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ROUNDTABLE ON COMPETITIVE NEUTRALITY IN COMPETITION ENFORCEMENT

-- Note by the European Union --

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This document reproduces a written contribution from the European Union submitted for Item 9 of the 123rd meeting of the OECD Competition Committee on 16-18 June 2015.

More documents related to this discussion can be found at www.oecd.org/daf/competition/competitive-neutrality-in-competition-enforcement.htm.

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EUROPEAN UNION

1. In this paper the EU will address a number of competitive neutrality related issues identified in the OECD Competition Committee's note of 17 February 2015.

1. Competitive neutrality' and the role of the state in the market

1.1 *What does competitive neutrality mean to you? Is it a useful or necessary goal for competition? Is it an objective of your competition authority? What is the ultimate goal in promoting a level playing field or undistorted markets in your jurisdiction?*

2. Competitive neutrality is a concept of high importance to the EU. To start, competitive neutrality is essential for maintaining a level playing field in the internal market of the EU and it underpins competition policy since the beginning of European integration. Without e.g. submitting State owned Enterprises (hereinafter SOEs) to the same antitrust rules, the Single market could not work. The economic rationale behind implementing competitive neutrality measures is to allow privately-owned businesses and government-owned businesses to compete on an equal footing. It is believed that the accompanying increase in competition would bring about greater efficiencies and better quality products and services at lower prices, leading to an increase in consumer welfare. Greater efficiencies in the public sector also mean a more effective use of taxpayers' resources.

3. Its rationale extends however beyond the borders of the EU. Taking into account the increasing level of globalisation and the degree to which our respective economies have become interconnected, also on a global level there are good reasons for competitive neutrality to underpin the basic values on which our trading relations and the application of our competition rules are based. This explains why the EU expressed strong support for the OECD Competition Committee to put the topic of competitive neutrality on its agenda and why the EU is also consistently advocating it in its trade negotiations.

4. Although there is internationally little disagreement about the importance of competitive neutrality, finding a consensus on a workable definition remains a challenge. Many definitions used are phrased too narrowly and seem to focus primarily on one particular aspect of competitive neutrality, i.e. SOEs. Although the EU recognises the importance of this particular aspect of the competitive neutrality concept, in our view it should be more broadly defined and cover all forms of direct and indirect public interventions of whatever nature, which may provide public or private undertakings with undue advantages over their actual or potential competitors, thereby distorting the competitive process.

5. The following definition proposed by the OECD would be a good starting point for reflections on the scope and the application of this concept.

6. Competitive Neutrality policy is a 'regulatory framework (i) within which public and private enterprises face the same set of rules and (ii) where no contact with the state brings competitive advantage to any market participant.'¹

¹ OECD (2009), 'Policy Roundtables, State Owned Enterprises and the Principle of Competitive Neutrality', introduction: <http://www.oecd.org/daf/ca/corporategovernanceofstate-ownedenterprises/50251005.pdf>.

It follows from the above definition that competitive neutrality may have an impact on many policy areas. Apart from the field of competition policy, which in the EU covers the fields of antitrust, cartels, mergers, State owned enterprises and companies with special and exclusive rights as well as the rules on State aid control, the competitive neutrality principle also plays a key role in areas such as public procurement, taxation and property ownership.

1.2 *In your experience, what type of State measures can distort the playing field? Do you think that State-controlled or supported firms enjoy advantages or disadvantages (e.g. higher labour costs due to public status of their employees)? What types of distortions are you mostly concerned with?*

7. There are many situations conceivable where firms (State controlled or not) receive advantages from the State which may distort the level playing field. One good example hereof concerns situations of cross-subsidisation, i.e. situations where the firm receives a compensation from the State for the performance of services of general economic interest (SGEI), which is higher than the costs of such a service, so that part of the compensation can be used for an activity falling outside the scope of the public service obligation. Areas where such a risk of cross-subsidisation exists are the network sectors, for instance the area of broadcasting. It is Commission policy that State aid to companies entrusted with public service broadcasting obligations should be necessary to cover the net costs of providing a clearly defined and entrusted public service broadcasting task. Whenever a public broadcaster carries out other economic activities in addition to providing services of general economic interest, one has to ensure that the compensation paid by the States covers the cost of the SGEI and is not used to support the other economic activities to avoid that competition with firms active in the field of the same activities is distorted. This means that no cross-subsidisation should take place to commercial activities. For instance, in its decision on ZDF Media Park the Commission assessed whether the investment by a subsidiary of the German public broadcaster in a theme park related to the programmes of ZDF constituted incompatible State aid². As the subsidiary acted as a private investor and all transactions would be done at market conditions, the Commission concluded that in that case no cross-subsidisation from the broadcasting fees took place.

8. State controlled firms have to deal also with structural disadvantages that their competitors do not bear (e.g. related to the special status of their employees).

9. Such disadvantages may justify measures that escape the qualification of State aid when they are not aimed at conferring an advantage on the undertaking but rather at freeing it from the structural disadvantage burdening it compared to its private-sector competitors. On this basis the Court of First instance (CFI) found in *Combus* that the payment by a Member State of an amount of money to employees of a bus transport undertaking in order to finance their giving up their status as officials is not State aid within the meaning of the Treaty on the Functioning of the European Union (hereinafter TFEU) provisions on State Aid. A "no aid" finding of the Court was possible in this case because the advantage was ultimately granted to individuals whereas one of the conditions of the State aid is an advantage granted to an undertaking.³

10. However, in most cases, such measures provide the recipient undertaking with an advantage and are considered to be aid. They are authorised by the European Commission, if they are limited to what is necessary to achieve an objective of common interest and do not distort competition and trade to an extent which would be contrary to the Community interests. For instance, the Commission found that the reform of the financing of the pensions of the officials of La Poste was a compatible aid⁴. The

² NN 2/2002, Germany, ZDF Mediapark Mainz-Lerchenfeld, OJ C 137 of 8 June 2002.

³ In similar cases the Commission has focused on the advantage granted to the undertaking and consistently taken the compatible aid route (OTE, La Poste, RATP, Royal Mail).

