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Subject:	<i>Preparation of the Council meeting (<u>Transport</u>, <u>Telecommunications and Energy</u>) on 3 December 2014</i> Fourth Railway Package: Proposal for a Directive of the European Parliament and of the Council amending Directive 2012/34/EU of the European Parliament and of the Council of 21 November 2012 establishing a single European railway area, as regards the opening of the market for domestic passenger transport services by rail and the governance of the railway infrastructure Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EC) No 1370/2007 concerning the opening of the market for domestic passenger transport services by rail - Progress report

I. Introduction

The Italian Presidency gave a high level of priority to the market pillar of the 4th Railway Package, scheduling a large number of meetings and debates with a view to making decisive progress on the files. This progress report aims at providing a solid basis for future discussions in the Council.

The Commission presented its proposals and the related impact assessment to the Land Transport Working Party on 8 and 15 July 2014, followed by a first exchange of views. Further debates took place on 22 July, 2, 9, 19, 30 September, 2, 16, 24, 28 October, 4 and 6 November 2014.

The Italian Presidency's approach to this complex files was to document discussions and opinions within the Council in a Non-Paper which reflected the evolving state-of-play of the debate. After some rounds of in-depth discussion within the Working Party, an orientation debate was held at the Transport Council of 8 October. Based on the Ministers' policy guidance on three key issues emerging from the debate in the Working Party (granting open access rights and conditions of their introduction, additional measures to ensure non-discriminatory access to the network, introducing the principle of competitive award for public service contracts for rail and conditions of its introduction), the Presidency started the article-by-article examination of the proposal for a Directive amending Directive 2012/34/EU establishing a Single European Railway Area, as regards the opening of the market for domestic passenger transport services by rail and the governance of the railway infrastructure (hereafter "the draft Governance Directive"), and of the proposal for a Regulation amending Regulation (EC) No 1370/2007 concerning the opening of the market for domestic passenger transport services by rail (hereafter "the draft PSO Regulation"). The first examination of the articles of the draft Governance Directive and of the draft PSO Regulation was concluded, respectively, on 4 and 6 November 2014.

II. Content of the proposals

The aim of the above Commission proposals is to improve the quality and efficiency of rail transport services in Europe. To achieve that goal, the Commission has proposed to:

- open the market for domestic passenger services by rail by granting open access rights to all EU railway undertakings (commercial services outside public service contracts);
- improve the regulatory framework for the governance of railway infrastructure, notably by establishing rules on:
 - a) a coherent 'perimeter of functions' attributed to infrastructure managers and the conditions to be fulfilled to ensure their impartiality. The objective is to ensure equal and non-discriminatory access to the railway infrastructure network;

- b) the transparency of financial flows within vertically integrated undertakings, with a view to avoiding the risk of cross-subsidisation between infrastructure managers and railway undertakings;
- c) improved coordination mechanisms for the main players in the rail market;
- d) a strengthened role for national regulatory bodies;
- introduce the principle of competitive tendering for the award of public service contracts in rail transport.

III. Comments on the main issues

Some Member States consider the new legislative package to be premature as the currently applicable legislative texts either have not yet been transposed into national law¹ (recast of Directive 2012/34/EU and its implementing acts) or are subject to an ongoing transitional period (Article on contract award of Regulation (EC) No 1370/2007)². Many Member States indicated that, in their view, priority should be given to the technical pillar of the package, on which promising progress was made under previous Presidencies. However, under the impetus given by the Italian Presidency to progress on both pillars of the package in parallel, Member States contributed substantively to the debate on the Market Pillar, started for the first time during the current semester.

The Presidency hopes that this debate will be continued in the future.

Directive 2012/34/EU

A number of Member States welcomed the idea of introducing competitive pressure in domestic markets by opening up to competition those passenger rail services which can be provided on a commercial basis. Other Member States expressed a cautious reaction to the principle of market opening, and saw a close link between the provisions of this directive for commercial services, and the rules proposed in the PSO Regulation for public service contracts. They notably voiced the concern that market opening should be accompanied by strong safeguards to avoid compromising the economic equilibrium of public service contracts. Yet, other Member States remain concerned that there is little prospect for commercial services in some markets.

