	-2,382
2004	600	-3,135
2005	702	-3,999

(note – The numbers in the 3rd column have been adjusted for additional depreciation that will arise due to planned capital spending of 113 m PLN till 2005.)

Important additional points to be considered in deciding on the separation / disposal of the Welfare Vertical are :

- The PKP pays 38.5% additional to salary costs to the Social Fund which has for example financed a new resort at Cisna
- All properties are effectively owned by the Social Fund / employees
- This vertical is forecast to have a profit by 1999

Thus the options to be considered include :

- Transfer the Welfare Vertical to the Social Fund
- Transfer the Welfare Vertical to the Staff Investment Fund (see 5.3.4)
- Create a new subsidiary and transfer the shareholding to the Staff Investment Fund
- Separate as a new SOE or subsidiary

In any case, the PKP itself should stop any capital expenditure. The net adjusted loss for 2005 of 4m PLN is only 25 PLN per person and should in principle paid for by the Social Fund (which receives 38.4% of salary costs). In addition, the Social Fund should fund the cashflow shortfall till 2005 of 103 m PLN.

3) Housing Vertical

In the interim report , we had suggested giving the apartments to staff as a form of redundancy payment. The PKP have identified 2 flaws in this approach :

- proceeds of sales should be transferred to the Social Fund e.g. if an apartment valued at 50,000 PLN is given to an employee as a redundancy payment, then 50,000 PLN must be paid by the PKP to the Social Fund.
- all staff should be treated equally i.e. even those employees not living in PKP apartments should have the right to receive an apartment as redundancy pay.

The net result seems to be that the Social Fund and current residents enjoy all the benefits while the PKP pays the greater portion of the costs. The PKP are legally obliged to maintain the flats in good condition even if this cannot be recovered from tenants.

Thus about the best that the PKP can expect is that someone will take the flats over from the PKP for no payment. The current favorite candidates are Local Authorities and Housing Associations.

The PKP is allowed to transfer flats free to Housing Associations from 6-5-1997 to the end of November 1997. It has been claimed that the PKP cannot make use of this opportunity because of 15,159 buildings, the PKP has ownership papers for only 546.

It is strange that the PKP has use of the flats and is treated as the owner but unlike an owner cannot give away the flats.

It is recommended that the PKP impose an accounting system so that only the monies collected from any house / apartment blocks are spent on it. Thus the only additional cost to the PKP will be the administrative employees costs which are expected to reduce from 45m PLN in 1999 to 34m PLN in 2005. The PKP currently makes a loss of about 120m per year from housing of which depreciation is about 30m PLN.

It is interesting to note that the Investment Department have forecast capital expenditure on housing of 16.7m PLN for 1997 rising to 39.2m PLN in 2005 – a total of 253 m PLN. This too should stop immediately.

The PKP should consider the following options :

- To create a Housing Association and to transfer the rights use the houses to this Housing Association for free before the end of November 1997. (There is a rule that if ownership records are missing, the manager of any property on 5.12.90 is deemed to be the "real owner". The "real owner" can sell this right).
- To create a subsidiary and to transfer the housing properties to this subsidiary. Thus all incomes and expenditures will be the responsibility of this subsidiary and not the responsibility of the PKP. The PKP should then subsidize this subsidiary only to the extent of the administrative employees salaries.
- To transfer the Housing to the Social Fund
- To transfer the Housing to the Staff Investment Fund

Of the various options, the first is probably best i.e. transfer ownership into Housing Associations. The PKP could thus save up to 120m PLN per year.

4) Pensions Vertical
This vertical administers the pensions for about 330,000 ex-PKP staff. Both the costs of the monies disbursed and of the administrative staff are being covered by the National Insurance Company (ZUS). Thus for all practical purposes, this vertical can be treated as non-existent within the PKP (i.e. already separated) and thus not a consideration for the privatization of the PKP.

5) Railway Health Service Vertical
The Railway Health Service Vertical (RHSV) is treated as having been separated from the PKP as at 1st January 1997. Thus the RHSV keeps all its incomes and pays for all its costs including payments to other parts of the PKP for repairs. It is responsible for all it properties and has even taken over some buildings maintenance staff from the previous Buildings Sections. Staff allocations were based on RHSV "technical units" as a proportion of total "technical units".