⁴ La Poste, Commission Decision of 10 October 2007 (see IP/07/1465).

reform was designed to align gradually the costs borne by La Poste in respect of retirement pensions paid to its public-service employees with the pension costs of its private competitors.

1.3 *In which sectors do you find the highest degree of State intervention and influence? Is the State's presence growing or decreasing in your economy? What is the weight of SOEs, regulated companies and/or public services in your economy?*

11. Traditionally SOEs can be found in sectors such as post, telecoms, electricity, transport, energy, financials, health etc.

12. Although it is difficult to find comprehensive and reliable data on the number of SOEs and on their evolution over time, it seems clear that their role in national economies is still significant and in certain parts of the world even increasing. It is estimated by research that more than 10% of the world's largest firms are State owned (204 firms). They come from 37 different countries and their joint sales amount to \$3,6 trillion in 2011⁵. There appear however to be significant differences in the relative importance of SOEs to individual economies. There is data suggesting that State companies make up 80% of the value of the stock market in China, 62% in Russia and 38% in Brazil⁶. In the same vein, countries which have the highest SOE presence among their top firms, on the basis of equally weighted average of shares of state owned enterprises in sales, assets and market value of the country's top ten firms, include China (96%), the United Arab Emirates (88%), Russia (81%), Indonesia (69%) and Malaysia (68%)⁷. The estimates for EU Member States are significantly lower: Germany 11%, Finland 13%, Greece 15%, Ireland 16% and France 17%⁸.

13. For the EU as such it is difficult to give precise indications as to the expected evolution of the influence of State owned Enterprises. It is possible though to describe the effects which the liberalisation of certain sectors of the economy has had on the position of State monopolies.

14. For instance, starting in 1988, through a step by step approach, the EU liberalised all segments of the telecoms market: terminal equipment, value-added services, satellite equipment and services, cable TV networks and mobiles communications. The effects of liberalisation have been significant. There are now hundreds of licensed local, long-distance and international operators for fixed voice telephony. There are also more than 50 licensed mobile operators offering GSM services. Tariffs have fallen dramatically, especially in international and long distance calls. In addition, liberalisation has had a very positive impact on incumbent operators. In a matter of a few years, most of them have evolved from public administrations to innovative and competitive companies that expand internationally.

2. Rules and tools to address competitive neutrality distortions available to competition authorities

2.1 Rules/Tools

2.1.1 *What is the scope of your competition law vis-à-vis State activities in the market? Are there exemptions, exceptions, immunities or defences that may limit the scope of your intervention?*

15. The EU system is characterised by the fact that the principle of competitive neutrality between public and private enterprises is explicitly recognised in law, i.e. the TFEU and that the

⁵ Kowalski, Büge, Sztajerowska and England, 2013

⁶ The Economist, January 21, 2012

⁷ Idem see footnotes 3

⁸ Idem see footnotes 3

Commission has operational tools to implement this principle. The following sections will shed more light on the way in which this principle is reflected in EU rules.

2.1.1.1 *Ownership neutrality*

16. The TFEU guarantees the neutral treatment of all undertakings, irrespective of whether they are publicly or privately owned. This principle is enshrined in Article 345 TFEU, which provides that the Treaty shall “*in no way prejudice the rules in Member States governing the system of property ownership.*”

2.1.1.2 *Scope of the competition rules: entities engaged in economic activities*

17. The neutrality principle is also reflected in the application of EU competition rules as laid down in the TFEU: EU competition rules apply to all businesses or undertakings, irrespective of whether they are publicly or privately owned, provided that they qualify as an “undertaking”. An undertaking is an entity which performs an “economic activity”. It is not dependent on whether the entity is considered a company under company law, or whether it is privately or publicly financed. An “economic activity” is defined as “any activity consisting in offering goods and services on a given market”⁹. Under EU law it is therefore not a prerequisite that the activity is intended to earn revenues or to be profit oriented.

18. The European Court of Justice (ECJ) clarified the meaning of ‘undertaking’ in its Höfner/Marcotron judgement (Case C-41/90). In line with the above, it held that: “It must be observed, in the context of competition law ... that the concept of an undertaking encompasses every entity engaged in an economic activity, regardless of the legal status of the entity and the way in which it is financed.” Therefore like any “undertaking”, SOEs which are engaged in an economic activity are subject competition rules including State aid.

19. The EU competition rules therefore have a relatively wide coverage with a narrow margin for exemptions. Activities of public authorities are not automatically exempted from the application of the competition rules. This implies for instance that part of the activity of a public authority can be an economic activity qualifying the entity as an undertaking under Article 101/102 TFEU while other parts of its activity might be the classical tasks performed by an authority (i.e. the exercise of public powers) falling outside the scope of the competition rules.

2.1.1.3 *Duty for Member States not to deprive the EU competition rules of their effectiveness*

20. One of the most important goals of the EU is the creation of a single European market (i.e. a market without barriers *de facto* working as one integrated market). A key pillar for achieving a fully integrated market is an efficient competition policy. With the goal of market integration in mind, Community law prohibits instruments such as tariffs, quotas and the like which can impede the attainment of this goal. This type of prohibitions is directly addressed to Member States and their legislative measures.

21. The articles of the Treaty on anti-competitive agreements (Art 101 TFEU) and abuse of a dominant position (Art 102 TFEU) are, in contrast to the prohibitions just mentioned, addressed to companies engaged in economic activities. The duty of the Member States to respect the rules of the Treaty together with the concept of supremacy of Community law, however also leads to an obligation for the Member States not to enact any legislative measure which could risk endangering the effectiveness of the Treaty.

⁹ The concept of “economic activity” is also used in the revised OECD Guidelines on Corporate Governance of State-owned Enterprises and the related draft Recommendation on the Guidelines on Corporate Governance of State-Owned Enterprises.

22. According to the case-law of the ECJ, a Member State may not adopt or maintain in force any measure which would deprive the competition rules, of their effectiveness or prejudice their full and uniform application¹⁰. A state can be in breach of this obligation either when it requires or encourages companies to conclude cartels which are in violation of Article 101, or when it divests its national provisions of their public nature by, in effect, delegating to the firms the responsibility for taking decisions about the boundaries of competition.

