



MOBILITY AND TRANSPORT

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Introductory speech by Mr. Matthew Baldwin,

Deputy Director-General - DG MOVE

- Welcome to this seminar on tendering of public service contract for rail passenger transport.
- Granted, it is a technical topic. This is why, before we go into the details of it, I would like to recall why we are here: we are here because **we believe in rail** and we want to make it work better, to the benefit of the users, the environment and the economy.
- The advantages of rail transport are indeed many: it is one of the **safest** modes of transport. It is also one to the **greenest**: its development is essential to reach our goals of low carbon and reduce congestion. It is a crucial part of multimodal transport network, essential for the EU economy.
- Yet, this mode of transport is **stagnating** in several Member States and is not fulfilling its full potential: infrastructure is aging, rail services are costly for the taxpayers and/or the users, the quality of service falls short of travellers' expectations in terms of punctuality, frequencies and comfort. Intermodal competition (from cars and buses in particular) is fierce. As a result, the modal share of rail has stagnated at around 7.5%, while passenger volumes have grown significantly.
- One of the reasons is the fact that the single market, the Single European Railway Area, has not been completed yet. Some of the difficulties have been

of a technical nature, as networks developed in isolation from one another, with different national standards and equipment. But a large part of the problem is the lack of efficiency and customer orientation. We believe that **effective market opening and competition** can go a long way in addressing this issue.

- The **benefits of competition** are clear, whether it takes the form of open access on commercial lines or competition for public service contracts. These benefits are illustrated by the success stories in some Member States that embraced competition at an early stage, such as Sweden, Germany or Italy (on high speed lines).
- These Member States have witnessed positive developments: railway companies, in particular incumbents, are more responsive to customer needs and to innovation. As a result, **choice and quality** of service have increased, and railway companies have diversified their offers to tailor them to the needs of specific travellers, from cash-poor students to executives.
- As regards **train fares**, the impact of competition can be significant. In Italy, fares have gone down considerably, generating new demand and growing the market when competition was introduced on high speed commercial lines.
- Prices on lines under public service contracts are often regulated and depend on subsidies, so the effect of market opening may be more indirect. But, and this is very relevant for you as competent authorities, the **level of subsidies** required to operate non-profitable lines under public service obligations dropped by 20 or even 30% when the authorities started awarding PSO contracts competitively. This was the case in Sweden, Germany and the Netherlands.
- At the EU level, progress on market opening has been incremental, starting with the liberalisation of freight, international passenger transport, and now domestic passenger transport under the **fourth railway package**. The EU regulatory framework should be stable for the foreseeable future.
- The fourth railway package provides for wide-ranging rules. Its **technical pillar** aims to reduce red tape, reduce the number of national rules and improve interoperability. In parallel, the **market pillar** sets the stage for the complete opening of the domestic passenger transport and the gradual introduction of competitive tendering. It also sets clear rules to ensure that there is a level playing field between established operators and new entrants as regards access to the infrastructure.

- The introduction of open access for domestic passenger transport **in 2019** means the end of the remaining legal monopolies on rail transport in the EU.
- As regards **public service obligations**, which is our main topic today, let me first recall that the Commission fully supports public rail services, which are essential for citizens and protected by the Treaty. In line with the package, from 2019, the use of the **competitive tender procedure** for the award of public service contracts will be the norm, and **from 2023**, it will become compulsory. This will have significant impact as two thirds of railway traffic in the EU is currently carried out under public service contracts.
- Let's be clear: market opening in the rail sector brings benefits, but it is a complex process. The **objective of today's seminar** is specifically to assist you in preparing for the use of the competitive tendering procedure.
- Indeed, conducting a competitive tender procedure can be a **challenge**. For example, as competent authorities, you will have:
 - to design the geographical perimeter of PSCs so that they are contestable for new entrants.
 - to lower barriers to entry by facilitating bidder's access to **rolling stock and ticket distribution systems**.
 - to elaborate **criteria** for the selection of the bidders that strike the right balance between quality and price and ensure service continuity over the duration of the contract.
- Some Member States opened their markets quite some time ago. Pioneers are those who get the arrows in their backs, and yes, some of them experienced set-backs such as the failure of franchises. Others have been largely successful. In all of them, competent authorities have acquired experience and developed solutions to overcome problems in organising tender procedures.
- **Today's seminar** brings together experienced competent authorities and authorities who are now facing the same challenges.
- I hope this workshop will enable participating competent authorities to learn from this exchange of good **practices**.
- It is also an opportunity for establishing personal contacts with colleagues in other MS. It could possibly become the nucleus of an **EU platform** for the exchange of best practices over the coming years.

- Other important stakeholders are also present and will explain how they can help in this process: they include the **rail regulatory bodies**, represented today by ART, from Italy, the **EIB**, which has a long-standing experience in providing loans and advice for the purchase of rolling stock, in particular to regions and on the same theme a representative of a rolling stock leasing company (or ROSCO).
- Finally, a representative of **railway undertakings** will share his view of the "other side" of the tendering procedure, in particular on how tender procedures should be designed to ensure that there will be a successful outcome for the competent authority but also a fair chance for all railway undertakings.
- I would like to thank all the speakers who have agreed to come to Brussels to share their experiences. I would also like to thank the Committee of Regions for the use of their venue today. By doing so, it helps regions to make rail market opening a success!

