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Services of General Economic Interest in the EU: A 50-Year-Battle Between Liberalization, Deregulation and Subsidiarity

Dita Sole*

This article seeks to illustrate that the current treatment of services of general economic interest in European Community law creates legal uncertainty, obstructs the functioning of the internal market, and impairs the operation of the market economy more generally.

A substantial part of this article is devoted to establish the current shortcomings in the treatment of services of general economic interest and to propose improvements for the future. With regard to the former, I have come to the conclusion that the current legislative framework for services of general economic interest reduces legal certainty, fails to achieve fundamental Community objectives, and does not respond adequately to changing market circumstances. Furthermore, the judicial and supervisory authorities have not achieved the results, which could have been expected from them by society.

In relation to the proposed remedies, the main emphasis is placed on the completion of sector-specific legislation. However, the deletion of Article 86 (2) from the EC Treaty is identified as an alternative, and also as a remedy that could be more effective or even necessary in the long-run. This article concludes with an argument that the completion of sector-specific legislation is beneficial. Besides strong support for this remedy by Member States and undertakings, this approach has had positive, though incomplete, results. Therefore, with further action on the part of the Community through effective amendments of current sector-specific legislation and introduction of a new institutional framework extensively involving both the Commission and national competition authorities, the disadvantages of sector-specific legislation can be eliminated or at least substantially minimized.

A. Introduction: Competition Law and State Activities

Since the beginnings of the Coal and Steel Community in the 1950s, one of the EC's objectives is to achieve an effectively functioning market with fair and competitive conditions for all economic operators. For this reason Community competition policy has taken four directions: it deals with cartels and trusts, mergers, state aid, and liberalisation of general interest sectors, as embodied in

* LL.B., Concordia International University Estonia School of Law; LL.M., Harvard University School of Law; Attorney-at-Law, New York. This article is based on my final thesis at Concordia.

European Journal of Law Reform, Vol. V, no. 3/4, pp 335-408.
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Articles 81 to 89 ECT. The same way as other Community policies, European competition law is based on common principles such as promotion of economic growth, improvement of living standards, solidarity between Member States, higher competitiveness of the EU in world markets, etc. In order to attain the highest level of practical effectiveness of EC competition policy, Article 10 ECT requires Member States to take "all appropriate measures" to fulfil these Treaty obligations.[1] This requires positive action by the Member States to guarantee fair competition in the internal market of the EU.

Even though EC competition policy provides a solid base for establishing an effectively functioning market with fair and competitive conditions, Member States keep interfering with the functioning of the market. In several cases this has led to serious distortions of competition law, sometimes obvious, sometimes hidden. Anti-competitive legislation,[2] political statements,[3] state monopolies,[4] exclusive or special rights,[5] taxes,[6] and state aid are some examples of negative action on the part of Member States.[7] In most of these cases the Court and the Commission have been successful in restraining anti-competitive state activities, but this is not entirely the case with regard to general interest sectors like transport, postal services, gas and electricity. In spite of the introduction of many pieces of secondary legislation for the protection of competition in the internal market, not all legal problems have been solved. Furthermore, it was not before

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[1] EC Treaty. Treaty Establishing the European Community (formerly the European Economic Community) 1957, as amended, Arts. 2-3, 10.

[2] The problem is that the Commission is not empowered to review national law before its adoption. Thus, anti-competitive national provisions are frequently adopted by Member States. Although the Treaty provides for post-adoption control through the ECJ under Arts. 226, 234 and 243, it is often too late, as the damage to the functioning of the single market has already occurred, and in many cases is irreversible. In addition, these control mechanisms are only available if measures substantially affect intra-Community trade. Furthermore, Art. 30 exceptions can distort competition in the single market, e.g. market access is more limited by allowing one Member State to maintain stricter requirements for the protection of consumer health; see *C.M. von Quitzow*, State Measures Distorting Free Competition in the EC: a Study of the Need for a New Community Policy Towards Anti-Competitive State Measures in the EMU Perspective, 2002, pp. 27-29; EC Treaty, Arts. 30, 226, 234 and 243.

[3] It has been stated by the ECJ that competition may be distorted by political measures, whether express or implied. In *Commission v. France*, where the French government failed "to protect deliveries from being attacked by aggressive French farmers' associations," the French farmers implied government support in this respect, even though it was contrary to EC law (distorted competition and free movement of goods); see Judgment of 9 December 1997 in *Case 265/95, Commission of the European Communities v. France*, [1997] ECR I-6959.

[4] State monopoly is a *per se* violation of EC competition law, as it forecloses the market to competitors; see also *Von Quitzow*, *supra* note 2, at 36.

[5] See id. at 38.

[6] Differences in tax rates are also *per se* distortions of competition. It is unfortunate that Member States are resisting the harmonisation of tax law, and with a 25-member EU it will be impossible to harmonise tax law due to the unanimity requirement; see *Von Quitzow*, *supra* note 2, at 41.

[7] *Von Quitzow*, *supra* note 2, at 39; state aid is also considered as an activity, which *per se* distorts competition because some undertakings have a chance to operate on more favourable terms than others.

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the 1980s that any action was taken with respect to services of general interest, and even then new inefficiencies were created by the Community institutions themselves. This article will analyze privileges granted by Member States to public or private undertakings for the provision of 'universal services,' and more particularly, the regulation of services of general economic interest in the Community.

To better understand the regulation of services of general economic interest, a short look back into history is necessary. The reasons for exempting services of general economic interest from most competition rules date back to the time after World War II, when governments were the only providers of such services as gas, electricity, water, public transportation and telecommunications. To build up Europe after the war, states provided these services to all people at universal terms and affordable rates. This was deemed necessary because of the high start-up investment required for the provision of these services, and governments propagated the idea that these services should be regarded as 'natural monopolies.' This article will demonstrate, however, that this treatment of services of general economic interest has created long-term problems in the economic development of the EC. In particular the lack of real competition in these areas has led to higher prices, lower quality and less efficiency.[8]

The development of EC measures on state distortions of competition can be divided into four stages. The first stage refers to the late 1970s, when the Court of Justice ruled that not only undertakings but also Member States have to respect EC competition law. With this case law the Court prohibited Member States from taking measures that would allow undertakings to exercise anti-competitive behaviour otherwise prohibited under Articles 81 to 89 EC Treaty.[9] The second stage refers to the mid 1980s, when the Court's practice was largely dominated by the recognition of a need for liberalization of general interest sectors. The Court generously extended the scope of Articles 3, 10, 81 and 82 in order to prohibit anti-competitive state practices.[10] The third stage of the development was heavily influenced by the inclusion of the subsidiarity principle into the Treaty. As a result, local regulation was favoured by the Court allowing Member States to protect domestic regulation of services of general economic interest.[11] The final stage, which continues today, is characterized by serious criticism in legal literature,[12] of the current regulation of services of general economic interest and the resulting favourable treatment of anti-competitive state measures. This is also the aim of the present article.

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[8] *M. Cint & L. McGowan*, Competition Policy in the European Union, 1998, pp. 161-162.
[9] For example, see Judgment of 16 November 1977 in *Case 13/77*, *GB-Inno-BM NV v ATAB,* [1977] ECR 2115.
[10] For example, see Judgment of 21 September 1988 in *Case 267/86, Van Eycke Pascal v. ASPA NV*, [1988] ECR 4769; Judgment of 30 April 1986 in *Case 209-213/84*, *Criminal Proceedings against Lucas Asjes and others*, [1986] ECR 1425.
[11] For example, see Judgment of 17 November 1993 in *Case C-245/91*, *Officier van Justitie v. Ohra Schadeverzekeringen*, [1993] ECR I-5851; Judgment of 17 November 1993 in *Case C-185/91, Reiff – Bundesanstalt für den Güterfernverkehr*, [1993] ECR I-5801.
[12] *Von Quitzow*, *supra* note 2, at 241 – 245.

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For a long period of time the Commission has denied the need for the liberalization of services of general economic interest, and has only attempted gradual legislative changes, which have made minor or no improvements to the competitive situation in the EU.[13] As market circumstances changed, it could have reasonably been expected from the Commission that it would develop an action plan in order to adjust the legislation. However, the need for further changes in regulation of services of general economic interest has received closer attention from the Commission only recently.[14] Such an attitude has delayed improvements in the efficiency of the service infrastructure, thus also the possibility for the economy to grow, which has become particularly painful in recent years given the economic slowdown across the EU. The importance of services of general economic interest has to be seen in their interdependency with other economic sectors. As a result, ineffective regulation of these services produces negative spill-over effects on the rest of the economy. Specifically, the current treatment of services of general economic interest in Community law creates legal uncertainty, obstructs the functioning of the internal market and damages the functioning of a market economy. Thus, although resistance may be expected from the Member States, the harmonization of sector-specific legislation should either be completed or services of general economic interest should be fully deregulated.

To analyze the current and future regulation of services of general economic interest, this article is divided into seven chapters. The introduction is followed by Chapter B, which defines 'services of general economic interest' and is devoted to the analysis of their current treatment under EC competition law. Chapter C looks shortly at the treatment of services of general economic interest under WTO-GATS.

Chapter D analyses in detail the shortcomings of the current regulation. Firstly, it establishes that the protection of providers of services of general economic interest from competition has reduced legal certainty and fails to achieve fundamental Community objectives. Secondly, the shortcomings of the judicial process are identified as contributors to the problematic situation at present. Thirdly, this chapter established the claim that the need to differentiate between public service obligations[15] and private services, and to provide higher protection to the former in order to satisfy market needs, has decreased. While it cannot yet be claimed that universal service obligations should be entirely abolished, technological advancements in various general interest sectors may one day make this possible. The final part of this chapter looks at the

[13] *Cint & McGowan*, *supra* note 8, at 160.

[14] Mario Monti, former Member of the European Commission and Commissioner for competition matters, stated that "the Commission promises that where new issues arise in the field of services of general [economic] interest … to provide further clarification in the interest of legal certainty;" see *M. Monti*, Services of General Interest in Europe, 6 EuZW 161 (2001), at http://www.beck-online.de.

[15] The notion 'public service obligations' will be used interchangeably with the notion 'universal service obligations' throughout this paper. The different wording is important to better illustrate the various shortcomings of the current regulatory framework.

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Commission's failure to act.

Chapter E is devoted to a debate of previously suggested remedies, and finally, Chapter F contains the conclusions from the preceding chapters and proposes remedies to improve the competitive situation in the EU. The article concludes that the harmonization of sector-specific legislation should either be completed or services of general economic interest should be fully deregulated by removing Article 86 (2) from the EC Treaty. The advantages of the former suggestion would be the achievement of a high level of legal certainty and effective functioning of the internal market. In addition, the Community is already half way towards achieving this goal.

The advantage of the latter solution is the possibility of restoring competition without the time-consuming adoption process of multiple legal acts. In addition, as changes will be made to the EC Treaty, which has a higher authority in the hierarchy of EU legal norms, the level of enforcement would also be higher. This would allow EU inhabitants and businesses to protect their rights more effectively.

B. Services of General Economic Interest and Their Treatment Under EC Competition Law

The term 'services of general economic interest' is neither defined in the EC Treaty nor in the secondary Community legislation. According to Community practice it "refers to market services which the Member States subject to specific public service obligations by virtue of a general interest criterion."[16] The wide definition covers both network and non-network based services. Network-based services are services such as public water, gas, electricity, fixed-line telecommunications and railway services. Other or non-network based services include postal services, port services, maintenance of non-commercially viable air routes, ambulance services and others.[17]

It should also be mentioned that the term 'services of general economic interest' particularly refers to 'economic' services. It does not cover social and cultural matters, which are still considered sensitive topics that Member States want to regulate at the national level. This can also be seen in the EC Treaty, which only allows the Community to 'support' and 'complement' the actions of Member States in social and cultural matters.[18] Nevertheless, the border between economic and non-economic services cannot always be clearly drawn. Nowadays many activities have become of increasing economic importance, e.g. health care and social security schemes. Nevertheless, they do not fall within the scope of services of general economic interest as they are "intrinsically

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[16] Services of General Interest in Europe, OJ 1996 C 281/3.
[17] See Section III of this chapter.
[18] *R. Lane*, EC Competition Law, 2000, p. 231; EC Treaty, Arts. 136-151. See also *infra* Chapter B, Section III.

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prerogatives of the State."[19]

Furthermore, due to different economic, political and social conditions in the Member States, each Member State is largely free to determine which sectors it considers 'services of general economic interest' and to regulate them in a manner that does not violate the obligations under the Community law. However, national regulation is subject to judicial review by EC institutions to prevent abusive Member State protection of their industries. Certain conditions have been developed for determining whether or not a service falls under the notion of 'services of general economic interest': "[the] service [is] fulfilling certain essential needs of the population … [and provided] throughout a defined territory … to all consumers within [that] territory … under affordable conditions."[20] On the basis of these criteria not all economic activities of the Member States will be of general economic interest.

The term 'services of general economic interest' appears in two places in the EC Treaty: firstly, in Article 16, and secondly, in Article 86 (2). These will be considered in turn.

I. Articles 16 and 86 (2) EC Treaty

Article 16 was introduced by the Treaty of Amsterdam in 1999. This article stipulates that

> [w]ithout prejudice to Articles 73, 86 and 87, and given the place occupied by services of general economic interest in the shared values of the Union as well as their role in promoting social and territorial cohesion, the Community and the Member States … shall take care that such services operate on the basis of principles and conditions which enable them to fulfil their missions.

Even though Article 16 affirms the value of public service obligations in the Union, this provision can be interpreted in two ways.[21]

Firstly, it could be seen as a change in the legal situation in that a continuous provision of services of general economic interest is now one of the objectives of the Community, as this article places a positive obligation both on Member States and on the Community. Therefore, public service obligations have obtained a *special rather than exceptional* treatment under the Community law.[22]

Secondly, it could be argued that Article 16 has brought no change in the legal situation after Amsterdam. This may be true especially when considering Declaration 13, which was annexed to the Treaty of Amsterdam, and "states that

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[19] Green Paper on Services of General Interest [2003] COM/2003/270 final, at pp. 14-15.

[20] *F. Blum, & A. Logue*, State Monopolies Under EC Law, 1998, pp. 222-223; Judgment of 10 December 1991 in *Case C-179/90, Merci Convenzionali Porto di Genova v. Gabrielli*, [1994] ECR I-5889, at paragraph 27.

