FIDE 2010 – National Report for the United Kingdom

DRAFT of 14 December 2009

Topic 3.

Public Capital and Private Capital in the internal market –
Securing a level playing field for public and private enterprises

Wolf-Georg Ringe*

A. Constitutional law or other fundamental/framework laws

At Member State level, it is, first of all, interesting to ask the question whether there are rules that require that certain activities to be performed by the State and/or to remain in the public sector. The Constitutions of some Member States contain such rules.

Q 13.Please state whether the Constitution of your Member State contains rules that require certain goods or services to be provided by the government. **Q 14**. Are there special laws that lay down similar requirements? The term special laws refers to laws that have a special hierarchical nature in the sense that they have priority over ordinary laws. **Q 15.** Does the Constitution of your Member State contain guarantees that certain activities are reserved for the private sector?

Q 13-15: The UK does not have a written constitution, nor does its legal system provide for special laws which are hierarchically on a higher level than normal statutes. There is a body of unwritten constitutional conventions as well as two statutes which have priority over ordinary laws (the Human Rights Act 1998 and the European Communities Act 1972), but these do not cover rules concerning goods or services to be provided by the government. Consequently, the decision on whether or not certain activities are carried out by the public or private sector is political decision only, without any legal constraints.

---

* Dr Wolf-Georg Ringe, Lecturer in Law, University of Oxford; Deputy Director, Institute of European and Comparative Law, email: georg.ringe@law.ox.ac.uk. I have benefitted from conversations with colleagues and have received input from the Department of Business, Innovation & Skills and from HM Treasury. In particular, I would like to thank Stephen Amos, Paul Berman, Ulf Bernitz, Paul Craig, Ariel Ezrachi, Heike Schweitzer, Susan Smith, Philippa Watson, Stephen Weatherill and Katja Ziegler.

Q 16. Are there any rules that prohibit nationalising undertakings or certain sectors of the economy? **Q 17**. Are there rules that subject nationalising to procedures or specific rules? **Q 18**. Are there, in the absence of such rules, other procedures or mechanisms that have to be followed for the nationalisation of undertakings? **Q 19**. Are there rules for the acquisition or sale of shares of enterprises by the government? **Q 20.** Are these rules different depending on whether the acquisition leads to control or not? And do different rules apply to a sale leading to a loss of control?

Q 16-20. There are no rules prohibiting the nationalisation of undertakings and no general procedural rules concerning a nationalisation. Nor does the UK have rules on the sale of government-owned shares. All of these issues are at the discretion of the government. Of note is the controversial sale of shares in the 1980s privatisation programme, in which it was claimed that the formerly state-owned companies were sold too cheaply, and consequently the proceeds to the government were therefore too low.[1] However, there was no legal mechanism to enforce this claim or even no procedure to invoke it.

To this general proposition, one exception exists: partial provisions have been recently made for the banking sector: the Banking Act 2009[2] contains specific provisions for the nationalisation of 'banks', as defined in s 2 of the Banking Act, in very limited circumstances. The conditions to be fulfilled are that the bank is failing, and no reasonable prospect exists that it will be able to remain viable, plus that a serious threat to the stability of the financial system of the United Kingdom exists or that the nationalisation is necessary to protect the public interest.[3] The Banking Act 2009 also enables the Bank of England to transfer the business (in whole or in part) of a deposit taker to a company wholly owned by the Bank of England ('bridge bank') or to a private sector purchaser. This legislation was introduced following the financial crisis in 2007/08 and replaced the temporary Banking (Special Provisions) Act 2008.[4]

Q 21. Are contracts concluded by state-owned enterprises subject to normal civil law? Please specify.

Within the boundaries of public procurement, English law does not distinguish in principle between public and private law contracts in the manner that is common within most civil law legal systems.[5] There is no such thing as a distinct 'law of public contracts'. Since public corporations are normally not 'servant or agent of the Crown', they are consequently subject to the normal rules of the law in such matters as contractual and tortuous liability in almost the same way as a commercial company or a private person.[6] One of the tenets of the interpretation of English law to the effect that a statute shall not bind the Crown unless it is expressly so provided[7] consequently does not entitle state-

[1] J Vickers and G Yarrow, *Privatization: An Economic Analysis* (MIT Press, Cambridge Mass 1988) 171 ff.
[2] The Banking Act 2009 (c. 1) entered into force in part on 21 February 2009.
[3] Banking Act 2009, ss 7, 9.
[4] See in detail R Tomasic, 'Creating a template for banking insolvency law reform after the collapse of Northern Rock' [2009] Insolvency Intelligence 65; A McKnight, 'The Banking Act 2009' (2009) 4 Law and Financial Markets Review 325.
[5] P Craig and M Trybus, 'Public contracts: England and Wales' in R Nogouellou and U Stelkens (eds), *Traité de droit comparé des contrats publics/Comparative Law on Public Contracts Treatise* (Bruylant, Brussels 2010) forthcoming.
[6] JF Garner, 'Public Corporations in the United Kingdom' in W Friedmann and JF Garner (eds), *Government Enterprise – A Comparative Study* (London, Stevens & Sons 1970) 3, 5.
[7] *Willion v Berkley* (1561) 1 Plowd 227.

owned enterprises to any special position. A prior existing different regime of limitation applicable to the liability of public corporations was abolished as early as 1954.[8]

This analysis concerns above all the 'contract management' phase, ie the phase after the contract has been concluded. This phase is, broadly speaking, subject to the same contract law as the contracts of private parties.[9] In contrast, the (prior) phase leading to the award of public contracts and the basis on which contracts are awarded is subject to public procurement regulation, heavily influenced by European public procurement law.[10]

Even for the 'contract management' phase, however, there are certain rules or principles of contract law that apply in a modified version. Most of these rules take the form of 'soft law' (guidance, communications etc): For instance, government departments have developed principles on the objectives to be pursued by government contracts.[11] These principles, although not legally binding, nonetheless de facto provide a framework within which public contracts are made. Moreover, government departments lay down 'model conditions' for public contracts, which specify in considerable detail matters such as the provisions of the services and payment; liabilities; compliance with legal obligations; control of the contract; default, breach and termination; and finally dispute resolution.[12] These 'conditions' often form the basis for the standard terms found in public contracts. Hence, it is fair to say that these two pillars – principles and model conditions – perform a function coming close to a separate 'public law of contract'.

Apart from this general framework, exceptions exist where a public corporation is required by the statute to act for and on behalf of (a Minister of) the Crown.[13] These statutory provisions are rare and, for the most part, historical.[14] These exceptions concern mostly procedural rights in litigation – eg in respect of documents, choice of venue, freedom from liability to an injunction or a prerogative order etc, but not proper contract or tort law. Moreover, other exceptions may exist where statutes confer special privileges on a particular public corporation in an attempt to enable these corporations to perform their statutory function efficiently.[15]

Finally, one important qualification has to be made. Unlike natural persons, public corporations are all subject to the *ultra vires* doctrine. This may be described as a check on the constitutional power of a public body: a legal person created by statute can execute only those functions that it is expressly or by necessary implication empowered to do by its constituent statute.[16] In the local government context, this principle is given statutory form in the shape of s 111 of the Local Government Act 1972. The principle, however, is not entirely free from problems and is far from offering a comprehensive control on public bodies.[17]

---

[8] Law Reform (Limitation of Actions) Act 1954. Cf WA Robson, *Nationalized Industry and Public Ownership* (2nd edn, Allen & Unwin, London 1962) 69.
[9] S Arrowsmith, *The Law of Public and Utilities Procurement* (2nd edn, Sweet & Maxwell, London 2005) 9.
[10] For details, see Craig and Trybus (n 5).
[11] These principles have chiefly been developed by the Office of Government Commerce (OGC) <www.ogc.gov.uk>.
[12] HM Treasury Central Unit on Procurement, *No. 59D: Documentation: Model Conditions of Contract* (July 1997); Office of Government Commerce, *Procurement Policy Guidelines* (2001).
[13] See eg *Nottingham No 1 Area Hospital Management Committee v Owen* [1958] 1 QB 50; *Tamlin v Hannaford* [1949] 2 All ER 327 (concerning British Railways).
[14] For instance the Regional Hospital Boards and the Hospital Management Committees established by the National Health Service Act 1946.
[15] Garner (above n 6) 11.
[16] Garner (above n 6) 12.
[17] See A Davies, 'Ultra vires problems in government contracts' (2006) 122 Law Quarterly Review 98 ff.

Q 22. Is there a rule or practice that one ministry is responsible for enterprises that are controlled by the government or are there different ministries responsible according to their sectoral responsibilities?

Historically, the ownership of state-owned enterprises has been dispersed among a wide number of ministries.[18] For each public corporation or each company in which the Government has a financial interest, one sector-specific ministry is responsible. For example, the Government's stakes in BNFL plc are managed by the Department for Business, Innovation and Skills, whereas Northern Rock plc is run by HM Treasury. All together, these companies are under the responsibility of twelve different Departments, Ministries or Offices.

Alongside these responsibilities, however, the British Government has established a central body, called the 'Shareholder Executive', responsible within the Government for managing the government's financial interest in a range of public companies.[19] Originally established within the Cabinet Office in 2003, it has since 2004 been part of the now so-called Department for Business, Innovation and Skills (and its predecessors, the Department of Trade and Industry [DTI] and the Department for Business, Enterprise & Regulatory Reform [BERR]). It is staffed by civil servants, many of whom are corporate finance professionals with private sector experience. The Shareholder Executive currently manages a portfolio of 26 businesses, with a combined turnover of around £20 billion. It either advises Ministers directly ('directly managed') or advises shareholder teams in shareholding departments ('advisory').

Moreover, since the end of 2008, the Government's shares in UK banks are managed by UK Financial Investments Ltd (UKFI)[20]. UKFI is a regular company, formed under the Companies Act 2006, with HM Treasury as its sole shareholder. The company's activities are governed by its board, which is accountable to the Chancellor of the Exchequer. Currently, UKFI holds stakes in various banks including the Royal Bank of Scotland (RBS), Lloyds TSB/Halifax Bank of Scotland (Lloyds Banking Group), Northern Rock and Bradford & Bingley.

Q 23. Are there rules that restrict the possibilities for other governmental bodies, states, provinces, municipalities etc. to participate in the capital of private enterprises?

Because of the lack of a (written) constitution, as discussed above, there are generally no limits for public investments in private enterprises. Two important qualifications have to be made, however: one concerns the *ultra vires* doctrine, which limits the powers of public bodies generally, and procedural rules for local authorities, aiming at guaranteeing efficient spending of taxpayer's money.

As described above, public bodies are subject to the *ultra vires* doctrine. This may be described as a check on the constitutional power of a public body: a legal person created by statute can execute only those functions that it is expressly or by necessary implication empowered to do by its constituent statute.[21] Therefore, a contract that goes beyond the limits imposed by the statute will be unenforceable.[22] In the local government context, this principle is given statutory form in the shape of s 111 of the Local Government Act 1972. This provision states: '[…] a local authority shall have power to do any thing (whether or not involving the expenditure, borrowing or lending of

[18] OECD, *Corporate Governance of State-Owned Enterprises – A Survey of OECD Countries* (2005) 44.
[19] The Shareholder Executive has a website at <http://www.shareholderexecutive.gov.uk/>. See also OECD (n 18) 53.
[20] <http://www.ukfi.gov.uk/>.
[21] Garner (above n 6) 12.
[22] *Crédit Suisse v Allerdale Borough Council* [1997] QB 306*; Crédit Suisse v Waltham Forest London Borough Council* [1997] QB 362.

money or the acquisition or disposal of any property or rights) which is calculated to facilitate, or is conductive or incidental to, the discharge of any of their functions.' The principle can be highlighted by the famous *Hazell* case[23], where a local authority was held to have no legal power to enter into speculative interest rate swap contracts, which would result in profits or losses depending upon movements in interest rates.[24] The local authority which relies on its own illegal conduct in order to evade its contractual obligations can lead to unfair results[25] and may even constitute a breach of the European Convention of Human Rights (right to property).[26]

For local governments, we find further regulation on how local authorities provide services in legislation. The current approach is based on the 'Best Value' regime, adopted by the new Labour Government in 1997.[27] This regime replaced the old 'compulsory competitive tendering' system with a strategy designed to secure the efficient and effective provision of local services, while preserving greater local autonomy and choice.[28] In order for Local Authorities to be measured against Best Value, so-called Best Value Performance Indicators (BVPIs) were introduced.[29] They are a statutory set of 90 indicators developed by Government Departments to measure the performance of local authorities, that is, all local authorities must measure themselves against BVPIs. The data is collected and audited annually by the Audit Commission. Where a local authority fails to meet a statutory target, the Secretary of State may take action, particularly where an authority is not meeting its duty of continuous improvement. In practice, the Secretary of State can direct the Council to take specific action to secure improvement, or, in extreme cases, remove the function(s) concerned from its control altogether. The whole regime was overhauled in 2007[30] in order to reduce the regulatory burden imposed by the 1999 Act on local authorities.[31]

Q 25. Has there been any discussion about the need to have recourse to Article 295 EC (now Article 345 TFEU) for the protection of national public interests?

The UK government had tried to defend its position with regard to its 'golden' shareholding in the British Airport Authority (BAA) *inter alia* with reference to (then) Article 295 EC.[32] Since this strategy turned out to be unsuccessful, no further attempt has been made to rely on (now) Article 345 TFEU, nor did any discussion about the role of this provision take place.

