11TH CONFERENCE ON COMPETITION AND OWNERSHIP IN LAND PASSENGER TRANSPORT

Delft University of Technology (The Netherlands)
20-25 September 2009

DEVELOPMENT OF RAILWAY CONTRACTING FOR THE NATIONAL PASSENGER RAIL SERVICES IN THE NETHERLANDS

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ABSTRACT

This article mainly gives an overview of the policy developments in the Dutch railway sector over the past decade. The sector has come a long way and the outlook now looks positive. Customer satisfaction and performance have improved and the number of people that travel by train is rising. The development of a more long-term policy window for the sector seems to have brought rest and stability and room for continuous growth of passenger numbers. The combination of a policy making and negotiation regulatory style seems to have worked out very well on the performance of the sector. In a second section the paper also considers a theoretical framework on regulation schemes and develops a first tentative attempt to apply these schemes on an analysis of the Dutch railway sector by giving some statements for discussion.

INTRODUCTION

In this article we describe the development and the use of regulatory styles in the railway market in the Netherlands over the past decade. A document containing the government position on the railway legislation evaluation report, including the evaluation of the current regulation model, has been sent to the Dutch parliament in

June 2009 (Ministerie van Verkeer en Waterstaat, 2009). This document and its underlying reports are, amongst other documents, used in this article.

The article is organized as follows. The first section provides an overview of railway policy development in the Netherlands from 1995 until 2008. Section two considers a theoretical framework on regulation schemes. The third section applies these schemes on the Dutch railway sector and gives some statements for discussion.

OVERVIEW OF RAILWAY POLICY DEVELOPMENT 1995-2008

The rail sector has been in continual flux ever since the 1990s. Over the years, views on the ultimate objectives for its organisation have changed. European legislation on market opening for rail freight was one of the drivers that started the restructuring process of the Dutch railway sector. Directive 91/440 asks for an administrative separation between infrastructure management and transport of passengers and freight. This separation is meant to encourage competition on the tracks for freight.

In 1992 the Wijffels Committee, appointed by the Minister of Transport, worked out the new European rules and designed a new relation between the railway company and the state (Commissie Wijffels, 1992). The main idea of the reform was that passenger transport should become a non-subsidized commercial activity while building and maintaining the infrastructure remained a responsibility of the government. The Dutch railways (NS) was reorganized according to the recommendations of the Committee.

Railway reform and transitional contract in the years 95-99

The railway reform initiated in 1995 in the Netherlands aimed to increase the market share of railways in overall transportation and intended to lead to a lower burden on the public purse (van de Velde, 2005). NS undertakings were split up in 1995 (within the NS holding) into a number of separate companies each with its own account.

The split up resulted in an organizational separation between the commercial activities – such as passenger transport, the exploitation of railway stations and development of real estate – and the infrastructure activities and infrastructure development and maintenance. The latter activities were placed in the so called ‘task organizations’. The three task organizations created in 1995 were: Railned, NS Traffic Control (NS Verkeersleiding) and NS Rail Infrastructure Management (NS Railinfrabeheer). Their costs were covered directly by the Ministry of Transport even though these organizations were still part of the NS concern. Passenger transport (NS Reizigers) and freight (NS Cargo) became separate organizations within the NS-holding. Later, the freight division was sold to the German Railion consortium, belonging to DB (Deutsche Bahn), being the state-owned rail operator of Germany.

This new course resulted in a contract between the state and NS, which aimed at giving NS more freedom to make its own commercial decisions. It should be noted that this reform did not involve a privatization of NS, since NS has always been a joint-stock company (‘naamloze vennootschap’) with all shares held by the state. It refers more to the withdrawal of the subsidies. NS became an independent company free of the direct control by the Ministry of Transport even though the state remained as sole shareholder. The transitional contract between the state and NS for the period 1996-2000 was also

meant to allow the development of a new railway legislation to replace the Railway Act of 1875. For this period the transitional contract foresaw a gradual reduction of subsidies to NS and the possibility to stop operating non-profitable passenger services. This resulted in the separation of a number of non-profitable lines from the NS network. These were then, gradually, contracted out (based on government subsidies) to private parties[1]. Also, in a first stage up to the year 2000, the government decided to set the charges for using the infrastructure at zero.

