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## VDV comments on the Commission's draft guidelines for Regulation 1370/2007

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### I. Preliminary remarks

The German Transport Association (VDV) welcomes the fact that the interpretative guidelines for Regulation (EC) No. 1370/2007 (2014/C 92/01) are to be updated and adapted to Regulation (EU) 2016/2338.

However, the Commission's draft ("non-paper") of December 2, 2021, leads to serious disadvantages for public transport in Germany and Europe. It also contradicts the goals of the European Commission for climate protection, see below section II. (re. 2.2.3.)

One gets the impression that the Commission wants to leave the path of controlled competition, which is clearly favored by the regulation, in favor of a system of maximum deregulation, in which the awarding of transport contracts only represents the exception, see also section II. (re. 2.2.3.)

It is also irritating that the Commission intends to apply the rules on overcompensation (reasonable profit, etc.) to all tendered contracts. In doing so, it contradicts its own fundamental position, namely that the price that came about in a competitive tender represents the market price, see section III. (re. 2.5.3 and 2.5.4.)

Large parts of the draft apparently refer to rail transport, which is however not explicitly stated. There is no clear differentiation in the text as to which legal or factual statements relate to rail transport, public passenger transport by road or both. A differentiation between local and long-distance traffic is at most implicitly recognizable.

Several references in the text – referring to the Member States on the one hand, and the competent authorities on the other hand – are not comprehensible and lead to a lack of clarity as to which tasks are to be assigned to the national level and which to the local/regional level.

We therefore see a fundamental need for revision of the text presented. In addition, we have some suggestions to complement the text. In section III. the individual points are presented in the order in which they appear in the draft guidelines.

### II. PT and services of general interest in the internal market (re. 2.2.3)

#### On 2.2.3 (Art. 2 point (e) and Art. 2a) Definition of the nature and extent of public service obligations and of the scope of public service contracts

The guidelines first refer – quite correctly – to Article 1 of Protocol No. 26 to the TFEU, in which the broad discretion of the Member States in defining services of general economic interest was confirmed.

However, the guidelines go on to say: "The member state's wide discretion to establish public transport services is therefore subject to the demonstration of a demand for those services." This effectively reduces the wide discretion to the requirements of the guidelines.

The Commission bases its arguments primarily on the judgments in SNCM and Analir. Both judgments deal with sea ferries, in the first case from various French mainland ports to Corsica, in the second case it is about a Spanish law on shipping connections between the Spanish mainland and all Spanish islands. It is obvious that in this constellation the question of whether public service obligations are necessary or whether there is a market failure cannot be answered as a matter of course.

### **The Commission's statements omit the special features of local public transport by rail and road.**

This applies in particular to the question of a **demand**: The text says on top of page 9 that the Member States "must demonstrate the existence of a real demand". However, an important element of transport policy is to first create a bus and train service in order to convince the population to switch from cars. This means that the public sector must first take the risk of whether an offer will actually be accepted. The supply creates a demand. According to the Commission, this approach would be prohibited - this counteracts the Commission's own goals in the area of climate protection and is diametrically opposed to the "Fit for 55" package and the Urban Mobility Framework that has just been presented.

In addition, no operator would be willing to provide a service on such grounds: If a public authority (responsible for transport) initiates an very optimistic expansion of the transport service beyond the actual demand, then according to the guidelines this would be a violation of state aid law. Consequently, any awarded transport contract would also be illegal. According to the Commission's explanations on page 10, this would mean that all the compensation payments represent illegal aid which the operator has to return.

### **Subsection "Consistency with the objectives of Member States' public transport policy"**

The wording in this section of the guidelines gives the impression that the "public transport policy documents" referred to in Art. 2a must be drawn up at Member State level. This corresponds neither to the wording nor to the spirit of Art. 2a. The wording "public transport policy documents in the Member States" is used in the text of the regulation. It should therefore be made clear that the strategy papers can also be drawn up at regional or local level.

### **Subsection „Analysis of the market failure“ (page 9)**

In our opinion, this subsection does not sufficiently take into account the Andersen judgment of the ECJ (Judgment of the General Court, 18 January 2017, T-92/11 RENV), according to which no market failure has to be examined. Even if one wanted to affirm the Commission's view, the procedure envisaged by the Commission would be harmful for public transport, because a procedure for each individual line/route ("for each route") completely ignores the network idea and opens the door to cherry picking.

### **Subsection „Selection of the least harmful approach to the functioning of the internal market.“ (pages 9/10)**

Article 3(1) of Regulation 1370/2007 defines the public service contract as a standard instrument to be used by the public authority. As an exception, article 3(2) provides for the enactment of general rules. In contrast, the present subsection of the draft guidelines presents the public service contract as being generally harmful to the internal market and promotes the general rule as an alternative that is supposedly less harmful. The paragraph should therefore be modified, and the last sentence be deleted.