The prevailing view in the academic literature is to interpret Article 345 TFEU narrowly. In essence, Article 345 TFEU only limits the application of the Treaties to the way in which Member States deal

[23] *Hazell v Hammersmith and Fulham London Borough Council* [1992] 2 AC 1.
[24] Davies (n 17) 101.
[25] This was recognised in *Stretch v West Dorset District Council* (2000) 2 LGLR 140.
[26] *Stretch v United Kingdom (44277/98)* (2004) 38 EHRR 12.
[27] See on this P Craig *Administrative Law* (6th edn, Sweet & Maxwell, London 2008) para 5-021.
[28] Department of the Environment, Transport and the Regions, *Modernising Local Government: Improving Local Services through Best Value* (1997).
[29] Local Government Act 1999, s 4.
[30] Local Government and Public Involvement in Health Act 2007. See on this S Bailey and M Elliott, 'Taking local government seriously: democracy, autonomy and the constitution' (2009) 68 Cambridge Law Journal 436, 463 ff.
[31] Department for Communities and Local Government, *Strong and Prosperous Communities – The Local Government White Paper Implementation Plan: One Year On* (2007), paras 26 ff.
[32] Opinion of Advocate General Ruiz-Jarabo Colomer delivered on 6 February 2003 on cases C-463/00 and C-98/01 *Commission v Spain* and *Commission v United Kingdom* para 17.

with the system of ownership of undertakings.[33] In other words, it can be seen as a sort of EU agnosticism as to the regime of ownership within any particular state.[34]

Although Article 345 TFEU does not call into question Member States' right to establish a system for the acquisition of property, such a system remains subject to the fundamental rules of EU law, including those of non-discrimination, freedom of establishment and free movement of capital.[35] The UK Government's view is, therefore, that it is not obvious that Article 345 TFEU has any real role to play in nationalisation decisions.

[33] P Crag and G de Búrca, *EU Law – Text, Cases, and Materials* (4th edn, OUP 2007) 1071; A Arnull and others, *Wyatt and Dashwood's European Union Law* (5th edn, Sweet & Maxwell, London 2006) paras 26-002, 26-007.
[34] See recently B Akkermans and E Ramaekers, 'Article 295, its meanings and interpretations' (2009) 15 Eur L J forthcoming.
[35] See eg Case C-452/01 *Margarethe Ospelt and Schlössle Weissenberg Familienstiftung* [2003] ECR I-9743 para 24.

B. Company law

The rules of company law of a Member State can be seen as the basic charter for private business, outlining the rules of the game for the market sector. The rules may contain specific features that impact on the distinction between private and public capital. The following questions are designed to draw out such features.

Q 26. What was the reaction to the ECJ judgments in the *Golden Share* cases in your Member State? Have there been measures taken to amend legislation?

The golden share cases were met with mostly approval, but also with a certain indifference. Most of the discussion took place after the ECJ judgment on the UK golden share in BAA (British Airports Authority) had been handed down. A typical comment came from Mike Hodgkinson, former CEO of BAA, who stated that the abolition of the golden share in BAA 'should have no effect on the way that we manage our relationships with Government, investors and all other stakeholders'.[36]

The government, which has fought hard to keep the BAA golden share, said it accepted the judgment and announced a review of the situation at BAA and other golden shares.[37] In September 2003, the UK Government announced that it would redeem its golden share in BAA; at the same time, the company stated it would remove the golden share from its articles of association.[38] Following the ECJ ruling, the UK government undertook a review of the special shares held in several energy companies and redeemed several of them, including National Grid Transco, Scottish Power, Scottish and Southern Energy and Ireland's Viridian Group and Phoenix Natural Gas. However, in the years following the BAA case, the UK has still been using golden shares in a range of other companies. Such companies in which the government retains a golden share until today include British Energy, BAE Systems and Rolls-Royce. In the case of British Energy, the UK held a golden share ensuring that no investor could hold more than 15% of the shares and that BE could not dispose of any of its nuclear power stations without the consent of the relevant Secretary of State. Following the BAA case, this was amended so as to ensure that UK Government consent can only be refused on the grounds of national security.[39] This special share was retained even after the take-over by Electricité de France (EdF) in early 2009.[40]

The latter two companies are within the sensitive defence sector. Rolls-Royce makes reactors for Britain's nuclear submarines, while BAE is behind most of the country's advanced weapons systems (including Eurofighter and the Type 45 frigate). Through its golden share – expressed by special clauses in the companies' articles of association – the government is still exercising controls within both companies. Until 2002, foreign investors were prevented from owning more than 49.5% of either group. Individual foreign shareholders or groups deemed to be acting in concert are still barred from holding more than 15% each. There are also restrictions on the companies' leadership. A majority of directors must be British, as should the most senior executive director. In 2008, the two companies applied to the government to abolish the nationality requirement for their directors.[41]

---

[36] BAA press release of 3 June 2003, www.baa.com.

[37] A Osborn, 'State's golden share in BAA is illegal – Takeover shield scrapped' *The Guardian* (London, 14 May 2003).

[38] M Harrison, 'Government to redeem golden share in BAA' *The Independent* (London, 17 September 2003).

[39] SEC Report of 5 May 2004, <http://www.secinfo.com/d14Bmp.1p2.htm>.

[40] Economist Intelligence Unit, 'The operating environment: State role in the economy' 23 October 2008 p 10; cf <http://www.shareholderexecutive.gov.uk/performance/britishenergy.asp>.

[41] J Waples and D O'Connell, 'Rolls-Royce and BAE in secret plea to Downing Street' The Times (London, 16 March 2008). Cf also <http://www.theregister.co.uk/2008/11/19/turner_parliamentary_evidence/>. However, the new CEO of BAE Systems, Ian King, is a British national.

Another golden share is found in the National Air Traffic Services group. The government partly privatised this service in 2001 by selling 46% of the shares to the Airline Group, a consortium of seven British airlines plus BAA. Another 5% was allocated to staff, and the government retains 49% plus a golden share which gives it veto power over changes in control of the company or in its articles of association, including the ability to set limits on particular shareholdings.[42]

As is well-known, the rules on the internal market also include harmonisation of legislation. In the area of company law, directives on harmonisation of national company law rules have had a major effect. **Q 27**. Have there been any specific characteristics of the company laws of your Member State that were deemed to be imperiled by the EC company law directives? E.g. the German system of co-determination (*Mitbestimmung*).

British company law is of a very flexible nature and leaves most of the internal matters to the discretion of the company. In general, therefore, it is fair to say that most of the harmonisation directives have not had an exceptional influence on English company law.[43] This may be illustrated by the example of the third and sixth company law directives on mergers[44] and divisions[45]: These directives have been duly implemented in the Companies Act, but are hardly ever used in practice. Instead, English companies tend to make use of the scheme of arrangement procedure (ss 895 ff CA 2006) or prefer a takeover (ss 942 ff CA 2006) over a merger.

A few exceptions are noteworthy. First, the second company law directive[46] stands out from the other directives in that it provides for a mandatory system of capital requirements for public limited companies. Historically, British law had not attached much significance to minimum capital rules, and the private limited company still does not require any minimum capital for an incorporation. However, as a result of the Second Directive, a minimum capital requirement was introduced for public companies. It was set at a level of £50,000, which is above the level required by the Directive. Moreover, the Second Directive tightened the rules on dividend distributions and introduced other changes, all of which are now very controversial in practice and in the academic literature.[47]

Secondly, but less controversially, the first company law directive[48] triggered a review of the common law rules on *ultra vires* and agency as they apply to companies.[49] This directive has equally shaped

---

[42] Economist Intelligence Unit (n 40).

[43] The substantive content of these directives is often said not to very demanding, see L Enriques, 'EC Company Law Directives and Regulations: How Trivial Are They?' (2006) 27 U of Pennsylvania J of Intl Economic L 1.

[44] Third Council Directive (EEC) 78/855 of 9 October 1978 based on Article 54(3)(g) of the Treaty concerning mergers of public limited liability companies [1977] OJ L295/36.

[45] Sixth Council Directive (EEC) 82/891 of 17 December 1982 based on Article 54(3)(g) of the Treaty concerning the division of public limited liability companies [1982] OJ L378/47.

[46] Second Council Directive (EEC) 77/91 of 13 December 1976 on coordination of safeguards, which for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, in respect of the formation of public limited liability companies and the maintenance and alteration of their capital, with a view to making such safeguards equivalent throughout the Community [1977] OJ L26/1, as amended by Directive 2006/68/EC [2006] OJ L264/32 ('Second Directive').

[47] See, eg, J Payne, 'Legal Capital in the UK following the Companies Act 2006' in J Armour and J Payne (eds), *Rationality in Company Law: Essays in Honour of DD Prentice* (Hart Publishing, Oxford 2009) 123.

[48] First Council Directive (EEC) 68/151 of 9 March 1968 on co-ordination of safeguards which, for the protection of the interests of members and others, are required by Member States of companies within the meaning of the second paragraph of Article 58 of the Treaty, with a view to making such safeguards equivalent throughout the Community [1968] OJ L65/8.

[49] PL Davies, *Gower and Davies' Principles of Modern Company Law* (8th edn, Sweet & Maxwell, London 2008) para 7-2.

the legal framework for companies in the UK, but is nowadays accepted and no longer seriously contested.

Finally, there are a few projects that were not adopted but would have had an immense effect on English company law. They are fiercely and almost unanimously rejected, because they would reach to the heart of British company law. They are the proposals for the 5th and the 9th directives[50] and the project of introducing a mandatory one-share-one-vote rule in the EU[51]. These proposals were met with strict opposition, equally vehement as any attempt to touch upon the *Mitbestimmung* in Germany. The main concern seems to be that they are mandatory and thus deviate from the traditional self-organisatorial approach which British law has chosen. Unlike these proposals would have prescribed, British companies are free to decide on their board structure, employee involvement or shareholder voting rights. The British lobbying in Brussels seems to have been successful, since these three projects are no longer discussed.

Q 28. Do the national company rules provide guarantees that secure a level playing field when the government pursues its objectives by way of undertakings which it controls wholly or partially? Please note that such guarantees may (also) be found in specific regulation as referred to above in section A Q 16-20.

British company law does not distinguish between the State or private parties as shareholders.[52] This implies that there are no specific provisions for the State as a market actor nor are there any 'guarantees' to secure a level playing field.

Private shareholders must refer to the general instruments of minority protection if they feel discriminated against. These are, above all, the derivative action (ss 260 ff CA 2006) and the unfair prejudice remedy (ss 994 ff CA 2006). The derivative claim may be brought by individual shareholders on behalf of the company in respect of a cause of action arising from certain wrongs done to the company. A minority shareholder can also claim 'unfairly prejudicial' conduct and seek a remedy under s 996 CA 2006. These are the two major remedies for minority protection, they are open to all shareholders.

Apart from these general minority protection tools, the British legal system has tried to develop separate mechanism to avoid conflicts upfront and not wait until litigation is needed. These are attempts to overcome the traditional, well-known corporate governance problems that state-owned enterprises face.[53] There are, for instance, procedures in place to mitigate the political influence in connection to appointment of board members. Since 1995, a Commissioner for Public Appointments regulates the processes by which Ministers make appointments to the boards of national and regional public bodies, including non-departmental public bodies and public corporations. There is a

---

[50] The fifth directive concerned the controversial topics of board structure and employee involvement, the ninth directive dealt with groups of companies. See on both Davies (n 49) para 6-9; S Grundmann, *European Company Law – Organization, Finance and Capital Markets* (Intersentia, Antwerpen and Oxford 2007) § 12 and § 31.

[51] On this project, see Commission, *Impact Assessment on the Proportionality between Capital and Control in Listed Companies of 12 December 2007*, SEC(2007) 1705; ISS Europe, ECGI, Shearman & Sterling, *Report on the proportionality principle in the European Union* (18 May 2007); G Psarakis, 'One Share – One Vote and the Case for a Harmonised Capital Structure' (2008) 19 Eur Business L Rev 709. On the decision to abandon the project, see the speech by Commissioner McCreevy at the European Parliament's Legal Affairs Committee, 3 October 2007, Speech/07/592.

[52] OECD (n 18) 71.

[53] See on this S Estrin, 'State Ownership, Corporate Governance and Privatisation' in OECD, *Corporate Governance, State-Owned Enterprises and Privatisation* (OECD 1998) 11, 15 ff.

specific ‘Code of Practice’ in place; the most recent version is from August 2009.[54] The aim of this Code is to guarantee that public appointments should be governed by a selection based on merit. The selection has to be scrutinised by an independent panel. Moreover, the Code guarantees equal opportunities, openness and transparency as well as proportionality.[55]

Moreover, companies like Network Rail and Glas Cymru[56] are subject to incentive regulation to overcome the problem that they have no shareholders. So-called performance-related pay (PRP) schemes seek to provide incentives to managers to improve the performance of the companies.[57] PRP ties managerial pay to company performance. In private for-profit organisations, equity-based pay or stock options link remuneration to the company’s profitability. However, management pay can also be linked to quality, safety, service delivery or other aspects of the company’s financial performance. But to be effective, the financial incentives need to be both well aligned with the objectives set for an organisation and of sufficient value to provide a real incentive to management.[58] There are two key characteristics of these schemes. The first is a high level of transparency not only in their internal operation, but details of the schemes are made available to their customers and the public at large via the companies’ websites. The second is that the schemes align the incentives of management with the interests of customers. These are critical elements which must be adhered to if such schemes are to be utilised. Additionally, in the case of Network Rail, it is the regulator which requires that the entity operate such a scheme under the terms of Network Rail’s Licence. While Network Rail determines the structure of the scheme it is subject to confirmation by the regulator that it meets the licence’s requirements.

Another, more recent, example is Bradford & Bingley plc, a victim of the recent financial crisis. Bradford & Bingley’s shares were delisted on 29 September 2008 and transferred to HM Treasury. As a consequence, the full requirements of the Listing Rules[59] and the Combined Code on Corporate Governance[60] no longer apply to the company. To this end, the company and HM Treasury drafted a ‘Framework Document’, intending to operate a corporate governance structure which mimics as far as possible best practice for a listed company, including the Combined Code.[61] This document describes for instance board structure and governance and provides for a framework on board appointments. A framework document is a frequent and common tool for mitigating problems of corporate governance and is found in many partly or wholly government-owned companies.