Q&A session with Mr. Per Haugaard, Director in DG MOVE and Mr Henrik Mørch, Director in DG COMP

Q&A with Per Haugaard

1) Per, we often hear in the news that the EU rules on market opening poses a threat for the small lines and for the public service in general. Is that true?

- Let's be very clear: the Commission pays the **greatest attention to the protection of public services** in all sectors, which is expressly guaranteed by the Treaties.
- Market opening does not pose a threat to public services. It reveals which services are profitable, and which ones need compensation to be operated. The decision to discontinue less used services is a policy decision which is solely in the hands of national authorities.
- As to Regulation 1370/2007, the so-called PSO [public service obligation] regulation, it only provides a legal framework to make public service of passenger transport work.
- To that end, it establishes the following principles:
 - Competent authorities should clearly spell out the public service obligations in **public service contracts** concluded with the operator.
 - They have a large room for manoeuvre in the definition of **geographical scope and detailed content of these public service obligations, but they should also ensure that the same services could not be provided on a commercial basis.**

2) And what is new in EU rules on public transport?

- The fourth railway package provides further rules on the specification of public service obligations, but the main novelty concerns the **procedure for the award of public service contracts**, as highlighted in the slide.
- Between 2019 and 2023, competent authorities will have the choice between directly awarding public service contracts and awarding them on the basis of a competitive tendering procedure.

The possibility of making an unconditional use of the direct award procedure will cease **in 2023.**

- Competition authorities will be allowed to use the direct award procedure only in specific and limited circumstances.

3) I hear that competent authorities can make use of the direct award procedure till 2023, so why do we have this seminar in 2018? What is the urgency?

- There is indeed a **transition period** between 2019 and 2023 during which the use of tendering procedure is possible but not compulsory.
- I will not hide that the Commission was not initially in favour of such a long transition period. With insight, I must admit that it is a good opportunity, provided competent authorities put it to good use by gradually introducing competitive tendering without waiting until the deadline is over.
- There are several reasons for this conclusion:
 - First, we want to avoid a situation in which all tender procedures would be launched in 2023 and the market would simply not be in a position to respond to all of them.
 - Secondly, as underlined by Matthew in his introduction, the use of the tendering procedure can be complex at the beginning. The transition period should be used to **start getting some experience** in the tendering of public service contracts, before tendering becomes compulsory in 2023.
 - Finally, the sooner competent authorities embrace the open tendering procedure, the sooner they will **enjoy its benefits**, for example in the form of lower compensation paid to the public service operators or more and better services
 - I know that some Member States and their regional competent authorities are convinced of the necessity of opening their markets as soon as possible and are already preparing for this change now. I know also that others are more reluctant. My main messages today are: "**the transition period is an opportunity to get started with tendering: use it. Today's event is for you: make the most of it!**"

4) You also mentioned the existence of certain exceptions to the use of the open tender procedure after 2013. Does it mean that competent authorities can continue to directly award PSCs?

- You are right Chris, these exemptions do exist, but they are limited to **specific situations**, for example when it can be established that certain types of markets or networks are not adapted to competitive tendering. They thus provide some flexibility.
- However, do not forget that competent authorities that want to use these exemptions **have to adopt duly substantiated decisions** to use a direct award procedure. In particular, they need to demonstrate that it will lead to performance improvements.

- These decisions have to be subject to independent scrutiny at national level and the Commission has to be informed accordingly.
- Let me be clear: the Commission will closely monitor these decisions and intervene in cases where there is an abusive use of these exemptions, for example by launching an infringement procedure.
- To conclude, these exemptions do not undermine the principle that the competitive tendering procedure will become **the norm** and the direct award **the exception**.

5) Turning now to the access to rolling stock, I understand from Matthew, and the programme of this workshop, that this is a key factor for the successful tendering of public service contracts. Could you explain what the fourth railway package specifically says about this?

- At the beginning, I mentioned that the main novelty of the fourth railway package is that it mandates the use of a competitive award procedure for the attribution of public service contracts.
- But the fourth railway package does more than that: it also introduces provisions in the PSO regulation that are meant to **facilitate tendering** and ensure a successful outcome.
- For example, a new provision in the PSO regulation requires operators and competent authorities to ensure the **access to information** necessary for the preparation of the tendering procedure and of the bids. Without this information, it is simply not possible for authorities to design the tender, and for railway undertakings to prepare their bids.
- Another new provision does indeed concern **access to rolling stock**. Why? Because it can be a major barrier for new entrants. We have concrete examples of tender procedures where access to rolling stock was not ensured and where the only bidder was the incumbent. This is why:
 - the fourth railways package provides that competent authorities must assess whether measures ensuring non-discriminatory access to rolling stock are necessary for the success of a competitive tender. And they must make this assessment public by publishing it.
 - Of course, if they identify that there is an issue, competent authorities should logically endeavour to find a solution.
 - To that end, the package also proposes examples of measures that competent authorities can use to ensure access to rolling stock by operators.
- We will discuss the different solutions at this afternoon's session.