23. The question rises if there is any responsibility for an undertaking when the State has breached its Treaty obligations as described above. It is clear that when the potentially anticompetitive practice is an autonomous decision of the undertaking the competition rules of the Treaty apply. If, on the contrary, an undertaking would be forced by legislation (or other types of binding state measures) to behave in a certain way, the undertaking can no longer act autonomously and may invoke the so called "state action defence", to escape responsibility under competition law. Only the state is responsible for state-imposed abuses or anti-competitive agreements. The lack of liability of the company in such cases is thus compensated for by the liability of the state.

24. If however the anti-competitive behaviour is only state-induced (as opposed to state imposed), both the state and the undertaking are liable. The mere state inducement does not remove the autonomous character of the actions of the (public) undertaking and thus the potential liability under EU competition law.

2.1.1.4 Public Undertakings and undertakings with special and exclusive rights

25. When it comes to SOEs ("public undertakings" in the words of the Treaty) or companies to which the state has given exclusive or special rights, the obligation for states not to adopt legislative measures which deprive the competition rules of their effectiveness is specifically provided for in the Treaty. Article 106 TFEU reminds the Member States that the competition rules apply also to SOEs and undertakings given special or exclusive rights (so-called "privileged" undertakings") and that national laws depriving the competition rules of their effectiveness would be in violation of the Treaty, unless such a measure is necessary for the provision of a service of general economic interest. It is important to note that the "competition rules" concerned to which Article 106 TFEU applies include the rules on State aid as laid down in Articles 107 and 108 TFEU and described in more detail in the following section.

26. Article 106(1) TFEU refers to "public undertakings" but does not further define these. This term is a concept of community law and is defined by the Commission in the Transparency Directive¹¹ as: "any undertaking over which the public authorities may exercise, directly or indirectly, a dominant influence by virtue of their ownership of it, their financial participation therein, or the rules which govern it". Conceptually this is equivalent to the question of control raised in merger proceedings and importantly goes beyond the issue of ownership alone.

27. Article 106 TFEU applies both to public undertakings as defined above, and to private undertakings with special or exclusive rights. An example in the case-law of a company having been granted an exclusive right is a company granted a monopoly over the provision of recruitment services, or a dock-work company entrusted with the exclusive right to organise dock work for third parties¹². Special rights, on the other hand, could be defined as rights that are granted by a Member State which limit the number of undertakings authorised to provide a certain service (having been

¹⁰ Judgment of the Court of 16 November 1977, SA G.B.-INNO-B.M. v Association des détaillants en tabac (ATAB), Case 13-77.

¹¹ Commission Directive 2006/111/EC of 16 November 2006 on the transparency of financial relations between Member States and public undertakings as well as on financial transparency within certain undertakings, OJ L 318, 17.11.2006, p. 17–25.

¹² C-22/98 Re Becu Ors [1999] ECR I-5665

designed otherwise than according to objective and non-discriminatory criteria). The logic with extending the scope also to undertakings having been granted special or exclusive rights is that the same rules should apply regardless of whether a Member State chooses to remain the owner of the undertaking performing the public service or whether it delegates this to a private company.

28. In a ruling of the ECJ of 17 July 2014 on Art 106(1) TFEU in the Greek Lignite case (C-553/12P) the Court clarified the nature of the test which the Commission has to apply in order to successfully demonstrate the existence of an infringement of 106(1) in conjunction with Article 102 TFEU in relation to companies with special and exclusive rights. Lignite is the most competitive fuel for the production of electricity in Greece. DEI (the state-owned Greek electricity incumbent) held exploration and exploitation rights for more than 90% of the public lignite deposits that had been licensed by the Greek State. Greece had implemented a number of measures granting rights enabling DEI to exploit all significant public lignite deposits for which exploitation rights had been granted.

29. The Commission held in two decisions (March 2008 (C(2008) 824 and August 2009 (C(2009) 6244) that the Greek State had infringed Art. 106(1) TFEU read in conjunction with Art. 102 TFEU, since the grant and maintenance of those rights created a situation of inequality of opportunity between economic operators: due to the privileged access to lignite – as the cheapest source for the production of energy – DEI had a significant and remaining competitive advantage in the wholesale electricity market.

30. The General Court annulled both Commission decisions on the basis of an action brought by DEI supported by the Greek State (By judgment of 20 September 2012 in Case T-169/08). In appeal however, the ECJ confirmed, in line with the Commission's position that an infringement of Article 106(1) in conjunction with Article 102 may be established irrespective of whether any abuse actually exist. The ECJ held that all that is necessary is for the Commission to identify a potential or actual anti-competitive consequence liable to result from the State measure at issue. Such an infringement may thus be established where the State measures at issue affect the structure of the market by creating unequal conditions of competition between companies, by allowing the public undertaking or the undertaking which was granted special or exclusive rights to maintain (for example by hindering new entrants to the market), strengthen or extend its dominant position over another market, thereby restricting competition, without it being necessary to prove the existence of actual abuse.

31. Article 106(2) TFEU provides for a narrow exception to the rule that competition law is applied to all types of undertakings. This exception shows similarities with the more widely known "public policy objective" exception as for instance laid down in the OECD Guidelines on Corporate Governance of State-owned Enterprises. Article 106(2) provides that undertakings entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly shall be subject to the rules contained in this Treaty, in particular to the rules on competition, in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Union.

32. Article 106(2) TFEU, which is (contrary to Article 106(1)) addressed to the undertakings themselves, thus specifies the conditions under which the competition rules can be set aside for public or privileged undertakings. Three cumulative conditions have to be satisfied before the exemption becomes applicable: 1. the undertakings in question must have been entrusted with the "operation of a service of general economic interest"; 2. the application of the Treaty would obstruct the performance (in law or in fact) of the tasks assigned to this undertaking and 3. the exemption is not available if the development of trade is affected to an extent contrary to the interests of the Union. Moreover, the exception will only apply if the restriction is proportionate, i.e. necessary for the fulfilment of the service of general economic interest. For example, in the Commission proceedings against British Telecommunications, its defence based on Article 106(2) TFEU was rejected as insufficient to meet the aforementioned criteria. On appeal the ECJ held that it had not been shown that British Telecom's

refusal to allow private message-forwarding agencies from using its network to forward messages from other Member States endangered the performance of its tasks¹³.