Rail Health Service activities in 1996 (in thousands PLN)

	Health only	Sanitation	Health & Sanitation
Income with subsides from current activities	419 104.45		419 104.45
incl. - own income	25 020.42		25 020.42
incl. – income from hospitals and policlinics	9 285.42		9 285.42
- income from pharmacy	15 699.21		15 699.21
- ABB donation	35.79		35.79
- current activities subsidy	392 198.12		392 198.12
Donation for investments	7 670.00		7 670.00
Costs without depreciation	420 096.16	8 478.22	428 574.38
incl. – salaries	192 718.69	5 036.11	197 754.80
- salaries overheads	93 658.63	2 347.97	96 006.60
- remaining costs	133 718.84	1 094.14	134 812.98
Costs with depreciation	434 808.87	8 655.74	443 464.61
incl. Depreciation	14 712.71	177.52	14 890.23
Financial result without depreciation	- 991.71	-8 478.22	-9 469.93
Financial result with depreciation	-15 704.42	-8 655.74	-24 360.16

The above table shows that the loss without depreciation was only 9.5m PLN and including depreciation 24.4m PLN. Assuming that the PKP provided subsidy of 24.4m PLN to the RHSV, this represents the true annual cost to the PKP of the RHSV.

It is worthwhile distinguishing 2 types of tasks performed by the RHSV i.e.

- General health service – any health service for any staff / ex-staff / relatives
- Occupational health service – checking key PKP staff to see if they are fit for work e.g. locomotive drivers / signalmen

The above table shows that the PKP effectively paid the RHSV only 9.5m PLN (or 24.4m PLN depending on the amount actually transferred) for the occupational health service (i.e. health checking). Whilst we assume that the RHSV is totally separated from the PKP in 1999, we have assumed an annual payment of 40m PLN by the PKP to the National Health Service for occupational health checks on PKP staff.

Thus the net cost to the PKP of paying for occupational health checks will be an increase in expenditure of 30m PLN per year if the RHSV is separated from the PKP.

6) Computerized Data Processing Vertical (CDPV)
During 1996, the Railway Information Center (CIK) costs were 36.8m PLN, partially offset by external sales of 1.5m PLN. The CIK, with 967 staff in 12 IT Centers, will be the main component of the new CDPV.

The CDPV with as many as 1,500 employees may become the largest computer services company in Poland. The income of the CDPV from sources external to the PKP is expected to increase to 15m PLN per year from the current 1.5m PLN within 2 to 3 years. One of the major problems is the lack of staff because PKP's wages are too low.

The CDPV would like to become an independent company so that they are free to pay market rates for computer programmers and to exploit opportunities to work for other external clients. The PKP will however remain the largest customer.

Separation of the CDPV is an important step toward increasing income as a Railway Related Business. It is recommended that the CDPV is transferred into a new subsidiary with PKP majority shareholding.

7) Telecommunication Vertical

Telecommunications provides one of the best opportunities for Related Business using the PKP's network which is possibly more modern than Telekomunikacja Polska's (TPSA).

Current managers are willing to manage their own affairs – and have identified besides the PKP, power stations and tramways as clients. It is claimed that if separated (or privatised separately), efficiency will improve, more money will be earned and the staff will work harder and less materials will be consumed.

Thus it is recommended that the Telecommunication Vertical should be transferred into a new subsidiary with PKP majority shareholding. At a later stage, it is also possible to convert into 30 new companies by direct privatization or the involvement of strategic investors.

8) Power Engineering Vertical

The Power Engineering Vertical (PEV) will be responsible for the maintenance of electrical equipment. They would purchase electricity from distributors, transform and supply to / for

- Traffic and traction
- Buildings (PKP's)

Certain PEV managers would like to be separated from the PKP with a system of "full settlement" for their services by the PKP.