---

[54] The Commissioner For Public Appointments’ Code of Practice for Ministerial Appointments to Public Bodies (August 2009), available at <http://www.publicappointmentscommissioner.org/Code_of_Practice/>.
[55] OECD (n 18) 134.
[56] Network Rail is the company which runs, maintains and develops Britain’s rail track, signalling system, rail bridges and tunnels etc. Glas Cymru is the company which owns Dwr Cymru, the Welsh Water Company. Both companies are private companies limited by guarantee, which means there are no shareholders but members who do not have ownership interests in the company. Both Glas Cymru and Network Rail are debt financed. However, part of Network Rail’s debt is backed by a Financial Indemnity (Government Guarantee).
[57] See in more detail J Bennett E Iossa and G Legrenzi ‘The Role of Commercial Nonprofit Organizations in the Provision of Public Services’ (2003) 19 Oxford Rev Of Economic Policy 335.
[58] A UK study found that PRP has a positive and significant impact on financial performance and labour productivity for UK listed firms, see MJ Conyon and RB Freeman, ‘Shared Modes and Firm Performance – UK Evidence’ in D Card and others (eds), *Seeking a Premier Economy: The Economic Effects of British Economic Reforms, 1980-2000* (NBER 2004) 109.
[59] UKLA, *Listing Rules*, available at <http://fsahandbook.info/FSA/html/handbook/LR>.
[60] Financial Reporting Council, *Combined Code on Corporate Governance*, available at <http://www.frc.org.uk/corporate/combinedcode.cfm>.
[61] The Framework Document is available at <http://www.bbg.co.uk/bbg/siteware/bb_sh_frame.pdf>.

Q 29. Are there rules that allow or oblige the government to make use of a special form of company if it wants to pursue public interests?

The UK Government can choose from various legal forms for pursuing its public interest objective via a separate body. There is no legal obligation to choose a particular legal form, but in some situations it might be more appropriate to prefer one legal form over the other. There are different legal forms and different classifications of such entities, both of which however do not necessarily need to coincide.

Legal Form

The government has the choice between various different legal forms. The most important of these are the following:

(1) Companies: Regular companies are set up under the Companies Act 2006 and thus have the same standard formal governance framework as private sector companies and are required to report to the same standards. The government has a range of shareholding percentages from 100% down to 33%. Public Bodies incorporated as companies limited by shares are rare and are set up expressly for trading purposes.

An alternative is the company 'limited by guarantee',[62] a variant of the company which may be regarded as particularly suitable for enterprises which carry out a not-for-profit activity. They are normally formed for charitable or for other non-trading purposes, although they may carry out some trading activities. Many Public Bodies constituted in this way are financially self-sufficient and do not receive grants-in-aid.

Incorporating a public body as a company can be relatively easy and straightforward. It is likely to be appropriate where:

- a body requires corporate status to give it legal personality but departmental expenditure is insufficient to justify new legislation;
- a corporate body is needed temporarily (eg for a short-term task such as a collaborative promotional venture which would not warrant legislation) or provisionally pending a decision whether it should continue on a statutory basis; or
- a body is set up as a limited company prior to privatisation, with assets transferred to it by enabling legislation.

(2) Statutory Corporations: A company can be incorporated by means of an act of Parliament or by charter granted by the Crown. These corporations are formed under specific legislation which, in the main, replicates or mimics the Companies Act. Additionally, s 1043 of the Companies Act 2006 and the relevant secondary law apply some provisions of the Companies Acts to such companies.[63]

On 31 March 2009, there were 47 companies in existence formed under specific Acts of Parliament and 803 incorporated by Royal Charter.[64] The statutory incorporation of companies was relatively

[62] See Companies Act 2006 s3(3).
[63] The Unregistered Companies Regulations 2009, SI 2009/2436.
[64] Department for Business Enterprise & Regulatory Reform, 'Statistical Tables on Companies Registration Activities 2008-09' Table E3.

common in the 19th century. After the Second World War, many of these statutory companies were nationalised, ie taken over by public boards or corporations set up by public Acts.[65]

(3) Limited Liability Partnerships: LLPs share many of the features of a normal partnership, but offer reduced personal responsibility for business debts. They can be characterised a hybrid between company and partnership.

(4) Trading Funds: A Trading Fund is a government department, or an executive agency or part of the department, which has been established as such by means of a Trading Fund Order made under the Government Trading Funds Act 1973. A trading fund can only be established with HM Treasury's agreement. One may only be set up where more than 50 per cent of the trading fund's revenue will consist of receipts in respect of goods and services provided by the trading fund, and where the responsible Minister and the Treasury are satisfied that the setting up of the trading fund will lead to 'improved efficiency and effectiveness in management of operations'.[66]

The significance of a trading fund is that it has standing authority under the 1973 Act to net off its revenues against costs. Some trading funds have, as their main function, the collection and supply of information to both public and private sectors; others do not.

National Accounts Classification

The legal form is to be distinguished from the official classification status, which is given to each body by the Office of National Statistics (ONS) in national accounts. Government-owned businesses are often classified by the ONS as public corporations (PC), independently from its legal form. Alternatively, an entity can be classified as a Non-Departmental Public Body (NDPB). If an entity is not controlled by the state, it will be classified as belonging to the private sector, possibly a private non-financial corporation.

(1) A Non-Departmental Public Body (NDPB) has a role in the processes of national government, but is not a government department, or part of one, and accordingly operates to a greater or lesser extent at arm's length from ministers.[67] NDPBs have a national or regional remit and carry out a wide range of functions. Their distance from government means that the day-to-day decisions they make are independent as they are removed from ministers and Civil Servants. Ministers are however ultimately responsible to Parliament for a NDPB's independence, its effectiveness and efficiency. There are four types of NDPB. These denote different funding arrangements, functions and kinds of activity. They are: Executive NDPBs – established by statute and carrying out administrative, regulatory and commercial functions, they employ their own staff and are allocated their own budgets. Advisory NDPBs which provide independent and expert advice to ministers on particular topics of interest. They do not usually have staff but are supported by staff from their sponsoring department. They do not usually have their own budget, as costs incurred come within the department's expenditure. Tribunal NDPBs – have jurisdiction in a specialised field of law. They are usually supported by staff from their sponsoring department and do not have their own budgets. Independent Monitoring Boards – formerly known as 'Boards of Visitors' – are 'watchdogs' of the prison system. Their duty is to satisfy themselves as to the state of the prison premises, their administration and the treatment of prisoners. The sponsoring department meets the costs.

[65] PL Davies, *Gower and Davies' Principles of Modern Company Law* (8th edn, Sweet & Maxwell, London 2008) 1-16.
[66] Government Trading Funds Act 1973 s 1(1)(b), as amended by Government Trading Funds Act 1990.
[67] Sir Leo Pliatsky, 'Report on Non-Departmental Public Bodies' Cmnd 7797, HMSO, January 1980.

(2) A Public Corporation (PC) is a market body, owned or controlled[68] by central or local government, that derives more than 50% of its income from the sale of goods and services. This includes government-owned companies, trading funds, and other market bodies. They have substantial day-to-day operating independence so that they are to be seen as institutional units separate from their sponsor departments. In terms of governance, Public Corporations are in most respects akin to an Executive NDPBs. Generally Public Corporations are governed in accordance with their constitutional documents. However, HM Treasury requires that a certain degree of information is provided to maintain an audit trail for public spending and to input data into the 'Whole of Government Accounts' (WGA) list[69]. Public Corporations will prepare their accounts in accordance with Generally Accepted Accounting Practice in the UK (UK GAAP). There is no requirement for Public Corporations (other than Trading Funds) to follow the Government Financial Reporting Manual ('FReM')[70] although, as information will be required for the purposes of the WGA, departments encourage their Public Corporations to have regard to the requirements of the FReM in, for example, the use of modified historical cost accounting.

The Government has a strong fiscal interest in the profitability of government-owned businesses. This is because the net operating surplus of PCs scores as a receipt in the National Accounts definition of the current balance. One of the government's fiscal rules is that over the economic cycle the current balance is in balance or surplus. Everything else being equal, a more profitable portfolio of government-owned businesses would increase the current balance surplus.

(3) If a business is not controlled by the State, it will not be classified as a public, but as a private corporation.[71] In the field of scrutiny here, it is likely that a borderline company may be classified by the ONS as a private non-financial corporation (PNFC). Nevertheless, they may still be advised by the Shareholder Executive.[72]

(4) Ultimately, there is a specific unique status for a Public Broadcasting Authority, currently encompassing the British Broadcasting Corporation (BBC) and S4C (Sianel Pedwar Cymru, the Welsh Fourth Channel Authority). The BBC is governed by Royal Charter and an associated Agreement with Government. These arrangements reflect the Corporation's independent status and its unique accountability directly to the 'licence fee payer'. The Charter and Agreement set out the BBC's accountability to Parliament for use of the public money it receives whilst at the same time preserving the BBC's independence on editorial policy and programming. S4C is a statutory corporation. Its governance arrangements and functions are set out in the Broadcasting Acts of 1990 and 1996 and the Communications Act 2003. S4C's Chair and members are appointed by the Secretary of State and the Authority is responsible for S4C's strategic policy and for ensuring the fulfilment of its statutory functions. S4C is funded primarily by a Government grant, the level of which is prescribed by statute.

Examples.

In order to illustrate the (non-)interdependence of legal form and statistical classification, the following provides an overview of a number of examples.

---

[68] This means over 50% government ownership or control by government. One exception to this is British Energy Group. It is classified as a Public Corporation despite the fact that it is wholly owned by the private sector, on the basis of the control that can be exercised by Government over the company.
[69] <http://www.wga.gov.uk>.
[70] <http://www.financialreporting.gov.uk/>.
[71] Consequently, these corporations do not impact on the government's fiscal position.
[72] Currently, four private non-financial corporations are in the Shareholder Executive's portfolio. These are NATS, Partnership-UK, QinetiQ and Working Links.

Body name	Legal form	Owned by / created by	Classification
British Energy	public limited company (plc)	private investors, but State retains special share[73]	PC
British Nuclear Fuels (BNFL)	plc	UK Government[74]	PC
Urenco	private limited company (ltd)	UK Government (33.3%)[75], Dutch Government (33.3%), RWE and E.On (33.3%)	PNFC
Nuclear Decommissioning Authority (NDA)	statutory corporation	Energy Act 2004	NDPB
UK Atomic Energy Authority (UKAEA)	statutory corporation	Atomic Energy Authority Act 1954	NDPB
British Waterways	statutory corporation	Transport Act 1962	PC
Channel Four Tele-vision Corporation (C4C)	statutory corporation	Broadcasting Act 1990	PC
Defence Science and Technology Laboratory (dstl)	trading fund	Ministry of Defence	PC

[73] No single shareholder can own more than 15% of the issued share capital. The Government does not own any shares, other than special shares giving certain administrative rights and exercisable only on grounds of national security.

[74] 49,999 ordinary shares of £1 each are owned by the Secretary of State for Business, Innovation and Skills and one ordinary share of £1 is owned by the Treasury Solicitor.

[75] The UK Government owns 56 million 'A' ordinary shares in Urenco Ltd through its wholly-owned subsidiary, Enrichment Holdings Ltd.

Q 30. Are there rules blocking unfriendly take-overs? Discuss the attitude of your Member State towards the take-over directive (Directive 2004/25, the 'Volkswagen directive').

English company law is one of the most takeover-friendly legal system in the world. A takeover, particularly a hostile one, is considered as being a healthy self-correction of the market: according to economic theory, the presence of an ineffective management leads to a lower share price, which in turn facilitates a takeover and subsequent efficiency gains.[76]

In this tradition, British company law is determined to facilitate takeovers where it can. The provisions governing takeover law are not contained in legislation, but in a self-regulating document of the British industry, the City Code on Takeovers and Mergers.[77] This instrument is governed by several tenets:

- neutrality of the board: ie obligation on the board of the target company not to frustrate the bid
- mandatory bid: a shareholder who reaches a certain threshold (control) has to launch a takeover bid
- disclosure of information: both bidder and target have to disclose adequate information to the shareholders of the target
- equality of treatment of the target shareholders

It is clear that the British takeover regime has inspired the original European takeover directive, which rests on similar basic principles.[78] However, the final version of the takeover directive (ie Directive 2004/25) allows for an opt-out from the board neutrality principle, which has not been well conceived by the UK. All in all, it is fair to say that the takeover directive does not go far enough from a UK perspective; most of the criticisms stem from the large number of exceptions of and permitted derogations from the Directive ('optionality' of the Takeover Directive).[79]

It is therefore not surprising to note that the UK has opted into the board neutrality rule according to Articles 9, 12 of the Directive. On the other hand, it has to be pointed out that the UK opted out from the breakthrough rule.[80] This rule concerns so-called pre-bid defences[81] like capital structures or appointment rights that make it more difficult to actually seize power in a target company. In fact, almost all Member States have opted out from this duty, but this comes at a surprise in the otherwise takeover-friendly legal regime of the UK. It corresponds to this decision, however, that deviations from a strict one-share-one-vote (OSOV) rule are allowed under British company law. The issue of voting rights, multiple voting shares, non-voting preference shares and similar matters are freely left to the company's articles of association. On some occasions, this may produce situations impeding a takeover and possibly deterring potential investors from other Member States. However,

[76] HG Manne, 'Mergers and the Market for Corporate Control' (1965) 73 J of Political Economy 110; R Romano, 'A Guide to Takeovers: Theory, Evidence, and Regulation' (1992) 9 Yale J on Regulation 119, 129 ff.

[77] Available at <http://www.thetakeoverpanel.org.uk/the-code>.

[78] JA McCahery and others, *The Economics of the Proposed European Takeover Directive*, CEPS Research Report in Finance and Banking no 32, April 2003.

[79] G Hertig and JA McCahery, 'Optional rather than Mandatory EU Company Law: Framework and Specific Proposals' (2006) 3 European Company and Financial Law Rev 341.