33. The practical effect of Article 106(2) TFEU is that undertakings entrusted with the task of performing a public service, or rather a "service of general economic interest", can escape the application of the competition rules if the application of competition law would prevent them from carrying out the tasks assigned to them by the Member State. This recognises the fact that State intervention in the economy is sometimes necessary and justified in order to ensure the provision of services of general interest. Although in the vast majority of cases, the market ensures the optimum allocation of resources for the benefit of society at large, there are instances where services of general interest will not be provided adequately (or at all) if left solely to market forces. This may be, for instance, because their market price is too high for consumers with low purchasing power or because the cost of providing these services could not be covered by the market price. It is therefore the responsibility of public authorities to ensure that services of general interest are preserved when market forces cannot achieve this.

34. It should be noted that the term "services of general economic interest" is not defined in the Treaty. It covers the conventional (public) utilities such as provision of postal services, telecommunication services, gas, electricity etc. However, the concept has also been applied to provision of services in the transport sector which are not viable on its own or to the treatment of waste material. In practice, the Member States has a wide discretion to define the scope of what they consider to be services of general economic interest.

35. Article 106(2) TFEU can be invoked, and is indeed often invoked, by companies as a defence in Article 102 TFEU proceedings (they are more rarely invoked in Article 101 proceedings even if technically possible). However, the exception can equally be invoked by the Member States in proceedings where it is alleged that state measures are in violation of Articles 106(1) in combination with Article 101 or the State aid rules of Articles 107 and 108 TFEU.

36. Article 106(3) TFEU allows the Commission to specify the meaning and extent of the exception under Article 106(2) of the Treaty, and to set out rules intended to enable effective monitoring of the fulfilment of the criteria set out in Article 106(2), where necessary. The Commission may use the powers under Article 106(3) either to deal with existing infringements of the Treaty or to take steps to prevent future infringements. Following a ruling of the ECJ on the assessment of public service compensations in the context of EU state aid rules (case C-280/00 *Altmark Trans*), the Commission adopted in 2005 a decision on the basis of Article 106(3) TFEU clarifying the application of Article 106(2) to State aid in the form of public service compensation granted to certain companies entrusted with the operation of services of general economic interest. In March 2011, the Commission launched a broad debate on the review of its decision, which led to the adoption in December 2011 of a revised package of EU state aid rules for the assessment of public compensation for services of general economic interest (SGEI). The new package which applies to national, regional and local authorities alike covers all undertakings independent of the ownership structure. It clarifies key state aid principles and introduces a diversified and proportionate approach with simpler rules for SGEIs that are small, local in scope or pursue a social objective, while better taking account of competition considerations for large cases. Amongst others, the package describes the conditions under which certain systems of compensation are compatible with Article 106(2) and are not subject to the prior notification requirement of Article 108(3)¹⁴. Moreover, in order to avoid unjustified distortions of competition, the SGEI package requires that compensation does not exceed

¹³ OJ [1982] L 360/36, [1983] 1 CMLR 457 and case 41/83 *Italy/83 Italy v Commission* [1985] ECR 873, [1985]2 CMLR 368

¹⁴ Commission Decision of 28 November 2005 on the application of Article 106(2) of the EC Treaty to State aid in the form of public service compensation granted to certain undertakings entrusted with the operation of services of general economic interest (OJL 312, 29 November 2005, p. 76)

what is necessary to cover the costs incurred by the undertaking in discharging the public service obligations, account being taken of the relevant receipts and a reasonable profit¹⁵.

2.1.2 *When a State-related distortion of competition amounts to an infringement of the competition law, what powers do you have? Can you also rely on rules other than competition law? E.g. subsidy control or state aid laws, rules governing public service obligations, competitive neutrality frameworks?*

2.1.2.1 *EU rules on State aid control*

37. In describing the EU rules on State aid control, it is important to note from the outset, that the EU considers that rules on State aid, in an international context often referred to as "subsidies", are an integral part of EU the rules on competition. The Treaty on the functioning of the European Union reflects this, as section 2 on "aids granted by states" is a subsection of Title vii chapter 1 of the TFEU on "rules on competition". Therefore, the EU considers that any comprehensive discussion dealing with the "competition" aspects of competitive neutrality should also include a discussion on State aid control.

38. The EU system of State aid control is based on the principle of neutral treatment of all undertakings. It ensures that private and public undertakings do not receive public aid which would distort competition and intra-community trade.

39. Pursuant to Article 107(1) of the TFEU, "Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the common market."

40. Therefore like any "undertaking", public undertakings which are engaged in an economic activity are not authorised to receive State aid unless the aid is authorised by the Commission, as provided for in Article 108 TFEU.

41. State aid can take many forms: not just grants or interest rate rebates, but also loan guarantees, accelerated depreciation allowances, capital injections, tax exemptions etc. Further, the aid can be granted by national, regional or local authorities or by public bodies. In principle, they all fall under the prohibition of Article 107(1) TFEU.

42. In defining what constitutes "aid" the Commission applies the Market Economy Investor Principle (MEIP). MEIP is the logical corollary of the competitive neutrality principle. Pursuant to the neutrality principle, the Commission may neither penalize nor favour public undertakings. Therefore, if a public intervention in favour of a public or private undertaking engaged in economic activities (for instance a capital injection) is in line with what a private investor would do this intervention cannot be qualified as a State aid and is not subject to Commission's scrutiny.

43. Conversely, if the terms of the transaction are more favourable than those observed on the market for similar transactions, there is normally an advantage to the recipient and the presence of aid cannot be excluded. The market economy operator test will consist in comparing the price and conditions present in the case under examination, with the market price and conditions under which such a transaction is usually made for comparable undertakings in comparable situations (this is the "counterfactual analysis"). If the price and conditions present in the case under examination are in line with the market price and conditions, there is no advantage granted to the beneficiary and therefore no aid. The MEIP is applicable to all forms of public interventions involving State resources, including the forgoing of income. For instance, it applies to capital injections, granting of guarantees and loans and the sale of land, buildings, public assets or public companies.