Performance contracts in the years 99-2001

In 1999 a policy document *De Derde Eeuw Spoor* (´The third Century of Rail´) (Ministerie van Verkeer en Waterstaat, 1999) on competition and development of the railway sector was published by the Ministry of Transport. It chose for competition for the tracks for passenger transport. According to the policy document a 10-year concession contract was to be directly awarded to NS. This concession should include performance indicators with financial incentives on passenger growth and punctuality. It would contain conditions on minimum service levels, fare increases, integrated ticketing and access for people with reduced mobility. These proposals would be laid down in a new railway law and concession law. To bridge the gap until this law would be finalised, a memorandum of understanding (MoU) was made up which set performance levels for punctuality and passenger growth in peak hours. The targets for these performance indicators were proposed by NS and agreed upon by the state. However, there were further delays in the legislation process. These delays made it necessary to make up a second transitional contract based on the MoU. This contract set performance levels for a period of 6 months and was extended twice for an additional period of 6 months.

In 1999 a report by the National Audit Office (Algemene Rekenkamer, 1999) concluded that the Ministry had failed in its supervisory and steering role of the task organizations, which were responsible for building and maintaining the infrastructure. The independence of the task organizations could not be guaranteed and adequate corrective action by the Ministry was overdue.

In these years the level of train punctuality fell to a level that was not compliant with the second transitional contract (see Figure 1). The Ministry concluded that there was insufficient focus on integral quality by the management of various railway organizations within NS (task organizations and passenger transport). At that time, there were also internal changes and plans to create a different type of operational groups within the NS company. These plans however received massive opposition from the unions and left the company to decline rapidly as many strikes followed. The urgency of the situation led the Ministry to introduce a policy change, called "*Herbezinning spoor*" (Railway reconsideration) in September of 2001. The punctuality indicator was reduced from 88% to 80%. When NS towards the end of 2001 failed marginally to achieve the 80% punctuality target, the full board of directors decided to resign.

The railways' poor performance in 2001 and the unrest this caused led to a reappraisal of the previous reorganisation plans. Parties in the rail sector and the government

[1] Over the last years passenger growth and quality improvements on these lines have been realized

focused after this reappraisal on working more closely together and on remedying and improving the railways' performance.