[21] *J. Stanciute*, The Status of Services of General Economic Interest in the European Community (2002) (LL.B. thesis, Concordia International University Estonia, on file with author), at p. 24.

[22] Id.

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the provisions in Article 16 on public services '*shall be implemented with full respect for the jurisprudence of the Court of Justice*,[23] inter alia in regard to the principles of equality of treatment, quality and continuity of such services'."[24] It would have been better to draft Article 16 in a less ambiguous manner. As an unclear provision, it cannot overrule the Court's case law because this would reduce legal certainty. In addition, if the purpose of Article 16 were to harmonize the provision of all services of general economic interest across the EU, it would have been necessary to delete Article 86 (2) from the EC Treaty in order to avoid contradictions.

A further indication of the insignificant legal value of Article 16 could be the absence references to this provision in the Court's case law, even though this article was introduced already five years ago. The President of the CFI in his order in *Poste Italiene* has merely stated that services of general economic interest constitute one of the objectives of the Community that help to achieve a higher degree of economic and social cohesion.[25] In three other cases Advocates General Alber and Jacobs have expressed slightly different opinions on Article 16, and have confirmed not only its political meaning but also its role as a mediator among various Community policies that intend to safeguard competition in the internal market of the EU.[26] The direction that the Advocates General have chosen is an indication that the inclusion of Article 16 into the EC Treaty may create problems, as Article 86 (2) is a derogation in comparison to Article 16, which is a positive obligation. Especially the wording of Article 16: operation "on the basis of principles and conditions which enable [undertakings providing services of general economic interest] *to fulfil their missions*"[27] seems misleading. It may well be understood as a 'green light' for those Member States which believe that undertakings providing services of general economic interest may not be subject to competition rules at all, as it may hinder the performance of their tasks. Ultimately, clearer ECJ judgments on this matter must be awaited

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[23] Emphasis added.

[24] *M. Ross*, Article 16 E.C. and Services of General Interest: from Derogation to Obligation?, 25/1 ELR 2000, 22, at p. 29. See also *Ch. Calliess & M. Ruffert*, Kommentar des Vertrages über die Europäische Union und des Vertrages zur Gründung der Europäischen Gemeinschaft [Commentaries to the European Union Treaty and European Community Treaty], 2002, pp. 524-531.

[25] Order of the President of the Court of First Instance of 28 May 2001 in *Case T-53/01, R Poste Italiane SpA v. Commission of the European Communities*, [2001] ECR II-1479, at paragraph 132.

[26] Opinion of Mr Advocate General Alber of 1 February 2001 in *Case C-340/99, TNT Traco SpA v. Poste Italiane SpA and Others,* [2001] ECR I-4109, at paragraphs 91-92; Opinion of Mr Advocate General Jacobs of 17 May 2001 in *Case C-475/99*, *Firma Ambulanz Glöckner v. Landkreis Südwestpfalz*, [2001] ECR I-8089, at paragraph 175; and Opinion of Mr Advocate General Jacobs of 30 April 2002 in *Case C-126/01, Ministere de l'Economie, des Finances et de l'Industrie v. GEMO SA*, [2003] ECR I-13769, at paragraph 124. In particular, Advocate General Jacobs states that state aid to undertakings providing services of general economic interest may not fall under the exception of Art. 86 (2), as this would lead to abusive reduction of competition in the internal market. Thus, Art. 16 has acquired a balancing role between various Community policies that intend to safeguard fair competition.

[27] Emphasis added.

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before final conclusions can be drawn with regard to the importance of Article 16.

Thus, the description of Article 16 as "a triumph for ambiguous drafting and diplomacy"[28] in order to achieve balance between multiple interests in the Community proves to be true. The Nice Treaty did nothing to change the situation regarding the regulation of services of general economic interest.[29] A positive movement forward is the inclusion of an EU citizens' right of access to services of general economic interest in Article 36 of the Charter of Fundamental Rights of the European Union, which guarantees "social and territorial cohesion," thus further integrating the Union.[30]

Article 86 (2) EC Treaty provides a derogation from Articles 81, 82, 86 (1) and 87 EC Treaty and states that:

> undertakings entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly shall be subject to the rules contained in this Treaty, in particular to the rules on competition, insofar as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Community.[31]

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[28] Cited in *A. Jones & B. Sufrin*, EC Competition Law: Text, Cases and Materials, 2001, p. 476.

[29] See Consolidated Version of the Treaty Establishing the European Community (Nice Treaty), OJ 2002 C 325/33.

[30] Charter of Fundamental Rights of the European Union, OJ 2000 C 364/1.

[31] The treatment of state measures affecting competition in the EU is rather confusing. At the time of negotiating the EEC Treaty, the contents of current Arts. 31 and 86 were combined in one Treaty article. However, the contracting parties decided to include two different Treaty provisions, even though there were no obvious differences between the two articles, as both are addressed to Member States, provide for similar prohibitions and talk about the same type of undertakings. The main contributors to the confusion have been the ECJ as well as legal scholars, who interpreted these provisions differently. Thus, Art. 31 was invoked in the 1950s to 1980s, but Art. 86 received attention only starting by the end of the 1980s; see *J.L. Buendia Sierra*, Exclusive Rights and State Monopolies Under EC Law: Article 86 (formerly Article 90) of the EC Treaty, 1999, pp. 257-258. This has led to the situation that a fifty-year-old provision (Art. 86(2) – services of general economic interest) has been interpreted by the ECJ in less than 100 judgments, and we cannot talk about a well-established Community policy.

Further confusion was created by the ECJ in that it applied Arts. 3(g), 10 and 81 or 82 in conjunction in order to prohibit state measures distorting competition. Regarding Art. 81 the ECJ has developed a 'closed list' of state measures, which distort competition: (i) if the state measure "imposes on undertakings" to enter into agreements, which contradict Article 81; (ii) if the measure "favours the entering into of agreements contrary to Article 81"; (iii) if the state measure is "reinforc[ing] the effects of such agreements"; and (iv) if private parties adopt decisions distorting competition after such a task was delegated to them by the state; see *Buendia Sierra*, at pp. 259-265.

With regard to Art. 82 (prohibition to abuse a dominant position) the Court has said that a law infringes Art. 86, if the undertaking in a dominant position (i) cannot avoid abusing its dominant position or (ii) when the rights granted by that law could create such a situation, where the undertaking would be forced to abuse its position; see Judgment of 10 December 1991 in *Case C-179/90, Merci Convenzionali Porto di Genova v. Gabrielli*, [1994] ECR I-5889, at paragraph 17. Art. 86 applies not only when the law requires the dominant firm to infringe the Treaty but also

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Thus, in comparison to Article 86 (1) it is not Member States, to which this provision is addressed, but undertakings – both public and private.[32] In particular, Article 86 (2) EC Treaty refers to two types of undertakings: (i) revenue-producing monopolies, which are also regulated under Article 31 EC Treaty, and (ii) undertakings providing services of general economic interest. The term undertaking has the same meaning under Articles 81, 82 and 86 EC Treaty, and covers "every entity engaged in an economic activity, regardless of the legal status … and the way in which it is financed."[33] Therefore, an economic activity will be any activity of commercial nature, if goods or services are provided for remuneration, the undertaking is accepting commercial risks and is enjoying the discretion to act on its own.

In addition, Article 86 (2) requires that the undertaking is 'entrusted' with the operation of services of general economic interest. As confirmed by the Court in multiple cases, 'entrusted' means that public authority must impose certain (specific) obligations upon the undertaking. This does not require an entrustment in form of legislation or administrative act, but it is necessary that the undertaking in question can be distinguished from other economic operators.[34] Thus, the granting of concessions will also be considered as 'entrustment'.[35]

Article 86 (2) imposes two other conditions, which need to be satisfied in order for the undertaking to escape from the application of competition rules: (i) the application of competition rules must obstruct the performance, in law or in

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when: (i) the dominant firm merely exercises exclusive rights; or (ii) if the exclusive rights were capable of creating a situation, where the dominant undertaking would be forced to abuse its position by one of the four acts: requiring payment for non-requested services, charging disproportionate prices, price discrimination or refusal to use modern technology; *Case C-179/90, Merci Convenzionali Posti di Genova v. Gabriella SpA,* [1991] ECR I-5889, at paragraph 24. The previous two paragraphs demonstrate the so-called *effet utile* principle, where Arts. 3(g), 10 and 81 or 82 in conjunction cover such cases that are not regulated under Art. 86 (1) EC Treaty; see *Buendia Sierra*, at 267. This creates extreme confusion because Art. 86 (2) provides for an exception to all above-mentioned configurations (including Art. 87 EC Treaty), thus allowing the abuse of a dominant position, the conclusion of agreements contrary to Art. 81 etc.

[32] Judgment of 27 March 1974 in *Case C-127/73, Belgische Radio en Televisie v. SV. SABAM and NV. Fonior,* [1974] ECR 313.

[33] Judgment of 23 April 1991 in *Case C-41/90, Klaus Höfner and Fritz Elser v. Macrotron GmbH,* [1991] ECR I-1979, at paragraph 21; Judgment of 17 February 1993 in *Joined Cases C-159/91 and C-160/91, Christian Poucet v. Assurances Generales de France and Caisse Mutuelle Regionale du Languedoc-Roussillon,* [1993] ECR I-637, at paragraph 17; Judgment of 12 September 2000 in *Joined Cases C-180/98 to C-184/98, Pavel Pavlov and Others v. Stichting Pensioenfonds Medische Specialisten,* [2000] ECR I-6451.

[34] Judgment of 27 March 1974 in *Case C-127/73, Belgische Radio en Televisie v. SV. SABAM and NV. Fonior,* [1974] ECR 313; Decision de la Commission 71/224 du 2 Juin 1971 relative a une procedure d'application de l'article 86 du traite (GEMA) [Commission Decision concerning the application of Article 86 EC Treaty], OJ 1971 L 134/15.

[35] Judgment of 27 April 1994 in *Case C-393/92, Municipality of Almelo and Others v. NV. Energiebedrijf IJsselmij,* [1994] ECR I-1477, at paragraph 47; Judgment of 23 October 1997 in *Case C-159/94, Commission of the European Communities v. French Republic*, [1997] ECR I-5815, at paragraph 66.

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fact, of the entrusted task, and (ii) the development of trade must not be affected to such an extent as would be contrary to the interests of the Community. The obstruction of the performance of the task was interpreted by the Court in *Höfner*,[36] where it was stated that the undertaking will be subject to competition rules "unless and to the extent to which it is shown that their application is *incompatible with the discharge of its duties*."[37] It was further clarified by the Court in *Corbeau*, where the Court stated that

> the exclusion of competition is not justified … in so far as such specific services, by their nature and the conditions in which they are offered, such as the geographical area in which they are provided, *do not compromise the economic equilibrium of the service of general economic interest* performed by the holder of the exclusive right.[38]

Thereby the Court assumed that a competing service may not stand in a close relationship to the universal service as the economic equilibrium of the latter would be threatened. The equilibrium infers that providers of services of general economic interest may offset losses that are likely to arise in some sectors due to universal service obligations with profits from other sectors ('geographic area' condition).

Later the Court added that for the non-application of competition rules "it is not necessary that the survival of the undertaking itself be threatened."[39] Thus, the undertaking in question should merely be able to perform the task entrusted to it.[40] The Court is thereby stressing that the economic conditions, under which the undertaking providing services of general economic interest has to operate, can be modified to ensure that consumer needs can be satisfied. Ultimately, this guarantees that the state is able to fulfil its public service obligations towards its citizens.

The second requirement for the non-application of the Treaty rules on competition is that the development of trade must not be affected to such an extent as would be contrary to the interests of the Community. For a long time, the Court did not define this condition in its case-law. It merely stated that it is the obligation of the Commission to assess whether trade is affected in a manner which is contrary to the Community objectives[41] because such an assessment requires detailed analysis of the market, which the Court is not able to make.

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[36] Judgment of 23 April 1991 in *Case C-41/90, Klaus Höfner and Fritz Elser v. Macrotron GmbH,* [1991] ECR I-1979.

[37] See id. at paragraph 24.

[38] Judgment of 19 May 1993 in *Case C-320/91, Criminal proceedings against Paul Corbeau,* [1993] ECR I-2533, at paragraph 19; emphasis added.

[39] Judgment of 23 October 1997 in *Case C-157/94, Commission of the European Communities v. Kingdom of the Netherlands,* [1997] ECR I-5699, at paragraph 43.

[40] Judgment of 23 October 1997 in *Case C-157/94, Commission of the European Communities v. Kingdom of the Netherlands*, [1997] ECR I-5699, at paragraph 53; Judgment of 23 October 1997 in *Case C-158/94, Commission of the European Communities v. Italian Republic*, [1997] ECR I-5789, at paragraph 53,54.

[41] For example, see Judgment of 23 October 1997 in *Case C-159/94, Commission of the European Communities v. French Republic,* [1997] ECR I-5815.

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The Commission is in a better position to do this, as it has sufficient resources and experience to make adequate market evaluations.

This approach was changed in a recent judgment in *Firma Ambulanz Glöckner*, where the Court stated – similarly to the established case-law on free movement in the internal market –

> [for an] agreement, decision or practice […] to be capable of affecting trade between Member States, it must be possible to foresee with a sufficient degree of probability […] that they may have an influence, *direct or indirect, actual or potential, on the pattern of trade between Member States* in such a way as to cause concern that they might hinder the attainment of a single market between Member States. [42]

Although the Court ruled that it is the national court which must make the evaluation whether or not the 'trade criterion' has been satisfied, it has expressly recognised the possibility of intra-Community effects of services of general economic interest that used to be denied in the past. Therefore, an indirect and/or potential effect on trade between Member States can now easily be established by claiming that prices charged for services of general economic interest are passed on to producers of other goods and services, which are potentially traded across national boundaries. After this judgment the Commission followed the Court and stated that the Community interest is established, if a "barrier to the single market" has been created, meaning that any practice partitioning the internal market is prohibited. Since undertakings should be able to provide services across the EU without any restrictions, they must have access to networks on equal terms and monopolies may not operate in such a manner as to influence the market structure.[43] This behaviour of the Commission is reactive showing that the Commission in its approach is not entirely guided by market conditions.

