



COMMISSION OF THE EUROPEAN COMMUNITIES

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Proposal for a

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on public passenger transport services by rail and by road

EXPLANATORY MEMORANDUM

Introduction

Since the second half of the 20th century, inland public carriers of passengers and freight, particularly the railways, have had to maintain services which are not commercially viable and have had their tariff policies strictly controlled.

In the 1960s, rail began a sharp decline in the face of competition from the motor car. In France, for example, use of regional rail services fell from 6.4 to 5.2 billion passenger kilometres between 1964 and 1969. At the time, the State paid practically no subsidies to SNCF; ten years later, subsidies relating to public service obligations (PSO) were around 2 billion francs. Inland public transport services have become structurally loss-making everywhere in Europe. Carriers in the sector have therefore had to ask States to either abolish these obligations or to compensate for the costs on a more systematic basis.

This question was one of the first to be tackled under the common transport policy. The main aim was to establish whether the benefits, particularly financial, granted by the authorities constituted fair compensation for the public service obligations imposed on operators or whether such compensation amounted to State aid. It had therefore become essential to establish detailed Community methods to calculate compensation in order to avoid the strict application of State aid procedures. In the absence of such a framework, the European Commission would have had to examine each of these compensation mechanisms, with the significant complication of procedures and risk of paralysis of the system that that would entail.

After an initial Council decision in 1965,¹ a Regulation was adopted in 1969 which still constitutes the Community framework applicable to inland public passenger transport services.²

This Regulation, which covers the transport of passengers and freight by rail, road and inland waterway, allows Member States to impose public service obligations aimed at guaranteeing the provision of services in accordance with certain conditions on tariffs, continuity, regularity or capacity, with States providing compensation for the costs incurred by the operator. It sets out the procedures to be followed before such compensation is paid and lays down detailed methods of calculation ensuring that the amount is appropriate. Compensation granted in accordance with these rules is not subject to the prior notification and authorisation obligation under Article 88(3) of the Treaty.

This legislative framework was last amended in 1991 in order, among other things, to extend it to local transport services.

1 Decision 65/271/EEC of 13 May 1965 on the harmonisation of certain provisions affecting competition in transport by rail, road and inland waterway.

2 Regulation (EEC) No 1191/69 of the Council of 26 June 1969 on action by Member States concerning the obligations inherent in the concept of a public service in transport by rail, road and inland waterway (OJ L 156, 28.6.1969, p. 1), as last amended by Regulation (EEC) No 1893/91 (OJ L 169, 29.6.1991, p. 1).

Until recently, it constituted a satisfactory framework in a public transport sector where the service providers were exclusively national, regional or local. Today it is inadequate and its implementation by the parties concerned is particularly problematical in a constantly evolving market. Derogations are the rule, particularly in local public transport,³ where derogations to the contractualisation obligation are scarcely compatible with the transparency and non-discrimination required by an increasingly open market. Moreover, the Regulation also fails to specify the procedures for the award of public service contracts. It has become a source of legal uncertainty which is already reflected in an increase in disputes and the reluctance of operators to commit major investments while the rules of the game are not clearly defined.

In 2004, inland public passenger transport services (train, underground railway, tram and urban bus) represented around 150 million passengers transported every day, 1.5 million jobs and an annual turnover estimated at €100 billion (EU-15 figures). In the last ten years or so, this sector has undergone profound changes with the emergence of operators providing services in more than one Member State and public authorities determined to compare different transport service offers.

Even though competition began to revive passenger transport, the latter's market share has continued to decline in the face of competition from the private car. Thus, between 1970 and 2001 the share accounted for by cars rose from 73.8% to 78.2% while inland public transport fell from 24.7% to 16%.⁴ This situation has highlighted the need to modernise public transport and increase its efficiency in order to maintain or even increase its market share and involve it in improvements to the environment and mobility.

Given the unsuitability of the Community legislative framework together with the clear need to improve the efficiency and quality of services, the Commission presented, in July 2000, a proposal for a Regulation of the European Parliament and of the Council on action by Member States concerning public service requirements and the award of public service contracts in passenger transport by rail, road and inland waterway.⁵ This proposal was aimed specifically at resolving the legal uncertainty affecting the sector and establishing a competitive regime which would lead to more efficient and attractive services for passengers. To this end, it was based on a number of principles:

- contractual arrangements between the competent authority and the operator or operators responsible for providing services where financial compensation or exclusive rights are granted;
- need for a periodic review of contract terms, so limits on its duration;
- competitive tendering for public service contracts, except in certain cases where direct award is possible (e.g. under certain conditions for railways or underground railways, or below a certain financial threshold).

After five years, this proposal is still blocked in the Council. It has not been possible to reach a compromise with a view to a common position, as the Member States are very divided on

3 Article 1(1) and (5) for urban, suburban or regional services.

4 Sources: EU energy and transport in figures, 2003.

5 COM(2000) 7 final – 2000/0212 (COD), amended by COM(2002) 107 final.

the actual extent to which inland transport should be opened up to competition given, among other things, their different experiences in this area.

Moreover, work in the Council was suspended for a long time pending the judgment of the Court in the Altmark case. Delivered in July 2003, it put an end to the legal debate on what qualifies as State aid by clearly defining the concept of financial benefit which is the essential criterion. Its impact is however limited for inland transport owing to the existence of specific rules established by Regulation (EEC) No 1191/69.

Having regard to the numerous amendments adopted by the European Parliament at first reading in 2001 and the blocking of the proposal in the Council (cf. chapter 4), the Commission is now seeking to reconcile the various positions adopted by revising its proposal in the light of in particular the latest developments in case law (Altmark judgment) and its recent White Paper on services of general interest.

The question of how to regulate compensation for public service obligations is not restricted to transport. It arises in many other sectors and accordingly constitutes one of the main elements of a broad horizontal debate in the Commission on the subject of services of general interest.

1. SERVICES OF GENERAL INTEREST

The term “services of general interest” cannot be found in the Treaty itself. It is derived in Community practice from the term “services of general economic interest”, which *is* used in the Treaty.⁶ It has a broader meaning, covering both market and non-market services which the public authorities class as being of general interest and subject to specific public service obligations.

The term “services of general economic interest” is not however defined in the Treaty or in secondary legislation. In Community practice there is broad agreement that it refers to services of an economic nature which the Member States or the Community subject to specific public service obligations by virtue of a general interest criterion.

The Commission White Paper on services of general interest published on 12 May 2004⁷ drew conclusions from the current public debate and launched discussions on how to guarantee services of general interest effectively within the internal market on the basis of a set of general principles incorporated in Community policies.

It underlines that, as regards services of general interest, responsibility is shared between the Union and the Member States.

It points out that it is for the “relevant national, regional and local authorities to define, organise, finance and monitor services of general interest”.