¹ The deadline for transposition of Directive 2012/34/EU is 16 June 2015.

² Art 5 of Regulation (EC) No 1370/2007 shall gradually be complied with until 2 December 2019.

As regards the regulatory framework for infrastructure management, many Member States expressed the view that the existing structural models (institutional separation and different forms of vertical integration with functional separation, including a holding system), should be put on an equal footing, and the possibility should be preserved for Member States to choose the model they consider most appropriate also in the future.

A concern was raised about the possible implication of the Commission proposal on Member States which consider that their railway system is efficient and which face competition from integrated undertakings from third countries. Some Member States objected to the broad set of functions attributed to infrastructure managers on the ground that:

- it would result in an extension of the 'essential functions' of infrastructure managers;
- it could be interpreted as limiting the prerogatives of Member States in terms of planning and financing of the infrastructure.

Some Member States asked for safeguards for existing and future public-private partnership solutions and possibility for certain sub-contracting arrangements.

There were calls for greater flexibility in this respect, preserving the 'essential functions' of the infrastructure manager, and for giving Member States the possibility to externalise other functions if necessary. Some Member States stated that it should remain possible for infrastructure managers and railway undertakings to be owned or controlled by the same Ministry or other public body.

Several Member States found the safeguards proposed to ensure the impartiality of infrastructure managers within vertically integrated structures excessively prescriptive, and called for substantially streamlined rules. There were calls for a transversal set of rules which would be applicable across different structural models. Certain Member States indicated that special rules for structural models that are not institutionally separated may be necessary to ensure a level playing field. A few Member States asked for greater flexibility in some of the financial transparency rules. Many Member States agree on transparency as a key factor to avoid the risk of cross-subsidisation.

As regards the proposed procedure for verification of compliance, many Member States found it disproportionate and called for the deletion of the proposed procedure. However, some Member States indicated a need to discuss simplification of the procedure. Concerns were also raised regarding the application of Article 61 of Directive 2012/34/EU, and on the need to assess its implications. Member States agreed on the importance of Regulatory Bodies in monitoring the equal and non-discriminatory access to the rail market.

Concerning the proposed Coordination Committees designed to facilitate cooperation between the main railway actors, some Member States were doubtful about the effectiveness of the proposed format of the Committees, warned of possible duplication of existing structures, and stressed the need to avoid unnecessary administrative burden.

As regards the proposed network of infrastructure managers, many Member States expressed appreciation for the existing informal network (PRIME). Some Member States expressed doubts as regards the added value of a formal network, the list of functions attributed to this forum, which was seen as excessively broad, and the role given to the Commission. Some Member States were open to the establishment of a formal network involving all infrastructure managers with a smaller set of functions and with a focus on the exchange of best practices.

Several Member States appeared cautious regarding the provisions concerning integrated ticketing schemes, and refused any compulsory provision.

A majority of Member States asked for a longer transposition deadline (36 to 48 months), and for a longer transitional period which may enable Member States to gradually open their markets.

Regulation (EC) No 1370/2007

Many Member States could accept the introduction of the general principle of competitive awards of public service contracts in rail, subject to appropriate exceptions. Some others were of the opinion that the possibility of direct award as a general rule should be maintained, taking account of specific national market features, including efficiency and quality features. In particular, some Member States were of the opinion that direct award and competitive tendering should remain on an equal footing.

Concerning the possibilities of direct award, as an exception regarding the principle of competitive award, many Member States indicated that they wanted to preserve more flexibility as to the conditions for directly awarding a contract to internal operators and therefore considered the definition of local competent authority proposed by the Commission as too restrictive. Furthermore, a few Member States wished clarity on the scope of public service contracts that should include national services. Some Member States asked for higher *de minimis* thresholds for direct award of rail contracts. Other specific derogations were discussed by some Member States, such as networks with specific characteristics (small, isolated or complex).

Concerning the transport plans, several Member States refused any provision that could limit the scope of public services, which should not be subject to any pre-approval or ex-ante control.