II. Core Elements of Services of General Economic Interest

The core elements of services of general economic interest have been developed by the Court and their application has been extended by the Commission to other services of general economic interest via secondary Community legislation. The Court identifies six different elements, which characterize services of general economic interest: universality, suitability, necessity, continuity, equality of treatment and availability, which will be considered in turn below. However, the Court has been resistant to clearly define how each of these elements is to be applied to avoid definite commitments for the future and negative criticisms from the Member States. The Member States might have regarded a clear

[42] *Case C-475/99, Firma Ambulanz Glöckner v. Landkreis Südwestpfalz*, [2001] ECR I-8089, in particular paragraphs 48 and 49 of the judgment.

[43] See the Preamble to the Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communications networks and services (Framework Directive), OJ 2002 L 108/33, at paragraph 38.

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definition as an extension of Community powers because clear applicability conditions for all elements would take away the possibility of Member States to flexibly invoke the Article 86 (2) exception. Nonetheless, in the Court's case law all elements of services of general economic interest are underlined by a single notion, namely whether each particular element is satisfied has to be judged in light of the fact whether the service at hand is provided in the 'general public interest,' as it is *consumer interests* that have to be observed.[44]

1. Universality

The meaning of the 'universality' element has been explained by the Court mainly in its case law on postal services. In comparison to other elements of services of general economic interest, it has laid down definite criteria for defining whether the service is to be considered as a 'universal service.' A service is universal, if it is provided to everyone at any time at a uniform cost. Any deviations from this may be justified only if based on objective criteria.[45]

Furthermore, Advocate General Alber alleges that a better explanation of the term 'universal service' can be obtained by looking at opposites. He suggests that the opposite of a universal service is a 'non-universal' or 'value-added' service.[46] From his opinion, the meaning of the latter is not clear. However, it seems that a service will be value-added, when it satisfies specific additional needs and is not necessarily essential for the consumers. In addition, Alber points out that a value-added service should normally be provided at a substantially higher price than a universal service. Thus, a value-added service could be classified as a 'luxury product,' but a universal service is a product satisfying basic needs and provided at affordable cost. Moreover, the distinction between universal and value-added services has in some cases been provided by secondary Community legislation. For example, in the case of postal services a value-added service would be overnight or express delivery of mail or packages, while basic postal services like the delivery of various postal items not exceeding two kilograms, packages not exceeding ten kilograms, registered mail and insured items are to be considered as universal services.[47]

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[44] Opinion of Mrs Advocate General Stix-Hackl of 7 November 2002 in *Joined Cases C-34/01 to C-38/01 Enirisorse SpA v. Ministero delle Finanze*, [2003] ECR I-14243, at paragraph 99.

[45] Cited in Opinion of Mrs Advocate General Stix-Hackl of 7 November 2002 in *Joined Cases C-34/01 to C-38/01 Enirisorse SpA v. Ministero delle Finanze*, [2003] ECR I-14243, at paragraph 97. For similar judgments, where the universality principle is discussed, see also Judgment of 10 February 2000 in *Joined Cases C-147/97 and C-148/97, Deutsche Post AG v. Gesellschaft für Zahlungssysteme mbH (GZS) (C-147/97) and Citicorp Kartenservice GmbH (C-148/97),* [2000] ECR I-825; Judgment of 18 June 1998 in *Case C-266/96, Corsica Ferries France SA v. Gruppo Antichi Ormeggiatori del porto di Genova Coop. arl, Gruppo Ormeggiatori del Golfo di La Spezia Coop. arl and Ministero dei Trasporti e della Navigazione,* [1998] ECR I-3949.

[46] Opinion of Mr Advocate General Alber of 1 February 2001 in *Case C-340/99, TNT Traco SpA v. Poste Italiane SpA and Others,* [2001] ECR I-4109, at paragraph 28; see also Judgment of 17 May 2001 in *Case C-340/99, TNT Traco SpA v. Poste Italiane SpA and Others*, [2001] ECR I-4109.

[47] Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on

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In addition, secondary Community legislation sets out conditions, under which universal services have to be provided, namely objectivity, transparency and non-discrimination.[48] This characterises the universal service as one that has to be provided on fair terms to everyone, and a service will not be universal, as soon as even the smallest market segment is excluded from the service.

2. Suitability and Necessity

Due to the fact that services of general economic interest are often provided by a single supplier under exclusive rights, the Court examines whether such exclusive rights, and subsequently a restriction on competition, are suitable and necessary for the undertaking to provide the task entrusted to it. In other words, the Court is applying the proportionality test by determining whether competitive substitutes exist for the provision of the service at issue. Furthermore, it takes due account of economic, financial and social aspects of the Member State and analyses whether the undertaking provides the universal service efficiently.[49] This means that the undertaking must not only be able to satisfy the demand but it also has to provide quality services. Since national market conditions have to be evaluated, the Court believes that it is the national court, which has the duty to apply the proportionality test.[50]

National courts may favour the choices of Member States regarding the suppliers of services of general economic interest or they can support free competition in the market. It is not likely that national courts will chose the latter option. Labour unions will start lobbying by arguing that increased competition could lead to the dissolution of the undertaking in question, thus increasing unemployment. This argument alone might be strong enough for the national court to say that there are no substitutable ways to provide the service and that it is provided efficiently. As it will be demonstrated in Section III of Chapter D, this has become an unfortunate reality.

3. Continuity

The Court has said that continuous supply of services of general economic

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common rules for the development of the internal market of Community postal services and the improvement of quality of service OJ 1998 L 15/14.

[48] Commission Directive 2002/77/EC of 16 September 2002 on Competition in the Markets for Electronic Communications Networks and Services, OJ 2002 L 249/21, Art. 6.

[49] Judgment of 23 October 1997 in *Case C-159/94, Commission of the European Communities v. French Republic*, [1997] ECR I-5815, at paragraphs 96-97, 106; Opinion of Mrs Advocate General Stix-Hackl of 7 November 2002 in *Joined Cases C-34/01 to C-38/01 Enirisorse SpA v. Ministero delle Finanze*, [2003] ECR I-14243, at paragraphs 101-102; Judgment of 4 June 2002 in *Case C-503/99, Commission of the European Communities v. Kingdom of Belgium*, [2002] ECR I-4809, at paragraphs 48-53; Judgment of 25 October 2001 in *Case C-475/99, Firma Ambulanz Glöckner v. Landkreis Südwestpfalz*, [2001] ECR I-8089. See also *infra* Chapter D, Section III.

[50] Judgment of 27 April 1994 in *Case C-393/92, Municipality of Almelo and others v. NV. Energiebedrijf IJsselmij*, [1994] ECR I-1477.

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interest "constitutes a matter of public concern,"[51] and that it is the obligation of Member States to ensure that these services are continuously supplied. This is explained by the fact that services of general economic interest are strategically important, and any problems in their supply may have adverse spill-over effects on other industries. For example, undertakings, in general, cannot operate if electricity is not supplied. Thus, not only the energy industry loses turnover, but also other industries.

Nevertheless, lost turnover is only a minor problem, as the interruption in the provision of electricity and communication services may threaten public security. Nevertheless, Member States will be able to rely on this justification only if "there is a genuine and sufficiently serious threat to a fundamental interest of the Community," and the invoking of this justification will be subject to judicial control by EC institutions.[52] In any case, the public security argument will not apply to all services claimed to be of general economic interest.

4. Equality of Treatment and Availability

Equality of treatment is a fundamental principle of the Community, which means that any kind of discrimination is prohibited. With regard to services of general economic interest it particularly refers to the fact that access to these services must be granted to everyone on equal conditions. Availability, on the other hand, is one of the least interpreted elements of services of general economic interest. It means that a Member State has a public service obligation to guarantee that services of general economic interest are available to everyone at any time and at uniform cost.[53] In addition, the 'availability' element has received particular attention with regard to postal services because their availability contributes to economic and social cohesion of the Community in that postal services ensure continuous communication between Member States thereby integrating the society,[54] which is one of the EU objectives. As a result, both elements are largely overlapping with the universality principle, which was already discussed above.

[51] Judgment of 4 June 2002 in *Case C-503/99, Commission of the European Communities v. Kingdom of Belgium*, [2002] ECR I-4809, at paragraph 23.
[52] Judgment of 13 May 2003 in *Case C-463/00 Commission of the European Communities v. Kingdom of Spain*, [2003] ECR I-4581, at paragraphs 44, 70-73.
[53] Judgment of 4 June 2002 in *Case C-503/99, Commission of the European Communities v. Kingdom of Belgium,* [2002] ECR I-4809, at paragraph 52; Judgment of 23 October 1997 in *Case C-159/94, Commission of the European Communities v. French Republic*, [1997] ECR I-5815; Opinion of Mr Advocate General La Pergola of 1 June 1999 in *Joined Cases C-147/97 and C-148/97, Deutsche Post AG v. Gesellschaft für Zahlungssysteme mbH GZS (C-147/97) and Citicorp Kartenservice GmbH (C-148/97)*, [2000] ECR I-825, at footnote 51.
[54] Notice from the Commission on the Application of the Competition Rules to the Postal Sector and on the Assessment of Certain State Measures Relating to Postal Services, OJ 1998 C 39/14.

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III. Classification of Services of General Economic Interest

One possible way to classify services of general economic interest is into network services and other or non-network services. With regard to the network services, the network and the actual provision of the services have to be separated. The separation is essential, as different measures have to be taken in order to introduce more competition in the internal market. Because it is either impossible or time-consuming and inefficient to establish a second network, the law has to ensure that mere *access to the one and only network*[55] is provided in order to allow multiple undertakings to compete in the provision of services through that network. The following services are considered as network services: public water,[56] gas,[57] electricity,[58] fixed-line telecommunication services,[59] railway[60] and broadcasting.[61]

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[55] In the Court's case law 'access to a network' is discussed as 'access to an essential facility.' The essential facility doctrine means that access to the facility (or network) will be granted only if the duplication of the facility is impossible or extremely difficult owing to physical, geographic or legal constraints. It would be necessary to establish that the level of investment required to set up a second facility would be such as to deter the competitor at issue from entering the market. The Court also states that there should be no actual or potential substitutes for the facility and that the refusal of access to the facility should eliminate all competition on the downstream market; Judgment of 26 November 1998 in *Case C-7/97 Oscar Bronner GmbH & Co. KG v. Mediaprint Zeitungs- und Zeitschriftenverlag GmbH & Co. KG*, [1998] ECR I-7817.

Access should be granted to everyone willing to obtain access, as Art. 12 EC Treaty requires treating market operators on a non-discriminatory basis. In addition, there are different facilities, e.g. railways that can and most likely will be operated by state entities, as for private operators it might be extremely costly. Therefore, to such a facility, access should be granted to all those interested (in exchange for royalties); Judgment of 15 September 1998 in *Joined Cases T-374/94, T-375/94, T-384/94 and T-388/94 European Night Services Ltd (ENS), Eurostar (UK) Ltd, formerly European Passenger Services Ltd (EPS), Union internationale des chemins de fer (UIC), NV. Nederlandse Spoorwegen (NS) and Societe nationale des chemins de fer francais (SNCF) v. Commission of the European Communities,* [1998] ECR II-3141.

In addition, Arts. 154 to 156 EC Treaty provide for the promotion of trans-European networks with the aim of their interconnection and interoperability, and to provide free access to networks in transport, telecommunications and energy sectors; see Treaty establishing the European Community (formerly the European Economic Community) 1957, as amended.

[56] Judgment of 8 November 1983 in *Joined Cases 96-102,104,105,108 and 110/82, NV. IAZ International Belgium v. Commission*, [1983] ECR 3369.

[57] Judgment of 23 October 1997 in *Case C-159/94, Commission of the European Communities v. French Republic,* [1997] ECR I-5815.

[58] Judgment of 23 October 1997 in *Case C-157/94, Commission of the European Communities v. Kingdom of the Netherlands,* [1997] ECR I-5699; Judgment of 27 April 1994 in *Case C-393/92, Municipality of Almelo and others v. NV. Energiebedrijf IJsselmij*, [1994] ECR I-1477.

[59] Judgment of 20 March 1985 in *Case 41/83, Italy v. Commission,* [1985] ECR 873.

[60] Regulation (EEC) 1191/69 of the Council of 26 June 1969 on action by Member States concerning the Obligations inherent in the Concept of a Public Service in Transport by Rail, Road and Inland Waterway, OJ 1969 L 156/1.

[61] Judgment of 30 April 1974 in *Case 155/73, Giuseppe Sacchi*, [1974] ECR 409; Judgment of 18 June 1991 in *Case 260/89, Elliniki Radiophonia Tileorassi v. Dimotiki Etairia Pliroforissis,* [1991] ECR I-2925; also Protocol (No 32) annexed to the Treaty establishing the European Community

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Other or non-network services include such services as postal services,[62] port services,[63] maintenance of non-commercially viable air routes,[64] ambulance services[65] and services of an employment agency.[66] Even though a few other services of general economic interest will be used to establish the shortcomings in the current regulatory framework, the rest of this article will mainly concentrate on electricity, telecommunications, railway and postal services in order to better illustrate the competitive situation. The other reason why this article is limited to the above-mentioned services of general economic interest is that in the case of electricity, telecommunications, railway and postal services cross-border effects are more easily established due to the scale of operation of these undertakings. Therefore, the presence of a Community interest is also more likely, which justifies further action on the part of the Community. However, in the case of other services of general economic interest, case-by-case assessment is needed in order to determine whether they can influence Community interests; for these services, it is probably not possible to establish a common approach.

1. Services Provided by Large Network Industries

The Community market for *electricity*[67] can be characterised as fragmented, as the level of market integration differs from one Member State to the other. The current situation can be understood in light of the historic treatment of this sector, which is characterised by intensive government regulation. As different Member States started the liberalisation process from a different state of play and chose a different pace of liberalisation, the current market opening varies across the EU. Germany, Austria, Sweden and UK have largely opened up their electricity markets, while Denmark, Greece and France are at present still much

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on the System of Public Broadcasting in the Member States (1997) recognises broadcasting services as services of general economic interest.

[62] Judgment of 19 May 1993 in *Case C-320/91, Criminal proceedings against Paul Corbeau* [1993] ECR I-2533; Judgment of 10 February 2000 in *Joined Cases C-147/97 and C-148/97, Deutsche Post AG v. Gesellschaft für Zahlungssysteme mbH (GZS) (C-147/97) and Citicorp Kartenservice GmbH (C-148/97),* [2000] ECR I-825.

[63] Judgment of 18 June 1998 in *Case C-266/96, Corsica Ferries France SA v. Gruppo Antichi Ormeggiatori del porto di Genova Coop. arl, Gruppo Ormeggiatori del Golfo di La Spezia Coop. arl and Ministero dei Trasporti e della Navigazione,* [1998] ECR I-3949; Commission Decision 97/745 of 21 October 1997 relating to a proceeding pursuant to Article 90(3) of the EC Treaty regarding the tariffs for piloting in the Port of Genoa, OJ 1997 L 301/27.