In point 4.3, the Commission further states:

6 Article 86(2).

7 COM(2004) 374 final.

“In principle, Member States have a wide margin to decide how to organise services of general interest. In the absence of Community harmonisation, the relevant public authorities ... are in principle free to decide whether to provide a service of general interest themselves or whether to entrust its provision to another ... entity. However, providers of services of general economic interest, including in-house service providers, are undertakings and therefore subject to the competition rules of the Treaty.”

The White Paper also underlines that sector-specific regulations should concentrate on “network industries such as telecommunications, postal services, transport and energy, which have a clear trans-European dimension”. Transport forms an essential sector in this analysis since the Community sectoral rules comprise a highly developed framework for regulating the provision of transport services to all citizens.

In its report,⁸ the European Parliament calls for the establishment, by way of the co-decision procedure with the Council, of a legal framework which sets out common principles for services of general interest in Community law.

The draft Constitutional Treaty, too, provides a legal basis for the adoption of laws establishing the principles and conditions, in particular economic and financial conditions, which enable services of general economic interest to fulfil their missions (Article III-122).

This revised proposal for a Regulation adopts a sectoral approach corresponding to the general line adopted by the Commission in this White Paper.

2. PUBLIC SERVICE OBLIGATIONS IN THE TRANSPORT SECTOR

2.1 *Acquis communautaire*

In the transport sector, Community rules allow Member States to introduce public service obligations, i.e. “obligations which the transport undertaking in question, if it were considering its own commercial interests, would not assume or would not assume to the same extent or under the same conditions”.⁹

In air¹⁰ or maritime¹¹ transport, Community legislation requires competitive tendering for public service contracts.

In inland transport, it is restricted to imposing strict methods of calculation for the amount of public service compensation pursuant to Article 73 of the Treaty.

This Article is implemented by two texts: Regulation (EEC) No 1107/70 on aid¹² and Regulation (EEC) No 1191/69 on public services.

8 European Parliament resolution on the Green Paper of 14 January 2004 (T5-0018/2004 of 14.1.2004) (Herzog Report).

9 For example, Article 2(1) of Regulation (EEC) No 1191/69.

10 Council Regulation (EEC) No 2408/92 of 23 July 1992 on access for Community air carriers to intra-Community air routes (OJ L 240, 24.08.1992, p. 1).

11 Council Regulation (EEC) No 3577/92 of 7 December 1992 applying the principle of freedom to provide services to maritime transport within the Member States (maritime cabotage) (JO L 364, 12.12.1992, p. 7).

Regulation 1191/69 establishes the general framework applicable to public service obligations in inland transport and lays down methods for calculating the corresponding compensation. It allows Member States to impose or maintain specific public service obligations,¹³ which they are however required to compensate if they entail costs for operators,¹⁴ and fixes detailed methods of calculation to guarantee fair compensation.¹⁵ The compensation granted in accordance with these methods is exempt from the obligation of notification to the Commission without prior verification of their possible State aid characteristics. The said Regulation did not apply to carriers operating mainly local or regional services.¹⁶

In 1991, the amending Regulation 1893/91 extended the scope to cover urban, suburban and regional operators, but allows Member States to derogate from this provision.¹⁷ It lays down that as a general rule the imposition of public service obligations should be replaced by the award of public service contracts,¹⁸ though the competent authorities may nevertheless continue to impose obligations for urban, suburban and regional services and in the matter of tariffs in favour of specific social categories.¹⁹ However, the amended Regulation of 1991 does not state how public service contracts should be awarded or, in particular, whether they should be the subject of competitive tendering.

Until recently, the EU had scarcely concerned itself with the method of awarding public service contracts in this sector given the absence of international competition. There was no reason to examine either the arrangements for awarding these tens of thousands of local contracts or the compensation granted to operators. The situation changed when certain public transport operators responded to invitations to tender in other Member States and brought complaints before national courts or the Commission²⁰ when they did not obtain those contracts. Some of these actions have been successfully referred to the Court of Justice.²¹

Rather than reacting on a case-by-case basis to these complaints, the Commission – the guardian of the Treaties – reaffirms the need to adopt regulations whose fundamental objective is a simple one: regulate competition, including for regions and towns, in order to ensure transparency in the way in which public service contracts are awarded and executed. The introduction of such regulations would remove the suspicion of State aid surrounding compensation granted without competitive tendering.

12 Regulation (EEC) No 1107/70 of 4 June 1970 on the granting of aids for transport by rail, road and inland waterway.

13 The obligation to operate, the obligation to carry and tariff obligations – Article 2 of the Regulation.

14 Article 6(2) of Regulation (EEC) No 1191/69.

15 Articles 3-13 of Regulation (EEC) No 1191/69.

16 Article 19(2) of Regulation (EEC) No 1191/69 (original text from 1969).

17 Article 1(1) of Regulation (EEC) No 1191/69.

18 Article 1(4) of Regulation (EEC) No 1191/69.

19 Article 1(5) and (6) of Regulation (EEC) No 1191/69.

20 Infringement 2003/5033 (DE) – public contracts for local and regional transport services – Letter of formal notice of 13 October 2004.

21 Judgment of the Court of First Instance of 16 March 2004 in Case T-157/01 *Danske Busvognmænd v Commission* “Combus” and judgment of 24 July 2003 in Case C-280/00 *Altmark Trans GmbH and Regierungspräsidium Magdeburg v Nahverkehrsgesellschaft Altmark GmbH*.

2.2 Opening up the market

Since 1969, the economic environment for inland public passenger transport services has changed a great deal. The markets of certain Member States have begun to open up to competition, whether in urban transport or the railways.

The United Kingdom began this trend in 1986 by eliminating the exclusive rights which were the rule in the bus transport sector. With the exception of London and Northern Ireland, any operator may provide whatever services it wishes. Operating costs have fallen sharply, but so have passenger numbers.

This attempt at deregulation has not been repeated within the Union. Those Member States which have opened up their markets have instead developed the so-called “regulated competition” system in which a competent authority grants an exclusive right for a specific period following an open and transparent invitation to tender which can set the service level, quality standards and/or tariffs.

This system functions fairly well and has produced good results in urban areas (Stockholm, Helsinki, Copenhagen, London, Lille, etc.), for regional railway services (Lisbon, Northern Netherlands, German Länder) and for long-distance services (buses in Spain, railways in Sweden). Usually, regulated competition goes with increased passenger numbers and a reduction in costs.²² In 2003, around 25% of the inland public transport market in the EU was opened to competition in this way.

This opening up has led to the de facto emergence of an international market for the provision of public transport services. Initially, certain private groups such as Connex (F), Arriva (UK) and Concordia (N) were the most active in seeking contracts outside their countries of origin. A number of these operators now achieve more than 50% of their turnover in countries other than their own. Public sector groups, such as DB (D), NS (NL) and RATP (F) have since joined them. The traditional national operators have benefited from this development by intervening in the operation or by acquiring participation in new markets, either in their own countries (e.g. RATP, the urban transport operator in Paris, in Mulhouse and Clermont-Ferrand) or in other countries (such as NS, the national railway operator in the Netherlands, which has won the contract for urban railway transport in Liverpool).