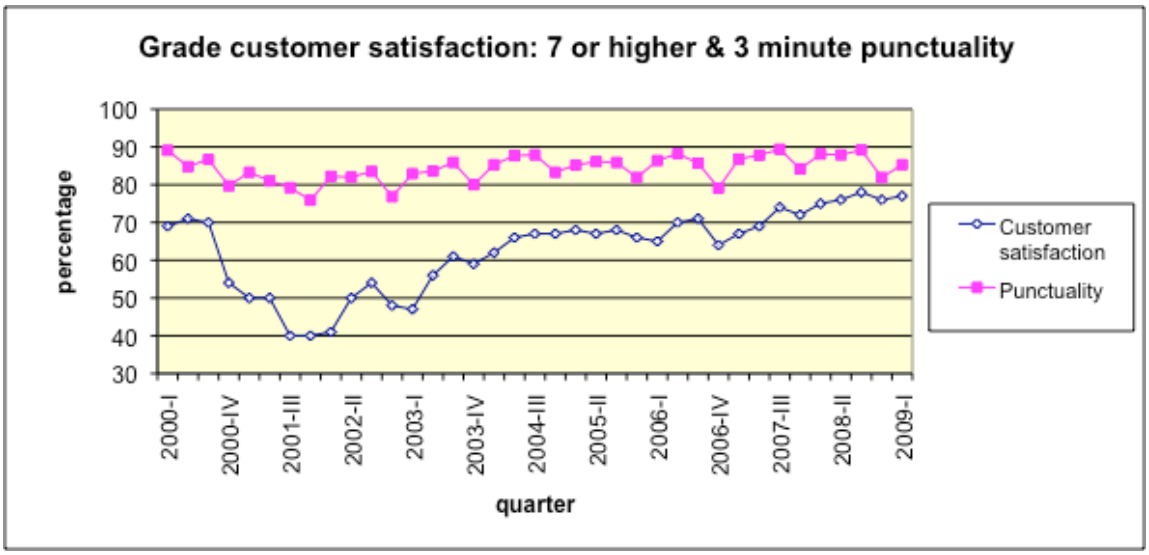

Figure 1: Evolution of customer satisfaction and punctuality 2000-2009

Preparing for new legislation in the years 2001-2005

Against this background, the second transitional contract was again extended for six months and subsequently for a period of one year until the starting day of the new Railway and Concession act. A full institutional separation between infrastructure management and train operations was implemented in 2002: all the infrastructure management tasks were separated from the other NS activities and these tasks merged into a new organisation called ProRail on 1 January 2003. This company is fully owned by the state, but entirely separate from NS. The minister of Transport acts as shareholder. It is responsible for rail capacity management, train path management, real-time passenger information, and management of the passenger transfer spaces at the stations, and infrastructure maintenance and development. ProRail operates within the framework set by the Ministry of Transport, concerning general policy on track usage and network development.

In April 2003 the new Railway and Concession act were approved by the parliament. However, final parliamentary agreement on the concession texts could not be reached before December 2004, allowing the new regime to come into force in 2005, five years later than the original reform plan. As a result, the current organisation, with the relevant legislation, was only introduced in 2005 (see Figure 2).

The organisation chosen in the Netherlands dovetails closely with European legislation and policy developments, which are aimed chiefly at opening up the market for freight transport and for international cross-border passenger transport. The Netherlands have always opposed opening up the national market because one railway undertaking with exclusive rights for the provision of passenger services in a region will be more able to optimise these services and secure reliability with both acceptable travel and transfer times especially in a densely used network such as in the Netherlands.

The Ministry of Transport has three distinct roles. Firstly it must oversee the public interest, secondly it awards the operating concession contracts and thirdly it is sole shareholder of ProRail. From 1 January 2005, the formal shareholdership of NS is transferred from the Ministry of Transport to the Ministry of Finance, such as to separate the role of regulator from that of owner. The government sets the rules and acts as a regulator according to the railway legislation. The mutual responsibilities of the infrastructure manager and train operating companies are stated in track access agreements.