It is recommended that the PEV be transferred into a new subsidiary with PKP majority shareholding. At a later stage, it is also possible to convert into 30 new companies by direct privatization or the involvement of strategic investors. Since all of these 30 units do not possess the same equipment, in order to create equal conditions, it is best to lease equipment rather than separating these units with their equipment.

9) Training Vertical

There are currently 8 training centers that employed 207 staff as at the end of 1996. It is assumed that the Training Vertical will be created from these training centers and staff.

It is recommended that this Training Vertical be converted into a new subsidiary with PKP majority shareholding or transferred to new operating / maintenance companies. Other parts of the PKP and external clients would then have to buy the services of this Training Company. Success of such a company depends on the capabilities of the staff and successful marketing to external clients.

10) Procurement Vertical

At the end of 1996, there were 1,917 staff employed in material supply and a further 93 in the Central Spare-parts Warehouse (CSCZ).

It is recommended that this Procurement Vertical be converted into a separate subsidiary with PKP majority shareholding.

11) Railway Security Service Vertical

At the end of 1996, there were 3,844 staff employed in the PKP Security Service. Once a Railway Security Service Vertical is created, this can be converted into a new subsidiary with PKP majority shareholding.

The MTME and DGPKP's offices that were previously guarded by the PKP Security Service are now contracted to a private security company.

12) Structural Units Subordinated to the Management Board of PKP Vertical

The various Structural Units that report to the Management Board will be grouped together in one vertical. Each of these units can also be transformed into subsidiary companies with PKP majority shareholding.

(3) Summary recommendations for all organization units and "organized portions of assets"

Organized portion	Recommendation
Real Estates Vertical	A new subsidiary with PKP majority shareholding
Welfare (Social units) Vertical	Privatize as commercial hotels etc.
Housing Vertical	Convert to Housing Associations
Pensions Vertical	To Government (already pays all costs)
Railway Health Service Vertical	Becomes part of National Health Service
Computerized Data Processing Vertical	A new subsidiary with PKP majority shareholding
Telecommunication Vertical (see below)	A new subsidiary with PKP majority shareholding
Power Engineering Vertical (see below)	A new subsidiary with PKP majority shareholding
Training Vertical	A new subsidiary with PKP majority shareholding or transferred to new operating / maintenance companies
Procurement Vertical	A new subsidiary with PKP majority shareholding
Railway Security Service Vertical	A new subsidiary with PKP majority shareholding
Structural Units Subordinated to the Management Board of PKP Vertical	New subsidiaries with PKP majority shareholding
Electric Feeding Sections	30 companies by direct privatization / strategic investors
Road Sections	43 companies by direct privatization / strategic investors
Mechanized Road Works	8 companies by direct privatization / strategic investors
Automatic and Telecom Sections	30 companies by direct privatization / strategic investors
Rolling Stock Plant	2 companies by direct privatization / strategic investors
Traction and Workshop Sector	35 companies by direct privatization / strategic investors
Railway Scientific-Technical Center "CNTK"	A new subsidiary with PKP majority shareholding
PKP Foreign Settlement Center "CBRZ"	A new subsidiary with PKP majority shareholding
Sale and Purchases Center "FERPOL"	A new subsidiary with PKP majority shareholding
Travelers' Service Center "POLRES"	A new subsidiary with PKP majority shareholding
Income Controlling Office, Lodz	A new subsidiary with PKP majority shareholding or transferred to freight operators
Income Controlling Office, Krakow	A new subsidiary with PKP majority shareholding or transferred to freight operators
Income Controlling Office, Olsztyn	A new subsidiary with PKP majority shareholding or transferred to freight operators
Free Ticket Office	A new subsidiary with PKP majority shareholding
Permanent Way Diagnosing and Welding Center	A new subsidiary with PKP majority shareholding
State Cable Railways "PKL"	A new subsidiary with PKP majority shareholding
Track Machinery Plant, Gdansk	A new subsidiary with PKP majority shareholding
Track Machinery Plant, Krakow	A new subsidiary with PKP majority shareholding
Track Machinery Plant, Wroclaw	A new subsidiary with PKP majority shareholding
Tie (sleeper) Regeneration Plant	A new subsidiary with PKP majority shareholding
Railway Printing Office, Warsaw	A new subsidiary with PKP majority shareholding
Railway Printing Office, Krakow	A new subsidiary with PKP majority shareholding
Railway Printing Office, Poznan	A new subsidiary with PKP majority shareholding

5.3.3 Recommendation for individual classes of assets

(i.e. to be separated and disposed of by the PKP)

(1) Surplus Rolling Stock

The table below shows surplus I)freight rolling stock ii) passenger rolling stock and iii) locomotives as calculated by the PKP.