3. THE COMMISSION PROPOSAL OF 2000, AMENDED IN 2002

The development of an increasingly competitive market for the inland public transport sector requires a regulatory framework for public service obligations which is transparent and which can prevent compensation from being classed as State aid.

On 26 July 2000, the Commission proposed a Regulation based on the principles of contractual relations between the authority and the operator and competitive tendering for public service contracts to make their award transparent and non-discriminatory. This proposal initially provided for a number of exceptions in which the public authority could,

²² See Report on public transport contracting, Colin Buchanan & partners, 2002, chapter 2 (http://www.europa.eu.int/comm/energy/en/fa_2_en.html).

under certain conditions, decide to award public service contracts directly without an invitation to tender:

- in the railway sector, for safety reasons;
- in the underground or light transit railway sector, for cost or safety reasons;
- in the field of integrated services, i.e. involving several transport modes, for example metro and bus services as is the case for the STIB contract in Brussels or that of RATP in Paris, for cost or safety reasons;
- where the annual value was estimated at less than €800 000.

In November 2001, the European Parliament adopted a position at first reading which, while welcoming the proposal, contained more than 100 amendments. The most significant of these is amendment 61, the effect of which is to protect local²³ public transport services from competition if the competent authority decides to provide the service itself on an exclusive basis. This position was determined by compliance with a reciprocity clause which the Commission accepted in its amended version of 2002 by including it for the transitional period.

Other amendments aimed to modify the list of exceptions (removal of exception concerning integrated services, expansion of base in other cases) or extend contract duration (as contracts which are too short could cause problems concerning continuity of provision of services, investments and personnel) and the transitional period.

On the basis of this position, the Commission adopted an amended proposal in February 2002 incorporating only some of these amendments:

- extension of the duration of contracts (8 years for buses, 15 for rail transport);
- extension of the transitional period (8 years);
- modification of the list of exceptions to the competitive tendering obligation, and in particular increase (from 800 000 to 3 million euros) of the threshold below which direct award is possible and removal of the exception for integrated services. The mechanisms introduced in connection with amendment 61 were not however adopted.

As stated above, the discussions in the Council quickly showed that a sufficient majority was unlikely to emerge and that there was no real political will to see the proposal succeed. Given the vast differences between their respective attempts at opening up the market, the Member States soon expressed disagreement as to the actual extent of opening up inland transport. Moreover, on the pretext of awaiting the judgment of the Court in the Altmark case, the Council suspended its work at the end of the Spanish Presidency (first half of 2002) and has not resumed it since. The Member States had profound differences on the key elements of the proposal:

23 The concept of local was defined as follows: “where the transport service does not exceed a maximum catchment area of 50 km”.

- certain States engaged at various stages in opening-up all or part of their inland public transport sectors were generally in favour of the proposal, although some regretted that it did not go far enough and left too many possibilities for the direct award of public service contracts;
- other States, especially some of those where there are still major public monopolies in the sector, were against the proposal and for the status quo;
- Member States were also divided on the scope of the Regulation and on the modes of transport that it should cover (only buses or all urban modes including trams and undergrounds? Should it apply to railways or not?).

4. THE ALTMARK JUDGMENT

Following recent developments in case law,²⁴ the question of whether compensation for public services in the various sectors of the economy constitutes State aid within the meaning of Article 87(1) of the Treaty has attracted a great deal of attention in recent years. The recent judgment of the Court of Justice in the *Altmark Trans GmbH* case²⁵ has undeniably made a fundamental contribution to the debate. Moreover, the Commission reacted quickly by proposing, as early as February 2004, a set of measures clarifying the consequences of the judgment. This legislative “package” was adopted in July 2005; it applies to all sectors of the economy except inland transport, which has its own legal basis on which this Regulation is based.

Facts of the case

The case concerns a dispute between two small public transport operators in the Stendal region in Germany. In 1994, one of them was granted licences to operate certain bus routes without a tendering procedure. The other, considering itself disadvantaged, contested the award and complained about the compensation that its competitor had received from the public authorities.

As German law permits the granting of certain types of compensation only on the basis of an invitation to tender, the national court had to rule whether the compensation in question fell into this category. To do this, it had to determine whether the public authorities could pay it without taking account of the Community rules on State aid. To this end, in 2000 it referred the matter to the Court for a preliminary ruling on the interpretation of Articles 73 and 87 of the Treaty and Regulation 1191/69.

In its judgment, delivered in July 2003, the Court clarifies how the provisions of the Treaty on State aid apply to public services in general and public transport in particular. Contrary to

24 Judgment of 27 February 1997 *FFSA* T-106/95 (ECR 1997 II-0229) and judgment of 10 May 2000 *SIC* T-46/97 (ECR 2000 II-2125). Judgment of 22 November 2001 *Ferring* C-53/00 (ECR. I-9067). See also the Opinion presented by Advocate-General Jacobs on 30 April 2002 in Case *GEMO* (C-126/01) and confirmed by judgment of 20 November 2003.

25 Judgment of 24 July 2003 in Case C-280/00 *Altmark Trans GmbH and Regierungspräsidium Magdeburg v Nahverkehrsgesellschaft Altmark GmbH*.

certain expectations, the Altmark judgment hardly entailed any fundamental changes for the transport sector.

Consequences of the judgment in the transport sector

For the inland passenger transport sector, the legal situation resulting from the analysis of the Altmark judgment is as follows:

- The judgment confirms that, since 1995, a number of Member States have opened up their transport markets to competition from undertakings established in other Member States. Accordingly, the compensation granted to public transport operators – even small local operators – can affect trade between Member States,²⁶ and the question of whether it constitutes State aid must in principle be examined by the Commission.
- As regards the inland public transport sector in particular, the Court notes the existence of a specific set of rules for the compensation of the operators concerned: those set out in Article 73 of the Treaty and in the corresponding secondary legislation, i.e. Regulations 1191/69, 1192/69 and 1107/70.²⁷ The Altmark judgment confirms that Article 73 constitutes a *lex specialis* in relation to Article 86(2) of the Treaty since it establishes rules applicable to compensation for public services in the public transport sector. As a result, compensation contrary to the provisions of Article 73, which has been exhaustively implemented by Regulations 1107/70 and 1191/69, does not constitute State aid compatible with the Treaty on the basis of Article 86(2) or any other provision of the Treaty.
- The judgment confirms therefore that compensation for public transport services is covered by Regulation 1191/69 on public services. Member States which do not apply these rules are failing to fulfil their obligation to ensure that Community law is correctly applied. Moreover, compensation which is contrary to these provisions may be judged to be State aid and declared incompatible with the Treaty.
- Lastly, the judgment highlights the situation of Member States which have introduced the possibility of derogating from the provisions of the Regulation for the local transport sector. In this case, compensation which does not meet the “four Altmark conditions” (see below) must be classed as State aid which may be authorised by the Commission.²⁸

This legal situation poses genuine difficulties insofar as, on the one hand, Regulation 1191/69, which applies to most cases of compensation for public transport, no longer corresponds to the economic realities of the sector and, on the other, in the event of derogation from the rules for local transport it is very difficult to verify compliance with the “four Altmark criteria”

26 Altmark judgment, paragraphs 77-82.

27 Regulation (EEC) No 1191/69 of the Council of 26 June 1969 on action by Member States concerning the obligations inherent in the concept of a public service in transport by rail, road and inland waterway; Regulation (EEC) No 1192/69 of the Council of 26 June 1969 on common rules for the normalisation of the accounts of railway undertakings; Regulation (EEC) No 1107/70 of the Council of 4 June 1970 on the granting of aid for transport by rail, road and inland waterway.