¹⁵ The SGEI package: http://ec.europa.eu/competition/state_aid/legislation/sgei.html.

44. Pursuant to Article 108 TFEU, the European Commission is given the task to control State aid and Member States are required to inform the Commission in advance of any plan to grant State aid. Implementing new State aid without notification leads to such State aid being considered ‘unlawful’ and the Commission, or a national judge, may request the Member State to suspend such aid, or to take all measures necessary to recover such aid from the beneficiary. The Commission also has the power to review existing State aid, that is aid granted to an undertaking by a Member State prior to such Member State’s accession to the European Union. The Commission may at any stage find that, due to changing market conditions, such State aid is no longer compatible with the common market and has to be terminated.

45. The principle of incompatibility of State aid does however not amount to a full-scale prohibition. Articles 107(2) and 107(3) TFEU specify a number of cases in which State aid could be considered acceptable (the so-called “exemptions”). The existence of these exemptions also justifies the vetting of planned State aid measures by the Commission, as foreseen in Article 108 of the Treaty. The assessment of aid compatibility is essentially a balancing of the positive effects of aid (in terms of contributing to the achievement of a well-defined objective of common interest) and its negative effects (namely the resulting distortion of competition and trade). In order to be declared compatible, aid must be necessary and proportionate to achieve a particular objective of common interest. Aids which can be found compatible include for instance aid for environmental protection, aid for research and development and innovation or regional aid.

46. There are various examples where the Commission has found, specifically in respect of public undertakings, that the advantages granted to such undertakings by the government amounted to State aid and where it has subsequently implemented measures to ensure that competition is not distorted, thus ensuring a level playing field between public and private businesses.

47. In its judgement of 19 March 2013 in France Télécom (joined cases C-399/10 P and C-401/10 P) the ECJ ruled, in line with the Commission Decision and contrary to the ruling of the General Court, that the public declaration of support for France Télécom by the Minister for economic affairs and the subsequent shareholder loan by the French State entailed a transfer of State resources – and thus constituted State aid. Although the loan was not taken up by France Télécom, it conferred an advantage granted through State resources that could potentially have burdened the State budget.

48. In its decision relating to Electricité De France (EDF)¹⁶, the Commission found that thanks to its public-law status, EDF was enjoying an unlimited State guarantee and that this guarantee was incompatible State aid. The Commission decision required the guarantee to be removed.

49. The Commission does not only control aids granted by public authorities *stricto sensu* themselves. As resources of public undertakings can be considered as public resources, the Commission also checks that public undertakings do not grant undue advantages to their subsidiaries through cross-subsidies (for instance by fixing too low transfer prices). This prevents public undertakings from distorting competition on the markets on which their subsidiaries are active from funds raised through activities reserved for them or from overcompensation to discharge public service obligations.

50. In *Syndicat français de l'Express international (SFEI) v La Poste*¹⁷, the ECJ of Justice stated that the provision of logistical and commercial assistance by a public undertaking to its subsidiaries, which are governed by private law and carry on an activity open to free competition, is capable of constituting State aid within the meaning of Article 107 TFEU. The test is whether the remuneration

¹⁶ OJ L 49, 22 February 2005, p.9

¹⁷ Case c-39/94, *Syndicat français de l'Express International v La Poste* [1966] ECR I-3547

received in return for this assistance is less than that which would have been demanded under normal market conditions.

51. Finally, In *Chronopost*¹⁸ the ECJ stated that, in the absence of a market benchmark, the criterion, necessarily hypothetical, of "normal market conditions", must be assessed by reference to the objective and verifiable elements which are available. The costs borne by the undertaking when providing assistance can constitute such objective and verifiable elements. On that basis, there is no question of State aid to the subsidiary if it is established that the price charged properly covers all the additional, variable costs incurred by the provision of that assistance, including an appropriate contribution to the fixed costs arising from use of the postal network and an adequate return on the capital investment in so far as it is used for the subsidiary's competitive activity. Secondly, it has to be established that there is nothing to suggest that those elements have been underestimated or fixed in an arbitrary fashion.

2.1.2.2 *The Transparency Directive*

52. Apart from tools directly based on Treaty provisions, the EU has also adopted rules by means of secondary legislation in furtherance of the principle of competitive neutrality. In order to effectively apply EU competition policy and ensure that public undertakings are not granted more favourable treatment than their private counterparts, the Commission has to be able to ascertain what advantages these undertakings receive. For this purpose, the Commission issued the Transparency Directive. The Transparency Directive¹⁹ has two objectives.

53. The first objective is to ensure the transparency of financial flows between public authorities and public undertakings. As described earlier in this paper, the Transparency Directive defines 'public undertakings' as any undertaking over which the public authorities may exercise, directly or indirectly, a dominant influence by virtue of their ownership of it, their financial participation therein, or the rules which govern it.

54. The Transparency Directive recognises that, in order to ensure equal treatment of private and public undertakings through a fair and effective application of the Treaty rules, the complex financial relations between national public authorities and public undertakings must be made transparent.

55. Article 1.1 of this Directive thus provides that: "The Member States shall ensure that financial relations between public authorities and public undertakings are transparent as provided in this Directive, so that the following emerge clearly:

- a) public funds made available directly by public authorities to the public undertakings concerned;
- b) public funds made available by public authorities through the intermediary of public undertakings or financial institutions;
- c) the use to which these public funds are actually put."

56. Some examples of financial relations existing between public authorities and public undertakings that have to be made transparent are: the setting-off of operating losses, the provision of capital, non-refundable grants, or loans on privileged terms, the granting of financial advantages by

¹⁸ Joint cases C-83/01 P, C-93/01P and C-94/01P *Chronopost* [2003] ECR I-06993]

¹⁹ Commission Directive 2006/111/EC of 16 November 2006 on the transparency of financial relations between member States and public undertakings as well as on financial transparency within certain undertakings, OJ L 318, 17 November 2006, p. 17

forgoing profits or the recovery of sums due, the forgoing of a normal return on public funds used; and compensation for financial burdens imposed by the public authorities.