	Surplus Freight Wagons	Value	Surplus Passenger Wagons	Value	Surplus Locos	Value	Total Units	Total Value
1995	3,488	7,673,600	210	525,000	151	906,000	3,849	9,104,600
1996	2,706	5,953,200	191	477,500	171	1,026,000	3,068	7,456,700
1997	1,842	4,052,400	411	1,027,500	286	1,716,000	2,539	6,795,900
Sub-total	8,036	17,679,200	812	2,030,000	608	3,648,000	9,456	23,357,200
1998	1,842	4,052,400	411	1,027,500	286	1,716,000	2,539	6,795,900
1999	1,842	4,052,400	411	1,027,500	286	1,716,000	2,539	6,795,900
2000	1,842	4,052,400	411	1,027,500	286	1,716,000	2,539	6,795,900
2001	1,780	3,916,000	354	885,000	239	1,434,000	2,373	6,235,000
2002	1,780	3,916,000	354	885,000	239	1,434,000	2,373	6,235,000
2003	1,780	3,916,000	354	885,000	239	1,434,000	2,373	6,235,000
2004	1,780	3,916,000	354	885,000	239	1,434,000	2,373	6,235,000
2005	1,780	3,916,000	354	885,000	239	1,434,000	2,373	6,235,000
TOTAL	14,426	31,737,200	3,003	7,507,500	2,053	12,318,000	19,482	51,562,700

Source: Bureau of Strategy and Restructuring, PKP, March 1997

The numbers are those to be scrapped each year and have been valued at an average of 2,200 PLN per freight wagon, 2,500 PN per passenger wagon and 6,000 per locomotive. It is assumed that these values are net book values. The total capital value thus is 0.2% of the net assets of the PKP. Getting rid of these assets over 8 years will have little effect on the profitability as defined by return on assets.

On the P&L side, these surplus assets can be a burden if they require revenue expenditure e.g. for maintenance or for parking. The PKP can stop maintaining such rolling stock and parking is free on thousands of kilometers of disused lines.

It is thus recommended that the rolling stock be cut up and sold for the scrap metal value of about US$100 per ton. The total proceeds will be about US$30m. This method is best because the incremental costs will be less than $30m based on transporting 332,000 tons of scrap (say $9m) plus conversion costs. Note: surplus labor in the traction / maintenance units can be used thus incurring little incremental costs for conversion[6].

(2) Land & Buildings

It is recommended that all properties should be given to a new SOE which could rent properties back to various sectors and verticals. This new SOE should be managed by property management & development specialists (chosen by tender) on behalf of the State. A full discussion is in 5.3.2(2)1) above.

Basically it is not recommended that land and buildings be treated as individual assets to be disposed of by the PKP but rather as an "organized portion of assets"that should be kept for its investment and development potential.[7]

(3) Light density lines (see chapter 5.4).