[64] Judgment of 11 April 1989 in *Case 66/86, Ahmed Saeed Flugreisen and Silver Line Reisebüro GmbH v. Zentrale zur Bekämpfung unlauteren Wettbewerbs e.V.,* [1989] ECR 803.

[65] Judgment of 25 October 2001 in *Case C-475/99, Firma Ambulanz Glöckner v. Landkreis Südwestpfalz,* [2001] ECR I-8089.

[66] Judgment of 23 April 1991 in *Case C-41/90, Klaus Höfner and Fritz Elser v. Macrotron GmbH,* [1991] ECR I-1979.

[67] Electricity is treated as a 'good' in Community law, thus Treaty articles on free movement of goods, and in particular Article 31 EC Treaty, are also applicable; see Judgment of 15 July 1964 in *Case 6/64 Costa v. ENEL*, [1964] ECR 1141.

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less integrated.[68]

The objective to create a single energy market was introduced in the mid-1980s. It was followed by the adoption of the Electricity Transit Directive in 1990, which required Member States to allow the transit of electricity through their territory to another Member State. At the time of adoption of this directive it meant, for example, that French electricity surpluses, which were generated in nuclear power plants, could be transported across Spain to Portugal.[69] However, this directive does not allow consumers to choose which supplier to contract for the provision of electricity.

In 1996, the Electricity Directive was adopted aiming at the separation of the generation, transmission, distribution and supply functions of electricity undertakings.[70] Vertically integrated undertakings were prohibited to keep one account for all these transactions to avoid cross-subsidization, which used to allow electricity undertakings to eliminate competition in the down-stream markets. In addition, it required third parties to be able to obtain network access rights either through an authorisation or a tendering procedure. Such an approach was required as the European market could be characterised at that time by vertically integrated electricity undertakings eliminating supply-side competition in the internal market.

Further liberalisation of the electricity sector was undertaken in 2003, when the Electricity Regulation[71] and the New Electricity Directive[72] were adopted. The Electricity Regulation has made a substantial step towards more competition in the internal market. It is the first regulation in this sector, and being directly applicable, it excludes the possibility that Member States adopt anti-competitive implementing legislation or that they do not implement the EU law into national legislation at all. The most important issues covered by the Electricity Regulation are the following:

- transmitters of electricity as well as network operators have a right to receive compensation for their services *only* in the amount of the actually incurred

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68 European Commission, EU Energy and Transport in Figures 35 (2002).

69 Council Directive 90/547/EEC of 29 October 1990 on the transit of electricity through transmission grids, OJ 1990 L 313/30, Art. 1; *H. Schröter et al.*, Kommentar zum Europäischen Wettbewerbsrecht [Commentaries to the European Competition Law], 2003, p. 1914.

70 Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity, OJ 1997 L 27/20, Arts. 2, 4-6, 14, 16, 17; also the Commission, in its Decision of 19 July 1999 declaring a concentration to be compatible with the internal market (Case No. IV/M.1606–EDF/SO WESTERN ELECTRICITY) according to Council Regulation (EEC) No 4064/89, OJ 1999 C 248/9, has stated that there is no single market for electricity, Rather, there are separate markets for generation, transmission, distribution and supply of electricity; at paragraph 10.

71 Regulation (EC) No 1228/2003 of the European Parliament and of the Council of 26 June 2003 on conditions for access to the network for cross-border exchanges in electricity, OJ 2003 L 176/1.

72 Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC-Statements made with regard to decommissioning and waste management activities, OJ 2003 L 176/37.

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costs;[73]

- access to the network must be granted through an auction system and the Member States have to ensure that any one undertaking would not buy or possess the network capacity to such an extent as to enable that undertaking to exercise anti-competitive behaviour amounting to a dominant position on the market.[74]

The New Electricity Directive also provides for considerably better harmonisation of the electricity sector. It reaffirms that electricity is a universal service, which has to be available to everyone on equal conditions and at reasonable prices. The directive further presumes that the existing capacity has already been divided among electricity undertakings. Therefore, it merely refers to the allocation of any new capacity, which might appear through investment and innovation, and provides again for the authorisation and tendering procedures for its allocation.[75] In addition, the directive for the first time speaks about the freedom of end-users to choose their electricity supplier and requires Member States to enact laws containing an enforceable right of consumers to withdraw form contracts *at no charge*.[76] This helps to avoid any potential foreclosures of the market since it is now more difficult for existing suppliers to bind consumers to their services in the long-run.

However, the new directive will provide for improvements in the competitive situation only in the long-run. The main problem is that Member States may delay the implementation of this directive until 1 July 2007.[77] In addition, as past experience indicates, very often directives have not been transposed into national legislation even long after the deadline for their implementation has expired. Thus, the situation may not change even until 2010. Moreover, as will be established in Chapter E, the new regulatory framework has several gaps.

With regard to the *telecommunications* sector, the old and the new regulatory framework have to be distinguished.[78] Already the old legal framework

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[73] Regulation (EC) No 1228/2003, OJ 2003 L 176/1, Arts. 3 and 4.
[74] Annex to Regulation (EC) No 1228/2003 of the European Parliament and of the Council of 26 June 2003 on conditions for access to the network for cross-border exchanges in electricity, OJ 2003 L 176/1.
[75] Directive 2003/54/EC, OJ 2003 L 176/37, Arts. 3, 6, 7.
[76] Annex A (Measures on Consumer Protection) to Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC-Statements made with regard to decommissioning and waste management activities, OJ 2003 L 176/37.
[77] Directive 2003/54/EC, OJ 2003 L 176/37, Art. 30.
[78] The old regulatory framework for the telecommunications sector consists of the following directives: Commission Directive 88/301/EEC of 16 May 1988 on competition in the markets in telecommunications terminal equipment, OJ 1988 L 131/73; Council Directive 90/387/EEC of 28 June 1990, OJ 1990 L 192/1 (no longer in force); Commission Directive 90/388/EEC of 28 June 1990, OJ 1990 L 192/10 (no longer in force); Commission Directive 95/51/EC of 18 October 1995, OJ 1995 L 256/49 (no longer in force); Commission Directive 96/2/EC of 16 January 1996, OJ 1996 L 20/59 (no longer in force); Commission Directive 96/19/EC of 13 March 1996, OJ 1996 L 74/13 (no longer in force); Directive 97/13/EC of the European Parliament and of the

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abolished all exclusive and special rights that could be granted to undertakings and regulated network access.

The new framework has been implemented since 25 July 2003, and consists of one general[79] and four specific directives.[80] It regulates not only telecommunications, but all types of electronic communications services, networks and facilities except television broadcasting. It restates once again the universal obligations of undertakings to provide qualitative and affordable services to everyone. In addition, it includes an indirect reference that it would be beneficial, if national authorities gave up ownership or at least control of electronic communications undertakings.[81] Thus, it has been finally explicitly recognised that legal unbundling does not always mean *de facto* separation, often leading to anti-competitive effects.

The Access Directive harmonises the rules to access to the electronic communications networks and requires that access to the network is provided to every undertaking. Furthermore, the national authorities have a positive obligation to ensure that the market of electronic communications services functions according to internal market principles. In this framework they have the duty to guarantee interoperability and interconnection of electronic communications services. National authorities may interfere in the market only if it is *necessary*. The necessity requirement is a positive development in the legislation, as it allows avoiding artificial regulation of the market.[82]

The Authorisation Directive aims at the establishment of an internal market for the actual electronic communications services. According to the new provisions, any undertaking that wants to provide electronic communications services may be subject only to 'general authorisation'. This means that the undertaking may be required to inform the national authorities of its intent to provide electronic communications services, but that authorisation may no

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Council of 10 April 1997, OJ 1997 L 117/15 (no longer in force); Directive 97/33/EC of the European Parliament and of the Council of 30 June 1997, OJ 1997 L 199/32 (no longer in force); Directive 98/10/EC of the European Parliament and of the Council of 26 February 1998, OJ 1998 L 101/24 (no longer in force).

[79] Directive 2002/21/EC of the European Parliament and of the Council of 7 March 2002 on a common regulatory framework for electronic communications networks and services (Framework Directive), OJ 2002 L 108/33.

[80] Directive 2002/19/EC of the European Parliament and of the Council of 7 March 2002 on access to, and interconnection of, electronic communications networks and associated facilities (Access Directive), OJ 2002 L 108/7; Directive 2002/20/EC of the European Parliament and of the Council of 7 March 2002 on the authorisation of electronic communications networks and services (Authorisation Directive), OJ 2002 L 108/21; Directive 2002/22/EC of the European Parliament and of the Council of 7 March 2002 on universal service and users' rights relating to electronic communications networks and services (Universal Service Directive), OJ 2002 L 108/51; Directive 2002/58/EC of the European Parliament and of the Council of 12 July 2002 concerning the processing of personal data and the protection of privacy in the electronic communications sector (Directive on privacy and electronic communications), OJ 2002 L 201/37.

[81] Directive 2002/21/EC, OJ 2002 L 108/33, Art. 11.

[82] Directive 2002/19/EC, OJ 2002 L 108/7, Arts. 1 and 3-5.

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longer require an administrative act.[83] Thus, also in relation to the actual provision of the electronic communications services the legislation has taken a positive direction by prohibiting artificial interference into the functioning of the market.

In addition, effective development of the electronic communications sector has been supported by the Court and the Commission throughout its stages. From their case law it follows that the tying of telecommunications equipment and telecommunications services,[84] the foreclosure of the telecommunications market with discriminatory state measures,[85] agreements that attempt to divide the market for telecommunications[86] and predatory pricing with the intent to keep out potential competition[87] are prohibited. Thus, the liberalisation of the telecommunications sector has been the most successful until now covering all three competition concerns: (i) trade with equipment; (ii) access to the network; and (iii) actual provision of services. However, the analysis in this article is done mainly for fixed-line telecommunications, not so much for mobile telecommunications and internet services.

2. Other or Non-Network Services

The beginning of the liberalisation of *postal services* dates back only to the early 1990s, when the Commission proposed the increase of competition in the postal sector. The main reason for the Commission's action was the status of postal services as an important integrator of the European society through effective and continuous communication that takes place within the Community.[88]

The first proposal was followed by the adoption of the Postal Directive in 1997, with the main aim of developing common rules for the postal sector, improving the quality of postal services and gradually introducing a single market for these services. However, the directive's final version is much more generous than the above-mentioned objectives – it mainly harmonises basic standards of a universal postal service. Therefore, the directive only states that Member States have the obligation to ensure the qualitative, continuous and affordable supply of postal services, which includes the clearance, sorting, transportation and distribution of postal items and packages. The universal service covers various postal items not exceeding two kilograms, packages not exceeding ten kilograms, registered mail and insured items. Furthermore, national authorities may include into the concept of 'universal postal service'

[83] Directive 2002/20/EC, OJ 2002 L 108/21, Arts. 1 and 3.
[84] Judgment of 16 November 1977 in *Case 13/77, GB-Inno-BM NV. v. ATAB,* [1977] ECR 2115.
[85] Commission Decision 95/489 of 4 October 1995 concerning the conditions imposed on the second operator of GSM radiotelephony services in Italy, OJ 1995 L 280/49.
[86] Commission Decision 93/668 of 24 November 1993 relating to a proceeding pursuant to Article 85 of the EEC Treaty (IV/32031 - Auditel), OJ 1993 L 306/50.
[87] Commission notice on access agreements in the telecommunications sector, OJ 1998 C 365/2, at paragraph 110.
[88] *L. Ritter et al.*, EC Competition Law: a Practitioner's Guide, 2000, pp. 744-745..

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also packages up to twenty kilograms including their door-to-door delivery.[89] However, the door-to-door delivery is not an absolute necessity and extends into the market of value-added services, in which couriers are active. Thus, the latter may find it more difficult to survive in the market, as they have to compete with a strong and well-established postal monopoly.

The amendments to the Postal Directive in 2002 made no further improvements with regard to competition in the market for postal services, as Member States may still reserve various postal services to their monopolies.[90] Thus, the postal sector still remains an area, in which little harmonisation has taken place, and can be considered as the least competitive in comparison to other general interest sectors in which Community measures have been adopted.

However, even though the harmonisation process of postal services has not been very successful until now, the Commission and the Court have used their case law to condemn anti-competitive practices of Member States under Article 86 (1) EC Treaty. Both institutions have held that postal undertakings are in a dominant position because there is only one provider of postal services in each Member State. In order not to abuse this dominant position, postal undertakings (the same way as providers of other services of general economic interest) must be able to satisfy the demand and must do it efficiently.[91] A particular competitive concern with regard to postal services is extensive cross-subsidization, where revenue from universal postal services is used to support other or value-added services, e.g. express mail. Cross-subsidazation is considered an abuse of a dominant position as such behaviour distorts competition in separate sub-markets.[92] With some exceptions (see Chapter D, Section IV), this has been prohibited.

Nevertheless, postal services are the only non-network services for which harmonisation measures have been adopted at the Community level. Further non-network services include port services, ambulance services, services of an employment agency and waste management. These services are subject to the internal market, competition and state aid rules as long as trade between Member States is affected. In addition, in several cases environmental rules of

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[89] Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service, OJ 1998 L 15/14, art. 3

[90] Directive 2002/39/EC of the European Parliament and of the Council of 10 June 2002 amending Directive 97/67/EC with regard to the further opening to competition of Community postal services, OJ 2002 L 176/21.

[91] Commission Decision 90/16/EEC of 20 December 1989 concerning the provision in the Netherlands of express delivery services, OJ 1990 L 10/47; Commission Decision 90/456 of 1 August 1990 concerning the provision in Spain of international express courier services, OJ 1990 L 233/19; Judgment of 23 April 1991 in *Case C-41/90, Klaus Höfner and Fritz Elser v. Macrotron GmbH*, [1991] ECR I-1979.

[92] See the Preamble to the Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service, OJ 1998 L 15/14, at paragraph 28; Judgment of 19 May 1993 in *Case C-320/91, Criminal proceedings against Paul Corbeau,* [1993] ECR I-2533.