57. The second objective of the Directive is to ensure the transparency of the internal organisational and financial structure of (private and public) undertakings enjoying special/exclusive rights or entrusted with the operation of a service of general economic interest that receives public service compensation and that carries on other activities.

58. The main aim is to prevent those undertakings from cross-subsidizing commercial activities with funds raised through activities reserved for them or from compensation to provide public service obligations which would exceed the actual costs incurred in providing those obligations.

59. Article 1.2 of the directive provides that the "Member States shall ensure that the financial and organisational structure of any undertaking required to maintain separate accounts is correctly reflected in the separate accounts, so that the following emerge clearly: (a) the costs and revenues associated with the different activities and (b) full details of the methods by which costs and revenues are assigned or allocated to different activities".

60. Pursuant to Article 2, "undertaking required to maintain separate accounts" means any undertaking that enjoys a special or exclusive right granted by a Member State pursuant to Article 106(1) of the Treaty or is entrusted with the operation of a service of general economic interest pursuant to Article 106(2) of the Treaty, that receives public service compensation in any form whatsoever in relation to such service and that carries on other activities".

61. The requirements imposed by the Transparency Directive have proven to be efficient means by which fair and effective application of the rules of competition to public undertakings can be assured. For instance, they allow the Commission to check that public service compensations do not exceed the costs incurred in discharging the public service obligations and are not used to cross-subsidize commercial activities.

2.1.3 What other, non-enforcement powers do you have to tackle anti-competitive State measures? E.g. market studies, advocacy powers, regulatory intervention, control over public procurement processes, subsidy grants and bailouts?

2.1.3.1 Liberalisation

62. Services such as transport, energy, postal services and telecommunications have not always been as open to competition as they are today in the EU. The European Commission has been instrumental in opening up these markets to competition (also known as liberalisation).

63. In the EU Member States, services like these were previously the domain of national organisations with exclusive rights to provide a given service. Opening up these markets to international competition meant that monopoly rights at national level had to be abolished, a legal framework to allow new market entry as well as access to the networks had to be created and consumers had to be empowered to choose freely their suppliers throughout the EU.

64. For this purpose, the European Commission adopted a number of Directives, on its own and/or in cooperation with the Council and the European Parliament. The following sectors which were previously dominated by state monopolised industries were opened to competition:

- Transport (air, road, rail, inland waterways);
- Telecommunications;
- Postal services;
- Energy (electricity and gas).

65. Before liberalisation the provision of these public services had been ensured through state ownership of undertakings or via sector-specific regulation. The opening of the electricity and gas markets for Community-wide competition raised many concerns, mainly on the side of the beneficiaries of the previous market organisation, as to the future of these services and their quality²⁰. Potential entrants in the liberalised markets, on the other hand, feared that enterprises entrusted with public service obligations would be granted special rights or public funding which would give them an unfair advantage in the competition for customers.

66. However, the liberalisation of markets and the provision of public services neither exclude each other, nor are both objectives necessarily in conflict with each other. The Directives are a clear demonstration of this. They require Member States to open up their markets for all European competitors and, at the same time, confirm the existence of public services²¹. They leave the freedom of Member States to introduce public services untouched and intact. Some public services typical for the energy sectors are even mentioned in the Directives, e.g. the obligation of distributors to connect and supply all consumers in a given area²², or the duty of network operators to give priority to environmentally friendly or indigenous fuel-using power installations when dispatching generating installations²³.

67. The Directives rule also how the competition and public service objectives can co-exist with each other. Both refer in this regard to the Treaty and in particular Art. 106(2) TFEU. This means mainly that, if Member States wish to maintain or create new public services, they have to define and explicitly entrust enterprises with such a mission. It does not longer suffice to instruct State-owned companies to perform public services. Furthermore, any restriction of competition introduced by a Member State in order to support the performance of a public service must not exceed what is necessary to guarantee effective fulfilment of the mission²⁴.

68. In the railway, electricity and gas industries, the network operators are now required to give competitors fair access to their networks. In these industries, monitoring fair network access by all suppliers is essential to allow the consumer to choose the supplier offering the best conditions. In the two markets which were first opened up to competition (air transport and telecommunications), average prices have dropped substantially, due to increased competition.

69. The liberalisation of the markets does not guarantee the creation of a level playing field by itself. When markets are liberalised, the European Commission's State aid control should prevent Member States from granting aid which would effectively reverse the market opening.

2.2 Challenges

2.2.1 *What challenges do you face when applying competition law to a State-influenced activity or entity? Is there any difference if the State-induced restriction of competition is at Federal/central level or at a local level? Have you encountered any undue State pressure or involvement when scrutinising the conduct of a State-influenced activity or entity?*

70. Companies that have received incompatible State aid have had an economic advantage over their competitors, who had to operate without state funding. This distorts competition in the internal

²⁰ See Michael Albers, Energy Liberalisation and EC Competition law Fordham 28th Annual Conference of Antitrust Law and Policy , 26 October 2001

²¹ See Art. 3(2) Electricity & Gas Directive.

²² See Art. 10(1) Electricity Directive & Art. 9(2) Gas Directive.

²³ See Art. 8(3) (4) Electricity Directive

²⁴ See Commission, Communication on services of general interest, OJ C17, 19.1.2001, p. 8 paras 22,

market. To remedy the effects of this distortion, it is therefore important that the beneficiaries of incompatible aid pay this undue advantage back as soon as possible.

71. That is why Article 14 of Regulation n° 659/99 and the Notice on the implementation of decisions ordering the recovery of unlawful or incompatible aid (see IP/07/1609) provide that Member States should effectively recover the aid from the beneficiary without delay.

72. If a Member State does not implement a recovery decision, the Commission may refer the matter to the Court of Justice under Article 108(2) of the Treaty on the Functioning of the EU (TFEU) that allows the Commission to directly refer cases to the Court for violations of EU state aid rules.

73. If a Member State does not comply with the judgment, the Commission may ask the Court to impose penalty payments under Article 260 of the TFEU. There are numerous examples of cases, where the Commission had to refer the case to the Court of Justice.