[80] Explanatory Notes on the Companies Act 2006, para 1232.

[81] As opposed to post-bid defences, which are subject to the board neutrality duty.

it has to be emphasised that deviations from the OSOV regime are very rare in practice, due to institutional investors' lobbying for good corporate governance structures.[82]

More recently, Lord Paul Myners, City Minister in the Department for Business, Innovation and Skills, has begun a debate on whether the British takeover law is too liberal. His remarks come in the context of growing concern that – due to its liberal take-over law – British firms might be at an increased risk of falling into foreign hands. This has been highlighted by Lord Myners against the background of the possible take-over of Cadbury by American competitor Kraft.[83] Despite him insisting not being xenophobic[84], his remarks clearly seem to be based on national interests.

Q 31. To what extent are the 2005 OECD Guidelines on Corporate Governance of State-owned Enterprises taken into account?

The OECD Guidelines on Corporate Governance of State-Owned Enterprises are built on five key priorities: (i) to ensure a level-playing field with the private sector, (ii) to reinforce the ownership function within the state administration, (iii) to improve transparency of SOE's objectives and performance, (iv) to strengthen and empower SOE boards, and (v) to achieve equitable treatment of minority shareholders. To ensure a level-playing field, the Guidelines stress the importance of separating regulation and shareholding functions. They also emphasise transparency of special obligations and the competitive conditions in gaining access to finance. To reinforce the ownership function with State administration, the Guidelines suggest that the ownership function be coordinated at the central level. Moreover, a clear and fully disclosed ownership policy is supported. To improve transparency, disclosing financial assistance from the state and transactions with the state are important. Further, the empowerment of SOE boards requires a structured and skill-based nomination process and the capacity of the board to appoint the CEO and who should be accountable to it. The number of state representatives should be limited and chairman of the board and CEO should not be one and the same person. These guidelines are not considered as particularly relevant for the UK and have not been taken into account for the governance of its state-owned companies.

Q 32. Are there any special features in your Member State's legislation that may be relevant for our topic?

Since the UK applies its general company law to state-owned enterprises, this implies that these companies do not have formal responsibilities towards stakeholders other than shareholders. The normal rule is s 172 of the Companies Act 2006, which places the interests of the 'members as a whole' at the top of the directors' obligations, thereby allowing them in doing so to have regard to other constituencies ('enlightened shareholder value')[85].

---

[82] See on this WG Ringe, 'Deviations from Ownership-Control Proportionality – Economic Protectionism Revisited' in U Bernitz and WG Ringe (eds) *Company Law and Economic Protectionism* (forthcoming, OUP 2010); ISS, Shearman & Sterling LLP and ECGI, *Report on the Proportionality Principle in the European Union*, available at <http://ec.europa.eu/internal_market/company/docs/shareholders/study/final_report_en.pdf>.

[83] J Treanor, 'Too many UK firms fall into foreign hands, warns crusading Myners' *The Guardian* (London 24 September 2009) 31.

[84] Ibid.

[85] Department of Trade and Industry, *Companies Act 2006: Duties of company directors – Ministerial statements* (June 2007).

An exception from this general regime applies to Trading Funds. These are arms' length executive agencies of Government Departments; as such, they are subject to individual Departmental policies on issues such as employment and supplier payment policy because they are bound by Civil Services rules.[86]

[86] OECD (n 18) 81.

C. Competition law

<u>Article 81, 82 and 86 EC (now Articles 101, 102, 106 TFEU)</u>

As was noted above, it is for the Member States to define which activities are in the domain of the public sector and which are not. **Q 33.** Has there been a debate about whether the provision of certain goods or services should be undertaken by the government or by the private sector? Please specify whether and to what extent such a debate has taken place on a general level or on a specific level, i.e. in the context of sector specific regulation? To the extent that there is no general legislative framework for answering such fundamental questions, there may be specific laws or policy documents. **Q 34.** Please identify such laws and/or policy documents.

Even if it is decided that certain activities are to be carried out by undertakings, governments may still want a specific regime for them. **Q 36.** Has there been any discussion of the question whether certain services should be guaranteed by identifying them as services of general economic interest? What are the questions that were discussed? **Q 37**. Has the implementation of the Services Directive 2006/123 led to a debate about services of general economic interest? **Q 38**. Has the introduction of Article 16 EC with the Treaty of Amsterdam given rise to a debate about the function of services of general economic interest and/or services of general interest?

Q 39. Has the equivalent of Article 81(3) EC (now Article 101(3) TFEU) in your national competition law been interpreted so as to allow exceptions for the protection of public interest? And has this led to a situation whereby public enterprises have been favoured over private enterprises?[87]

The history of private versus public ownership in the UK is marked by two contrasting periods. In the decades after the Second World War, the main industries of the country were nationalised under the initiative of a strong Labour Government.[88] Since 1979, however, the Conservative government led by Margaret Thatcher favoured increasing competition and reversed these decisions. Probably also partly motivated by budget deficits[89], the government started a programme of massive privatisations, and by 1990, 42 major businesses employing almost 900,000 people had been sold off, with large privatisations planned to continue into the middle of the decade. Even apparently implausible candidates – coal, railways and nuclear energy – passed into the private sector between 1994 and 1997. Despite the 'temporary public ownership' of various financial institutions since the 2007/08 crisis, it is fair to say that the UK has been at the forefront of liberalisation and privatisation of its public services since 1979.[90] This can be illustrated by the continued attempts to privatise public utilities: even most recently, the government has announced a sale of £16bn of state assets in order to get the national debt under control. The envisaged assets for sale are the Channel Tunnel Rail Link, the Dartford Crossing toll road and Tote, the nationalised bookmaker, along with a 33% stake in the uranium enrichment company Urenco. Around £11bn of the total is expected to come from sales by local authorities.[91] Even further than that, the Confederation of British Industry has recently called for a privatisation of every service run by the state other than the most sensitive (such as military operations).[92]

[87] In Case C-203/96 *Dusseldorp* [1998] ECR I-4075 and Case C-209/98 *Entreprenorforeningens Affald v Copenhagen* [2000] ECR I-3743, the questions were raised under the heading of Article [86](2) (= now Article 106(2) TFEU) but one could have imagined a discussion under Article 101(3) TFEU if the government had invited enterprises to conclude agreements with similar purposes.
[88] See on this WA Robson, *Nationalized Industry and Public Ownership* (2nd edn, Allen & Unwin, London 1962).
[89] J Foreman-Peck, 'How privatisation has changed Britain' <http://news.bbc.co.uk/1/hi/business/4061613.stm>.
[90] E Szyszczak, *The Regulation of the State in Competitive Markets in the EU* (Hart Publishing, Oxford 2007) 215.
[91] BBC News, 'Brown unveils £16bn assets sale' 12 October 2009, <http://news.bbc.co.uk/1/hi/8301927.stm>.
[92] A Gray, 'Call to outsource more state services' *Financial Times* (London, 19 October 2009) 2.

By way of introduction, this short overview is to illustrate the *political* nature of the attitude towards public or private ownership in the United Kingdom. However, there is no general legislative or constitutional framework for dealing with these fundamental questions, nor are there specific laws or policy documents. This does not exclude a serious legal impact of both EU and UK competition law on the role of the state in a more general sense. Moreover, the European debate on 'services of general economic interest' and on the services directive[93] have had far-reaching repercussions in the UK.

The following discussion is therefore to analyse the role of the state in competition law in a way slightly detached from the order of the questions as envisaged by the questionnaire. It will take into account several fields of controversy and discuss the various areas of current debate around the proper role of the state in competition law in turn. Essentially, five different topics can be distinguished.

First, there is a lively discussion around the concept of 'undertaking' in the context of Articles 101 and 102 TFEU (ex 81, 82 EC) and the corresponding 'Chapter I' and 'Chapter II' provisions in the UK Competition Act 1998 (CA 1998) which reflect the wording of Articles 101 and 102 TFEU. The question is here how far entities that belong to the State fall under the definition of 'undertaking' and are thus subject to competition law rules.

Another way of obtaining a similar result would be by introducing non-competition considerations into the application of into Article 101 TFEU and Chapter I of the CA 1998.

Thirdly, a different discussion around introducing public interests by Member States would be by means of Article 101(3) TFEU and the corresponding provision in the CA 1998. This is different from the previous two points discussed above in that Article 101(3) TFEU provides an ex post facto exception from competition law whereas the non-fulfilment of one of the conditions of Articles 101(1), 102 TFEU means the competition rules are not engaged at all.

The fourth gateway for public interests would be Article 102 TFEU (ex Article 82 EC); here, the question is how public interest arguments can be invoked for an assessment of an allegedly 'abusive' behaviour.

The final avenue of pursuing state policy within competition law seems to be Article 106(2) TFEU (ex Article 86(2) EC) and its national twin. This is a sectoral exception from competition law for services of general economic interest, subject to a complicated proportionality test.[94] Each of these aspects is considered in turn, whereby emphasis is put on national practices and developments.

(1) The notion of 'undertaking'

It is the notion of an 'undertaking' that opens the scope of both Articles 101 and 102 TFEU as well as the corresponding sections in the CA 1998. The starting point is the well-known definition of 'every entity engaged in an economic activity regardless of the legal status of the entity and the way in which it is financed'.[95] It has long been accepted that the criterion of an 'economic activity' is not

---

[93] Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market [2006] OJ L376/36.

[94] See on this in more detail JL Buendia Sierra, *Exclusive Rights and State Monopolies under EC Law* (OUP, Oxford 1999); D Edward and M Hoskins, 'Article 90: Deregulation And EC Law. Reflections Arising From the XVI FIDE Conference' (1995) 32 CML Rev 157; J Holmes, 'Fixing the Limits of EC Competition Law: State Action and the Accommodation of the Public Services' (2004) 57 Current Legal Problems 149.

[95] Case C-41/90 *Höfner and Elser v Macrotron GmbH* [1991] ECR I-1979.

fulfilled when the State acts in its capacity as or in connection with its public authority.[96] The most controversial debate, however, both in the EU and in the UK, has occurred when the State does not act under public authority but rather as a market participant. The leading case on this on the EU level is *FENIN v Commission*[97], in which both the CFI and the ECJ confirmed that the State, when acting as a regular purchaser on the market, but with the aim of subsequently using the purchased goods for non-profitable or social purposes, did not characterise as an 'undertaking' in the sense of the Treaty.[98] The *FENIN* approach has been confirmed by both CFI and ECJ in the *Selex* case.[99] This comes in stark contrast to the original position of the UK: in *BetterCare*[100], the (former) UK Competition Commission Appeal Tribunal (CCAT)[101] had to decide about the status of a Trust which was entrusted to provide nursing home and residential care services for the elderly. BetterCare, a provider of residential and nursing home care, complained at the (then) Director General of Fair Trading (DGFT)[102] that the Trust abused its dominant position by forcing it to agree to unduly low prices. The CCAT concluded that the Trust was indeed acting as an undertaking in that it was in a position to generate effects which the competition rules seek to prevent.[103] This finding is very different from the approach under European Union law. The situation became even more complicated when the case was remitted to the DGFT. The DGFT was in the difficult situation: should it apply the CCAT's judgment or, as a result of the requirement of equivalency in s 60 of the CA 1998[104], maintain consistency with the CFI's decision in FENIN? Finally, the DGFT reached the conclusion that the Trust had not abused its dominant position and thus avoided a decision on whether the Trust was an undertaking or not.[105]

However, the (renamed) Office of Fair Trading (OFT) took up the issue and after much debate published a paper in August 2004 where it clarified its position.[106] The OFT reversed its earlier approach and decided to follow the CFI's FENIN approach (later confirmed by the ECJ): 'Following the FENIN judgment, it is the OFT's view that, even if an entity is in a position to generate anti-competitive effects, it will not be an undertaking for the purposes of the competition rules if the subsequent related supply of the goods or services (for which the purchases are made) do not themselves constitute economic activities and the entity does not itself directly provide the

[96] Case C-343/95 *Diego Calì & Figli Srl v Servizi ecologici porto di Genova SpA (SEPG)* [1997] ECR I-1547; case C-309/99 *JCJ Wouters and others v Algemene Raad van de Nederlandse Orde van Advocaten* [2002] ECR I-1577.

[97] Case T-319/99 *FENIN v Commission* [2003] ECR II-357; case C-205/03 P *FENIN v Commission* [2006] ECR I-6295.

[98] See on this WG Ringe, 'Public Bodies and EC Competition Law – *FENIN v Commission*' [2007] Bulletin of International Legal Developments 39.

[99] Case T-155/04 *SELEX Sistemi Integrati SpA v Commission* [2006] ECR II-4797; case C-113/07P *SELEX Sistemi Integrati SpA v Commission and Eurocontrol* [2009] OJ C113/4.

[100] *BetterCare Group Ltd v The Director General of Fair Trading* [2002] CAT 7. See on this PJ Slot and AC Johnston, *An Introduction to Competition Law* (Hart Publishing, Oxford 2006) 268 ff.

[101] The CCAT has now been replaced by the Competition Appeal Tribunal (CAT).

[102] The DGFT was the UK competition authority at the time and has now been replaced by the Office of Fair Trading (OFT).

[103] See on the case eg A Ezrachi, *EC Competition Law – An Analytical Guide to the Leading Cases* (Hart Publishing, Oxford 2008) 10.

[104] S 60 reads: '[S]o far as is possible (having regard to any relevant differences between the provisions concerned), questions arising under this Part in relation to competition within the United Kingdom are dealt with in a manner which is consistent with the treatment of corresponding questions arising in Community law in relation to competition within the Community.'

[105] R Whish, *Competition Law* (6th edn, OUP 2009) 330.