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the Community may also apply.[93]

C. Services of General Economic Interest and WTO-GATS

The term 'services of general economic interest' neither appears in the WTO-GATS nor in any annexes or decisions to the agreement. However, GATS regulates services that are covered under the EU notion of 'services of general economic interest', such as telecommunications services and air transport services. Although discussions among WTO members also dealt with the energy sector, no agreement was reached, leaving these services outside of WTO law. Nevertheless, Article VIII of GATS (on Monopolies and Exclusive Service Suppliers) attempts to regulate activities of undertakings that are usually entrusted with the provision of services of general economic interest.[94]

GATS regulates all services with the exception of services relating to the exercise of governmental authority[95] and air traffic rights,[96] and, similar to the GATT, includes an MFN requirement for every member to "accord … to services and service suppliers of any other Member treatment no less favourable than it accords to like services and service suppliers of any other country."[97] As an exception to the MFN requirement, GATS identifies and respects a higher level of liberalization in service sectors with regard to two groups of counties, namely the EU and NAFTA.[98] A particular allowance to members exists with

[93] See footnotes 56-66; see also Green Paper on Services of General Interest, COM/2003/270 final, at 10-11.

[94] WTO Secretariat, Guide to the GATS: an Overview of Issues for Further Liberalization of Trade in Services, 2001, pp. 259-261, 270; The energy sector has been under debate already since the beginning of negotiations on GATT. The division between energy goods and services is not clear-cut due to the fact that energy services are often provided by vertically integrated undertakings. Nevertheless, some of the energy products can be identified as clear goods, e.g. oil. However, electricity and gas have not provided for such a good distinction, as their physical storage is difficult if not impossible, thus does not allow identifying a physical 'good.' After GATT was adopted, most of the members recognized electricity as a 'good' and made commitments under GATT. In addition, even though energy services are not regulated by an additional annex to GATS, GATS covers them in a way that members are required to observe the MFN provision, Art. VIII on monopolies etc.

[95] With services relating to the exercise of governmental authority we understand the adoption of law and administrative decisions of national authorities at regional, local and national level; see *H. Getaz et al.*, GATS-General Agreement on Trade in Services, 2001, p. 7.

[96] General Agreement on Trade in Services, 15 April 1994, available at http://www.wto.org, Art. I. See also WTO, GATS: Facts and Fiction (29 Oct. 1999), available at http://www.wto.org, at 6; *T. Stewart (ed.)*, The World Trade Organization: the Multilateral Trade Framework for the 21st Century and U.S. Implementing Legislation, 1996, p. 525; *M. Koehler*, Das Allgemeine Übereinkommen über den Handel mit Dienstleistungen (GATS) [General Agreement on Trade in Services], 1999, pp. 85-159. It was particularly identified that GATS attempts to liberalize but not to deregulate the market for services; see also *Getaz*, id. at 5.

[97] General Agreement on Trade in Services, 15 April 1994, available at http://www.wto.org, Art. II.

[98] General Agreement on Trade in Services, 15 April 1994, available at http://www.wto.org, Art.

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respect to *public services*. GATS does not prevent members from having public and private monopolies and allows them to choose whether or not to make GATS commitments in a specific sector.[99] Thus, GATS largely respects each member's discretion to organize activities in different service sectors, and is only a minor step in regulating services at the international level.

With regard to this paper, Article VIII of GATS is particularly interesting, as it covers monopolies and exclusive service providers.[100] As this article does not prohibit members from maintaining monopolies, it is a great disappointment for the enforcement of fair competition at the international level. Rather, the emphasis is put on the abolition of any kind of discrimination once a member has opened up its service markets to international competitors, but commitments resulting in the opening of the service markets are not obligatory. The possibility not to make commitments has been extensively used by the developing countries to safeguard domestic service sectors against stronger competitors from developed countries.[101] As a minimum standard, Article IX of GATS includes a prohibition of measures distorting competition, e.g. members allowing cartels in service sectors.[102]

Unfortunately, as GATS commentaries show, little liberalization was achieved with the main body of the agreement. Even though a need for the regulation of specific service sectors, e.g. telecommunications, was identified during the negotations process, agreement to regulate them within the framework of GATS was not achieved. Some attempts to change the unfortunate situation were made with the help of annexes that were attached to the agreement.[103] These annexes achieved at least a partial liberalization of two service sectors: air transport services and telecommunications services.

The Annex on Air Transport Services has limited application, as its scope was substantially reduced by members during the negotiations of GATS in the 1990s. The states still preferred to regulate most of these services via bilateral agreements adopted in the framework of ICAO. These bilateral agreements are based on reciprocal grants of one or more of the seven air service rights or

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V. (Economic Integration); it requires that any further and more intensive liberalization of services' trade is allowed as long as 1) it "has substantial coverage," which is "understood in terms of number of sectors, volume of trade affected and modes of supply," and 2) if it does not lead to discrimination.

[99] WTO, GATS: Facts and Fiction (29 Oct. 1999), available at http://www.wto.org, at 9.

[100] General Agreement on Trade in Services, 15 April 1994, available at http://www.wto.org.

[101] See id. at Art. VIII (1) and (2). See also *Stewart*, *supra* note 96, at 532-533; *Koehler*, *supra* note 96, at 85-159.

[102] General Agreement on Trade in Services, 15 April 1994, available at http://www.wto.org. See also *Getaz*, *supra* note 95, at 10. Art. IX of GATS also allows members to request consultations, if another member is violating principles embodied in the article. For example, the annex on Telecommunications was used as the legal basis for consultations between USA and Mexico on the alleged violation by Mexico of the principles embodied in the annex, e.g. market access provision under the terms of commitments and non-discrimination; see WTO, Mexico-Measures Affecting Telecommunications Services: Request for Consultation by the United States, WT/DS204/1 (Aug. 2000), available at http://www.wto.org.

[103] *Stewart*, *supra* note 96, at 541; Koehler, *supra* note 96, at 85-159.

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freedoms.[104] After exclusion of sensitive elements from the scope of the Annex on Air Transport Services, it still regulates such issues as (i) aircraft repair and maintenance services; (ii) the selling and marketing of air transport services; and (iii) computer reservation system services.[105] Thus, even though air transport is separately addressed in an annex to GATS, this legal regime provides rather little regulation for the sector. Regarding other types of transportation services, e.g. road and railway, members have by and large denied a need for multilateral regulation because the geographic market for these services has traditionally been regarded as regional.[106]

The Annex on Telecommunications covers the use and access to telecommunication services.[107] However it was not until 1998 that the members included telecommunications services in their schedules of commitments, and even then they were not ready for a complete liberalisation of the telecommunications market.[108] The annex requires non-discrimination of service

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[104] See *International Civil Aviation Organization*, How It Works, available at http://www.icao.int (accessed on 12 Jan. 2004); *International Civil Aviation Organization*, ICAO's Aims, available at http://www.icao.int (accessed on 12 Jan. 2004); *United Nations Department of Public Information*, The United Nations System: Principal Organs of the United Nations (Feb. 2003), available at http://www.un.org/aboutun/chart.html; ICAO is a specialized agency of the United Nations working "through the coordinating machinery of the Economic and Social Council," and was established under the Convention on International Civil Aviation, which was concluded in Chicago in 1944. It regulates traffic rights and services, such as check-in and baggage, and aims at developing standards in international civil aviation, reducing obstacles that hinder free movement of passengers "across international boundaries," increasing the safety of civil aviation and developing international law in areas of civil aviation.
The seven freedoms of international air service are the following:
- the civil aircraft of State A may fly over State B;
- the civil aircraft of State A may have a non-traffic stop at State B for refuelling;
- the civil aircraft of State A may carry passengers or goods (traffic) to State B;
- the civil aircraft of State A may carry traffic back from State B;
- the civil aircraft of State A may carry traffic of State B to State C;
- the civil aircraft of State B may carry traffic back from State C to State A via State B; and
- there may be scheduled flights between two countries without serving the country that the civil aircraft flies over; see *Purdue University*, Bilateral Agreements and the Seven Freedoms of International Air Service, available at http://www.tech.purdue.edu (accessed on 7 May 2004) (the last three freedoms refer to the so-called 'Beyond Rights').

[105] General Agreement on Trade in Services: Annex on Air Transport Services, 15 April 1994, available at http://www.wto.org, at par. 3. See also *Stewart*, *supra* note 96, at 542; *Koehler*, *supra* note 96, at 85-159. Regulation of transportation falls also under GATT rules in that Article III of GATT applies to the transportation of goods. The term 'transport' covers all means of transportation. In addition, Art. V. regulates transit of goods; see General Agreement on Tariffs and Trade, 30 Oct. 1947, available at http://www.wto.org.

[106] *Getaz*, *supra* note 95, at 23.

[107] General Agreement on Trade in Services: Annex on Telecommunications, 15 April 1994, available at http://www.wto.org, at par. 2.

[108] WTO Secretariat, *supra* note 94, at 537, 540; The limitations that the members wanted to preserve were as follows: (i) coordination of the number of suppliers; (ii) allowance of foreign capital; and (iii) setting of rules regarding the type of legal entity allowed for the telecommunications undertakings. In particular, it has to be mentioned that the limitations were

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suppliers if and when commitments have been made by a member, and seeks to ensure continuous provision of telecommunication services to the public and "'technical integrity' of the telecommunications network."[109] The reference paper also prohibits the abuse of a dominant position, which is a substantial achievement due to the fact that telecommunications sectors around the world are still largely dominated by monopolies. Furthermore, it includes a requirement that monopolies must grant access to their networks to competitors on reasonable conditions.[110] If monopolies were not required to open up their networks, they would rarely do it voluntarily. At the same time, monopolies tend to be inflexible and poorly able to adjust to changes in technology and market conditions. Therefore, the above-mentioned provision is of major importance because it lays a foundation for the creation of effective supply-side competition. Although the GATS annexes achieve substantial liberalisation of the telecommunications sector at the international level, this has no significant impact within the EU, as the EU telecommunications legislation (electronic communications legislation) is far better developed than that of the WTO.

D. Shortcomings of the Current Situation

The purpose of this chapter is to analyze the current regulatory framework for services of general economic interest in the EU, and to ascertain its shortcomings in order to later develop a strategy for addressing these problems and for moving ahead. While there are many specific shortcomings, it is also clear that the treatment of services of general economic interest in the EU is a broad and general problem. If it were otherwise, the Commission would not have adopted a Green Paper[111] launching an open discussion at European level.

This chapter will mainly consider the individual shortcomings that distort the functioning of the internal market. Section I establishes that commercial activities of undertakings engaged outside large network industries are exposed to considerable legal uncertainty. Section II analyzes how the protection of providers of services of general economic interest from competition has made it more difficult to achieve fundamental Community objectives, such as fair competition, market integration, efficient production and the satisfaction of customer needs. Section IV discusses how the current legislation maintains an artificial gap between public service obligations and the rest of the market, even though such a need has decreased in comparison to the past. Finally, Sections III and V analyze how institutions entrusted with law enforcement in the EU (the European Court of Justice, the Commission, as well as national courts and competition authorities) have contributed to the current problematic situation.

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mostly imposed by the non-industrialized members of WTO.

[109] General Agreement on Trade in Services: Annex on Telecommunications, 15 April 1994, available at http://www.wto.org, at par. 5. See also *Stewart*, *supra* note 96, at 545.

[110] ***G.*** *Henri et al.*, GATS-General Agreement on Trade in Services, 2001, pp. 21-22.

[111] See Green Paper on Services of General Interest, COM/2003/270 final.

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I. Reduced Legal Certainty in the Internal Market

The regulation of services of general economic interest is characterised by a significant level of legal uncertainty, which increases commercial risks for economic operators. Article 86 (2) EC Treaty, similar to several other Treaty provisions, produces considerable uncertainties because it is result-oriented and does not prohibit a particular conduct.[112] It states that providers of services of general economic interest will escape the application of competition rules "insofar as the application of such rules … obstruct[s] the performance, in law or in fact, of the particular tasks assigned to them." Thus, according to the Court's interpretations, competition law will not be applied, if its application compromises the economic equilibrium of providers of services of general economic interest.[113] Uncertainties will arise, as 'economic equilibrium' is a broad term, and undertakings cannot predict with reasonable certainty, in which situations their economic equilibrium will be compromised, and therefore, whether competition rules are applicable to their activities or not. The applicability of competition rules can be assessed only on a case-by-case basis, which is the responsibility of the Court and the Commission.

The Court has further contributed to legal uncertainty by being inconsistent in interpreting Article 86 (2) EC Treaty. The most striking example is the unclear status of state financing of universal service obligations, an area where the CFI and the ECJ have taken a different approach. The CFI regards any amount provided by the state that exceeds the actual costs of universal service obligations as state aid. By contrast the ECJ excludes profits from the concept of 'state aid', i.e. it allows Member States to finance the actual costs plus a reasonable profit margin.[114] Thus, providers of services of general economic interest are forced to operate in uncertainty since the Commission may follow the more restrictive approach of the CFI[115] and declare state aid (financing

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[112] *T.C. Hartley*, Constitutional Problems of the European Union, 1999, p. 67. The European Centre of Enterprises with Public Participation and of Enterprises of General Economic Interest [hereinafter CEEP] has suggested that Art. 16 EC Treaty also contributes to more legal uncertainty in the internal market. However, this is a minor problem, as the analysis in Section I of Chapter B has shown that Art. 16 can produce no legal effects in that Declaration 13 annexed to the Treaty of Amsterdam requires this provision to be implemented with regard to the current case law of the Court; see Chapter B, Section I; European Centre of Enterprises with Public Participation and of Enterprises of General Economic Interest, Proposal for a Charter for Services of General Interest (15 June 2000), available at http://www.europa.eu.int.

[113] See Chapter B, Section I.

[114] See Chapter D, Section III.

[115] In the argumentative part of the Judgment of 17 October 2002 in *Case T-98/00, Linde AG v. Commission of the European Communities*, [2002] ECR II-3961, it is possible to observe that the Commission shares the attitude of the CFI that state funding of universal service obligations falls under Art. 87 EC Treaty, even though in this case the Commission was not successful, as it failed to provide adequate reasoning. In subsequent decisions the Commission has condemned the financing of public service obligations as illegal state aid thereby following the more restrictive and market-oriented approach of the CFI, but it is not possible to exclude that an appeal will be filed and that the Court will not reverse this decision; for example, see Commission Decision

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exceeding costs) incompatible with the internal market, and require a provider of services of general economic interest to repay some of the funds received.