5.3.4 Staff Investment Fund

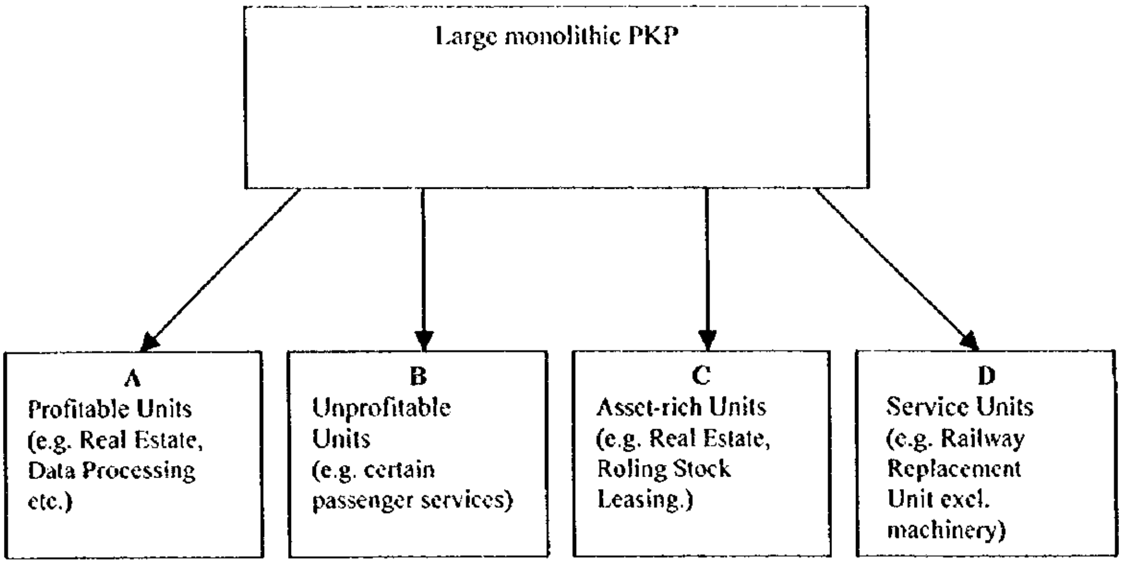
It is recommended that the PKP in conjunction with the MTME (and supported by other Ministries as well) should set up a Staff Investment Fund (SIF).

(1) Rationale for a Staff Investment Fund

One of the basic problems is to get the support of the employees in privatization by separating units from the PKP that can be privatized.

[6] The use of a Restructuring Agency is thus not required to get rid of surplus rolling stock. The problem that remains however is one of who will be responsible for identifying the surplus rolling and arranging for its disposal. If all rolling stock were to be transferred to rolling stock leasing companies who would lease required rolling stock to the operators, it would immediately become clear as to the extent of surplus rolling stock i.e. that which is not leased.

[7] A new SOE would treat all properties as investment / development properties i.e. leasing them for rental income and developing for capital growth. A Restructuring Agency on the other hand would sell properties and use the proceeds to cover its daily running costs.



The diagram above is meant to show that if the PKP is divided into smaller units, these will exhibit certain characteristics e.g.

- Category A Profitable Units
- Category B Unprofitable Units
- Category C Asset-rich Units
- Category D Service Units having few assets

Clearly employees would not like to be separated into units like Category B or Category D. Alternately those who would be left behind in units with the characteristics of Category B or Category D would not want Category A or Category C units to be separated and / or privatized.

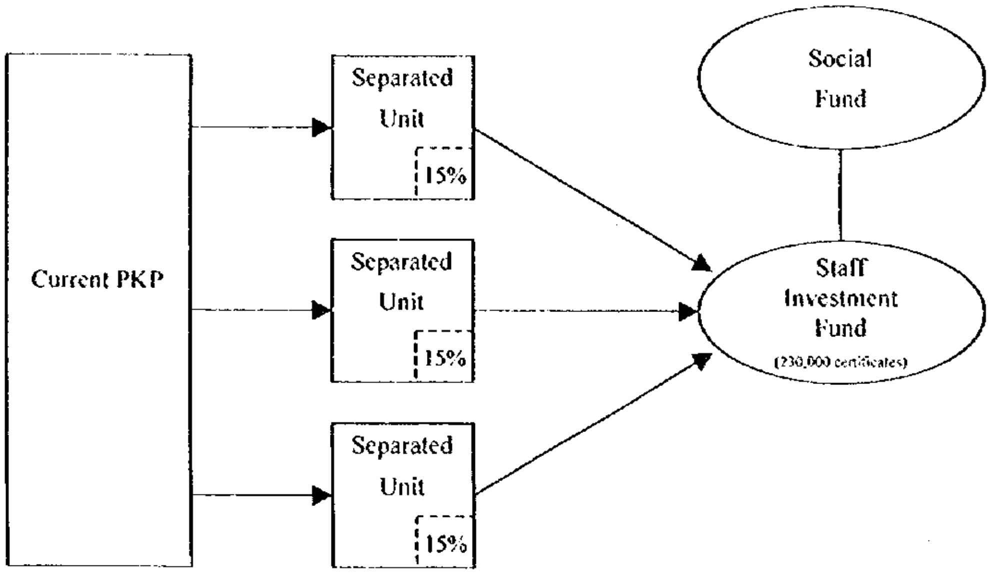
The concept of the SIF is that all the employees should get shares in all the separated parts of the PKP