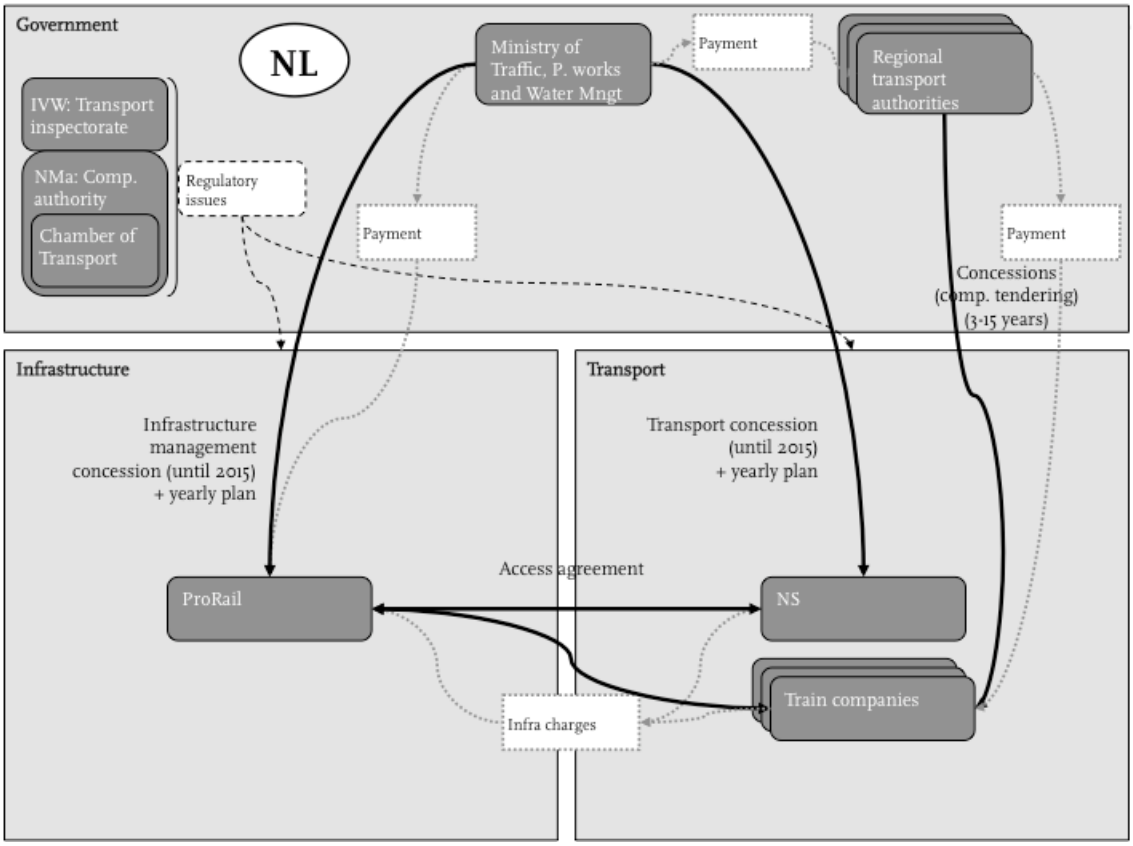

Figure 2: Current institutional configuration (van de Velde and Röntgen, 2009)

The intensification of the cooperation between the infrastructure manager and the train operating companies is essential to the new regime. An example of forms of cooperation is the quarterly meetings under the name of *Samensporen* (´Tracking Together´) between the directors of ProRail, NS, Railion and a representative of the other freight operators. These meetings discuss interfaces between the three parties and monitor the progress of the better usage of capacity and the reliability of the entire railway system, to accommodate future growth.

Building a new system: improving in the years 2005-2008

Ten-year concession contracts for NS and ProRail were drawn up and enacted in January 2005. These concessions set performance indicators for NS and ProRail. NS and ProRail have to propose every year improved values for these indicators in so called transport and infrastucture plans. These values have to show continuous improvement or NS or ProRail have to explain why this is not possible in a certain year. Using yearly

plans makes the system flexible and makes adjustment to changing circumstances possible. The government analyses and then approves these proposals. In a transitional period up till 2007 both companies were allowed to learn to work with this indicator regime. The aim was to get ProRail and NS ready for output steering after a few years. This was to be reached in 2008 as from then on penalties are given if indicator levels are not met.

Encouraging growth, better performance by NS and ProRail and development in the years 2008-2015

The current railway legislation entered into force on 1 January 2005. The law required an evaluation of the regime in 2008. The four main conclusions of the final report of these evaluation were:

- The rail sector now has a decent structure, but it needs to be put to better use.
- Use of the railways by the public is improving.
- The transport operators and the infrastructure manager are primarily responsible for day-to-day management.
- The legal system could work better.

The government concluded that a radical reorganisation is not required. However, the government has also come to the conclusion that the organisation needed some improvements which are laid down in a policy document.. The frameworks for user charges and allocation of capacity needs tightening up, needs to be improved and made more transparent, the position of regional authorities in the management of stations needs to be improved, and the position, role and management of the infrastructure manager ProRail, as well as NS need to be made more transparent.