Some Member States questioned the added value of transport plans and asked to delete the provisions or make them not compulsory. A majority of Member States were afraid that establishing an excessively close link between transport policy objectives in public transport plans and the definition of the scope of PSO could lead to requests for legal reviews following award procedures and hence endanger legal certainty. Others considered the proposed provisions concerning the contents of transport plans as too detailed. Some Member States were concerned that the proposed provisions on the maximum size of contracts could lead to territorial and administrative and network fragmentation. Other Member States referred to the practical difficulties in linking railway public service obligations with the transport plans, as provided for in the draft PSO Regulation. Certain Member States indicated that any impact on other modes of transport, and especially on the road sector, has to be avoided or at least minimised.

The absence of fair, non-discriminatory and equal access to suitable rolling stock is widely recognised by Member States to be an important market entry barrier leading to low numbers of bids submitted by railway undertakings in a competitive award procedure for public service contracts. However, many Member States considered that the specific national market situations differ and that the Commission proposal would not leave sufficient leeway to choose appropriate measures to address the entry barrier, while controlling their budgetary and administrative implications.

The majority of Member States rejected the proposal to require all public service contracts for non-rail modes to have been competitively awarded by the end of the transitional period, 2 December 2019. Several Member States requested longer transition period for the direct award of rail contracts. A majority of Member States underlined that existing directly awarded contracts should be able to continue until they expire. Some Member States asked for a gradual market opening at national level during the transitional period, and a few maintained the proposal for additional measures (such as using the reciprocity criterion during this period, while others were not in favour).

The Presidency worked intensively to accommodate the views of the delegations. Given the complexity of the issues, the time available and the calls for a substantively modified architecture of the governance provisions, it was not possible to agree on concrete solutions. However, the delegations are positive about the progress made so far. The Presidency would like to summarise below a number of general principles and ways forward that, in its view, reflect the concerns of most delegations and could thus constitute a minimum common denominator for further developments.

IV. Suggestions for further negotiation

The following list of issues is an indication of areas for further discussion. It is not an exhaustive list and does not preclude other areas being addressed in future. Neither does anything in this document prejudice the negotiating position of Member States in future discussions.

a) Directive 2012/34/EU

Functions of the infrastructure manager

Only the current 'essential functions' should remain subject to the highest degree of separation. Greater flexibility should be envisaged as regards the outsourcing of functions to other entities, subject to appropriate safeguards. It should be made clear that the functions related to financial and investment planning are without prejudice to the prerogatives of Member States in these areas, as laid down in national legislation.

Public-private partnerships

Public-private partnerships are an important instrument for implementation of transport policies and may require specific provisions.

Structural models

The text of Article 7 should be restructured to put vertically integrated structures on the same footing as separated structures. It should be possible for Member States to choose the structural model they consider most appropriate at any point in time. There should be a core of common governance rules, designed to ensure the effective impartiality of infrastructure managers and the transparency of financial flows, which should apply regardless of structure. Certain Member States indicated that special rules for structures that are not separated may be necessary to ensure a level playing field. The emphasis should be on effective rules rather than on specific structural models. Further work needs to be carried out on definitions.

Verification of compliance

The regulatory oversight of the governance set-up in Member States should not be entrusted ex-ante to the Commission. Some Member States underlined the need to discuss appropriate safeguards. The implications of Article 61 of Directive 2012/34/EU should also be assessed.

Coordination structures (Coordination Committees, Network of Infrastructure Managers)

There should not be a duplication of structures that already exist in Member States and at the EU level. New coordination structures, if any, should be kept proportionate to avoid undue administrative burden.

The provisions on implementing acts should be deleted.

Market opening for domestic passenger transport - commercial services

Given the close link between market opening for commercial services and for services provided under public service obligations, there should be appropriate safeguards designed to preserve, on the one hand, the economic equilibrium of public service contracts, and on the other, commercial open access services. Further work needs to be carried out on these safeguards.

Appropriate safeguards should be put in place to avoid 'cherry picking'. In establishing the scope of public service contracts, it should be possible for Member States to bundle profitable and unprofitable lines.