Furthermore, the Court has been inconsistent in applying the proportionality test by taking a restrictive approach concerning free movement rules, but a generous attitude regarding competition law. In several judgments, the Court has taken the restrictive approach with regard to certain services of general economic interest, in effect prohibiting anti-competitive behaviour.[116] While this may be good, the Court created more legal uncertainty, since it did not clarify whether its interpretation applies only to the sector at issue[117] or whether it can be extended to other types of services of general economic interest.

In several respects, sector-specific legislation at the European level is itself a contributor to legal uncertainty. Even though the European legislation defines illegal anti-competitive behaviour, Member States have retained considerable discretion regarding the organization of the provision of services of general economic interest, and may even impose "more far-reaching or additional obligations."[118] For example, Member States may impose quality, availability and performance conditions on service providers, and it is up to the Member States to define these conditions.[119] Thus, undertakings will never be sure whether they fulfil all criteria, especially as Member States are free to change them at any time.

Undertakings in areas not regulated by sector-specific legislation are even more severely exposed to legal uncertainty as they have to rely mainly on case-by-case assessments of the Commission and the Court of Justice, which, as demonstrated above, tend to be contradictory.

II. Failure to Attain Fundamental Community Objectives

The fundamental objectives of the Community include the goal to achieve a high degree of market integration, to ensure that goods and services can be provided under fair competitive conditions, to protect consumer interests and to guarantee efficient production.[120] These objectives not only provide direction for any

2002/753 of 19 June 2002 on measures implemented by the Federal Republic of Germany for Deutsche Post AG, OJ 2002 L 247/27.

[116] See Chapter D, Section III.

[117] Strict application of the proportionality test can be observed mainly in cases concerning air transport; see Judgment of 19 June 1997 in *Case T-260/94, Air Inter SA v. Commission of the European Communities*, [1997] ECR II-997.

[118] Green Paper on Services of General Interest, COM/2003/270 final, at 23.

[119] Council Directive 95/18/EC of 19 June 1995 on the licensing of railway undertakings, OJ 1995 L 143/70, art. 8 and 10; Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service, OJ 1998 L 15/14, art. 9.

[120] This is not an exclusive list of Community objectives. However, in order to better demonstrate the shortcomings in the regulation of services of general economic interest, this paper fill focus only on the five objectives mentioned above in the text. For additional information, see *V. Korah*, An Introductory Guide to EC Competition Law and Practice, 7th ed., 2000, pp. 9-18.

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Community action, they form an indispensable foundation for the internal market, as the latter cannot function without intensive participation of undertakings and consumers. However, as the conclusions in this section indicate, the current regulatory framework for services of general economic interest does not promote the above-mentioned objectives, or at least does not do so very well. Thus, the completion of the internal market and the functioning of an open market economy have not really been achieved in this area.

1. Market Integration

Market integration shall be understood as the establishment of the internal market or as the Court has stated the 'elimination of all obstacles to intra-Community trade in order to merge the national markets into a single market'.[121] This concept not only covers the 'internal market' as an area where the four freedoms are ensured. It also covers the establishment of a market with fair competitive conditions. Therefore, an essential aim of market integration is the prohibition of anti-competitive activities of states and undertakings, because these kind of activities can lead to the partitioning of the internal market and preventing such partitioning is at the heart of the free movement rules.[122] Moreover, if anti-competitive practices were not prohibited effectively, the internal market could not effectively function, since the "free movement of goods, freedom to provide services and freedom of establishment … are only possible in a fully open market."[123] In spite of its importance, however, European market integration has failed at least in part.

With regard to services of general economic interest, Article 86 (2) EC Treaty itself, and the way the European Court has interpreted it, already hinders market integration. Firstly, each Member State is free to determine sectors that it qualifies as 'services of general economic interest'.[124] Secondly, it is less than clear how competition rules apply to undertakings operating in this area. The mere possibility of Member States to regulate Member State services of general economic interest at national level impairs market integration, because national regulation usually differes from one Member State to another and, in this way, reintroduces national boundaries. The partitioning of the EU market in this area is particularly severe because anti-competitive effects in the markets for services of general economic interest have adverse spill-over effects in other product markets because no undertaking can successfully operate without electricity, postal services, telecommunications etc. An even better example to illustrate this interdependency is a look at prices – prices charged for services of general economic interest have to be passed on to producers of other goods and services.

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[121] Cited in *K. Lenaerts & P. van Nuffel*, Constitutional Law of the European Union, 1999, p. 75.
[122] See id. at 76-77.
[123] See Preamble to Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC-Statements made with regard to decommissioning and waste management activities, OJ 2003 L 176/37, at paragraph 4.
[124] See Chapter B, Section I.

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Excessive prices in one Member State may considerably increase operating costs for a broad range of undertakings. As a result, the free movement of goods and services entirely outside the category of services of general economic interest can be undermined.

In spite of these adverse effects, the European Court has continuously supported the regulation of services of general economic interest at the national level. It has repeatedly ruled that potential competition should be kept out of profitable sub-markets of a universal service, based on the rationale that this was a suitable way of ensuring the provision of services of general economic interest (see also the end of this sub-section for more discussion on this). In addition, on most occasions the European Court failed to require Member States to provide additional market information for it to make appropriate and correct assessments in applying the proportionality test.[125] The European Court's approach gives Member States a broad license to protect domestic sectors, which, in turn, may lead to the partitioning of the internal market.

Koen Lenaerts, formerly a judge on the CFI and now a judge on the ECJ, has suggested that market integration is hindered because undertakings have to operate in different Member States under different conditions.[126] Not only has excessive national discretion made market integration more difficult by creating different market conditions across the EU, flexible sector-specific legislation also led to different degrees of market opening. The market opening range in the electricity sector is between 30% in France and 100% in Germany, Austria, Finland, Sweden and the UK. Similar differences can be identified in the gas sector with the lowest market opening in Denmark (35%) and Member States like Germany, Austria and the UK having a market opening of 100%.[127] In addition, the requirements for unbundling differ considerably from one Member State to another. Some Member States have chosen ownership unbundling between network operators, service generators, transmitters, distributors and suppliers, but other Member States rely only on account, legal or management unbundling.[128]

Thus, undertakings are exposed to different conditions in different Member States making the cross-border provision of services of general economic interest more difficult. In particular, mere legal, management or account unbundling allows Member States close national markets to competition from other Member States, because in these Member States the influence of the state on providers of services of general economic interest still persists through total or partial state ownership. In addition, the respective undertakings in these

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[125] See Chapter D, Section III.
[126] *Lenaerts*, *supra* note 121, at 77.
[127] European Commission, EU Energy and Transport in Figures 35-36 (2002).
[128] See European Commission, EU Energy and Transport in Figures 35-36 (2002). The discussion of other types of services of general economic interest is irrelevant here, as no substantial harmonisation has been done in other areas; see Chapter B, Section III. The regulation of the telecommunications sector is an exception, as its liberalisation has been the most successful until now covering all three competition concerns: (i) trade with equipment; (ii) access to the network; and (iii) provision of services. Therefore, any concerns regarding market integration have ceased.

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Member States are likely to cooperate with each other, as they do not regard themselves as separate undertakings, thus distorting competition by foreclosing the market for potential supply-side competitors.[129] Moreover, sector-specific legislation has allowed substantial derogations in Greece, Portugal and Finland.[130] Therefore, also sector-specific regulation has also contributed to the disintegration of the internal market.

Another group that has an influence over the level of European market integration are the consumers. As will be discussed in detail below,[131] consumer satisfaction in terms of price and quality of the products is an essential goal of the internal market. However, as consumers have not been entirely satisfied with the provision of services of general economic interest, this goal of the European market has also not been adequately achieved.

However, critics may argue that only sub-optimal market integration is possible because of the 'market failure' with regards to services of general economic interest.[132] In light of this, it is necessary to determine whether there could be an effectively functioning internal market in this area.

It is true that services of general economic interest can be characterised by such peculiarities as high start-up costs and the impossibility of duplication of a network. Furthermore, they must be available to everyone due to their general interest nature. As the conclusions in this chapter and Chapter F indicate, state interference into the functioning of the market should be limited to the absolute minimum, rather than be abolished at any cost. Legislation should be continuously adjusted to technological developments in this area and this does not exclude the possibility that one day we may achieve such a level of technological advancement that we can have an entirely integrated internal market.

The WTO has also held that it would be possible to gradually establish an effectively functioning market for services of general economic interest. This does not exclude the possibility that the reduction of state intervention in these sectors could bring losses in the short-term, but it remains highly probable that long-term profits would be much more significant for the functioning of the market. Furthermore, the economic analysis conducted by the WTO has revealed that non-adjustment of current legislation to technological changes would entail much higher losses in the long-run.[133] Therefore, even though an entirely integrated market is perhaps only an ideal case, which is not realistic at the current stage of market development, "a *competitive situation must be the*

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[129] The Commission has also identified that legally unbundled network operators, service generators, transmitters, distributors and suppliers have a tendency to cooperate in order to delimit supply-side competition; see *European Commission Directorate-General for Competition*, European Union Competition Policy: XXXIst Report on Competition Policy 2001, 2002, p. 27.

[130] See *European Commission*, EU Energy and Transport in Figures, 2002, pp. 35-36.

[131] See Chapter D, Section II (3).

[132] Commission Communication-Third Progress Report on Economic and Social Cohesion, COM/2004/0107 final.

[133] *WTO Secretariat*, *supra* note 94, at 3.

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overall goal."[134] "We must *get away from the idea that market failure is the rule* and market success is the exception for ensuring full supply at fair and reasonable conditions in the sector for every citizen."[135]

2. Satisfaction of Consumer Needs and Consumer Protection

The establishment of the internal market has created a fundamental right for European consumers to obtain high-quality goods and services throughout the Community at affordable prices.[136] In addition, in exercising these rights, consumers have to be protected from undertakings practising anti-competitive behaviour.[137] Consumers should receive this protection because the internal market could not function without consumer involvement, as purchases across borders would not be made, if there is no trust in price and quality of goods and services of other Member States.[138] Therefore, consumer satisfaction in terms of price and quality is an essential element for an effective functioning of the internal market.

For purposes of this article, the question is: are consumers satisfied with the provision of services of general economic interest at present? This does not seem to be the case. Eurostat has found that only two thirds of all consumers have been satisfied with electricity, gas, fixed telephone and postal services. Satisfaction with railway services is even lower at 55.2%.[139] As price and quality were the main elements of the questionnaires, this means that many consumers were satisfied with neither of them. In addition, as the Eurobarometer of Spring 2003 indicates, only 15% of EU consumers (in comparison to 47% unsatisfied consumers) declared that they felt that their interests in relation to price and quality are well represented by Community policies on transport, energy, telecommunications and competition.[140] Moreover, consumers identified that special rights granted to providers of services of general economic interest have decreased the quality and the choice of products, and approximately 50% of consumers have claimed that they are not satisfied with the quality of services as provided. Consumers particularly referred to postal services, and complained that daily collection of mail has decreased while delivery duration has increased.[141]

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[134] Emphasis added; *H. Ungerer*, Future Challenges-1999 Review (July 6-7, 1998), available at http://www.europa.eu.int/comm, at paragraph 3.
[135] Id (emphasis added).
[136] Services of General Interest in Europe, OJ 1996 C 281/3, at paragraph 7.
[137] Judgment of 20 September 2001 in *Case C-453/99, Courage Ltd v. Bernard Crehan and Bernard Crehan v. Courage Ltd,* [2001] ECR I-6297, at paragraph 12.
[138] The Internal Market-Ten Years without Frontiers, [2003] SEC/1417, at 15.
[139] Satisfaction rates: electricity-73.8%; gas-68.5%; fixed telephones-69.8%; postal services-73.9% (all data refers to 2000); see *Eurostat*, An Essential Tool to Better Understand EU Consumers Behaviour, Press release, 135/2001, Luxembourg, 19 December 2001.
[140] *European Commission*, Eurobarometer 59, Consumer Protection (2003), available at http://www.europa.eu.int, at 46.
[141] Notice from the Commission on the Application of the Competition Rules to the Postal Sector and on the Assessment of Certain State Measures Relating to Postal Services, OJ 1998 C 39/2, at

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These consumer attitudes not only show that the internal market is not effectively functioning; they also indicate that the current treatment of services of general economic interest has significant drawbacks, which have to be addressed. Nevertheless, consumer dissatisfaction is not surprising due to the monopolistic or oligopolistic structure (depending on the sector) of the market for services of general economic interest, which is either caused or perpetuated by special rights granted to the undertakings.[142] Potential competition has had difficulties in entering the market due to high start-up costs required in several sectors. Even if such investments were not required, most providers of services of general economic interest were already strongly established in the market, and their position has additionally been strengthened by long-term support of the government and the judiciary. As a result, without effective competitive pressures, undertakings had little incentive to improve the quality of services of general economic interest, the choice of products has remained limited and prices have been kept at high levels. At the bottom line, consumer interests were not taken into account sufficiently.

Furthermore, not all consumers throughout the EU can equally enjoy the benefits of liberalisation, as the implementation of the Community secondary legislation has been very flexible with regard to services of general economic interest.[143] This especially refers to electricity prices, which differ from one Member State to another by 70% to 150% of the EU average.[144] Thereby, consumers in some Member States are largely deprived of the benefits of the internal market, while consumers in other Member States can more fully enjoy them. Moreover, taking into account such price differentials across the EU it is not possible to conclude that the European market has been integrated.

3. Efficiency

Efficient production closely relates to the protection of consumer interests – the objective analyzed in the previous sub-section. I would agree with the contention that "an unduly high price for products that people continue to buy is not necessarily undesirable"[145] as long as these products are luxuries or, in other words, products intended to satisfy other needs than those of basic necessity. However, services of general economic interest are not luxury products. Already from the wording it is clear that they are intended to satisfy 'general' or 'basic'

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footnote 17; see also Annex C3 in European Commission, Quality of Service Objectives, Performance and Measurement in Relation to Community Universal Postal Service, Sector Studies (August 2003), available at http://www.europa.eu.int.

[142] European Commission, Enterprises in Europe 31 (1996). In addition, for examples identifying that the market for services of general economic interest is dominated by large-scale undertakings, see also the following web pages of undertakings: http://www.deutschepost.de (Deutsch Post); http://www.bahn.de (Deutsche Bahn); http://www.laposte.fr (La Poste); http://www.eon.de (EON AG); http://www.edf.fr (Electricité de France).

[143] See also Section V. of this Chapter and Chapter E.

[144] *European Commission*, Price Levels and Price Dispersion in the EU, European Economy (July 2001), available at http://www.europa.eu.int/comm, at 15-16.