[106] Office of Fair Trading, *Policy note 1/2004 – The Competition Act 1998 and public bodies* (August 2004).

services.'[107] As a result, the UK approach the notion of 'undertaking' seems to be in line with the EU's interpretation now.[108]

Equally, the supply of goods or services in the execution of an exclusively social function (such as the provision of health services on a non-profit making basis on the principle of solidarity, where the entitlement to services is not dependent on the amount of contributions by members) is unlikely to be an economic activity.[109] For instance, the UK government takes the view that the British healthcare system, operated by the NHS (National Health Service), does not provide Treaty-regulated services when providing health care.[110] NHS bodies do not provide economic services nor are they undertakings within the meaning of Articles 101 ff TFEU, since they are engaged in an activity aimed at social and health objectives which is carried out on a not-for-profit basis for no remuneration.[111] [112]

(2) Article 101(1) TFEU and the 'rule of reason'

The second important aspect under consideration here is the question to what extent it is possible to introduce non-competition objectives into the assessment that is carried out under Article 101(1) TFEU and the corresponding UK legislation.[113] The well-known *Wouters* case[114] seemed to suggest that – in certain cases – it may be possible to balance such non-efficiency objectives against a restriction on competition and that the latter may even be outweighed by the former.[115] This case has stirred a fierce debate about the availability of policy considerations under Article 101(1) TFEU. In a broader context, this can be seen as the controversial 'rule of reason' debate – does or should Article 101(1) be open to more considerations than just competition law aspects?[116] Ultimately, such

---

[107] Ibid para 22.

[108] Cf M Krajewski and M Farley, 'Non-economic activities in upstream and downstream markets and the scope of competition law after FENIN' (2007) 32 Eur L Rev 111, 122.

[109] Joined cases C-264/01, C-306/01, C-354/01 and C-355/01 *AOK Bundesverband and others v Ichthyol-Gesellschaft Cordes and others* [2004] ECR I-2493. See also Cases C-159/91 and 160/91 *Poucet v Assurances Générales de France* [1993] ECR I-637. See also OFT Policy Note 1/2004 (n 106).

[110] UK response to questionnaire on social services of general interest, <http://ec.europa.eu/employment_social/social_protection/docs/replies/uk_en.pdf>.

[111] For a more nuanced view, see A Cygan, 'Public Healthcare in the European Union: Still a Service of General Interest?' (2008) 57 Intl and Comparative L Q 529.

[112] It is uncertain whether the provision of health-care services by the NHS amount to the provision of a commercial service under the rules on the free movement of services (now Articles 56 ff TFEU), see case C-372/04 *Watts v Bedford Primary Care Trust* [2006] ECR I-4325 paras 90-91: cf P Craig and G de Búrca *EU Law – Text Cases and Materials* (4th edn, OUP Oxford 2008) 822.

[113] On this topic generally C Townley, *Article 81 EC and Public Policy* (Hart Publishing, Oxford 2009).

[114] Case C-309/99 *JCJ Wouters and others v Algemene Raad van de Nederlandse Orde van Advocaten* [2002] ECR I-1577.

[115] On this case, see G Monti, 'Article 81 EC and Public Policy' (2002) 39 Common Market L Rev 1057; R O'Loughlin, 'EC competition rules and free movement rules: an examination of the parallels and their furtherance by the ECJ Wouters decision' (2003) 24 Eur Competition L Rev 62; A Jones, 'Regulating the legal profession: article 81, the public interest and the ECJ's judgment in Wouters' (2008) 19 Eur Business L Rev 1079.

[116] See V Korah, 'Rule of reason: apparent inconsistency in the case law under Article 81' (2002) 1 Competition L Insight 24; Monti (n 115); M Furse, *Competition Law of the EC and UK* (4th edn, OUP 2004) 183-185.

a US-like approach has been rejected by the CFI in a series of cases,[117] and also by the Commission in its Guidelines.[118]

The 'Chapter I' prohibition of the CA 1998 (which mirrors Article 101 TFEU) is generally applied by the competent bodies in the UK in the same way as Article 101 with respect to what constitutes a distortion of competition.[119] Consequently, this should also include the problem whether a balancing of non-efficiency considerations is permissible. To the writer's awareness, however, this is not an issue that is much discussed under domestic law. Neither the case-law nor the academic literature seem to pick up the European 'rule of reason' debate under UK competition law. We can only deduce from this that (because of s 60 CA 1998) the UK authorities will generally follow the Commission practice, ie reject the rule of reason approach.

However, there is an additional important element on the national level that needs to be mentioned. Schedule 3, paragraph 7 CA 1998 gives the Secretary of State the power to exclude a particular agreement from the Chapter I prohibition if 'there are exceptional and compelling reasons of public policy why the Chapter I prohibition ought not to apply'.[120] [121] This power even includes the possibility for a retrospective exclusion.[122] Three orders have been made under this provision, all of them concerning the defence industry: the first excluded agreements relating to the maintenance and repair of warships from the Chapter I prohibition[123], the second excluded the application of the Chapter I and II prohibitions to agreements and conduct affecting strategic and tactical weapons and their supporting technology[124], and the third excluded certain agreements concerning nuclear submarines developed or manufactured for the Secretary of State if the agreement has the purpose of protecting the essential security interests of the United Kingdom.[125] In a way, this development seems to move into the direction of the general exception for defence matters laid down in Article 346 TFEU, although the legal structure of the two regimes is obviously very different.

(3) Article 101(3) TFEU

Article 101(3) TFEU provides for an exception to the general 101(1) prohibition and lies down several conditions for its application.[126] The national provision in the UK that mirrors Article 101(3) TFEU is section 9 CA 1998. It reads:

> This section applies to any agreement which—
> (a) contributes to—
> (i) improving production or distribution, or
> (ii) promoting technical or economic progress,
> while allowing consumers a fair share of the resulting benefit; but
> (b) does not—

[117] Case T-112/99 *Métropole Télévision (M6) and others v Commission* [2001] ECR II-2459 paras 72-77; case T-65/98 *Van den Bergh Foods Ltd v Commission* [2003] ECR II-4653 paras 106-107; case T-328/03 *O2 (Germany) GmbH & Co OHG v Commission* [2006] ECR II-1231 para 69.
[118] European Commission, *Guidelines on the Application of Article 81(3) of the Treaty*, [2004] OJ C101/97 para 11.
[119] Whish (n 105) 335; Furse (n 116) 202 f.
[120] The corresponding provision for Chapter II is found in sub-paragraph 4 of the same provision.
[121] Cf Office of Fair Trading, *Agreements and concerted practices* (December 2004) para 6.2.
[122] Schedule 3, paragraph 7(3).
[123] Competition Act 1998 (Public Policy Exclusion) Order 2006, SI 2006/605.
[124] Competition Act 1998 (Public Policy Exclusion) Order 2007, SI 2007/1896.
[125] Competition Act 1998 (Public Policy Exclusion) Order 2008, SI 2008/1820.
[126] See generally Whish (n 105) 148 ff; Ezrachi (n 103) 38 f.

(i) impose on the undertakings concerned restrictions which are not indispensable to the attainment of those objectives; or

(ii) afford the undertakings concerned the possibility of eliminating competition in respect of a substantial part of the products in question.

The wording of this section is quite similar to Article 101(3) TFEU, albeit with small differences. One of them is that Article 101(3) applies an improvement of the production or distribution 'of goods' only, while the text of s 9 CA 1998 does not have this limitation. This means that s 9 CA 1998 can be applied to an improvement of services as well.[127] However, the OFT has stated in general that it will 'have regard' to the Commission's Guidelines on Article 101(3) TFEU[128] when interpreting s 9.[129] Moreover, the parliamentary debates show that the lawmakers expected s 9 CA1998 to be interpreted in the same way as Article 101(3) TFEU.[130] Thus, the same problems associated with the role of the State will be encountered here: Basically, the question is whether public interest arguments can be used to counterbalance an otherwise unlawful agreement, or in other words whether state-owned enterprises or enterprises pursuing public interest objectives enjoy more favourable treatment under the competition rules than private undertakings engaged in purely commercial activity.

There has been a lively debate in the case-law, but also in the academic literature, as to whether Article 101(3) TFEU and s 9 CA 1998 allow for considerations based on the pursuit of the public interest. It is obvious that the Commission's Guidelines do not reflect this view and rather apply Article 101(3) TFEU based on economic efficiency alone.[131] However, there is some case law that indicates the contrary, as for example the CFI case *Métropole Télévision SA v Commission*[132]: This case concerned the Commission's individual exemption to the regulations of the European Broadcasting Union (EBU) governing the exercise of television rights to sports events. On complaint from competitors, the CFI had to consider, inter alia, whether the 'particular public mission' of members of the EBU was relevant to an assessment under Article 101(3) TFEU – in a situation where Article 106(2) TFEU was not applicable. The Court stated that 'in the context of an overall assessment' the Commission is generally entitled to base itself on considerations connected with the pursuit of the public interest in order to grant exemption under Article 101(3) TFEU.[133] However, in the present case it failed to show that such considerations required exclusivity in the sense of the EBU regulations. Another example is the Commission's *CECED* decision.[134] The European household appliance manufacturers' association (CECED) had adopted an agreement phasing out production and imports of domestic washing machines in low energy efficiency classes, with the aim of reducing energy consumption of washing machines. The Commission recognised that the CECED agreement would mean that certain washing machines would be excluded from the market, but granted an exemption from (what is now) Article 101 TFEU nevertheless because the agreement was likely to reduce energy consumption and to benefit customers via lower bills.[135] The Commission's report

---

[127] Office of Fair Trading, *Agreements and concerted practices* (December 2004) para 5.4.

[128] European Commission, *Guidelines on the Application of Article 81(3) of the Treaty*, [2004] OJ C101/97.

[129] Office of Fair Trading, *Agreements and concerted practices – Understanding competition law*, December 2004, para 5.5.

[130] Whish (n 105) 352.

[131] Commission, *Guidelines on the application of Article 81 (3) of the Treaty* [2004] OJ C101/97.

[132] Joined cases T-528/93, T-542/93, T-543/93 and T-546/93 *Métropole télévision SA and others v Commission* [1996] ECR II-649.

[133] Ibid para 118.

[134] Commission Decision 2000/475/EC of 24 January 1999, case no IV.F.1/36.718 – *CECED* [2000] OJ L 187/47. See on this HR Basaran, 'How should Article 81 EC Address Agreements that Yield Environmental Benefits?' (2006) 27 Eur Competition L Rev 479; D Casey, 'Disintegration: Environmental Protection and Article 81 EC' (2009) 15 Eur L J 362.

[135] Ibid paras 55-57.

found that 'on the basis of reasonable assumptions, the benefits to society brought about by the CECED agreement appear to be more than seven times greater than the increased purchase costs of more energy-efficient washing machines'. Moreover, the Commission concluded that no reasonable alternatives to this agreement were available, and there were no elements of the agreement which were dispensable or directly eliminated competition. Consequently the Commission found that the conditions of (now) Article 101(3) TFEU were satisfied and the CECED agreement was exempted from Article 101(1).[136]

These controversial cases have stirred much debate, and many commentators argue that Article 101(3) TFEU admits or should admit broad, non-competition considerations.[137] On the other hand, as explained, the Commission follows a strict efficiency-based test and does not consider public interest reasoning within Article 101(3).[138] Moreover, there is also evidence in some case-law that would back this latter approach.[139]

On the national level, the OFT has announced that it will have regard to the Commission's Guidelines on Article 101(3) TFEU[140] when interpreting the UK competition law pendant.[141] Since the OFT's own guidelines do not provide a substantive analysis of the permissible considerations under s 9, it seems that the OFT will be inclined to follow the Commission on this issue.

There have been only a few applications of s 9(1) CA 1998 by the OFT in the years since it has been in force. One example concerning an arguable service of general economic interest was considered in *Memorandum of Understanding on the supply of oil fuels in an emergency*.[142] This case concerned a memorandum of understanding, drawn up by the Government following the September 2000 fuel crisis and signed by the Government, major oil companies, oil independents, road hauliers, the police and trade unions in order to preserve the supply of oil fuels and to protect supplies to essential users. The OFT concluded that this memorandum had indeed the effect and object of restricting competition but nevertheless merited an individual exemption from the 'Chapter I prohibition' (which corresponds to Article 101 TFEU). The reasons given were that the scheme would improve the distribution of oil fuels during an oil fuel emergency, that consumers in the form of essential users would benefit directly and that consumers in general would benefit indirectly from the services these essential users provide (emergency services, maintaining public safety or supply food). This is a clear indication that considerations of general economic interest play a role when deciding about exemptions from the cartel prohibition.

A second case that merits a short discussion here is *Mastercard UK Members Forum Ltd*[143], in which the OFT had to consider the collective fixing of an interchange fee for credit cards. In doing so, it

---

[136] For other cases, see WH Roth, 'Zur Berücksichtigung nichtwettbewerblicher Ziele im europäischen Kartellrecht – eine Skizze' in C Engel and W Möschel (eds), *Recht und spontane Ordnung. Festschrift für Ernst-Joachim Mestmäcker zum 80. Geburtstag* (Nomos, Baden-Baden 2006) 413; H Schweitzer, 'Competition law and public policy: reconsidering an uneasy relationship–the example of Article 81' in J Drexl, L Idot and J Moneger (eds), *Economic Theory and Competition Law* (Edward Elgar, Cheltenham 2009) 134.

[137] M Siragusa, in CD Ehlermann and L Laudati (eds), *Competition Law Annual 1997: Objectives of Competition Policy* (Hart Publishing, Oxford 1998) 543 ff; R Wessling, 'The draft-regulation modernising the competition rules: the Commission is married to one idea' (2001) 26 Eur L Rev 357; G Monti, 'Article 81 EC and Public Policy' (2002) 39 Common Market L Rev 1057; B Suffrin, 'The Evolution of Article 81(3) of the EC Treaty' (2006) 51 Antitrust Bulletin 915, 952 ff.

[138] Cf Whish (n 105) 155 f.