28 The Commission may authorise this type of State aid only on the basis of Regulation 1107/70 (see Article 3(1)).

since the assessment of the fourth criterion is particularly unsuited to the specific characteristics of the sector.

In this sector, only the adoption of a new Regulation establishing a transparent framework for the granting of and compensation for public service obligations will make it possible to avoid legal uncertainty.

Consequences of the judgment for other sectors

As regards public services in general, apart from inland transport, the Court clarified the four conditions according to which compensation relating to a public service obligation does not constitute a financial benefit and cannot therefore be classified as State aid:

- the recipient undertaking must actually have public service obligations to discharge and the obligations must be clearly defined;
- the method of compensation must be established in advance in an objective and transparent manner;
- the compensation must not exceed the costs incurred in the discharge of public service obligations;
- in the absence of a tendering procedure, the compensation must be determined on the basis of a comparison with a “*typical undertaking, well run and adequately provided with means of transport*”.

As already stated, following this judgment the Commission adopted in February 2004 a draft decision and a draft framework for the application of Article 86 of the Treaty to compensation for public services. However, as this Article does not concern transport, which is governed specifically by Article 73, these drafts will not apply to compensation for public services in the inland transport sector.²⁷

5. THE NEW APPROACH PROPOSED BY THE COMMISSION

On the basis of the above analysis the Commission has decided to present a revised proposal which takes into account the debate on its White Paper on services of general interest, the Altmark judgment and the other legislative projects under way concerning the transport of passengers by rail. It considers that this new Regulation needs to be adopted as soon as possible.

The revised proposal aims to establish a framework regulating those interventions by the competent authorities – award of exclusive rights and compensation for public service obligations – which are most likely to affect competition and trade between the Member States.

As part of the sharing of responsibilities between the Community and the Member States, the Commission is proposing that its text be made **simpler** and more **flexible** and that greater account be taken of the **subsidiarity** principle.

The **simplification** objective is seen above all in an attempt to clarify the proposed mechanisms and in a reduction in the number of articles.

The simplification concerns in particular the mechanisms for awarding public service contracts. One consequence is the disappearance of the formulas proposed in Article 7(a) or 8 of the 2002 proposal, which allowed public service contracts to be awarded on the basis of complicated mechanisms for comparing quality without a formal invitation to tender. The new proposal now provides for only two main methods of awarding contracts: invitations to tender and direct award.

This same desire for simplification guided the drafting of the Annex on the rules applicable to compensation in the absence of an invitation to tender. This Annex aims to establish objective, transparent and realistic methods based on well established principles of Community law (no overcompensation or cross-subsidisation, separation of accounts, verification of costs, promotion of quality and efficiency).

The objective of greater **flexibility** is seen in particular in the recognition of the competent authorities' option of providing public transport services themselves, or via an internal operator, without a competitive tendering procedure. This possibility is however strictly dependent on greater transparency and the establishment of precise criteria applicable to compensation for public service obligations. It is also subject to a condition concerning the geographical jurisdiction of the activity of the competent authority or its internal operator (cf. Article 5(5)).

Recognition of this option of self-provision (government operated system) of transport services, which can apply whatever the mode concerned (bus, tram, underground, railway, integrated services, etc.), is accompanied by the reduction of the list of exceptions to the obligation to put public service contracts out to competitive tendering (removal in particular of exceptions in favour of direct award of underground or light rail transit services). The exception concerning integrated services had already been abolished in the 2002 amended proposal following the request by the European Parliament. Accordingly, only regional and long-distance rail remain exempted from the obligation.

The objective is also apparent in the flexibility proposed for the duration of contracts in Article 4(5) and (6) and in the extension of the transitional period for rail transport services. Lastly, greater recognition of the **subsidiarity** principle is seen in the approach to the definition of regional or long-distance transport and the maintenance of thresholds below which direct award is possible.

The Commission is also giving the public authorities more freedom to organise competitive tendering in detail. For example, it has not fixed the list of selection criteria that the competent authorities have to observe when awarding public service contracts. It has also decided not to lay down, for the inland public transport sector only, specific rules on subcontracting (former Article 9(1)) or abuse of dominant position (former Article 9(2)), which, as the discussions to date have revealed, would have created undue inflexibility.

Similarly, the Commission has opted in its new proposal not to intervene in the definition of an adequate standard of public transport or passenger information, which explains the disappearance of the former Articles 4 and 4b. Its aim thereby is to give greater recognition to the diversity of approaches in this area while establishing a coherent framework.

This new proposal, which reflects the Commission's desire to strengthen the principles of fairness, transparency and access to information, will guarantee legal certainty while preserving the specific characteristics of services in the general interest, an essential component of the European model.

COMMENTS ON INDIVIDUAL ARTICLES

Overview of the proposed Regulation and explanation of the amendments as compared with the amended proposal of 21 February 2002²⁹

Article 1 Object and Scope

Article 1 adopts the scope of the previous legislation. It limits the objectives of the Regulation to the establishment of a framework for those interventions by the competent authorities – award of exclusive rights and compensation for public service obligations – which are most likely to affect competition and trade between the Member States. The former Articles 4, 4a, 4b, 7a (apart from paragraph 1), 8, 9 (apart from paragraph 3), 12 (apart from paragraph 1), 14 and 18 have been removed as a result of this limitation and the need to keep to what is strictly necessary.

Article 2 Definitions

Article 2 defines key terms. Those of public service operator and public service contract are defined in such a way as to cover all legal relationships between the authorities and operators. The concepts of internal operator, competent local authority, and regional or long-distance rail transport have been defined with the aim of allowing application of the possibilities for direct award of contracts specified in Article 5.

Article 3 Public service contracts and general rules

This Article incorporates the substance of the former Article 3 on the obligation to conclude a public service contract with the chosen operator and simplifies the former Article 10 on general rules in line with the objective of limiting the framework to the strict essentials.

²⁹ COM(2002) 107 final.