[145] *Korah*, *supra* note 120, at 9.

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needs of the society. Thus, prices should be kept at the lowest possible level. Prices being excessively high mean that they substantially exceed costs and reasonable profit margins. Thus, some consumers are not able to obtain the product, and their basic needs are left unsatisfied.

Dramatic price falls after partial liberalisation of several sectors of services of general economic interest could indicate that some consumers have had to refrain from purchasing certain services of general economic interest due to artificially high prices. Prices of electricity for industry have fallen by 25% since 1994. Price reductions for households have been slightly lower, about 10% since 1994. Nevertheless, even a small decrease recognises that it is possible for providers of services of general economic interest to supply these services at lower prices. Moreover, in the telecommunications sector, where the most liberalisation has taken place so far, price reductions have been even more impressive – 50% for domestic calls and 65% for international calls.[146] This means that over a long period of time consumer interests were not regarded as the main priority. Moreover, as liberalisation has not yet achieved 100% in any of the sectors of services of general economic interest, there probably is still considerable potential for further price reductions.

At this point I would like to oppose an argument presented by UK authorities. They consider that the liberalisation of general interest sectors is not the best solution for increasing competition in the EU because the experience of the UK (price reduction through liberalisation) has ultimately been negative. Among other consequences, it has led to financial crisis of railway undertakings and has decreased the quality and safety of railway services leading to several major accidents.[147] The negative experience of the UK with regard to liberalisation could, however, be explained by several factors other than price reductions. Firstly, the success of liberalisation depends on the level of technological advancement. It is possible that at the time of liberalisation, the UK had not yet reached the necessary level of technological advancement for a complete opening of this general interest sector. Secondly, the fact that the UK chose to liberalise its rail services market rapidly rather than gradually could also have contributed to the financial crisis and the loss of quality. Germany could be mentioned as a positive example in this regard. It chose to open its electricity and gas markets gradually, and has not experienced the kind of problems seen in the UK.

In addition to the consumer interest argument, it should be mentioned that high prices can be maintained only if market is foreclosed to competition. Therefore, in order to sustain high prices in the long run, undertakings have to engage in extensive lobbying with the government, which then regulates the

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[146] It would not be adequate to consider gas prices, as they are influenced by independent factors. The EU has a 45% dependency on gas imports from third countries, which influences gas prices; see *European Commission*, EU Energy and Transport in Figures, 2002, p. 30.

[147] London's European Office, Submission by the Mayor of London to the European Commission's Green Paper on Services of General Interest (15 Sept.2003), available at http://www.europa.eu.int.

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market in such a way, as to prevent potential competition from entering.[148] Such lobbying has taken place, and still does,[149] also with regard to the regulation of services of general economic interest. As a result, not only multiple resources are being wasted on artificial maintenance of market power, but as a result, markets are kept shut to potential competitors, which could provide more qualitative and better-priced products, better satisfying consumer needs. This could be an indication that current providers of services of general economic interest may often not be the most efficient ones, if they continuously seek to safeguard their market positions. If they were more efficient, they would not resist further liberalisation as much. Without any doubt, special rights that have been granted to providers of services of general economic interest, and the ability to sustain them,[150] reduce the need to improve production and marketing efficiency in the future. This is a grave problem, which has to be addressed by new legislation, since market partitioning has to be avoided to ensure an effective functioning of the internal market and in this way the provision of the best possible services at the lowest possible prices.

4. Fair Competition

Another aim of the Community is to ensure that undertakings can operate under fair competitive conditions.[151] This is a very broad term, but the main requirement is that goods and services are provided in competitive market environments, and that exceptions are permissible only in so far as they can be reasonably justified.[152]

Services of general economic interest are usually presented as an exception to the rule that the full application of competition rules ensures higher quality at lower prices better than any other measures. The question is whether an exception for services of general economic interest can be reasonably justified. However, this is not the case. As previous sub-sections indicate, the permission of anti-competitive practices in exchange for public service obligations has hindered European market integration, left consumer needs unsatisfied and led to the inefficient operation of providers of services of general economic interest. Moreover, the Commission has expressly stated that the current regulatory framework has allowed providers of services of general economic interest to

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[148] *Korah*, *supra* note 120, at 10.

[149] For example, see the Ministerial Decree of the German Economics Minister of 5 July 2002 in *Case B 1-22 08 40 / 129 EO.N / Ruhrgas*, available at http://www.bundeskartellamt.de, which clearly shows, how powerful undertakings can achieve the results they want, even though it leads to considerable anti-competitive affects.

[150] The Court and national competition authorities have not only ignored the efficiency argument, but have supported the maintenance of privileged rights of providers of services of general economic interest; see Chapter D, Section III. See also Green Paper on Services of General Interest, COM/2003/270 final, at 27; Judgment of 23 October 1997 in *Case C-159/94, Commission of the European Communities v. French Republic*, [1997] ECR I-5815, at paragraphs 78-83.

[151] *Korah*, *supra* note 120, at 11.

[152] Handbuch des Europäischen Rechts [Handbook of European Law] § 18, at 63-64 (1997).

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compete unfairly.[153] Thus, it would not seem appropriate to continue to represent providers of services of general economic interest as 'victims' of public service obligations.

A further requirement of 'fair competition' is that all undertakings are treated equally in the market.[154] In relation to services of general economic interest it means that access to the 'network' should be granted on equal terms to everyone and that all undertakings should be able to provide services of general economic interest under equal conditions. Therefore, any kind of privileges (financial or other), which lead to discrimination, should be prohibited. However, as will be analyzed in detail in Chapter E, the current regulatory framework contains considerable gaps, allowing certain undertakings to refuse access to their network and/or to impose various conditions that actually or potentially discriminate against supply-side competition.

III. Inconsistencies Created by the European Judiciary

The European judiciary has produced inconsistencies in the law and has tolerated or even generated protectionism for the benefit of existing providers of services of general economic interest. Even though EU law is a young legal system in comparison to civil law or common law systems, there is no credible argument to justify such treatment.as will be shown in the rest of this section, it would not be an exaggeration to say that the judicial process regarding services of general economic interest has not produced the expected results.

1. Excessive Protectionism of Providers of Services of General Economic Interest by the European Court of Justice

The effects of the Court's case law, which is excessively protecting providers of services of general economic interest, have reduced legal certainty, strengthened market partitioning and decreased the credibility of the Court as 'guarantor of justice' in the Community. To demonstrate excessive protectionism for the benefit of providers of services of general economic interest, this section will concentrate on the Court's unjustifiably different application of the proportionality test in interpreting competition law and free movement rules, and will consider other inconsistencies created by the Court.

Comparison between free movement rules and competition law is justified for the following reason: both free movement rules and competition law of the Community aim to integrate national markets by securing free market access for every undertaking meeting objective standards. Similarly, both rules contain exceptions to their (full) application, namely Articles 30, 46 and 55 EC Treaty,

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[153] Report from the Commission on the State of Play in the Work on the Guidelines for State Aid and Services of General Economic Interest, COM/2002/0636 final.

[154] Judgment of 13 December 1991 in *Case C-18/88, Regie des telegraphes et des telephones v. GB-Inno-BM SA*, [1991] ECR I-5941; Handbuch des Europäischen Rechts [Handbook of European Law] § 18, at 64 (1997).

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and Article 86 (2) EC Treaty respectively. Resort to these exceptions may lead to sub-optimal integration of European markets. In cases of Article 86 (2) competition may not achieve a workable level within the Community. Of course, this argumentation pre-supposes that judicial interpretation should follow a similar, if not identical, approach, in permitting or prohibiting justifications for the non-application of Community law with respect to fundamental freedoms on the one side and competition law on the other.

a. Unjustifiably different application of the proportionality test in interpreting various provisions of the EC Treaty

The Court has employed the proportionality test in interpreting various provisions of the EC Treaty in order to determine whether violations of the Community law can be tolerated. However, the flexible nature of this test has led to its unjustifiably different application which can be seen by comparing the Court's decision on free movement rules to those found in competition law.

In relation to free movement rules, whether free movement of goods, services or persons, the EC Treaty and the Court recognise different non-economic justifications[155] for violations of Community law. However, the mere fact that a restriction can be categorised as falling within the scope of one of the justifications does not mean automatically that restrictions of the basic freedoms are permitted. Additionally, the proportionality test has to be satisfied – the measure that the Member State wants to justify has to be appropriate to achieve the objective sought (means/ends analysis) and it has to be the least restrictive for attaining that objective.[156] Thus, the Court analyses not only whether the measure is suitable, but also whether it is necessary.

It is rather obvious from the case law of the Court that it has been very restrictive in applying the proportionality test in cases concerning free movement rules. In particular, it has ruled that Member States may not determine unilaterally whether the measure is necessary and suitable.[157] To escape the application of the Community rules, there must be a "genuine and sufficiently serious threat affecting … interests of [the] society."[158] According to the Court the proportionality test requires that a state measure is protecting *non-economic* interests of EU inhabitants before it can be justified as a restriction of free movement rights. In its further case law the Court expressly stated that Member States may not seek to justify national measures, which "pursue an

[155] Violations of the free movement rules can be justified on grounds of public morality, public policy, public security, protection of health, environmental protection, consumer protection etc.; see EC Treaty, art. 30, 46 and 55. See also Judgment of 20 February 1979 in *Case 120/78, Rewe-Zentral AG v. Bundesmonopolverwaltung für Branntwein (Cassis)* [1979] ECR 649.

[156] Judgment of 14 July 1994 in *Case C-17/93, Criminal proceedings against J.J.J. Van der Veldt,* [1994] ECR I-3537.

[157] Judgment of 28 October 1975 in *Case 36/75, Roland Rutili v. Ministre de l'interieur,* [1975] ECR 1219.

[158] Judgment of 27 October 1977 in *Case 30/77, Regina v. Pierre Bouchereau,* [1977] ECR 1999.

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economic aim."[159] Therefore, the Court aims at restricting Member States' attempts to protect domestic economic sectors, as this can lead to the partitioning of the internal market and be in contradiction with the principle of European market integration.

However, the Court has taken a more generous approach with regard to competition law, and in particular with regard to services of general economic interest. The first time that the Court spoke about the proportionality test under Article 86 was in *Corbeau*, where it stated that Member States may grant special or exclusive rights to providers of services of general economic interest, even though such rights reduce competition, as long as they are "necessary to ensure the performance of the … tasks [entrusted upon such undertakings]."[160] Thus, Article 86 (2) recognises universal service obligations as a justification for competition law violations. If the proportionality test were to be interpreted the same way, as under free movement rules, any justification should be of a non-economic nature. This is not the case, however.

In order to better demonstrate the disparities in the application of the proportionality test, it is important to differentiate between two elements of the proportionality test: suitability and necessity.

As already identified above, the suitability test requires a means/ends analysis that seeks to clarify whether the means are an appropriate and efficient way to attain the objective sought.[161] In its case law, the Court continuously repeats that potential competition should be kept out of *profitable sub-markets* of the universal service, because it characterises this as suitable for ensuring the provision of services of general economic interest. The Court considers that if providers of services of general economic interest were not compensated for their losses, they would refuse to provide universal services.[162] Such contention may be false, however, as current losses do not necessarily mean that it is not possible for the undertakings to operate under 'conditions of economic equilibrium' or 'economically acceptable conditions.'[163] Here we should take into account that the undertaking entrusted with the provision of universal services could offset losses incurred in some regions with profits from other geographic areas. By contrast, the reservation of sub-markets of the universal service leads to the creation of entry barriers for potential competitors and

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[159] Judgment of 5 June 1997 in *Case C-398/95, Syndesmos ton en Elladi Touristikon kai Taxidiotikon Grafeion v. Ypourgos Ergasias,* [1997] ECR I-3091; Judgment of 31 January 1984 in *Case 40/82, Commission of the European Communities v. United Kingdom of Great Britain and Northern Ireland,* [1984] ECR 283; Judgment of 14 December 1979 in *Case 34/79, Regina v. Maurice Donald Henn and John Frederick Ernest Darby*, [1979] ECR 3795.

[160] *Case C-320/91, Criminal Proceedings against Paul Corbeau,* [1993] ECR I-2533, at paragraph 14.

[161] *L. Moral Soriano*, How Proportionate Should Anti-competitive State Intervention Be?, 28 ELR 112, 117 (2003).

[162] *Soriano*, id. at 117; Order of the Court of 25 March 1998 in *Case C-174/97 P, Fédération française des sociétés d'assurances v. Commission of the European Communities,* [1998] ECR I-1303; *Case C-320/91*, *supra* note 160, at paragraph 18.

[163] *Soriano*, *supra* note 161, at 119.

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expands monopolistic structures beyond areas in which universal service obligations exist to areas that could have competitive structures.

Moreover, the Court's favourable attitude has allowed justifications of an economic nature. It not only permits the protection of domestic economic sectors by preventing potential competition from entering national markets, but clearly contradicts its own principles established under free movement rules, where only non-economic justifications are permitted. In addition, the Court completely ignores the efficiency analysis developed with regard to free movement rules, when assessing the suitability of the state measure.

The Court analyses the necessity requirement by looking at 'conditions of economic equilibrium' or 'economically acceptable conditions' instead of determining whether the same objective can be attained with less restrictive measures.[164] Although the Court is referring to the 'necessity element' in its judgments, it never really analyses it from the same perspective as under free movement rules. Instead, the Court encourages consideration of economic conditions (costs and legislation), under which the provider of services of general economic interest has to operate.[165] The Court allows and even encourages cross-subsidization – the offsetting of less profitable sectors against profitable ones.[166] These are clear indications that the Court is applying the proportionality test in different ways to different Treaty provisions.

Furthermore, the Court fails to consider alternatives to the chosen state measure, i.e. there is no question whether a less restrictive alternative measure would be readily available, which is an important element of the proportionality test used in free movement cases. Apparently, the Court does not believe that parties to the case can be trusted to provide adequate information regarding the market in question, or it may be more accurate to say that Member States do not want to provide that information, Therefore the Court seems to believe that it has no other realistic possibility but to accept the policy choice of the Member States in these types of cases.[167] The Court's own lack of complete information and economic analysis capacity results in Member States retaining broad discretion as to the organisation of services of general economic interest. As a result, there is still plenty of room for market partitioning.