Not all improvements can be brought about through legislation. Equally important are the behaviour of the parties in the rail sector and cooperation between them, since they are the ones who have to deliver services. It is perceived that it is possible and indeed necessary to maintain and step up cooperation. Moreover, the points for improvement listed in the final report of the evaluation indicate that existing instruments are not fully utilised.

The government has some ambitious aims for the rail sector in the Netherlands. It has identified four priorities for improving the quality and capacity of both passenger and freight transport. They are:

- frequent services on the busiest lines in and around the Randstad in the west of the country;
- cohesive regional public transport systems revolving around rail transport;
- the quality of travel times to the various parts of the country;
- a future-proof strategy for freight transport routes.

In its 2007 coalition agreement, the government aimed for 5% annual growth in passenger transport during its term in office. In the medium term, €4.5 billion has been earmarked for investment in the rail sector, through the *High Frequency Rail Transport Programme*. The government plans to achieve these ambitious aims by expanding the capacity and quality of the railways and by making the organisation of the rail sector,

the rules and regulations applicable to it and the distribution of responsibilities between the various parties more transparent and more effective.

Cooperation between the infrastructure manager and the transport operators has improved in recent years.

The government is also planning to present a clear, uniform policy framework for user charges, which will lead to more clarity and certainty. The main concern is for tariffs and the principles on which they are based to be clear and the costs and the system used by ProRail for user charges to be transparent. Stability of the system, tariff development and better utilisation of the railways are also major considerations.

NS and ProRail have improved their performance in the past few years. To keep them on track and stimulate growth, the government felt it is necessary to adapt its guidance of the two organizations in a number of areas. The government is planning to take a more hands-on approach to providing direction to the two parties. In 2010, the government will explore how the interface between the concession for the main rail network and existing regional concessions can best be designed in the new concession for the main rail network from 2015. It will do so in combination with its an exploration of the scope of the main rail network as opposed to regional networks.

The government sees ProRail first and foremost as a provider of public services. As such, it should focus on implementing its statutory, public responsibilities. In order to ensure that ProRail fulfils this role, the government will bring more pressure to bear through its position as shareholder and awarder of concessions and grants. It will amend the company's articles of association, give the State legal ownership of the main rail network infrastructure and expand its array of enforcement instruments.

In view of the outcome of the evaluation and the government's aims, NS' concession for the main rail network will be modified. The government is planning to introduce a number of new performance indicators and expand its array of enforcement instruments. It has opted to press for more efficiency by charging NS for the concession from 2009, and requiring it to provide more detailed financial information. The Policy Document on State-Controlled Companies, will give the Minister of Finance, as NS shareholder, more forceful direction to secure the public interest (Tweede Kamer, 2007).

On the basis of the evaluation, the government concludes that the position of provincial and regional authorities needs strengthening, and therefore plans to take statutory and organizational measures in a number of fields. Good regional transport networks are an essential and integral part of the transport chain that brings passengers from door to door. The government regards rail transport as the backbone of cohesive regional public transport systems, and is therefore in favour of more extensive cooperation with and between the authorities responsible for providing services. The provincial and regional authorities will be represented by their umbrella organisations in advisory groups, giving them the opportunity to provide input in assessing the management and transport plan.

THEORETICAL FRAMEWORK ON REGULATION SCHEMES

This paper will now attempt to match the regulation methods used in the Dutch railway industry with the three regulatory styles based on the models of Wirick (1999). Kuit (2002) summarizes these styles in his dissertation on regulatory styles and strategic behavior as such:

- **Policy-making model:** In this model the regulator is seen as a policy maker focusing on making effective objective decisions in the form of policy guidelines. Consultation of the involved parties takes place before setting these guidelines. The regulator uses a mechanistic-rational method to make decisions.
- **Regulation-by-negotiation model:** This model is based on constant interaction between regulator and actors involved. The regulator enters into negotiations with them and tries to create win-win situations and consensus. The regulator uses process regulations and management tools.
- **Adhocratic-chaotic model:** Regulators do not choose this model but end up using it when they have to deal with ambiguous issues. The outcome of this model is unpredictable. A conclusion can be reached using fixed procedures or negotiating with the involved parties.