(2) Concept of a Staff Investment Fund (SIF)

The concept of the proposed SIF comes from ideas that are characteristic of Polish privatisations, namely

- The 15 National Investment Funds
- Employees rights for up to 15% of privatized companies

It is recommended that the PKP set up a SIF, initially having no assets. Following this, ownership certificates should be issued to all staff. Following the issue of the valueless certificates, we would expect that the employees will demand that any parts of the PKP that can be separated / privatized be separated or privatized as soon as possible. The debate is likely to shift from being whether to privatize or not to how quickly and which parts of the PKP should be separated / privatized.



The above presents in diagrammatic form one of the many ways in which to organize the SIF. In this case :

- the SIF is managed / is part of the Social Fund
- the SIF issues certificates of ownership to all the employees of the PKP
- when any part is separated, privatized, proceeds of up to 15% are injected into the SIF

There is no precedent for such a scheme but it is probable that something similar to the SIF can be organized by the PKP. The main requirements for such a SIF are

- It should not break any existing laws
- (Ideally) It should not require the introduction of a new law

One of the important characteristics of the SIF as outlined above is the fact that as more and more units are separated / privatised, the value of the SIF will grow. On the other hand, if no units are separated / privatised, the SIF and hence its certificates will be worthless.

(3) Setting up the SIF

The following steps are recommended :

- employees of the PKP are asked to vote in favor of such a scheme

- a "paper organization" is set up and all staff as on 1/1/1988 be issued certificates
- the management of the fund can be initially undertaken by union representatives
- the register of certificate holders can be undertaken by the Social Fund or a professional firm

5.3.5 Separation & Disposals by Phases

A possible time-table is shown in the following table :
Separation & disposals by phases

Phase	
Phase 1 (1997-1998)	- New SOE's e.g. Infrastructure - Organization units and "organized portions of assets - Rolling stock
Phase 2 (1999-2000)	- Welfare, Housing, Pensions & Railway Health Service Verticals
Phase 3 (2001-2002)	- New subsidiaries with PKP majority shareholding
Phase 4 (2003-2005)	- Companies by direct privatization / strategic investors
Phase 5 (2006 -)	

Annex 5.3.1 : Analysis of WORG's and units

Official status as of September 1, 1997

	# WORGs & units : Sept. 1997	# WORGs & units : That can be separated	# WORGs & units : That can't be separated	# WORGs & units : 1996
Central DOKP, Warsaw	43	23	20	79
Eastern DOKP, Lublin	34	15	19	53
Southern DOKP, Krakow	24	10	14	54
Silesian DOKP, Katowice	42	21	21	75
Northern DOKP, Gdansk	41	21	20	68
Low Silesian DOKP, Wroclaw	32	16	16	63
Western DOKP, Poznan	35	18	17	61
Pomeranian DOKP, Szczecin	24	14	10	48
Traction and Workshop Sector	35	35	0	
Real Estate Vertical	16	16	0	
Railway Health Service Vertical	84	84	0	
Social Service Vertical	8	8	0	
Other organizational units	24	24	0	22
TOTAL	442	305	137	523

Annex 5.3.2 : Analysis of separable WORG's :

Electric Feeding Sections	30
Road Sections	43
Mechanized Road Works	8
Automatic and Telecom Sections	30
Flats	24
Security	1
Rolling Stock Plant	2
Traction and Workshop Sector	35
Real Estate Vertical	16
Railway Health Service Vertical	84
Social Service Vertical	8
Other Organizational Units	24
TOTAL	305