Q&A with Henrik Mørch

1) Henrik, this seminar is about rail transport regulation, so can you explain to us why DG COMP is present here today?

- You are right, this topic falls indeed within DG MOVE's remit. But DG COMP, and more generally competition law and competition agencies in Member States have a role to play, too.
- Let me first explain that DG COMP and DG MOVE work very closely together in order to make market opening in the rail sector a success. We have established a joint initiative in order to coordinate our respective enforcement activities in this sector: i.e. the infringement procedures launched by DG MOVE and the State aid and antitrust/merger cases investigated by DG COMP.
- Actually, DG COMP currently has quite some cases dealing with practices that affect competition in the rail sector in several Member States.

2) So what are the competition issues that the competent authorities present today should be aware of?

- Competent authorities must be aware that the legislative authority in the EU (the EU Parliament and Member States) have decided through the 4th Railway package to put an end to the "rail exception" and open the rail market to competition, just like all other transport sectors.
- In practice, this means that the rail sector will be increasingly subject to competition rules. Let me briefly mention what could be the nature of possible legal challenges tomorrow:
 - On the one hand, there could be violations of the competition rules by both contenders and the incumbents. The most serious violations of competition rules are cartels. This could happen, for instance, through so-called bid-rigging, whereby firms agree in advance who will win the tender.
 - We have also seen two examples of predatory pricing behaviour of an incumbent to undercut competitors and win the tender. I am speaking of the cases handled by the Dutch and the Czech national competition authorities. The case in the Netherlands related to the 2014 tender procedure for the public-transport contract in the province of Limburg. We do have a representative of the province of Limburg among us who can tell you more about this story. The case was handled by our colleagues from the Dutch competition authority, and I would

like to mention here that we at DG COMP work closely together with the national competition authorities, and increasingly also the national rail regulators, to put an end to violations of fair competition when needed.

- On the other hand, there could be competition problems created by competent authorities themselves. These problems would mostly relate to the public financing of rail services which will be subject to EU State aid rules. It is us in DG COMP who are investigating any such issues. Therefore it is paramount that competent authorities are aware of the potential problems and ensure that they comply with those rules.
- This is not an easy task for your authorities to take ownership of competition rules. Please let me highlight the biggest legal risks that the competent authorities will face when preparing and awarding public service contracts:
 - **Manifest errors in the definition of the public service obligations.** This could take the form of contracts covering lines already operated by commercial operators under the same conditions, or services obviously not proportionate to the public service need. This is the most serious problem because an ill-defined scope of the rail services will lead to the recovery of the entire compensation paid under that contract, with potential serious effects on the operator. This is why, as already emphasised by Per, competent authorities should pay very close attention to the correct definition of the public service obligations.
 - **Poorly designed compensation mechanisms** leading to more money transferred to the operator than economically justified. In that case, any overcompensation will have to be repaid.
 - **Problematic award procedures.** Competent authorities should ensure that the competitive award procedure will effectively be open, fair, transparent and non-discriminatory. Failing to do so could expose them to the cancellation of the contract and a risk of recovery of the entire compensation from the selected operator.

3) So you are saying that the open tender procedure is not sufficient to ensure effective competition and best value for money for the competent authorities and the travellers?

- In principle it is, but there are some risks and traps which can and should be avoided. That is why we are here today not only to encourage you to use the transition period to get prepared to the new legal requirements, but also to discuss with peers and learn from best practice.

- We at the Commission will also be there to help, but in many instances you may want to contact national rail regulators and national competition authorities first, which know the local context and the national regulatory framework better.
- Per has already underlined the importance of ensuring access to the information necessary to submit bids as well as access to rolling stock, especially to new entrants. It is also essential to guarantee non-discriminatory access to service and maintenance facilities. In this respect I'd like to mention our recent state aid case concerning three Slovak light maintenance workshops for passenger trains. While the primary beneficiary of the aid is the national incumbent ZSSK, in the future, once first PSC are tendered, winning competitors will operate the facility/ facilities.
- Another key condition for the successful opening of markets beyond tendering out PSCs is to guarantee access of new entrants to ticketing systems. This is also an area where competition authorities can have a role to play. In 2016, Deutsche Bahn committed to improve the ticket sales possibilities of its competitors following an investigation of the Bundeskartellamt. Among these commitments, I would highlight two of them. First of all, new entrants can now more easily sell passenger tickets in railway stations. Beforehand, rental contracts made it virtually impossible for shops located in these stations to sell tickets from DB's competitors. Today, new entrants can use this comparably low-cost alternative channel for selling tickets. Secondly, commission charges which are paid by DB and its competitors for the reciprocal sale of passenger tickets have been reduced to a large extent. Beforehand, commission charges were asymmetric and favourable to DB.
- I should also add that competent transport authorities also have a role to play in this area: In the 4th railway package there is a specific provision empowering Member States and competent authorities to oblige railway undertakings to participate in integrated ticketing schemes.