Article 4 Mandatory content of public service contracts and general rules

This Article incorporates the substance of former Articles 6, 6a, 9(3) and 16 on the content and duration of contracts, taking account of recent case law (Altmark judgment) concerning the obligation to define public service obligations and the methods of calculating compensation for such obligations.

Article 5 Award of public service contracts

Paragraph 1 clarifies the link with the *acquis communautaire* on public contracts (former Article 2). Paragraph 2 acknowledges that local authorities have the option of providing public transport services themselves or of entrusting them to an internal operator over which they exercise a control similar to that which they exercise over their own departments, on condition *inter alia* that the operator confine its activity to the geographical area over which the said authorities have jurisdiction.

Paragraph 3 adopts the principle of award by invitation to tender as well as the former Article 12(1) on the principles applicable to competitive tendering procedures. It also introduces the possibility of negotiations.

Paragraphs 4 (minor contracts³⁰), 5 (emergency measures) and 6 (regional or long-distance railways) contain some of the exceptions to the competitive tendering obligation in former Articles 7(4) and (1) and 7b.

Article 6 Public service compensation

Paragraph 1 refers to the provisions of Article 4 and the annex as regards the conditions and methods of calculating compensation in the event of direct award.

Paragraph 2 lays down the competent authorities' obligations to the Commission to ensure that the Regulation is properly applied.

Article 7 Publicity

This specifies the instruments (annual report and publication in the OJ of the EU) ensuring an adequate level of transparency.

Article 8 Transition

This Article incorporates the substance of the former Article 17 in a simplified manner. Along the lines of the provisions on contract duration, it makes a distinction between the duration of the transitional period in the bus transport sector (eight years) and that in the railway sector (10 years).

It provides for a mechanism for the gradual introduction of invitations to tender and regulates the question of contracts concluded before the entry into force of the Regulation.

30 Source: International Public Transport Union (UITP).

It maintains the principle of transitional reciprocity.

Article 9 Compatibility with the Treaty

This Article incorporates the substance of the former Article 11. It lays down that only compensation for public service obligations paid in accordance with the Regulation is compatible with the common market. Moreover, it exempts such cases from the notification requirement.

Article 10 Repeal

This Article incorporates the substance of the former Article 20 and also provides for the complete repeal of Regulation 1107/70, which has become obsolete. Article 73 of the Treaty, which applies only to inland transport, provides for two possible exemptions from the rules on State aid: for aid for the coordination of (inland) transport and for compensation for public service obligations which constitutes State aid. Regulation 1107/70 introduces the procedures for exemptions relating to coordination. Over the course of time and in the light of developments in the inland transport sector, the Commission has turned away from the exemptions listed in that Regulation, using in their place the horizontal exemption instruments which implement Article 87(2) and (3) of the Treaty. The repeal of Regulation 1107/70 will remove the restrictions (Article 3(1) of the Regulation) relating to the application of the provisions of Article 73 on the coordination of inland transport.

Article 11 Follow-up

This Article provides for the Commission to monitor the implementation of the Regulation and developments in the provision of public passenger transport in Europe.

Annex: Rules applicable to compensation in the cases referred to in Article 6(1)

This annex simplifies the former annex and is limited to what is strictly necessary to define the rules applicable in the absence of an invitation to tender.

Proposal for a

REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

on public passenger transport services by rail and by road

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Articles 71 and 89 thereof,

Having regard to the proposal from the Commission,

Having regard to the opinion of the European Economic and Social Committee,

Having regard to the opinion of the Committee of the Regions,

Whereas:

- (1) Article 16 of the EC Treaty confirms the place occupied by services of general economic interest in the shared values of the Union.
- (2) Article 86(2) of the Treaty lays down that undertakings entrusted with the operation of services of general economic interest are subject to the rules contained in the Treaty, in particular to the rules on competition, insofar as the application of such rules does not obstruct the performance of the particular tasks assigned to them.
- (3) Article 73 of the Treaty constitutes *lex specialis* in relation to Article 86(2). It establishes rules applicable to the compensation of public service obligations in inland transport.
- (4) The main objectives of the common transport policy as defined in the White Paper³¹ are to guarantee safe, efficient and high-quality transport services through regulated competition guaranteeing also transparency and performance of public transport services, having regard to social, environmental and regional development factors, or to offer specific tariff conditions to certain categories of travellers and to eliminate the disparities between transport undertakings from different Member States which may give rise to substantial distortion of competition.
- (5) At the present time, many inland transport services which are required in terms of general interest cannot be operated on a commercial basis. The competent authorities of the Member States must be able to act to ensure that such services are provided. The mechanisms that they can use to ensure that public passenger transport services are

31 COM(2001) 370 final.

provided include the following: the award of exclusive rights to operators, the granting of financial compensation to operators and the definition of general rules for the operation of public transport which are applicable to all operators.

- (6) Many Member States have introduced legislation providing for the award of exclusive rights and public service contracts in at least part of their public transport market, on the basis of transparent and fair competitive award procedures. As a result, trade between Member States has developed significantly and several public transport operators are now providing services in more than one Member State. However, developments in national legislation have led to disparities in the procedures applied and have created legal uncertainty as to the rights of operators and the duties of the competent authorities. Regulation (EEC) No 1191/69 does not deal with the way public service contracts are to be awarded in Europe, and in particular the circumstances in which they should be the subject of competitive tendering. The Community legal framework ought therefore to be updated.
- (7) To be able to organise their public transport service in the manner best suited to the needs of the public, all competent authorities must be able to choose their public transport operators freely, under the conditions stipulated in this Regulation. To guarantee application of the principles of transparency, equal treatment of competing operators and proportionality, when compensation or exclusive rights are granted, it is essential that a contract between the competent authority and the chosen operator define the nature of the public service obligations and the agreed reimbursement. The form or designation of the contract may vary according to the legal systems of the Member States.
- (8) Contrary to what was laid down in Regulation (EEC) No 1191/69, the scope of which extended to public transport services by inland waterway, it is not considered advisable for this new Regulation to cover the award of public service contracts in that specific sector. The organisation of public transport services by inland waterway is therefore subject to compliance with the general principles of the Treaty.
- (9) It is irrelevant from the viewpoint of Community law whether such transport services are operated by public or private undertakings. This Regulation is based on the principle of neutrality as regards the system of property ownership referred to in Article 295 of the Treaty, on that of the freedom of Member States to define services of general interest, referred to in Article 16 of the Treaty, and on those of subsidiarity and proportionality referred to in Article 5 of the Treaty.
- (10) Some services are operated mainly for their historical interest or tourist value. As the purpose of these operations is manifestly different from the provision of public passenger transport, they need not therefore be concerned by the rules and procedures applicable to public service requirements.
- (11) The competent authorities are responsible for the organisation of the public transport network. Apart from the actual operation of the transport service, this may cover a whole range of other activities and duties that the competent authorities must be free to either carry out themselves or entrust, in whole or in part, to an operator.
- (12) Contracts of long duration can lead to the closing of the market for a longer period than is necessary, thus diminishing the benefits of competitive pressure. To minimise

distortion of competition while protecting quality of services, public service contracts should in principle be of limited duration. It is however necessary to make provision for longer contracts where the operator has to invest in assets for which the depreciation period is exceptional.