Annex 5.3.3 : The other organizational units subordinated to PKP Board

1	Traction and Workshop Backup Sector	Krakow
2	Real Estate Vertical	Gdansk
3	Railway Health Care Vertical	Warsaw
4	Social Service Vertical	Gdansk
5	Railway Information Center "CIK" (Vertical)	Warsaw
6	Railway Training Center (Vertical)	Warsaw
7	Railway Retirement and Pension Office (Vertical)	Olsztyn
8	Railway Scientific-Technical Center "CNTK"	Warsaw
9	PKP Foreign Settlement Center "CBRZ"	Bydgoszcz
10	Sale and Purchases Center "FERPOL"	Warsaw
11	Travelers' Service Center "POLRES"	Warsaw
12	Income Controlling Office	Lodz
13	Income Controlling Office	Krakow
14	Income Controlling Office	Olsztyn
15	Free Ticket Office	Gniezno
16	Permanent Way Diagnosing and Welding Center	Warsaw
17	State Cable Railways "PKL"	Zakopane
18	Track Machinery Plant	Gdansk
19	Track Machinery Plant	Krakow
20	Track Machinery Plant	Wrocław
21	Tie (sleeper) Regeneration Plant	Ostrow Mazowiecki
22	Railway Printing Office	Warsaw
23	Railway Printing Office	Krakow
24	Railway Printing Office	Poznan

Annex 5.3.4 : Opinion / Model for Staff Investment Fund

Privatization Model of State-owned, Multi-unit Enterprise Acting on Separate Act
(the act from 25-09-1981 on state enterprise does not apply)

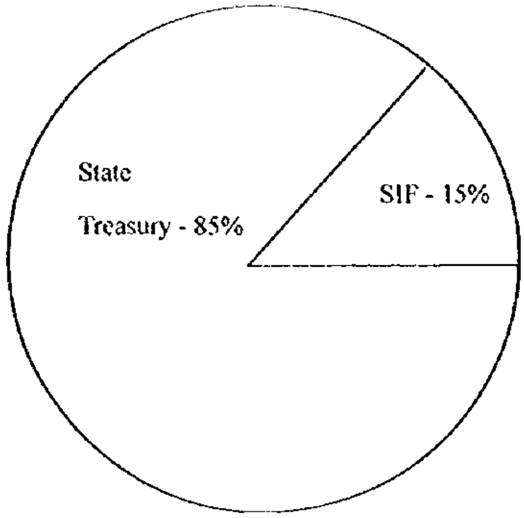
A model for use in the PKP.

I stage - Commercialization

In the first stage the enterprise is commercialized -- i.e. transformed from a State Owned Enterprise into one-man State Owned Partnership. This can be achieved only by the passing of a new , which must be passed by the Polish Sejm. This act should state that 15% of shares owed by the State Treasury should be transferred by the State Treasury Minister to the Staff Investment Fund. (*Polish* Fundusz Akcji Pracowniczych)

Every employee of the enterprise employed on the day it is commercialized will receive shares in the Staff Investment Fund (SIF). Thus unlike the currently applied regulations, employees of the commercialized enterprise would not receive shares in the commercialized enterprise but shares in the SIF, which would have 15% stake in the partnership created after transformation. It would concentrate shares and allow employees to have real impact on the partnership through the SIF.

We have to assume that the State Treasury would insert shares of the partnership to the SIF soon after its commercialization. Also employees should soon after that receive shares of the SIF.



As the result of shares insertion to EIF the structure of the capital would be as shown in the picture:

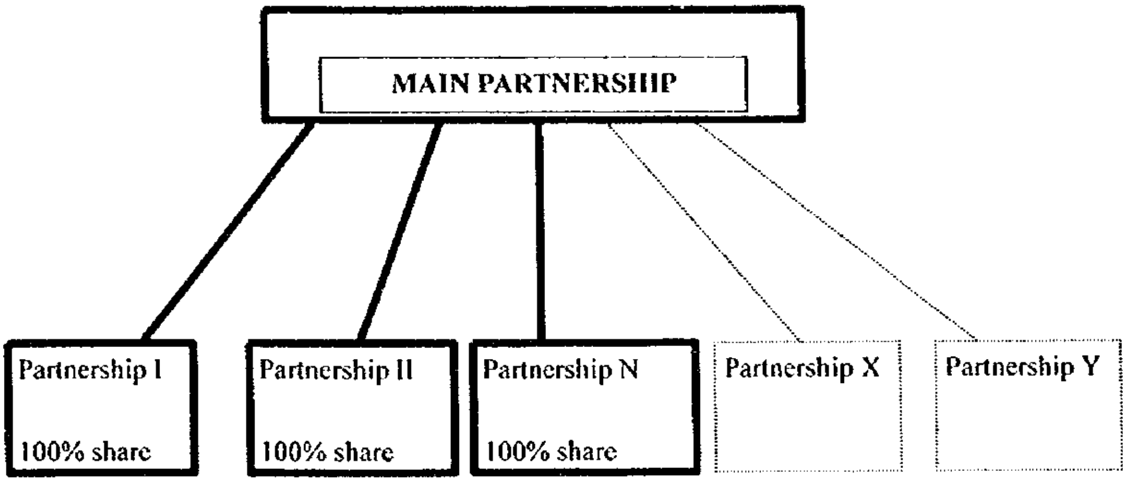
II stage - Assets (property) restructuring of the partnership

There are too many units in the PKP enterprise to be able to maximize the potential of the assets and of the staff. Thus any units that can be separated should become independent.

We can assume that there are 3 ways of doing so:

- Separation (from the partnership created after commercialization) of "organized portions of assets" (but only necessary for its statute activities) and insertion to other partnership (new-created) for its shares. New partnership would take over responsibilities of the unit. Also employees would be transferred to the new partnership.
- Activation of unit employees - employees set up the partnership and lease assets of the unit with option of purchasing used assets.
- Leasing of organized portions of property (units), but also real estates and other fixed assets to other partnerships, which will take part in tenders for performing transportation or service activities (maintenance, construction, etc.)

As the result of that stage a number of partnerships would be created, which would be capital dependent from the main partnership (holding) and partnerships connected through property by leasing necessary assets from the main partnership.



The picture shows chart of subordination of partnerships to the MAIN PARTNERSHIP. Partnerships I, II ..N are in 100% owned by the main partnership, partnerships X and Y - are partnership, which lease assets from the main partnership.

The main partnership would keep its responsibilities in setting up and proceeding with economic policy for the whole group.

After insertion and leasing of necessary assets the main partnership will have to solve problem of redundant assets. That part of property can be sold or given free by the partnership.

III stage - Privatization of "parter" (dependant) partnerships

As the financial results of the dependant partnerships improve, their shares would be sold. Non-effective partnerships would be liquidated.

Money from sale of shares would be used by the main partnership for development of the company, modernization and employment restructuring.

IV stage - Privatization of the main partnership -through making all or part of the shares owned by State Treasury available to other bodies including the SIF.

If the above model of privatization is to used in the PKP, the following issues must be considered:

- Necessity of separation of rail infrastructure from PKP property and establishing new body (partnership) on that property,
- Or separation of infrastructure in sector of PKP.

It is necessary because of 2 reasons:
- Free access to the infrastructure for other operators than PKP
- Investments on lines of state importance should be financed from central budget.

Staff Investment Fund - established as public limited partnership (S.A.) by the State Treasury. At the time when PKP employees receive shares, State Treasury would be the only shareholder.

The aim of the Fund would be to multiply property by increasing the value of shares of the partnership, in which the SIF would have 15% stake through:
- Realization of shareholder rights
- Purchasing and sale of shares of other partnerships and realization of shareholder rights
- Giving and taking loans, taking credits for realization of aims stated above and other statutory aims.

The SIF would act as investment fund. Its shareholders (former employees of commercialized state enterprise) would be able to increase the capital of the fund and give access to the Fund to other investors. The SIF could force privatization of the main partnership where the Fund would own 15% of shares (it could also have the right to purchase more shares from State Treasury). Fund could also force privatization of "parter" - dependant companies created as a result of the restructuring of the main partnership.