[139] Case T-17/93 *Matra Hachette SA v Commission* [1994] ECR II-595 para 139. Cf Ezrachi (n 103) 81.

[140] European Commission, *Guidelines on the Application of Article 81(3) of the Treaty*, [2004] OJ C101/97.

[141] Office of Fair Trading, *Agreements and concerted practices – Understanding competition law*, December 2004, para 5.5.

[142] Director General of Fair Trading, decision no CA98/8/2001 of 25 October 2001, [2002] UKCLR 74.

[143] *Mastercard UK Members Forum Ltd*, [2006] UKCLR 236, paras 650 ff.

applied s 9 CA 1998 (unsuccessfully, in the end) and thereby considered the potential benefits for the position of consumers generally in addition to that of consumers who were 'customers' in the narrow sense, meaning users of the card payment scheme (ie cardholders and merchants). Despite a submission made by the defendants[144], the OFT concluded that it was appropriate to consider the 'society in general', and not only the consumers of the specific service under scrutiny, thereby accepting a more far-reaching role for competition law.[145]

Another example is a block exemption adopted by the Secretary of State concerning public transport ticketing schemes.[146] These schemes allow passengers to purchase tickets that can be used on the services of the participating travel operators. The OFT acknowledged that such schemes could have beneficial effects for consumers. These benefits included improvements in the efficient use of resources, thus promoting economic progress. Moreover, benefits can accrue to consumers through cost or time savings, or reductions in external costs such as atmospheric or noise pollution.[147] Again, public services seem to play an important role under the section 9 exemption. It has to be noted, though, that the OFT does not draw a distinction between state-owned or private travel operators.[148]

This overview is to illustrate how public policy arguments can be invoked for both the Article 101(3) TFEU and the section 9 CA 1998 exceptions. Most frequently, they will be disguised under the label of 'economic efficiency' or 'lower cost' for consumers, but a closer look reveals how other interests (like environmental issues, for instance) underlie the official argumentation.

(4) Article 102 TFEU

Public interest arguments have also been invoked in the context of Article 102 TFEU (ex Article 82 EC). This frequently happens in the context of the notion of 'abuse' of the dominant position, or as a defence against allegedly abusive behaviour ('objective justification').[149] Such was the argument raised in the *Hilti* case[150], where safety considerations and the prevention of false and misleading advertising were put forward in order to justify Hilti's practice of requiring purchasers of Hilti nail cartridges to also purchase Hilti nails. The CFI held that laws in the UK were attaching penalties to the sale of dangerous products and to the use of misleading claims as to the characteristics of products, and that authorities were enforcing these laws; it was not for Hilti itself to take steps on its own initiative to eliminate products which it regarded as dangerous or inferior to its own. Similarly, in *Tetra Pak*, neither the Commission nor the courts accepted a public policy defence, as they believed that is not for an undertaking to autonomously take steps to protect public safety or public health, as these are taken care of by the national legislation of Member States.[151] However, a recent statement

---

[144] ibid 657.
[145] ibid 658, 661 ff. Cf J Vickers, 'Public policy and the invisible price: competition law, regulation and the interchange fee' (2005) 4 Competition L J 5, fn 16.
[146] The Competition Act 1998 (Public Transport Ticketing Schemes Block Exemption) Order 2001, SI 2001/319; amended by Competition Act 1998 (Public Transport Ticketing Schemes Block Exemption) (Amendment) Order 2005, SI 2005/3347.
[147] Office of Fair Trading, *Public transport ticketing schemes block exemption*, November 2006, para 3.4.
[148] The OFT however points to the fact that also state-owned enterprises can benefit from this block exemption, see OFT (n 147) paras 2.7 and 2.9.
[149] See PJ Loewenthal, 'The Defence of "Objective Justification" in the Application of Article 82 EC' (2005) 28 World Competition 455; A Albors-Llorens, 'The Role of Objective Justification and Efficiencies in the Application of Article 82 EC' (2007) 44 CML Rev 1727.
[150] Case T-30/89 *Hilti AG v Commission* [1991] ECR II-1439 paras 102-119.
[151] Case T-51/89, *Tetra Pak* [1990] ECR II-309.

given by the European Commission is not entirely clear as regards to what can constitute an objective justification.[152]

The UK competition authorities seem to be more open towards an 'objective justification'. Cases like *Floe Telecom Ltd* and *VIP Communications* clearly recognised an objective justification for the chapter II prohibition. In *Floe*, Vodafone's refusal to supply certain services in the telecommunications sector to Floe was under scrutiny, which Vodafone defended with reference to the alleged illegality of Floe's intentions. The relevant special competition authority OFTEL[153] found Vodafone's behaviour to be objectively justified[154], and the CAT agreed in principle about the availability of this excuse, however said that the illegality of Floe's behaviour was far from clear.[155] The same line of reasoning applied in *Re-investigation of a complaint from VIP Communications Ltd*.[156] A recent example of a decision where the behaviour was found to be justified is *NTM Sales*, as decided by the Office of Rail Regulation ORR.[157]

(5) Articles 106(2) and 14 TFEU (ex Articles 86(2) and 16 EC)

The fifth way of conflict between competition law and the State is the exception for services of general economic interest from the scope of applicability. This complex topic merits a discussion under different aspects.

(a) General Remarks – UK law

UK domestic law is structured similarly to Article 106(2) TFEU. Schedule 3, paragraph 4 of the Competition Act 1998 excludes services of general economic interest from the scope of the Competition Act:[158]

> Neither the Chapter I prohibition nor the Chapter II prohibition applies to an undertaking entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly in so far as the prohibition would obstruct the performance, in law or in fact, of the particular tasks assigned to that undertaking.

By and large, it is recognised that the OFT follows broadly the model of Article 106(2) and the case-law that has developed thereunder when it applies both Article 106(2) and Schedule 3 paragraph 4.[159] This has been confirmed by British courts.[160]

The OFT has published separate guidelines on this issue, 'Services of general economic interest exclusion (OFT421)'.[161] The most important point is that it is intended to apply the exclusion restrictively.[162] The exclusion's application is narrow, with undertakings seeking to benefit from the exclusion having to prove that they meet all of its requirements. This is because the OFT is convinced

[152] See DG Competition, *Discussion Paper on the application of Article 82 of the Treaty to exclusionary abuses* (December 2005).
[153] Office of Telecommunications, the predecessor of OFCOM (Office of Communications).
[154] Decision of 3 November 2003, [2004] CompAR 313.
[155] Case No 1024/2/3/04 [2004] CAT 18.
[156] OFCOM decision of 28 June 2005, [2005] UKCLR 1112.
[157] ORR decision of 12 August 2005, [2006] UKCLR 12, paras 168-185.
[158] See on this Whish (n 105) 345; Slot and Johnston (n 100) 267 ff.
[159] Slot and Johnston (n 100) 270.
[160] *Attheraces Limited and Another v The British Horseracing Board Limited and Another* [2005] EWHC 1553.
[161] Office of Fair Trading, *Services of general economic interest exclusion*, December 2004.
[162] Ibid para 1.9.

that 'in general, effective competition will best serve the interests of consumers over time'.[163] It notes that in the UK, privatisation and liberalisation efforts as well as EU initiatives have already significantly reduced the number of exclusive rights held by undertakings.[164]

In particular, the OFT would need to be satisfied that the undertaking has been 'entrusted' with the operation of a service of general economic interest and that the application of the prohibitions of the Act or Articles 101 and 102 TFEU would obstruct the performance, in law or in fact, of the particular task entrusted to it. Again, these notions are and will be interpreted closely corresponding to Commission practice and ECJ case law.[165]

(b) Proportionality Test

The interesting question, however, is how strict the proportionality test is applied. In the well-known European debate, from the case of *Corbeau* (1993) onwards, the ECJ has been more willing to accept that providers of public services may need to be immunised from competition law and has become more flexible in the way Article 106(2) TFEU is applied.[166] It is possible that the more lenient approach adopted by the courts was affected, inter alia, by Article 16 EC (now Article 14 TFEU) which was added by the Treaty of Amsterdam in 1996, and acknowledges the place occupied by services of general economic interest in the shared values of the Union and their role in promoting social and territorial cohesion. In this context, it is debatable how strictly the proportionality test contained in Article 106(2) TFEU will be applied. The OFT has stated that it would need to be satisfied that the obligations on the undertaking 'could not be discharged in ways which would have a less restrictive or distorting effect on competition'[167], indicating that it will apply a tough and strict proportionality test.[168] However, it has to be noticed that, over the last two decades, privatisation and liberalisation in the UK have significantly reduced the number of services provided by way of grant of exclusive rights.[169] In addition, the introduction of directives concerning common rules for the internal market in electricity, natural gas and postal services and the development of measures to promote competition in electronic communications and rail services will also render the problem less relevant in the EU as more of the markets are opened up to competition and the number of exclusive rights over aspects of services are reduced.[170]

Following the recent financial crisis, the question was raised whether Member States might be tempted to classify system banks receiving state aid as 'services of general economic interest' (SGEI) so as to escape from the applicability of competition rules or, in the alternative, whether a nationalised bank has acquired SGEI-status implicitly.[171] This, it is submitted, is not the case, at least not in the UK. The ECJ case-law on the 'entrustment', requiring a separate act of public authority, was respected, and in no bail-out cases the SGEI exclusion was invoked.

(c) The impact of Article 14 TFEU

Things were made more difficult through the insertion of (then) Article 16 EC by means of the Treaty of Amsterdam. The wording of (now) Article 14 TFEU, its legal status and its precise objective have

[163] Ibid para 3.6.
[164] Ibid para 3.5.
[165] On the 'entrustment' see ibid paras 2.9-2.15, on the extent of the exclusion see paras 3.1-3.8.
[166] See on this L Moral Soriano, 'How proportionate should anti-competitive state intervention be?' (2003) 28 Eur L Rev 112; E Szyszczak, *The Regulation of the State in Competitive Markets in the EU* (Hart Publishing, Oxford 2007) 127.
[167] Office of Fair Trading, *Services of general economic interest exclusion*, December 2004, para 3.2.
[168] ibid para 3.6.
[169] ibid para 3.5.
[170] Szyszczak (n 166) 127.
[171] F Vogelaar,'Editorial' (2009) 36 Legal Issues of Economic Integration 1, 5.

given rise to much speculation. In the academic discussion, the provision does not seem to have solved but rather reinforced the conflict between 'those who wish to regulate to protect public utilities and those who wish to make them competitive'.[172]

Commentators have invoked a range of interpretations on this provision.[173] Some see Article 14 as a protectionist measure, aiming at counterbalancing the growing privatisation and liberalisation that occurred in the 1990s.[174] It has has argued that Article 14 'does not modify Article [106(2) TFEU] at all but rather reaffirms the logic behind the provision'.[175] Yet, by contrast, another view is that Article 14 even restricts Article 106(2) TFEU: since Amsterdam, a deviation from the competition rules should be allowed only when the continued existence of services of general economic interest enhances market economy.[176]

Other, more differentiated contributions point out that Article 14 TFEU may be seen as a declaration of a new endorsement of the Treaty's social objectives positively exempting certain public services from the free market and competition rules.[177] Rather than the traditional exception from competition law, it is argued, the new provision creates a positive obligation on the Community to protect services of general economic interest.[178] Thus, Article 14 TFEU reinforces a growing recognition that the values associated with public services have a role as limits on the scope of competition rules and as expressions of citizenship rights.[179]

In its current wording, Article 14 TFEU of the Treaty seems to represent the synthesis of two opposite views advanced by different Member States at the Intergovernmental Conference that led to the adoption of the Amsterdam Treaty. Some states thought that a modification of the Treaty was necessary as Community law was too much in favour of competition principles, disregarding other general interests; while other Member States did not share this view. For this reason, Article 14 TFEU has not in practice provided a clear basis for solving the potential conflict between general interest and competition principles. Settling this conflict requires an efficient trade-off between the two principles.

(d) The impact of the Services Directive

The Services Directive[180] takes a confusing and incoherent approach towards SGEIs. The terminology in that instrument is incoherent and introduces several new unidentified categories of services (eg 'non-economic services of general interest' or 'healthcare services').[181] At the outset, the scope of the Directive does not cover 'non-economic' services of general interest, such as public administration or public education, which are provided by the state or public entities in fulfilment of

---

172 A Duff, *The Treaty of Amsterdam* (Sweet & Maxwell, London 1997) 84.

173 M Ross, 'Promoting Solidarity: From Public Services to a European Model of Competition?' (2007) 44 CML Rev 1057, 1071 ff.

174 L Flynn, 'Competition Policy and Public Services in EC Law After the Maastricht and Amsterdam Treaties' in D O'Keefe and P Twomey (eds), *Legal Issues of the Amsterdam Treaty* (Hart Publishing, Oxford 1999).

175 LJ Buendia Sierra, *Exclusive Rights and State Monopolies under EC Law* (OUP, Oxford 1999) 313. Similarly, J Pelkmans, 'Making EU Network Markets Competitive' (2001) 17 Oxford Rev of Economic Policy 432, 436.

176 HP Schwintowski, 'The common good, public subsistence and the functions of public undertakings in the European internal market' (2003) 4 Eur Business Organization L Rev 353, 371 f; cf D Chalmers and others, *European Union Law* (Cambridge University Press, Cambridge 2006) 1143 f.

177 M Ross, 'Article 16 E.C. and Services of General Interest: From Derogation to Obligation?' (2000) 25 Eur L Rev 22. Cf A Jones and B Sufrin, *EC Competition Law* (3rd edn, OUP 2008) 674.

178 Ibid. See also E Szyszczak, 'Public Services in Competitive Markets' (2001) 21 Ybk of Eur L 35, 64.

179 T Prosser, *The Limits of Competition Law – Market and Public Services* (OUP, Oxford 2005) 161.

180 Directive 2006/123/EC of the European Parliament and of the Council of 12 December 2006 on services in the internal market [2006] OJ L376/36.