- (13) Where the conclusion of a public service contract may entail a change of operator, the competent authorities must be able to ask operators to apply the provisions of Directive 2001/23/EC of 12 March 2001 on the approximation of the laws of the Member States relating to the safeguarding of employees' rights in the event of transfer of undertakings, businesses or parts of undertakings or businesses.³²
- (14) Studies carried out and the experience of States where competition in the public transport sector has been in place for a number of years show that, with appropriate safeguards, introduction of regulated competition between Community operators leads to more attractive and innovative services at lower cost and is not likely to obstruct the performance of the specific tasks assigned to the operators. This approach is endorsed by the European Council under the so-called Lisbon Process of 28 March 2000 calling on the Commission, the Council and the Member States, each in accordance with their respective powers, to “speed up liberalisation in areas such as ... transport”.
- (15) Any local authority may choose to provide its own public passenger transport services in the area it administers or to entrust them to an internal operator without competitive tendering. However, this self-provision option needs to be strictly controlled to ensure a level playing field.
- (16) Where, on the other hand, a public authority chooses to entrust a general interest service to a third party, it must select the operator in accordance with Community law on public contracts and concessions, as established by Articles 43 to 49 of the EC Treaty, and the principles of transparency and equal treatment. In particular, the provisions of this Regulation are to be without prejudice to the obligations applicable to public authorities by virtue of the directives on the award of public contracts, where public service contracts fall within their scope.
- (17) Some invitations to tender require the competent authorities to define and describe complex systems. Authorities should therefore be empowered, when awarding such contracts, to negotiate details with some or all of the potential operators after tenders have been submitted.
- (18) Invitations to tender for the award of public service contracts should not be mandatory where the contract relates to modest amounts or distances.
- (19) Where there is a risk of disruption of the provision of services, the authorities must be empowered to introduce emergency short-term measures pending the award of a new public service contract.
- (20) Public passenger transport by rail raises specific issues of investment burden and infrastructure cost. In March 2004 the Commission presented a proposal to amend Directive 91/440/EEC so as to guarantee access for all Community railway

32 OJ L 82, 22.3.2001, p. 16.

undertakings to the infrastructure of all the Member States for the purpose of operating international passenger services.

- (21) In the case of public services, this Regulation allows each competent authority, within the context of a public service contract, to select its operator of public passenger transport services. For these reasons, and given the differences in the way Member States organise their territory in this respect, competent authorities may justifiably be allowed to award public service contracts directly for regional or long-distance railway travel. The Commission will continue to monitor developments in the provision of public passenger transport closely, especially access to rail infrastructure in Europe; it will produce a report on this subject two years after this Regulation is adopted. In addition, it will present a report on the implementation of this Regulation no later than two years after it enters into full application.
- (22) The compensation granted by Member States may in no case exceed the amounts required to cover the costs incurred in discharging each public service obligation. Where a competent authority plans to award a contract without putting it out to competitive tender, it must also respect detailed rules ensuring that the amount of compensation is appropriate and reflecting a desire for efficiency and quality of services.
- (23) With a view to the award of public service contracts, the competent authorities must take the necessary measures to advertise the fact at least one year in advance, so that potential operators are able to react.
- (24) Given that competent authorities and operators will need time to adapt to the provisions of this Regulation, provision should be made for transitional arrangements which take account of the specific characteristics of the various modes of transport.
- (25) During the transitional period, the introduction of the provisions of this Regulation by the competent authorities will probably take place at different times. It may therefore be possible, during this period, that operators from markets not yet affected by the provisions of this Regulation tender for contracts in markets that have been opened to controlled competition more rapidly. In order to avoid, by means of proportionate action, any imbalance in the opening of the public transport market, competent authorities should be able to refuse tenders from undertakings performing a majority of their activity in markets that will be opened in future but are not yet open, provided that this is applied without discrimination and decided in advance of an invitation to tender.
- (26) In its *Altmark Trans GmbH* judgment, the Court of Justice of the European Communities ruled that compensation for public service does not constitute an advantage within the meaning of Article 87 of the EC Treaty, provided that four cumulative conditions are satisfied (judgment of 24 July 2003 in Case C-280/00, paragraphs 87 to 95, ECR I-7747). Where these conditions are not satisfied and the general conditions for the application of Article 87(1) of the Treaty are met, public service compensation constitutes State aid which is subject to the provisions of Articles 73, 86, 87 and 88 of the Treaty.
- (27) Compensation for public service may prove necessary in the inland passenger transport sector so that undertakings responsible for public services operate on the

basis of principles and under conditions allowing them to carry out their tasks. Insofar as such compensation takes the form of State aid, it may be compatible with the Treaty pursuant to Article 73 under certain conditions. Firstly, it must be granted to ensure the provision of services which are indeed services of general interest within the meaning of the Treaty. Secondly, to avoid unjustified distortions of competition it may not exceed what is necessary to cover the net costs incurred through discharging the public service obligations, taking account of the revenue generated thereby and a reasonable profit.

- (28) Compensation granted by the Member States in accordance with the provisions of this Regulation may therefore be exempted from the prior notification required by Article 88(3) of the Treaty.
- (29) This Regulation replaces Regulation (EEC) No 1191/69 of the Council of 26 June 1969 on action by Member States concerning the obligations inherent in the concept of a public service in transport by rail, road and inland waterway;³³ that Regulation should therefore be repealed.
- (30) The scope of Regulation (EEC) No 1107/70 of the Council of 4 June 1970 on the granting of aids for transport by rail, road and inland waterway³⁴ is covered by this Regulation. As the earlier Regulation is now obsolete, it should be repealed in order that Article 73 of the Treaty may be properly applied to continuing developments in the sector without prejudice to this Regulation or Regulation (EEC) No 1192/69 of the Council of 26 June 1969 on common rules for the normalisation of the accounts of railway undertakings.³⁵

HAVE ADOPTED THIS REGULATION:

Article 1

Purpose and scope

1. The purpose of this Regulation is to define how, in accordance with the rules of Community law, the competent authorities may act in the field of public passenger transport to guarantee the provision of services of general interest which are among other things more numerous, safer, of a higher quality or at a lower cost than those that mere market forces would have allowed.

To this end, this Regulation lays down the conditions under which competent authorities may compensate transport operators for the costs incurred in meeting public service obligations and grant exclusive rights for the operation of public passenger transport services.