### **Subsection „Possibility to group cost-covering and non-cost-covering services in the public service contract“ (page 10)**

The Commission's statements on the combination of cost-covering and non-cost-covering services impose restrictions that are not contained in Regulation 1370/2007. The regulation does not contain any requirement as to whether cost-covering and non-cost-covering services are combined primarily for traffic or financial reasons.

In most cases, the formation of networks will be unproblematic and not controversial. But there will be borderline cases. The main problem here is that from the bidder's point of view it is not clear in the run-up to a competition whether the authority is acting here for predominantly financial or traffic-related reasons.

If a transport authority awards a transport contract in which the condition set by the Commission is not met, according to the Commission, this would constitute an illegal state aid and would lead to operators having to return all compensation payments, even if they were awarded the transport contract in a correct competitive award procedure.

As a result, in future cases, operators will only apply for transport contracts if they are certain that this requirement has been met. This leads to a restriction of the market and thus to the opposite of what the regulation wants.

In the introduction to 2.2.3, the Commission writes that the specifications of the public service obligation are only to be called into question in the event of a "manifest error". But the explanations that follow and the interpretation of Art. 2a give the impression that such a manifest error **always** exists when the above-mentioned requirements are not met.

Overall, the Commission also ignores the history of Art. 2a. This article has been significantly toned down compared to the original Commission draft (proposal of January 30, 2013, COM[2013] 28 final, 2013/0028 [COD]). This means that, according to the co-legislator, no detailed substantive specifications should be made as to how the Member States / the competent authorities must define the scope and specifications of the public service obligations (i.e. the public service contract to be awarded). With regard to the procedure, Art. 2a points only to the strategy papers in the Member States and stipulates that relevant interest groups must be consulted for this purpose. The TFEU, in particular the principle of proportionality, remains the substantive benchmark.

### **III. Further comments in the order of appearing in the draft guidelines**

#### **About 2.1.5 Art. 1(2) Multimodal public service obligations**

The regulation applies to passenger transport by rail and "road". Under point 2.1, the draft only mentions buses (buses and coaches), apart from the various rail services. However, the regulation does not contain any limitation to buses. Car transport can also fall under the regulation.

Public passenger transport is defined in Art. 2 letter a) of Regulation 1370/2007 as "passenger transport services of general economic interest provided to the public on a non-discriminatory and continuous basis."

In VDV's opinion, the guidelines should clarify that this does not only mean traffic according to a fixed timetable and on a fixed route.

It should also include certain transport services that are carried out „on demand“. The regulation stipulates that the transport services must firstly be of general economic interest, secondly for the general public, thirdly non-discriminatory and fourthly must be provided continuously.

These requirements can also be met in the case of a transport service that operates „on demand“. Regulation 1370/2007 does not consider a fixed route as a requirement. On-demand transport services are also provided for the general public if the order for a vehicle/transport service can be triggered by all citizens and these orders must be accepted within a fixed time and space frame. The aspect of the obligation to serve the common good is also expressed by the fact that tariffs are fixed and integrated into the general public transport tariff that applies in the respective area.

The transport services are subject to public service obligations (obligation to operate, obligation to transport, obligation to respect tariffs). Within the specified service area and service hours, passengers are transported at fixed prices. In doing so, they replace or complement the classic regular (bus) service.

This on-demand transport must be distinguished from occasional transport, which is provided outside of Regulation 1370/2007. If there is no obligation to operate and transport, and fares are set at the companies' full discretion, the requirements of Art. 2 letter a) are not met.

VDV would welcome a clarification that on-demand transport – if the above-mentioned requirements are met – also falls under Regulation 1370/2007. If the Commission considers this to go too far, we would welcome a clarification that such transport can at least be part of a public service contract.

#### **About 2.2.5 Art. 4 and 8 – Duration of public service contracts (...)**

In this paragraph, the Commission is concerned with the "mobilisation phase" between the conclusion of the contract and the start of operation and notes that the maximum duration of the contract can only be calculated from the start of operation. From our point of view, these statements are generally correct, but the way they are formulated could lead to misunderstandings in one point. The Commission should add a clarification that, in the context of a public service contract, payments from the competent authority to the transport company are allowed even before the start of operations, for example for the procurement of vehicles.

#### **About 2.2.6 – here: Art. 5(2) (e) – Conditions of subcontracting**

According to Art. 5 Para. 2 letter e) of Regulation 1370/2007, the internal operator is obliged to provide "the major part" of the public passenger transport service itself. The draft guidelines state in 2.2.6: "Without prejudice to a case-by-case analysis, it would seem reasonable to consider that subcontracting more than one third of the public transport services would require a strong justification, in particular in view of the objectives of Article 5(2)(e)." This wording in the guidelines gives the impression that subcontracting of more than 33% requires a special justification. VDV's understanding of the regulation is that it sets the limit at 49.9%. This should not be restricted by the guidelines. Subcontracting is a very good way of giving smaller companies, which could never take part in tenders for entire city networks, a chance to become active in the competition.