181 M Ross, 'Promoting Solidarity: From Public Services to a European Model of Competition?' (2007) 44 CML Rev 1057, 1059.

their duties towards their population and without any economic consideration (Article 2(2)(a)). It does, however, not exclude as such services of general interest if they are of an economic nature – these seem to refer to the concept of services of general economic interest (SGEIs).[182] Thus, in so far as education is provided for remuneration, it is covered by the directive.[183] Nevertheless, the directive states that it 'does not deal with' the liberalisation of SGEIs (Article 1(2)). Moreover, the Directive 'does not affect the freedom of Member States to define, in conformity with Community law, what they consider to be services of general economic interest, how those services should be organised and financed, in compliance with the State aid rules, and what specific obligations they should be subject to' (Article 1(3)). Finally, Article 17 excludes the chapter on free movement of services from 'services of general economic interest which are provided in another Member State'. The latter exclusion, however, apparently does not apply when the recipient crosses the border and receives the service in its Member State of origin.[184] Moreover, Article 15(4) modifies the requirements that are permissible against service providers under the freedom of establishment and provides for an exclusion where these requirements would obstruct the performance of the service.[185]

These inconsistencies show that the Directive is not based on a coherent approach towards the relationship between SGEIs and the liberalisation of services.[186] One of the most delicate problems concerns the impact of the Directive on services that have been excluded from its scope.[187] Many policy-makers were certainly under the impression that by excluding SGEIs they were protecting them from the requirements of free movement, and the political argument will certainly be made that this should be its result – it is apparently, at least possibly, what was intended. However, it is difficult to see any way in which the Directive can prevent or diminish the (long-established) application of Article 56 TFEU (ex Article 49 EC). The most that can happen is that the Court can take a hint as to the political mood from the exclusion and be more sympathetic to Member State objections to free movement in this sphere.

The Directive has been implemented in the UK by means of the Provision of Services Regulations 2009.[188] These Regulations mirror the exclusions laid down in the Directive: reg 5, 22(4) and 25 implement Articles 1, 15(4) and 17 respectively. These provisions intend to do only what is necessary to implement the Directive and try to stay close to the text of the directive. Only reg 22(4)[189] departs somewhat from the text of Article 15(4) of the Directive and seems to introduce a more restrictive test towards SGEIs in the context of establishment: instead of a 'non-obstruction' test, as established by Article 15(4), reg 22(4) requires that the domestic requirements ought not to be disproportionate.

---

182 Enterprise Europe Network in London, *Single Market for Services* (June 2008) 3. However, certain SGEIs concerning transport and port services are explicitly excluded, see Article 2(2)(d).

183 BERR, *Implementing the Services Directive - Consultation Document on Implementing the EU Services Directive in the UK* (November 2007) 88 fn 16; cf G Davies, 'The Services Directive: extending the country of origin principle, and reforming public administration' (2007) 32 Eur L Rev 232, 233.

184 Davies (n 183) 234.

185 Chapter III (Articles 9-15) do not contain a comparable exclusion.

186 J van de Gronden, 'The services directive and services of general (economic) interest' in M Krajewski and others (eds), *The Changing Legal Framework for Services of General Interest in Europe* (Cambridge University Press, Cambridge 2009) ch 12; Ross (n 181).

187 This is ignored by Davies (n 183) 237 f.

188 SI 2009/xxxx.

189 Reg 22 reads:
'(1) – (3) […]
(4) The preceding paragraphs of this regulation do not apply in relation to any requirement applying to a person entrusted with the provision of a service of general economic interest where the requirement is proportionate and necessary for the provision of that service by that person.
(5) In paragraph (4) 'service of general economic interest' means a service which the competent authority determines, in accordance with Community law, to be of general economic interest.'

Otherwise, there has been no serious discussion about the Directive's impact on SGEIs. The only sensitive issue seems to be healthcare[190], but this topic is completely eliminated from the scope of the Services Directive.

[190] See eg A Cygan, 'Public Healthcare in the European Union: Still a Service of General Interest?' (2008) 57 Intl and Comparative L Q 529, 551 f.

Another area of competition law where Member States' governments may intervene in a way that may be relevant for our topic is merger control.

Q 40. Do the merger control rules in your member state provide for special authorisation of mergers when public interests are deemed to be at stake**? Q 41**. Have such powers been used? Give a brief overview of the cases. **Q 42.** Have these decisions been appealed to courts? What was the outcome of these appeals?

Q 40-42:

Historically, the competition aspects of mergers have been regulated formally in the UK since 1965. The review of merger transactions was conducted by the Monopolies and Mergers Commission (MMC), but ultimately determined by the Secretary of State by reference to the conception of the 'public interest', giving much room to political interests.[191] Only in 2002, the Enterprise Act brought UK merger control in line with the European standard, thereby largely following the European Merger Regulation (ECMR).[192] However, differences remain, and ss 42-70 of the Enterprise Act 2002 still provide for the possibility to examine mergers in 'public interest' and other cases, thereby deviating from the general rule that mergers should only be examined on their detrimental effect on competition and should only be assessed by competition authorities.[193] These provisions give the Secretary of State the exceptional power to intervene in such cases.

The peculiar development in this matter is not unproblematic. It had been one of the key goals of the Enterprise Act 2002 to remove politics from the merger clearance process, in all but exceptional cases. Over the last years, the scope of ministerial intervention has however been widened. Originally, the residual power for the Secretary of State to intervene (by issuing an intervention notice) and take over the decision making process where he considers that the merger raises a 'public interest consideration' had been confined to issues of national security.[194] The Secretary of State also has power to intervene on public interest grounds in certain situations where the merger is not subject to review by the OFT due to insufficient size (the special public interest intervention regime, ss 59-66 of the Enterprise Act 2002). In 2003, the Communications Act 2003 added a number of media merger specific considerations such as freedom of expression to the notion of public interest.[195] These are at stake in a case concerning the acquisition of a major stake in ITV by BSkyB, currently pending before the Court of Appeal.[196]

Moreover, in October 2008, the public interest was extended to include 'the stability of the UK financial system' as a new public interest consideration; at the same time, the Secretary of State issued an intervention notice in respect of the proposed merger of HBOS and Lloyds TSB, relying on

[191] On the history of UK merger control, see A Scott, 'The Evolution of Competition Law and Policy in the United Kingdom' LSE Law, Society and Economy Working Paper 9/2009, <http://eprints.lse.ac.uk/24564/1/WPS2009-09_Scott.pdf>.

[192] Council Regulation (EC) 139/2004 of 20 January 2004 on the control of concentrations between undertakings (the EC Merger Regulation) [2004] OJ L24/1.

[193] Whish (n 105) 951.

[194] Enterprise Act 2002, s 58(2). This power has been used on a number of occasions, see <http://www.berr.gov.uk/whatwedo/businesslaw/competition/mergers/public-interest/national-security/index.html>.

[195] Now Enterprise Act 2002, s 58(2a)-(2c). See on this DTI, *Enterprise Act 2002, Public Interest Intervention in Media mergers*; A Pryor, 'The New Regime for the Regulation of Newspaper Mergers' (2004) 3 Competition L J 63.

[196] K Holton, 'BSkyB appeals ruling to cut ITV stake' Reuters 29 October 2009, <http://uk.reuters.com/article/idUKTRE59S27N20091029>.

this new public interest consideration.[197] The merger was cleared on 31 October 2008. The Secretary of State has broad powers to add new public interest considerations to this canon at any time by issuing a statutory instrument, but this would require the approval of Parliament.[198]

This development casts serious doubts over the state of UK merger control law. Ahead of the enactment of the Enterprise Act, the UK Government had maintained that decision-making would become more predictable if mergers were no longer influenced by political considerations. The old test of whether a merger was in the public interest would be replaced with an independent decision on whether there would be a substantial lessening of competition (SLC). But, as shown, the Secretary of State may still intervene in mergers that raise public-interest considerations; and, what is more, they can redefine the public interest with parliamentary approval – as done in the Lloyds/HBOS merger. This redefinition had originally been questioned by the Merger Action Group, an association of HBOS shareholders and business customers in Scotland that challenged the public interest intervention at the Competition Appeal Tribunal.[199] They complained that the merger would reduce choice in the banking sector. At the hearing, it became however clear that the group was not challenging the Business Secretary's decision to add a new public-interest consideration. Their broader argument that the Government had pre-judged the case for a merger was dismissed in December 2008.[200] Nevertheless, the case has demonstrated that UK competition law has not been successfully de-politicised; a fact that has been strongly criticised.[201]

The position is different when a merger is subject to the jurisdiction of the EU Commission rather than the OFT. In such circumstances, the Secretary of State can also intervene on public interest grounds, by issuing a European Intervention Notice under s 67 of the Enterprise Act.[202] However, while the Secretary of State can prohibit a merger or clear it subject to commitments under the European intervention scheme, he is not able to override a prohibition of a merger by the EU Commission. European intervention notices have been issued on four occasions; each case was settled on the basis of undertakings accepted by the secretary of state to safeguard UK national security.[203]

---

[197] Office of Fair Trading, *Anticipated acquisition by Lloyds TSB plc of HBOS plc – Report to the Secretary of State for Business Enterprise and Regulatory Reform* (24 October 2008); C Pouncey and I Bukovics, 'Merger control, credit-crunch style: UK Government intervention in the Lloyds/HBOS merger' (2009) 30 Eur Competition L Rev 67.
[198] Enterprise Act 2002, s 58(3), (4).
[199] <http://www.mergeractiongroup.org.uk/>.
[200] Case 1107/4/10/08 *Merger Action Group v Secretary of State for Business, Enterprise and Regulatory Reform* [2008] CAT 36.
[201] L Smith, 'The Lloyds-TSB and HBOS Merger: Competition Issues' House of Commons Standard Note SN/BT/4907, 15 December 2008; J Rozenberg, 'Go-ahead for Lloyds TSB merger with HBOS leaves competition law in tatters' *The Evening Standard* (London 16 December 2008). Cf also the debate in the Scottish Parliament in May 2009, <http://www.theyworkforyou.com/sp/?id=2009-05-13.17400.0>.
[202] Whish (n 105) 954.
[203] Whish (n 105) 954.

State aid

Q 43. Does your Member State have national rules on the granting of state aid? Are there any procedural rules on the granting of state aid?

The UK does not have national rules on state aid as such, nor are separate procedural rules in place. However, the Office of Fair Trading (OFT) has been very active over the past years to enforce European state aid rules and to provide guidance on domestic subsidies.

Beginning in 2004, the OFT has produced a report[204] and a case study[205] on state aid law.[206] These two instruments provided the background for the official OFT proposals to reform European state aid control, presented to the European Commission in November 2005.[207] The proposals set out how state aid law could be changed to introduce a more effects-based approach to state aid approval. This could reduce the risk that state aid that distorts competition significantly is permitted while less distorting aid is prohibited or subjected to lengthy scrutiny. The OFT also recommended a formal advisory role for national competition authorities in helping the Commission to decide whether to approve state aid.

Moreover, a joint paper by the OFT and HM Treasury from January 2007 sets out 'Guidance on how to assess the competition effects of subsidies'.[208] This document is to help subsidy providers to assess whether a proposed subsidy is likely to have a significant effect on competition and, if this is the case, incorporate this effect into the wider appraisal of the subsidy. Irrespective of whether European state aid rules are violated or not, the paper recommends following the self-assessment. If the subsidy falls within the remit of European state aid law, it might be easier to convince the European Commission to approve the aid if a competition assessment has been carried out.[209] If not, the guidance document does not carry any direct legal sanction, but the subsidy might give cause for competition concerns, depending on the outcome of the self-assessment.

Q 44. Has the application of the guidelines for state aid to the financial sector mentioned above been successful in addressing the distortions of competition resulting from the massive aid operations and the accompanying measures? **Q 45.** Discuss the main Commission decisions concerning your member state so far. As these decisions all contain a revision clause that the effects of the aid have to be assessed after six months it is appropriate to describe/analyse the follow up measures. Such analysis should be focused on the main theme of this questionnaire, as set out above.

As a response to the recent financial crisis and the massive state interventions in the UK, state aid law issues have become relevant under two headings. Whilst the early measures to fight the crisis were based on the 'rescue aid' exception (Article 107(3)(c) TFEU, ex Article 87(3)(c) EC), the Commission later developed its own framework of guidelines, making use of what is now Article 107(3)(b) TFEU which allows for exceptions to remedy a serious disturbance in the economy of a Member State.

---

[204] OFT, *Public Subsidies* (OFT paper 750), November 2004.
[205] OFT and Nera Economic Consulting, *Case studies of public subsidies* (OFT paper 828), January 2006.
[206] See the speech by OFT chairman Sir John Vickers of 14 July 2005, 'State aid and distortion of competition', Speech 06/05.
[207] OFT, *European state aid control* (OFT paper 821), November 2005.
[208] HM Treasury and OFT, *Guidance on how to assess the competition effects of subsidies* (OFT paper 829), January 2007.
[209] ibid para 1.7

(1) Rescue aid

The early crisis victim Northern Rock came into serious difficulties as early as September 2007, due to its dependence on wholesale funding, including issuing mortgage-backed securities, covered bonds and medium and short term unsecured funding. The Commission found that the emergency liquidity assistance provided by the Bank of England on 14 September 2007, which was secured by sufficient collateral and was interest-bearing, did not constitute state aid. However, the guarantee on deposits and other measures granted by the Treasury later were considered to constitute state aid, but could be authorised as rescue aid in line with the Community Guidelines[210] on state aid for rescuing and restructuring firms in difficulty.[211]

About one year later, in September 2008, the UK government designed a package of measures to rescue Bradford and Bingley. This comprised measures to ensure financial stability, protect retail depositors and support the orderly winding down of the company, while its retail deposit book was sold to Abbey National after a competitive process. These measures were also cleared[212] under the rescue aid exception, although this time the Commission went to the limits of what could be approved as rescue aid under the guidelines.[213] The winding down of a company and the sale of the deposit book to a competitor constitute a structural measure which can only exceptionally be justified under the guidelines.