2. This Regulation shall apply to the national and international operation of public passenger transport services by rail and other track-based modes and by road, except

33 OJ L 156, 28.6.1969, p. 1, as last amended by Regulation (EC) No 1893/91 (OJ L 169, 29.6.1991, p. 1).

34 OJ L 30, 15.06.1970, p. 1; Regulation last amended by Regulation (EC) No 543/97 (OJ L 84, 26.3.1997, p. 6).

35 OJ L 156, 28.06.1969, pp. 8 to 20.

for services which are operated mainly for their historical interest or their tourist value.

Article 2

Definitions

For the purpose of this Regulation:

- (a) “public passenger transport” means transport services of general economic interest organised by the competent authority and provided to the public on a non-discriminatory and continuous basis;
- (b) “competent authority” means any public authority or group of public authorities of a Member State which is competent to organise public passenger transport and award public service contracts in a given geographical area, or any body vested with such authority;
- (c) “competent local authority” means any competent authority whose geographical area of competence is not national;
- (d) “public service operator” means any public or private undertaking or group of such undertakings which operates public passenger transport services or any public body which provides public passenger transport services;
- (e) “public service obligation” means a requirement defined or determined by a competent authority in order to assure passenger transport services in the general interest that an operator, if it were considering its own commercial interests, would not assume or would not assume to the same extent or under the same conditions without reimbursement;
- (f) “exclusive right” means a right entitling an operator to operate certain public passenger transport services on a particular route or network or in a particular area, to the exclusion of other operators;
- (g) “public service compensation” means any benefit, particularly financial, granted directly or indirectly by a competent authority from public funds during the period of implementation of the public service obligation or in connection with that period;
- (h) “direct award” means the award of a contract to a given operator without any prior competitive tendering procedure;
- (i) “public service contract” means one or more legally binding acts confirming the agreement between a competent authority and an operator to entrust to that operator the management and operation of services subject to public service obligations; depending on the law of the Member States, the contract may also consist of a decision adopted by the competent authority:
 - taking the form of an individual legislative or regulatory act, or

- containing conditions under which the competent authority itself provides the services or entrusts the provision of such services to an internal operator;
- (j) “internal operator” means a legally distinct entity over which the competent authority exercises complete control similar to that exercised over its own departments. For the purposes of determining whether such control exists, factors such as the degree of representation on administrative, management or supervisory bodies, specifications relating thereto in the articles of association, ownership, effective influence and control over strategic decisions and individual management decisions have to be taken into consideration;
- (k) “value” means the value of a service, a route, a contract, or a compensation scheme for public passenger transport corresponding to the total remuneration, before VAT, of the operator or operators, including compensation of whatever kind paid by the public authorities and revenue from the sale of tickets which is not repaid to the competent authority in question;
- (l) “general rule” means a measure which applies without discrimination to all transport services of the same type in a given geographical area for which a competent authority is responsible;
- (m) “regional or long-distance transport” means a transport service which does not cater to the transport needs of an urban centre or conurbation or connect a conurbation with its suburbs.

Article 3

Public service contracts and general rules

1. Where a competent authority decides to grant the operator of its choice an exclusive right or compensation, of whatever nature, in return for the discharge of public service obligations, it must do so within the framework of a public service contract.
2. By way of derogation from paragraph 1, public service obligations which aim to establish maximum tariffs for all passengers or for certain categories of passenger may either be included in a public service contract or be the subject of general rules. In accordance with the principles set out in Articles 4 and 6 and in the annex, the competent authority shall compensate the operators for the net costs incurred in complying with the tariff obligations established through general rules.

Article 4

Mandatory content of public service contracts and general rules

1. Public service contracts and general rules must clearly define the public service obligations with which the operator must comply, and the geographical areas concerned.
2. Public service contracts and general rules must establish in advance, in an objective and transparent manner, the parameters on the basis of which each compensation payment must be calculated. These parameters shall be determined in such a way that

no compensation payment may exceed the amount required to cover the net costs incurred in discharging each public service obligation, taking account of revenue relating thereto kept by the operator and a reasonable profit.

3. Public service contracts and general rules shall determine the arrangements for the allocation of costs connected with the provision of services. These costs shall include the costs of staff, energy, maintenance and repair of rolling stock and, where appropriate, fixed costs and a suitable return on capital.
4. Public service contracts and general rules shall determine the arrangements for the allocation of revenue from the sale of tickets which may be kept by the operator, repaid to the competent authority or shared between the two.
5. The duration of contracts shall be limited and shall not exceed eight years for coach and bus services and fifteen years for rail transport services. The duration of public service contracts relating to several modes of transport shall be limited to fifteen years if rail transport represents more than 50% of the value of the services in question.
6. If necessary, having regard to the conditions of depreciation of assets, the duration of the contract may be extended by a maximum of 50% if the operator provides assets which are both significant in relation to the overall assets needed to carry out the transport services covered by the public service contract and are linked exclusively to the transport services covered by the contract.
7. Under the contract, the competent authority may require the selected operator to grant staff taken on previously to provide services the rights to which they would have been entitled if there had been a transfer within the meaning of Directive 2001/23/EC. The authority shall list the staff and give details of their contractual rights.

Article 5

Award of public service contracts

1. Paragraphs 2 to 6 of this Article shall apply without prejudice to the obligations applicable to the competent authorities under Directives 92/50/EEC,³⁶ 93/36/EEC,³⁷

36 Council Directive 92/50/EEC of 18 June 1992 relating to the coordination of procedures for the award of public service contracts (OJ L 209, 24.7.1992, p. 1).

37 Council Directive 93/36/EEC of 14 June 1993 coordinating procedures for the award of public supply contracts (OJ L 199, 9.8.1993, p. 1).

93/37/EEC³⁸ and 93/38/EEC³⁹ as amended and Directives 2004/17/EC⁴⁰ and 2004/18/EC⁴¹ on the award of public contracts.

2. Any competent local authority may decide to provide public transport services itself or to award public service contracts directly to an internal operator, on condition that the internal operator and any entity over which the latter exerts even a minimal influence perform all their public passenger transport activity within the territory of the competent authority and do not take part in competitive tenders organised outside the territory of the competent authority.
3. Any competent authority which has recourse to a third party must award public service contracts via an invitation to tender, except in the cases specified in paragraphs 4, 5 and 6. The procedure adopted for the invitation to tender shall be open to all operators, shall be fair and shall observe the principles of transparency and non-discrimination. Following the submission of tenders and any preselection, the procedure may involve negotiations in accordance with these principles in order to determine how best to meet specific or complex requirements.
4. The competent authorities may decide to award public service contracts directly where their average annual value is estimated at less than €1 million or where they concern the annual provision of fewer than 300 000 kilometres of transport services.
5. In the event of the disruption of services or the immediate risk of such a situation, the competent authority may take an emergency measure. This emergency measure shall take the form of a direct award or formal agreement to extend a public service contract. The award or extension of a contract by emergency measure shall not exceed the period needed by the competent authority to organise a new procedure for the award of a contract in accordance with the provisions of this Regulation and in any event shall not exceed one year.
6. The competent authorities may decide to award public service contracts directly where they concern regional or long-distance transport by rail.