Table 1: properties of regulatory styles

	Policy-making model	**Regulation-by-negotiation model**	**Adhocratic-chaotic model**
Metaphor	Regulator as policy-maker	Regulator as mediator	Regulator as troubleshooter
Focus	Taking objective and effective decisions	Creating win-win situations	Not known in advance
Instruments	Information collection Decision-making methods	Negotiating skills	Dependent on the issue
Outcomes	Policy Guidelines Decisions	Agreements Partnership agreements	Dependent on the issue and process
Regulation	Substance based Active interference Mechanistic-rational	Based on rules of the game Facilitated/conservative Consensus based	Coincidence-based Active of facilitated Unpredictable

DISCUSSION

This section provides a few tentative statements for discussion. These are formulated on the basis of a first brief analysis of the developments of the railway policy in the Netherlands over the past 10 years as presented earlier in this paper. Note that further research and analysis is needed before being able to refine and validate these discussion statements.

Uncertainties on the final organisation of the sector have a negative effect on performance

Looking into the past decade of railway policy, one can see that the views on the ultimate objectives for its organisation have changed. Competition on the track was for example foreseen combined with a possible privatisation of the state-owned company NS. Around the turn of the century, the policy was changed in competition for the track and privatisation was abolished.

Uncertainties on the final organisation of the sector seem to have a negative effect on performance. NS refrained from investing in new trains because they were uncertain on their licence to operate in the forthcoming years, which made it unclear if they could make enough return on investments in the forthcoming years.

After launching a more long-term policy window in 2001 and securing that NS would have a ten-year concession, one could observe that investments were made and that performance (like customer satisfaction and number of trains that run on time) improved (see Figure 1).

Changing roles of players influence performance

Over the past decade the three regulatory styles mentioned in the theoretical framework were all used by the government. In the first period form 1995 till 1999 NS had a great amount of autonomy. This lead to political pressures to make firmer arrangements to secure public values. These public values were secured in ad hoc contracts which were prolonged several times awaiting new legislation. These contracts can be characterised as instruments used in the policy making model. After consultation the government sets clear performance indicators and gives penalties for the event that these were not met by NS. The change in policy windows and prolongation of the contracts also fit the adhocratic chaotic model.

The new legislation combines the policy making and negotiation model. The government sets performance indicators but the NS proposes the values. Before setting the final levels these are discussed between NS and the government. Once they levels are set the government will give penalties if performance indicators are not met which fits into the policy making model. The negotiations that take place between train operating companies and ProRail on track access and usage also fit into the negotiation model with the railway regulator as back up in case they do not come to an agreement.

Hybrid position of railway companies complicates the system

Railway companies have conflicting goals. On the one hand they want to secure public values like customer satisfaction and travel times. On the other hand, they want to improve efficiency and cut costs. The past period showed that these goals can be conflicting (for example NS proposed to shut down train stations in more rural areas with a low number of travellers or the closing down of toilets in some trains that run on short journeys).

CONCLUDING REMARKS

This article has given an overview of the policy developments in the Dutch railway sector over the past decade. The sector has come a long way and the outlook now seems positive. Customer satisfaction and performance have improved and the number of people that travel by train is rising. The government has deemed that the policy that was set out in 2001 does not need big adjustments and it appears that the development of a more long-term policy window for the sector has brought rest and stability and room for continuous growth of passenger numbers.

Further research and analysis is needed to refine and validate the statements on regulatory styles formulated above, but it seems that the combination of a policy making and negotiation regulatory style have worked out very well on the performance of the sector.

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