#### **About 2.4.1. iii) (Prohibition for an internal operator to participate in tender procedures elsewhere)**

Paragraph 2.4.1. iii) specifies the non-competition clause for internal operators. While VDV generally agrees with this approach, we need to point out however that one special feature is not taken into account: the so-called rail replacement service (Schienenersatzverkehr). In cases of disruption to operations due to accidents or natural disasters, as well as in the case of construction work, it is often necessary to set up a bus service to replace a rail or tram connection, sometimes at very short notice. It should be made clear here that the internal operator may provide rail replacement services outside of its area. The commissioning of such services by neighbouring competent authorities or other transport companies does not negatively affect the internal market, but rather serves to manage exceptional situations most economically.

#### **About 2.4.1. (iv) (Result from the non-respect of Art. 5 (2))**

The Commission is of the opinion that the illegal participation of an internal operator in a tender should result in the ineffectiveness of the (previously made) direct award to the internal operator and refers to the opinion of the Advocate General in proceedings C-350/17 and C-351/17 (*Mobit*). The ECJ did not take up these statements by the Advocate General.

In our opinion, the only consequence of an inadmissible tender participation of an internal operator is that he is to be excluded from the relevant tender. The original effectively attributed direct award remains unaffected. The draft should be modified accordingly.

#### **About 2.4.7. – Emergency awards**

In addition to the existing text of the draft guidelines, we ask for an addition about emergency awards for the following reasons:

Besides the direct award, article 5(5) also mentions the "requirement" to provide certain public service obligations ("Auflage"). We suggest that the guidelines should include a clarification on the concept of imposed public service obligations in art. 5(5) sentence 2 of Regulation 1370/2007.

From our point of view, it should be clarified that, in the case of imposed public service obligations ("requirement"), it is not necessary to check whether the legal relationship between the competent authority and the operator who is obliged to provide transport services as an emergency measure fulfils the public procurement law / economic requirements for a service concession.

For buses and trams, art. 5(1) of Regulation 1370/2007 contains in general the division into public procurement contracts on the one hand, for which the general public procurement law (Directive 2014/24/EU) applies, and service concessions on the other hand, for which e.g. art. 5 paragraph 3 of reg. 1370/2007 applies. In the case of service concessions, the operator must bear a risk that is sufficient from the point of view of public procurement law: "The part of the risk transferred to the concessionaire shall involve real exposure to the vagaries of the market, such that any potential estimated loss incurred by the concessionaire shall not be merely nominal or negligible". (Extract from Article 5 No. 1 of Directive 2014/23/EU)

In the case of an emergency measure that the state imposes on a company and which thus represents state intervention, the additional risk of whether e.g. sufficient tickets are sold, cannot be passed on to the company. If Article 5 para. 5 of Regulation 1370/2007 was only applicable for bus transport if the economic risk reached the extent of a service concession even in case of imposed public service obligations, then this instrument would be meaningless in practice.

We therefore ask for clarification that the emergency measure as a restrictive form of the establishment of a public service contract is also possible if the public service contract is not a service concession as defined in the procurement directives.

#### **About 2.5.3 and 2.5.4 – here: Application of the Annex to competitive transport contracts**

In the above sections, the Commission states several times that even if a public service contract has been awarded in competition, an ex-post overcompensation control must be carried out, which must also include a review with regard to reasonable profit.

In doing so, the Commission contradicts its own fundamental premise that a price arrived at through fair competition is per se appropriate. The purpose of the tendering competition is precisely that an appropriate market price is determined.

The guidelines should make this clear. If all the transport services specified in a tendered public service contract have been provided, the question of overcompensation or reasonable profit does not arise.

#### **About 2.5.5. Preventing the cross-subsidisation of commercial activities**

The guidelines say in points 2.5.1. and 2.5.5. that in cases where an operator has several public service contracts, accounting and overcompensation control must be carried out separately for each public service contract. We explicitly welcome the aim pursued by the Commission of avoiding the use of compensation for commercial activities. However, there are cases where a company has two public service contracts with one Competent Authority, or a public service contract from one Competent Authority and the general rule from another Competent Authority, which address the same public passenger transport services. The same applies to public service contracts from several competent authorities that are aimed at either overarching or directly interrelated public passenger transport services.

From our point of view, it would be sufficient if, for such public service contracts or general rules that relate to the same or interrelated public passenger transport services, there was also a uniform overcompensation control, especially for cases in which the "reasonable profit" is defined uniformly due to the connection between the transport services concerned.

#### **About 2.5.8 – Requirement to pay operators 'appropriate' compensation for public service obligations**

Article 2a, paragraph 2, letter b of Regulation 1370/2007 and point 7 of the Annex stipulate that transport services should be appropriately and sustainably financed in order to provide high-quality passenger transport services. The comments in section 2.5.8 of the guidelines are therefore highly welcomed. However, they must be supplemented with a clarification to the effect that the regulation itself does not result in a legal right to compensation payments. Regulation 1370/2007 is part of state aid law. This generally only deals with the question of whether companies are overcompensated and therefore cannot establish any legal claims to receive state resources.