Article 6

Public service compensation

1. All compensation connected with a general rule or a public service contract must conform to the provisions laid down in Article 4, irrespective of how the contract was awarded. All compensation, of whatever nature, connected with a contract

38 Council Directive 93/37/EEC of 14 June 1993 concerning the coordination of procedures for the award of public works contracts (OJ L 199, 9.8.1993, p. 54).

39 Council Directive 93/38/EEC of 14 June 1993 coordinating the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors (OJ L 199, 9.8.1993, p. 84).

40 Directive 2004/17/EC of the European Parliament and of the Council of 31 March 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors (OJ L 134, 30.4.2004, p. 1).

41 Directive 2004/18/EC of the European Parliament and of the Council of 31 March 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts (OJ L 134, 30.4.2004, p. 114).

awarded directly in accordance with Article 5(2), (4), (5) or (6) or connected with a general rule must also conform to the provisions laid down in the annex.

2. At the written request of the Commission, Member States shall communicate, within a period of twenty working days or any longer period as may be fixed in that request, all the information that the Commission considers necessary to determine whether the compensation granted is compatible with this Regulation.

Article 7

Publicity

1. Each competent authority shall publish once a year a detailed report on the public service obligations for which it is responsible, the selected operators and the compensation payments and exclusive rights granted to the said operators by way of reimbursement. This report shall allow the performance and quality of the public transport network to be monitored and assessed from the standpoint of best possible use of public funds.
2. Each competent authority shall take the necessary measures to ensure that at least one year before the launch of the invitation to tender procedure or one year before the direct award the following information at least is published in the Official Journal of the European Union:
 - (a) The name and address of the competent authority;
 - (b) The type of award chosen;
 - (c) The services and areas covered by the award.

Article 8

Transition

1. Paragraphs 2 to 6 of this Article shall apply without prejudice to the obligations applicable to the competent authorities under Directives 92/50/EEC,⁴² 93/36/EEC,⁴³ 93/37/EEC⁴⁴ and 93/38/EEC⁴⁵ as amended and Directives 2004/17/EC⁴⁶ and 2004/18/EC⁴⁷ on the award of public contracts.
2. Each competent authority shall ensure that:
 - (a) at least half of its public service contracts for transport by coach and bus, by value, are awarded in accordance with this Regulation within four years of its entry into force; and

42 See footnote 35.

43 See footnote 36.

44 See footnote 37.

45 See footnote 38.

46 See footnote 39.

47 See footnote 40.

- (b) all of its public service contracts for transport by coach and bus are awarded in accordance with this Regulation within eight years of its entry into force.
- 3. Each competent authority shall ensure that:
 - (a) at least half of its public service contracts for transport by rail, by value, are awarded in accordance with this Regulation within five years of its entry into force; and
 - (b) all of its public service contracts for transport by rail are awarded in accordance with this Regulation within ten years of its entry into force.
- 4. In the case of public service contracts covering several modes of transport, the transitional periods provided for in paragraph 3 shall apply where transport by rail represents more than 50% of the value of the services in question.
- 5. For the application of paragraphs 2, 3 and 4, no account shall be taken of public service contracts awarded before the entry into force of this Regulation on the basis of a fair competitive tendering procedure, provided that they are of limited duration comparable to the durations specified in Article 4(5) of this Regulation. Such contracts may continue until they expire.
- 6. The competent authorities may, in the second half of the transitional periods specified in paragraphs 2 and 3, exclude from participation in the award of contracts by invitation to tender those operators which cannot provide evidence that the value of the public transport services for which they are receiving compensation or enjoy an exclusive right awarded in accordance with this Regulation represents at least half the value of all the public transport services for which they are receiving compensation or enjoy an exclusive right. For the application of this criterion, no account shall be taken of contracts awarded by emergency measure as specified in Article 5(5).

Where competent authorities make use of this possibility, they shall do so without discrimination, exclude all potential operators fulfilling this criterion and inform the potential operators of their decision at the beginning of the procedure for the award of public service contracts.

They shall inform the Commission of their intention to apply this provision at least two months before the publication of the invitation to tender.

Article 9

Compatibility with the Treaty

Insofar as it constitutes State aid within the meaning of Article 87(1), only compensation paid in accordance with this Regulation shall be compatible with the common market. Such compensation shall be exempt from the prior notification requirement laid down in Article 88(3) of the Treaty.

Article 10

Repeal

1. Regulation (EEC) No 1191/69 is hereby repealed.
2. Regulation (EEC) No 1107/70 is hereby repealed.

Article 11

Follow-up

1. Two years after this Regulation is adopted, the Commission shall present a report on developments in the provision of public passenger transport in Europe.
2. No later than two years after the end of the transitional period specified in Article 8(3), the Commission shall present a report on the implementation of this Regulation.

Article 12

Entry into force

This Regulation shall enter into force on the twentieth day following that of its publication in the Official Journal of the European Union.

This Regulation shall enter into force on the XXX day following that of its publication in the Official Journal of the European Union.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Brussels,

For the Parliament
The President

For the Council
The President

ANNEX

Rules applicable to compensation in the cases referred to in Article 6(1)

1. The compensation connected with contracts awarded directly in accordance with Article 5(2), (4), (5) or (6) or with a general rule must be calculated in accordance with the rules laid down in this Annex.
2. The compensation may not exceed an amount corresponding to the net financial effect equivalent to the total of the effects – positive or negative – of compliance with the public service obligation on the costs and revenue of the operator. The effects are to be calculated by comparing the situation where the public service obligation is met with the situation which would have existed if the obligation had not been met and if the services covered by the obligation had been operated under market conditions.
3. The calculation of the financial effect must take account of the impact that compliance with the public service obligation has on demand for transport services over the entire network concerned.
4. Costs and revenue must be calculated in accordance with the accounting rules in force.
5. In order to increase transparency and avoid cross-subsidies, where an operator not only operates compensated services subject to public transport service obligations but also engages in other activities, the accounts of the said public services must be separated so as to meet at least the following conditions:
 - the operating accounts corresponding to each of these activities must be separate and the proportion of the corresponding assets and the fixed costs must be allocated in accordance with the accounting rules in force;
 - the costs connected with any other activities of the operator must cover all variable costs, an appropriate contribution to the fixed costs and a reasonable profit. These costs may under no circumstances be charged to the public service in question;
 - the costs of the public service must be balanced by operating revenue and payments from public authorities, without any possibility of transfer of revenue to another sector of the operator's activity.
6. Reasonable profit must be taken to mean a rate of return on capital that is normal for the sector and that takes account of the risk, or absence of risk, incurred by the operator by virtue of the intervention by the public authority.
7. The method of compensation must promote the maintenance or development of:
 - effective management by the operator, which can be the subject of an objective assessment, and
 - the provision of transport services of a sufficiently high standard.