74. For instance, in November 2013, the European Commission referred Germany to the ECJ for failing to comply with a Commission decision of January 2012 ordering the recovery of incompatible state aid from Deutsche Post (see IP/12/45 and MEMO/12/37). The Commission's decision had previously found that a combination of high regulated prices and pension subsidies granted by Germany gave Deutsche Post AG an undue economic advantage over competitors and was therefore incompatible with EU State aid rules. The Commission ordered Germany to recover the incompatible aid from Deutsche Post and abolish the relevant provisions for the future. As, almost two years after the Commission's decision, this had not been done, the Commission had to take follow-up actions. The beneficiaries of the aid and Germany have appealed the Commission's 2012 decision before the EU General Court (cases T-143/12 and T-152/12). These appeals are pending, however they have no suspending effect on the recovery of the aid.

75. In the area of antitrust similar challenges may come up when enforcing competition law against SOEs.

76. For instance, in 2008, the Commission requested Slovakia to re-open competition in the hybrid mail sector after deciding that an amendments to its postal legislation infringed EU Treaty rules on abuse of a dominant position (Article 102 TFEU) in conjunction with Article 106 TFEU. The amendment in question extended the monopoly of the incumbent operator, Slovenská Pošta, to the delivery of hybrid mail services, while this activity had until then been open to competition. As a consequence, Slovak postal operators which had already entered this market were prevented from continuing their activity and their economic viability was endangered. On 18 June 2008, the Commission asked Slovakia to clarify the amendments in question because it had doubts as to their compatibility with EU competition law (see IP/08/969). However, the replies had not dispelled these doubts. Therefore the Commission was forced to bring the case before the General Court, which confirmed the views of the Commission²⁵.

77. Pressure may arise from various sources and the European Commission adopts a neutral position as to the ownership or "nationality" of companies involved, irrespective of whether they come from within or outside the EU. As an example, in 2012, the European Commission opened antitrust proceedings against Gazprom (in which the Russian government owns a 50.002% controlling stake) in relation to its alleged conduct in a number of central and eastern European gas markets. The opening of the proceedings was due to the Commission's concerns that Gazprom may have and may be abusing its dominant position in upstream gas supply markets in central and Eastern Europe, in some of which Gazprom is virtually the sole supplier. Following the opening of investigation by the Commission, the Russian government adopted a decree prohibiting Gazprom from replying to information requests issued by the Commission. This has however neither prevented the investigation

²⁵ Judgment of the General Court of 25 March 2015 — Slovenská pošta v Commission (Case T-556/08)

from moving forward, nor prevented the Commission from treating SOEs like any other company and in this case from issuing a Statement of Objections²⁶.

3. Specific issues related to public and private competition enforcement

3.1 *Questions concerning the appropriateness and effectiveness of the legal standards which have been developed for private, profit-maximising companies. What obstacles do you face when applying turnover-based rules (for merger jurisdictional purposes) to the State as a market player? For example, what is the appropriate method for computing the "group turnover" in case of State-owned enterprises?*

78. Only operations with a European Union dimension fall within the exclusive competence of the European Commission (the "Commission"). Article 1 of the EU Merger Regulation (the "EUMR") sets out the thresholds that a concentration has to meet in order to be considered as having a Union dimension and therefore falling under the obligation to notify. Article 5 of the EUMR sets out the rules for calculating the turnover of the undertakings concerned for the purposes of determining jurisdiction and in case the undertaking concerned belongs to a group, its paragraph 4 establishes detailed criteria to identify undertakings whose turnover must be aggregated for these purposes.

79. In the case of acquisitions of undertakings by a State or by SOEs, special rules are needed to avoid that every concentration involving such undertakings would be caught under the EUMR. In these cases, Article 5(4) of the EUMR must be read in conjunction with the specific rule set out in Recital 22 of the EUMR²⁷, which provides that "in the public sector, calculation of the turnover of an undertaking concerned in a concentration needs, therefore, to take account of undertakings making up an economic unit with an independent power of decision, irrespective of the way in which their capital is held or the rules of administrative supervision applicable to them".

80. Therefore, when applying turnover-based rules in transactions involving a State or a SOE, account must be taken only of the turnover of the relevant economic unit with independent power of decision and of the undertakings for which the criteria in Article 5(4) are met with respect to such economic unit²⁸. In order to determine which are the relevant economic units to take into account, the Commission follows a two-step approach:

- first, to establish whether the undertaking in question has an independent decision-making power concerning its commercial activities,
- if this is not the case, to determine which is the ultimate State entity which enjoys such independent decision-making power and which are the other undertakings controlled by this entity, whose turnover will have to be included in the calculation.

81. The concept of an "economic unit with independent power of decision" was assessed in detail in the substantive assessment of the EDF/Segebel case²⁹. In that case, the Commission examined the possible risk of coordination between GDF Suez (Electrabel) and EDF due to the shareholding of the French State in both companies and concluded that there was no such risk given that EDF had an independent power of decision. The factors that the Commission took into account to reach this conclusion include the degree of interlocking directorships between undertakings owned by the same entity and the existence of adequate safeguards ensuring that commercially sensitive

²⁶ http://europa.eu/rapid/press-release_IP-15-4828_en.htm.

²⁷ See paragraph 192 of the Commission Consolidated Jurisdictional Notice (the "Jurisdictional Notice"), available at: http://ec.europa.eu/competition/mergers/legislation/draft_jn.html.

²⁸ See paragraph 193 of the Jurisdictional Notice.

²⁹ Case M. 5549, *EDF/Segebel*.

information is not shared between such undertakings. The Commission's reasoning in the EDF/Segabel case can also be applied to jurisdictional elements such as turnover calculation.

82. The above mentioned rules are applicable to all transactions involving SOEs both under the control of EU Member States and of third countries. In particular, those principles have been applied in recent years to a series of transactions involving Chinese SOEs. In this regard, it must be noted that the ownership of Chinese SOEs generally lies either with the central government (under the State Council) or under regional or municipal governments. SOEs under the central government's ownership report to the State-owned Assets Supervision and Administration Commission ("SASAC"), established directly under the State Council. SOEs owned by regional authorities report to about 30 regional-level SASACs.