(2) Systemic crisis aid

It became apparent that the rescue exception would not be an adequate provision to tackle the wider financial crisis. Member States, and especially the UK, felt a need to address the problems on a larger scale, also providing aid to firms that were not in a 'rescue' state. Following the fall of Lehman, many companies that were otherwise fundamentally sound had become unable to obtain credit on the financial markets.

Now based on Article 107(3)(b) TFEU, the Commission therefore adopted (sectoral) guidelines for the banking sector in 'The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis' ('Banking Communication')[214], 'The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition' ('Recapitalisation Communication')[215] and on the 'treatment of impaired assets in the Community banking sector' ('Impaired Assets Communication').[216] These were followed up and summarised in a communication on the return to viability.[217]

---

[210] Communication from the Commission – Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty [2004] OJ C244/2.

[211] European Commission, decision NN70/2007 of 5 December 2007, Northern Rock, [2008] OJ C43/1. Cf J Lever, 'Northern Rock's rescue state aid' (2008) 7 J of Intl Banking and Financial L 227.

[212] European Commission, decision NN41/2008 of 1 October 2008, Bradford and Bingley, [2008] OJ C290/2.

[213] C Quigley, *European State Aid Law and Policy* (2nd edn, Hart Publishing, Oxford 2009) 337.

[214] European Commission, *Communication from the Commission of 13 October 2008 – The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis* [2008] OJ C270/8.

[215] European Commission, *Communication from the Commission of 5 December 2008 – The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition* [2009] OJ C10/2.

[216] European Commission, *Communication from the Commission of 25 February 2009 on the treatment of impaired assets in the Community banking sector* [2009] OJ C72/1.

[217] European Commission, *Commission communication of 14 August 2009 on the return to viability and the assessment of restructuring measures in the financial sector in the current crisis under the State aid rules* [2009] OJ C195/9.

These sectoral communications were accompanied by a (horizontal) 'temporary framework for State aid'[218] to help Member States address the exceptional difficulties of companies to obtain finance during the financial and economic crisis. In particular, the framework enables Member States to grant the following types of aid, under certain conditions, until the end of 2010:

- up to €500,000 per company over the next two years
- state guarantees for loans at a reduced premium
- subsidised loans, in particular for the production of green products (meeting environmental protection standards early or going beyond such standards)
- risk capital aid up to €2.5 million per SME per year (instead of the current €1.5 million) in cases where at least 30% (instead of the current 50%) of the investment cost comes from private investors

Any measures introduced under the framework must be in the form of a scheme, and must be notified to the Commission. The UK has four major schemes approved under the framework[219]:

Small amounts of compatible aid (N 43/2009). This scheme enables aid of up to €500,000 per undertaking to be awarded provided the conditions of the framework (section 4.2 in particular) are met.

Temporary Aid in the Form of loan guarantees (N 71/2009) enables guarantees to be given at a subsidised annual premium. A reduction in the grant premium can be offered for a maximum of 2 years. The methodology used for the calculation of guarantees should be that provided in the EU's safe harbour provision, with a reduction of up to 25% for SMEs, and up to 15% for large companies.

Temporary Aid for the Production of Green Products (N 72/2009) allows subsidised interest rates for investment in environmental products. The subsidised rate can be applied for a maximum of 2 years following the granting of loan towards production of new products which significantly improve environmental protection or which involve early adaptation or going beyond community standards. The interest rate should be calculated using the methodology set out in the framework (paras 4.4.2 & 4.5.2) with a reduction of up to 50% for SMEs, and 25% for large companies.

Aid in the form of Subsidised Loans (N 257/2009): This scheme is open to all sectors of the economy and applies to loan contracts concluded from the date of the Commission approval (14 May 2009) to 31 December 2010. The reduced interest rates may be applied for interest payments due before 31 December 2012.

Outside the Temporary framework, the Commission has adopted a number of decisions concerning the UK, clearing eg the aid scheme to the banking industry in the UK (guarantees, recapitalisation & other)[220] and the working capital guarantee scheme.[221] The former of the two has already been

---

[218] European Commission, *Temporary Community framework for State aid measures to support access to finance in the current financial and economic crisis (consolidated version)* [2009] OJ C83/1.

[219] In all four cases, the Commission decided not to raise objections.

[220] European Commission, decision N507/2008 of 13 October 2008, Financial Support Measures to the Banking Industry in the UK, [2008] OJ C290/4; European Commission, decision N650/2008 of 22 December 2008, Modified Financial Support Measures to the Banking Industry in the UK, [2009] OJ C54/3. See on this N Tait and J Croft, 'UK banks' state aid plan backed by Brussels' *Financial Times* (London 23 December 2008).

[221] European Commission, decision N111/2009 of 24 March 2009, Working Capital Guarantee Scheme, [2009] OJ C143/7.

prolonged until October 2009, since the problems continued to exist[222], whereas the second scheme has in an unusual move been approved for 12 rather than 6 months.

The restructuring scheme for **Northern Rock** is still under assessment.[223] After the initial emergency rescue package was cleared (see above), the UK submitted in March 2008 a comprehensive restructuring plan for Northern Rock. On 2 April 2008, the Commission opened a formal investigation procedure according to (what is now) Article 108(2) TFEU.[224] Subsequently, the plan was substantially altered by the UK, ultimately notified on 2 April 2009. On 7 May 2009, the Commission initiated a detailed investigation into the plan, at this time sceptical that the measures included in the new restructuring plan are compatible with the common market.[225] On the one hand, the Commission doubts that the aid is limited to the minimum necessary and that the own contribution by Northern Rock is adequate; on the other hand, the Commission doubts that the negative spill-over effects of the measures for competitors have been sufficiently limited.

(3) Assessment

All in all, while showing some flexibility on government support in emergency situations, the Commission was and is determined to exercise strong control when it comes to restructuring so as to minimise the distortions to competition caused by state aid. Article 107(3)(b) TFEU has been invoked to a large extent. After initial measures based on Article 107(3)(c) TFEU, the Commission has rightly acknowledged that there is serious disturbance in the UK economy and that measures supporting banks are apt to remedy serious disturbance in the UK economy. Therefore the legal basis for the assessment of the aid measures was chosen to be Article 107(3)(b) TFEU.

As the Commission has set out in the various Communications adopted in the context of the current financial crisis,[226] aid measures granted to banks in the context of the ongoing financial crisis were nevertheless assessed in line with the principles of the rescue and restructuring aid guidelines[227], while taking into consideration the particular features of the systemic crisis in the financial markets.[228] That means that the principles of the rescue guidelines had to be adapted when applied to any restructuring measure in the financial crisis, assessed on the basis of Article 107(3)(b) TFEU. The application of the rescue and restructuring aid guidelines is questionable: they are designed to solve individual problems and tailored for individual companies, but not for systemic problems. The state aid challenges that surfaced during the financial crisis often concerned these latter systemic problems, eg state aid to otherwise healthy banks.

When the economic and social consequences of the crisis unfolded, the calls for a suspension or weakening of competition enforcement became stronger everywhere. Such arguments might appear altogether reasonable to the public, and it is precisely here that the danger lies. The UK, with its huge financial sector, was one of the leading Member States to avail itself of the relaxed state aid rules.

---

[222] European Commission, decision N193/2009 of 15 April 2009, Extension of Credit Guarantee Scheme (CGS), [2009] OJ C145/3.
[223] European Commission, decision C14/08 (ex 1/08) of 2 April 2008 to initiate the formal investigation procedure according to Article 4(4), Northern Rock, [2008] OJ C135/21; decision of 7 May 2009 to extend proceedings, [2009] OJ C149/16.
[224] European Commission, decision C14/08 (ex 1/08) of 2 April 2008, Northern Rock, [2008] OJ C135/21.
[225] European Commission, decision C14/08 (ex 1/08) of 7 May 2009, Northern Rock, [2009] OJ C149/16.
[226] See above n 214 ff.
[227] Above n 210.
[228] Banking Communication (n 214) para 42.

Whether the Commission has been successful in addressing the distortions of competition resulting from the various state aid operations is difficult to judge at this stage, since the restructuring phase of most state aid recipients has not been completed. In my preliminary view, the Commission nevertheless has so far managed to strike the right balance between sticking to established principles and giving room for temporary exceptional measures.[229] Article 107(3)(b) TFEU, which allows state aid to remedy a serious disturbance in the economy of a Member State (which had rarely been used before) has been interpreted by the Commission in a thoughtful and balanced way. In particular, the Commission has insisted that aid measures be not applied in a discriminatory way.[230] Surely, the Commission has taken into account that all state aid measures undertaken by the UK in the financial crisis are of a temporary nature, and that most loans or guarantees come at punitive conditions. Even more important, the Commission has repeatedly stressed that measures need to be limited to the minimum necessary and that the beneficiaries have to provide sufficient own contributions; moreover, negative spill-over effects of the measures on competitors have been carefully examined. This is exemplified by the Northern Rock case, where the Commission reacted very flexibly in the early emergency situation, and cleared the emergency package in 2007. However, the comprehensive restructuring plan is still subject to a thorough examination and gives rise to competition concerns.[231]

In fact, it is submitted, a weakening of the competition or state aid rules would be ill-advised economic policy. Not only would consumers be penalised, but the longer-term prospects for economic growth and employment would also be compromised. The process of 'creative destruction', conducive to innovation and development, would be turned into its opposite: 'destructive conservation'. It is the role of social policies, not a suspension of competition policy, to ease the transition.

[229] Cf the preliminary judgment by T Jaeger, 'How much flexibility do we need? Commission crisis management revisited' (2009) 8 European State Aid Law Quarterly 3.
[230] On this, see Quigley (n 213) 339 and the Commission decision NN48/2008 of 13 October 2008, Irish Banks, [2008] OJ C312/2.
[231] See text accompanying n 223.

D. Miscellaneous

Q 46. If you are of the opinion that financial regulation and supervision has an effect on the cleavage between public and private capital in your Member State please provide your views. **Q 47.** Is there a risk that the measures taken to address the financial crisis including the nationalisation of some banks, will lead to less stringent financial supervision?

Q 48 Are there any other areas of the law that are designed to secure a level playing field between public and private capital?

I do not believe that the nationalisation of banks will lead to less stringent financial supervision, or that financial supervision has any direct impact on the public/private divide in the business sector. However, I would like to highlight one problem that has been discussed in this context, namely a potential conflict of interest that could be inherent to every government shareholding: There is a conflict between supporting the 'taxpayer's interest' and the objective of guaranteeing competition.

Take the example of UK Financial Investments (UKFI), which manages the Government's holdings in (partly) nationalised banks.[232] This company, wholly owned by HM Treasury, has been set an express overarching objective which includes both 'protecting and creating value for the taxpayer as shareholder' and 'acting in a way that promotes competition'.[233] These two goals could come into conflict as limiting competition could boost profits for the banks in which they own shares: It would be in the interest of the taxpayer as a shareholder to decrease competition, thereby increasing the profits. That would, in turn, help generate a better return for the major stakeholder in the bank, the government – and ultimately the taxpayer.[234] UKFI is faced with the demands of EU competition interests and the other shareholders of the banks, including their employees and management. If they are too much focused on securing money for 'the taxpayer', the UK domestic banking system could suffer from a lack of innovation and competition. This conflict has been illustrated by a statement by UKFI's chief operating officer, Mr Sam Woods, who said: 'If our sole objective was to protect and create value for the shareholder, then obviously a narrow reading of that could lead you to behave in a way that was not good for competition. So it was very important both for us because clearly that will be contrary to the Government's interest, but also for the competition bodies, the Office of Fair Trading, etc., that there was some offsetting element in there to make sure that we had that balance in terms of our activities'.[235]

A similar, related, point relates to the high interest rate that the Government charged when supporting banks and the objective that banks increase lending. The UK government charged extremely high interest rates to ensure that the taxpayer does not 'lose out'. Funding banks on terms which are disadvantageous to them will incentivise the banks to pay the loans back as quickly as they can, and that usually means not expanding their balance sheet through increased lending to the business sector.[236] This conflict concerns especially part-nationalised banks. For example, there is an inherent conflict between ensuring that the banks maintain high capital ratios, protecting the

[232] See on this above n 20.
[233] 'UK Financial Investments Limited: Shareholder Relationship Framework Document' para 3, available in UKFI, *An introduction: who we are, what we do, and the framework document which governs the relationship between UKFI and HM Treasury* (2009) 13.
[234] House of Lords Select Committee on Economic Affairs, *Second Report – Banking Supervision and Regulation*, (HL Paper 101-I, June 2009) para 202.
[235] ibid.
[236] House of Commons Treasury Committee, *Banking Crisis: dealing with the failure of the UK banks – Seventh Report of Session 2008-09* (21 April 2009) paras 151-155. See the Government's Response in House of Commons Treasury Committee, *Banking Crisis: dealing with the failure of the UK banks: Government, UK Financial Investments Ltd and Financial Services Authority Responses to the Seventh Report from the Committee – Seventh Special Report of Session 2008-09* (21 July 2009) 7.

taxpayer interest and wanting the banks to increase lending levels. This tension was demonstrated by the Government's initial decision to charge a 12% coupon on its preference shares which may have adversely impacted on the ability of the part-nationalised banks to increase lending levels. To this end, there has been a pressing need for the Government to clarify its strategic objectives and priorities with respect to the part-nationalised banks as well as towards other banks that are also facing conflicting pressures from Government.

Bank bail-outs always involve an agonising balancing act: for instance the problem of systemic stability versus moral hazard or of fighting recession by lending to small businesses versus safeguarding the taxpayer's investment. We cannot offer a solution to these problems here. It is only intended highlight the problem and the conflict that arises in almost every bail-out decision, however most prominently in bank bail-outs.