Regulatory Bodies

Member States agreed on the importance of the role played by Regulatory Bodies under Directive 2012/34/EU, in order to guarantee a 'level playing field'. However, some Member States questioned the need to further strengthen such a role.

Common information and integrated ticketing schemes

The establishment of such schemes should remain voluntary.

Transposition and entry into force of the market access provisions

There should be a longer transposition deadline to take into account the length of national legislative procedures in Member States. There should be a gradual approach as regards the entry into force of the market opening provisions.

b) Regulation (EC) No 1370/2007

Competitive award and direct award of public service contracts in rail

Addressing some concerns of Member States, the Presidency would like to remind that the current legislation provides significant procedural leeway for competent authorities to organise a competitive award in the most appropriate manner for each Member State (for instance, through a call of manifestation of interest and a consecutive negotiation procedure suitable in case of small market volumes, of particularly complex contracts or in case of technical or physical isolation of the rail network) while respecting general Treaty principles such as transparency and non-discrimination.

However, some Member States remain concerned that the costs of the reforms proposed to create the conditions for market opening and competitive award of public service contracts may outweigh the benefits in certain markets, even using more limited tendering procedures.

Exceptions to the principle of competitive award of public service contracts in rail

In case the principle of competitive awards is accepted, Member States agreed that the following exceptions could form a starting point for future discussions:

- in case of an internal operator controlled by a local competent authority - the definition of "local" competent authority as proposed by the Commission should be either extended to better reflect particularities of national markets and administrative structures in Member States or deleted to maintain the definition in force at the moment;
- in case of small scale contracts - it is proposed to increase the *de minimis* threshold proposed by the Commission to adequately balance the expected benefits of competitive tendering with the cost of organising tender procedures;
- in emergency situations - it is proposed to adapt the scope of emergency situations to cover situations where competent authorities have to reschedule launch dates of competitive tender procedures in view of obtaining higher response rates from bidders.

It could be assessed whether the definition of other exceptions to the rule, for instance to address issues related to certain parts of Member States' networks which exhibit particular characteristics would be required under the condition that they are well-defined and justified. Certain Member States wish to further analyse the possibility of exceptions linked to the efficiency and quality of rail services measured through performance indicators.

Definition of PSO and their scope & public transport plans

As regards transport plans, Member States wish to rely as much as possible on existing public policy documents and to keep the scope of application and the level of detail proportionate to avoid any undue administrative burdens. Moreover, a reflection should be promoted on the nature of the transport plans and of the link between the objectives established in such public policy documents and the scope of public service obligations laid down in the contracts to avoid the risk of litigation. It should also be investigated whether ex-ante control of the codified procedure to define public service obligations and their scope could be envisaged and accepted by the Member States.

Maximum size of public service contracts

Concerning the provision on the maximum size of a public service contract in rail sector, the Presidency proposes to reflect on whether it could be left to competent authorities to determine the economically optimal volume of contracts, in view of achieving the objectives of transport policy in a cost-effective manner.

Non-discriminatory access to rail rolling stock

Member States agree on the importance of non-discriminatory access to rail rolling stock. However, delegations indicated that Member States and their competent authorities should have the possibility to choose the appropriate measure to ensure non-discriminatory access to rolling stock from among a 'toolbox' of equal options compatible with EU state aid rules.

Member States and competent authorities would thus be free to choose a cost-effective approach which keeps budgetary impacts to a minimum. Some Member States are concerned about the potential budgetary / financial impacts of ensuring access to rolling stock and argued in favour of a voluntary non-binding approach.

The text of an amended Regulation should be sufficiently precise so that an implementing act would not be required.

Transitional arrangements

The Presidency suggests not modifying the transitional arrangements for non-rail modes. For rail, there should be more flexibility as to the date of introduction of the principle of competitive award of public service contracts compared to the Commission proposal (as from 3 December 2019) and existing contracts should be able to continue until their expiry. The arrangements concerning the maximum duration of contracts that will have been directly awarded during the transition period should be set in a manner to ensure legal certainty and to avoid costly re-negotiation of contracts. There were calls for a gradual market opening at national level during the transitional period. A request has also been made to discuss the introduction of possible additional measures.