83. One of the issues that might arise when examining those transactions is the actual relationship between central and local SASACs (and the companies under their ownership). However, this might have a limited relevance for the purposes of establishing jurisdiction in cases in which the turnover thresholds are already met by the Chinese SOE and the other undertakings concerned alone. This was the case in the China National Bluestar/Elkem transaction³⁰, where the Commission concluded that there was no need to decide whether the turnover of other companies owned by the Chinese State and reporting to SASAC should be taken into account, as the turnover thresholds were met on the basis of ChemChina's and Elkem's turnovers alone.

3.2 *What obstacles do you face when applying control-based rules in establishing whether two or more State-controlled players are independent from each other? For example, are three State-controlled companies responding to different Ministries considered as a single economic entity in a merger control context?*

84. The mere fact that two or more undertakings are owned by the same State does not necessarily mean that they belong to the same group for the purposes of merger control. In order to determine whether an acquisition of control by a State-controlled company over another company owned by the same State constitutes a notifiable concentration or an internal restructuring, paragraph 52 of the Jurisdictional Notice establishes that "*where both the acquiring and acquired undertakings are companies owned by the same State (or by the same public body or municipality) and forming part of different economic units having an independent power of decision, the acquisition of control of the latter by the former will be deemed to constitute a concentration*".

85. Therefore, also for the purposes of applying control-based rules, the key element that needs to be assessed is whether the undertakings concerned are parts of different economic units having an independent power of decision, despite being owned by the same State³¹. This will be the case when the entities in question have the power to determine their commercial conduct and commercial policy independently.

86. In light of the above, in order to assess whether three SOEs responding to different Ministries constitute independent economic units or a single economic entity for the purposes of merger control, account must be taken of whether their commercial policies are determined independently.

87. The reasoning above was applied by the Commission in the Neste/IVO case³², which consisted in the acquisition of sole control by the holding company IVO-Neste, owned by the Finnish

³⁰ Case No COMP/M.6082, *China National Bluestar/Elkem*.

³¹ See paragraph 153 of the Jurisdictional Notice.

³² Case No IV/M.931, *Neste/IVO*

State, over Imatran Voima Oy ("IVO"), also owned by the Finnish State³³. The Commission concluded that the second part of the transaction constituted a notifiable concentration for the following reasons:

- both Neste and IVO's operative matters were run independently by their respective operative managements,
- the Finnish State only exercised its ownership control in questions relating to its shareholding and not to the commercial conduct of the undertakings and
- there were no indications that the commercial conduct of Neste and IVO had been coordinated in the past.

3.3 *What obstacles do you face in designing remedies when the government has already negotiated or 'sealed' the deal? Which remedies have proven effective or ineffective when applied to State-influenced entities? What obstacles do you face in designing effective remedies and in monitoring compliance in this context?*

88. When it comes to remedies implementation, no major distinction should be drawn between cases involving SOEs and private undertakings, since obstacles in remedies implementation might arise in both cases.

89. The acquisition of ABN AMRO Asset by Fortis in October 2007 may serve as an example in this regard³⁴. On 3 October 2007 the Commission cleared the acquisition of certain assets of ABN AMRO by Fortis subject to some prior divestments. Subsequently, on 2 July 2008, Fortis, ABN AMRO and Deutsche Bank announced that they had signed an agreement by which Deutsche Bank would acquire the Divestment Business from ABN AMRO. In October 2008, the Dutch State acquired a controlling interest in the Dutch business of Fortis (and thereby also in ABN AMRO). The Dutch State tried to reopen the negotiation of the commitments but after extensive discussions with the Commission, it assumed in 2009 responsibility for the implementation of the remedies. In this type of cases, the acquiring entity (private/public undertaking or the State) inherits both the contractual and non-contractual obligations of the acquired undertaking, including possible merger remedies, following a conditional clearance decision.

90. Another interesting scenario that has arisen in recent years is the inter-play between merger and state-aid rules in the context of transactions involving undertakings which have received rescue and restructuring aids. As the involvement of the State is prominent in these transactions, close contacts need to be established between the State and the Commission.

3.4 *What obstacles do you face when applying turnover-based rules (e.g. for calculating corporate fines to the State as a market player)? For example, if the maximum sanction is turnover-based, how is this computed when fining a State-owned company?*

91. When applying turnover based rules to impose fines on state owned companies the Commission applies its standard approach as set out in the its Guidelines on Fines. The fine would be based on state owned entity's turnover (value of sales) of goods or services to which the infringement directly or indirectly relates in the EEA. For the purposes of calculating the legal maximum sanction

³³ The transaction was structured in two parts: first, all Neste shares (the 83.17% owned by the Finnish State and the remaining shares held by minority shareholders), were transferred to IVO-Neste, a holding company set up for the purposes of implementing the transaction between the two State-owned companies. The second part consisted in the acquisition by IVO-Neste of all the IVO shares (95.6% of which were held by the Finnish State).

³⁴ Case M.4844 - Fortis /ABN AMRO Asset.

the Commission would normally use the worldwide turnover of the highest incorporated legal entity which controlled (exercised decisive influence) over the infringing state owned company.

3.5 *What obstacles do you face when applying control-based rules in establishing whether two or more State-controlled players are independent from each other? For example, are three State-controlled companies responding to different Ministries considered as a single economic entity when applying cartel rules?*

92. Generally, in cartel cases we have not faced significant obstacles involving state owned companies as the standard rules on control, as outlined above, apply. It would be unusual to find 'sister' companies responding to different ministries to be involved in a cartel concerning the same product but if such a scenario were to arise, separately incorporated state controlled companies would be regarded as separate legal entities in the absence of any legally incorporated controlling parent.

4. Concluding remarks

93. The EU considers that there would be merit for the OECD Competition Committee to further examine the different definitions of competitive neutrality which are currently in use and to explore in close contact with the delegates and other OECD Committees which are active in this field whether a consensus can be found on a definition which is broad enough to contain all constituting elements.

94. An agreed definition would facilitate possible follow-up discussions, which, amongst others, could explore support from delegates for an OECD instrument on competitive neutrality, essentially recommending that competition rules should be based on the principle of competitive neutrality.