Leonor Moral Soriano, a lecturer of public law at Granada University, provides specific examples where the Court has inconsistently applied the proportionality test – in a highly restrictive manner in cases concerning free movement rules and in a much less restrictive manner, recognising extensive discretionary powers of Member States as far as universal service obligations are

[164] *Case C-475/99, Firma Ambulanz Glöckner v. Landkreis Südwestpfalz*, in particular paragraph 57 of the judgment. See also Chapter B, Section I.
[165] Judgment of 27 April 1994 in *Case C-393/92, Municipality of Almelo and others v. NV. Energiebedrijf Ijsselmij*, [1994] ECR I-1477, at paragraph 49.
[166] *Case C-320/91, Criminal Proceedings against Paul Corbeau*, [1993] ECR I-2533, at paragraph 17; *Case C-475/99, Firma Ambulanz Glöckner v. Landkreis Südwestpfalz* in particular paragraph 57 of the judgment.
[167] *Soriano*, *supra* note 161, at 120.

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concerned.[168]

Having established that the proportionality test under free movement rules and competition law is interpreted differently, it is necessary to consider whether the difference in treatment can be justified. Both Community policies pursue the same objective – integration of national markets by granting free access to every undertaking, which wants to obtain it. This would pre-suppose that actions taken at the Community level, whether judicial or legislative, should be consistent in order to ensure legal certainty.[169] Therefore, in the absence of valid justifications, it would seem that the differential treatment cannot be justified.

b. Inconsistency in the Court's case law

Although the inconsistencies in the Court's case law have decreased with time, several problems can still be identified.

As stated in the previous section, the proportionality test is usually generously applied in the context of services of general economic interest, thus tolerating broad discretionary powers of Member States as far as universal service obligations are concerned and accepting anti-competitive behaviour. However, sometimes the Court has taken a more restrictive approach. For example, in the *Air Inter*[170] case, the Court refused to apply the Article 86 (2) exception to exclusive rights that a Member State granted to an air carrier, even though the facts of the case were similar to those in other cases where the Court found it appropriate to justify anti-competitive state measure.

The air carrier alleged that it was under a universal service obligation to operate non-profitable routes, and in exchange the air carrier wanted and received exclusive rights to operate two profitable air routes. Thus, the undertaking used profits in potentially competitive markets to compensate losses incurred in performing universal service obligations, which is an argument that has usually been accepted by the Court. However, in *Air Inter*, without actually identifying a specific alternative to exclusive rights, the Court condemned the state measure by saying that there would be less restrictive measures available for achieving economic and social cohesion. Although this interpretation might be limited to the air transport sector, the Court did not expressly say so. Therefore, at least potentially, the Court could interpret any other case concerning universal service obligations in a similar way.

Another grave problem is that the CFI and the ECJ have taken different approaches in determining whether state financing of universal service obligations constitutes state aid. The CFI has ruled that any such financial help falls under Article 87 EC Treaty and that the Commission is responsible for assessing whether the aid can be justified under Article 86 (2).[171] The ECJ, on

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[168] Id. at 112.

[169] Id.

[170] Judgment of 19 June 1997 in *Case T-260/94, Air Inter SA v. Commission of the European Communities*, [1997] ECR II-997. For case commentaries, see also *J. Faull, & A. Nikpay* (eds.), The EC Law of Competition, 1999, pp. 318-319.

[171] Judgment of 27 February 1997 in *Case T-106/95, Fédération française des sociétés*

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the other hand, has followed the suggestion of Advocate General Tizzano, who claimed that financial advantages do not constitute state aid as long as they have economically neutral effects by merely eliminating disadvantages, which have been imposed on providers of services of general economic interest via universal service obligations. Thus, the ECJ rejected the argument that financial support to providers of universal services necessarily constitutes state aid.[172]

Before we can be sure that the Court has clarified this situation, further developments in the case law have to be observed. Unfortunately, there have been only two subsequent cases, where the Court had to adjudicate on the same issue – one before the CFI and one before the ECJ. In 2002, the CFI referred to the judgment of ECJ in *Ferring*, and agreed with the ECJ that financial support does not constitute state aid in so far as it is intended to cover the costs for performing universal service obligations.[173] Later in 2003, the ECJ once again stated that reimbursement of the costs of the performance of universal service obligations cannot constitute state aid, but added that "reasonable profit" would also be exempted from the notion of 'state aid'.[174] At the time when this article was written, the situation , therefore, remained unclear.

Recently the Commission has adopted a paper entitled 'Community Framework for State Aid in the Form of Public Service Compensation' with the intention to clarify the situation.[175] The Commission restates the latest judgment of the ECJ, where the Court ruled that the costs for the performance of universal service obligations including reasonable profit cannot constitute state aid. The Commission suggests calculating the costs by adding variable costs, fixed costs and an adequate return on capital. Furthermore, in order to simplify judicial control, the Commission requested that public service obligation should be allocated by an administrative act, which precisely states the public service obligation, the geographic area of operation, the nature of exclusive or special rights, the method for the calculation of costs and the repayment procedure in case of over-compensation. However, the Commission did not solve the most important problem – it did not entirely explain and justify the inclusion of 'reasonable profit' in the public service compensation. Therefore, undertakings still have to operate under conditions of reduced legal certainty (see further

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d'assurances (FFSA) v. Commission of the European Communities, [1997] ECR II-229; Judgment of 10 May 2000 in *Case T-46/97, SIC - Sociedade Independente de Comunicação SA v. Commission of the European Communities,* [2000] ECR II-2125.

[172] Judgment of 22 November 2001 in C*ase C-53/00, Ferring SA v. Agence centrale des organismes de securite sociale (ACOSS)*, [2001] ECR I-9067; Opinion of Mr Advocate General Tizzano of 8 May 2001 in *Case C-53/00, Ferring SA v. Agence centrale des organismes de securite sociale (ACOSS)*, [2001] ECR I-9067.

[173] Judgment of 17 October 2002 in *Case T-98/00, Linde AG v. Commission of the European Communities*, [2002] ECR II-3961.

[174] See operative part of Judgment of 24 July 2003 in *Case C-280/00, Altmark Trans GmbH and Regierungspräsidium Magdeburg v. Nahverkehrsgesellschaft Altmark GmbH, and Oberbundes-anwalt beim Bundesverwaltungsgericht*, [2003] ECR I-7747.

[175] Community Framework for State Aid in the Form of Public Service Compensation (2004), available at http://www.europa.eu.int/comm/competition/state_aid/others/public_service_comp/en.pdf.

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discussion on the financing of public service obligations in Section IV of this chapter and in Chapter F).

2. Protectionism in Favour of Providers of Services of General Economic Interest by National Courts and Competition Authorities

As it would be difficult to cover the entire case law of competition authorities and courts of all Member States, this section will introduce a few examples, showing how excessively national authorities protect providers of services of general economic interest. For the most part there is little case law regarding services of general economic interest at national level. This may be caused by the anti-competitive decisions of national authorities leading to widespread hesitations by potential competitors to take cases to the courts, or before the competition authorities, because it might just be too costly and time-consuming, with little or no chances of success.

The two main problems underlying the case law regarding services of general economic interest at national level are the refusal to recognise the inter-Member State effects of these services and the provision of little or non-convincing reasoning in the decisions.

Both Dutch and Greek courts have refused to acknowledge the inter-Member State effects of services of general economic interest.[176] Thus, national authorities have escaped the application of Community law (at the time of these decisions, the relevant Community law was limited to Article 86 EC Treaty, since sector-specific legislation did not exist back then). Community law, however, would hve been more restrictive than national provisions, which at that time expressly allowed monopolists to exclude (potential) competitors from access to their networks. Until action was taken at the Community level,[177] these national decisions allowed market foreclosure, as access to a network is a pre-condition for establishing any supply-side competition.

The Dutch case[178] is of particular interest, as it not only failed to take into account Community competition law, but also the free movement rules.[179] Legal scholars have correctly identified that the Dutch court expressly protected the domestic provider of telephone services by allowing it to refuse the connection

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[176] Judgment of 1988 in *Case 989/1987 Private Broadcasting Undertakings*, cited in *P. Behrens (ed.)*, EEC Competition Rules in National Courts V., 2000, pp. 316-317 (Greek case); Judgment of 27 March 1986 in *Case J.G.S.S. and De Consumentenbond v. Staat der Nederlanden*, cited in *P. Behrens (ed.),* EEC Competition Rules in National Courts II, 1994, p. 212.

[177] See Chapter D, Section V.

[178] Judgment of 27 March 1986 *Case J.G.S.S. and De Consumentenbond v. Staat der Nederlanden*, cited in *P. Behrens (ed.),* EEC Competition Rules in National Courts II, 1994, p. 212.

[179] It would have been possible for the national authorities to invoke Art. 86 (2) EC Treaty, which permits the non-application of the Community competition rules, but the authorities did not do this. Instead, they stated that obviously anti-competitive behaviour, whether that of the state or undertakings performing universal service obligations, is not producing anti-competitive effects. It seems that they have purposefully avoided the application of Art. 86 (2) to the behaviour, which national authorities allowed. This could not have been classified as suitable and necessary for the performance of the entrusted universal task.

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of telephones which were provided by other undertakings.[180] The court did not take into account the fact that the effect on trade between Member States could have been easily established by considering that telephones, which were to be connected to the network, could have been supplied by producers from other Member States. Thus, the court also failed in its reasoning in that it alleged the existence of pure intra-Member State effects.

With regard to the fact that national competition authorities provide little reasoning, we could refer to a series of cases on postal services where the Irish Competition Authority did not consider the anti-competitive consequences of tying. Postal services were provided by *An Post* only in so far as customers also obtained postal franking machines (including their inspection, repair, maintenance and replacement) from it.[181] The Authority accepted such behaviour as necessary to prevent fraud, and one can only guess what the Authority meant by this, as it provided no further explanations. This reasoning is not only weak but unacceptable reasoning, since the Authority completely overlooked the main problem of the agreements under consideration – the tying.

It is well established that a tie can be anti-competitive because an undertaking with a dominant position in the market – where competition may or may not be feasible – uses its market power to strengthen its position in another market, where competition still exists. The tie not only threatens the survival of existing competitors but also creates barriers to entry for potential competitors because customers cannot easily switch to other products. Thus, competition can be entirely eliminated. The tie at issue could not be justified, as it would not satisfy the Court's requirement of 'ordinary commercial practice'.[182] It does not meet the indispensability criterion. At the very least, inspection, repair, maintenance and replacement of the postal franking machines could also have been provided by other undertakings. Therefore, the Irish Authority primarily protected commercial interests of the national postal undertaking by allowing it to continue anti-competitive behaviour.

Another case of importance decided by the Irish Competition Authority concerned a notified agreement, which intended to impose exclusive purchasing rights on customers. This time the argumentation was contradictory. The Competition Authority stated that exclusive rights foreclose markets from potential competition. On the other hand, it identified that "access to the market is not entirely ruled out, and the exclusive purchasing systems do not operate [so

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[180] *Behrens*, *supra* note 178, at 212.

[181] Decision of Irish Competition Authority of 20 March 2001 relating to a proceeding under Section 4 of the Competition Act 1991 (*Case CA/10/00-An Post*), available at http://www.tca.ie; Decision of Irish Competition Authority of 18 December 1995 relating to a proceeding under Section 4 of the Competition Act 1991 (*Case CA/18/95-An Post/Neopost/BNP*), available at http://www.tca.ie; Decision of Irish Competition Authority of 18 December 1995 relating to a proceeding under Section 4 of the Competition Act 1991 (*Case CA/17/95-An Post/Pitney Bowes/Barclays*), available at http://www.tca.ie.

[182] Judgment of 6 October 1994 in *Case T-83/91, Tetra Pak International SA v. Commission of the European Communities (Tetra Pak II),* [1994] ECR II-762, at paragraph 136.

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as] to foreclose new entry."[183] As already established by the ECJ in the *Hoffmann-La Roche* case, exclusive purchasing obligations restrict competition as they foreclose markets from potential competition. Furthermore, these obligations are not based on market forces but unilaterally determined by the undertaking. In addition, consumers have a limited choice of products.[184] It is pretty obvious that the Irish Competition Authority did not take due account of the standing practice of the European Court leading to only partial enforcement of Community competition law at national level.

To conclude this section, I will briefly discuss the practice of the German Federal Cartel Office [hereinafter FCO], whose conservative attitude towards more competition in the universal service markets of the past has evolved into a more liberal, pro-Community attitude.

Still in its decisions of 1999, the FCO held that access to a network could be refused once an undertaking can prove that it uses its full capacity and overcapacity would decrease the security of supply. In addition, with regard to network access fees, the FCO identified that it is not necessary to determine whether they are adequate or excessive.[185] However, while in the case under consideration the plaintiff would have been able to cover these costs, other potential competitors would have been prevented from access to the network due to financial difficulties. Thus, by allowing the denial of network access and the maintenance of high network access fees, the FCO prevented the expansion of supply-side competition.

Nevertheless, the FCO has since changed its attitude, which could be explained by the fact that the German market is more liberalised than that of other Member States, e.g. gas and electricity markets are now 100% open in Germany[186] In one instance, the President of the FCO expressed his regrets that an appeal pending before the German Supreme Court was withdrawn, since a judgment would have made it easier for the FCO to prohibit long-term supply contracts for gas and electricity. Such contracts have the effect of precluding other undertakings form entering the market and potentially constitute a violation of both German and Community competition rules.[187] In addition, the

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[183] Decision of Irish Competition Authority of 10 April 1995 relating to a proceeding under Section 4 of the Competition Act 1991 (*Case CA/540/92E-Blugas Limited*), available at http://www.tca.ie, at paragraph 29.

[184] Judgment of 13 February 1979 in *Case 85/76, Hoffmann-La Roche v. Commission of the European Communities*, [1979] ECR 461, at paragraphs 89-91.

[185] Decision of the FCO of 30 August 1999 in *Case B8-40 100-T-99/99 BEWAG*, available at http://www.bundeskartellamt.de.

[186] European Commission, EU Energy and Transport in Figures 35-36 (2002). In 2003, the FCO has gone even further and has requested energy undertakings to reduce network access fees; see Decision of the FCO of 14 February 2003 in *Case B11-40 100-T-45/01 TEAG*, available at http://www.bundeskartellamt.de; Decision of the FCO of 21 March 2003 in Case B11-40 100-T-38/01 Stadtwerke Mainz AG, available at http://www.bundeskartellamt.de.

[187] *Bundeskartellamt* zur Verhinderung einer BGH-Entscheidung zu langfristigen Energie-Lieferverträgen [Federal Cartel Office Comments on the Impossibility of the German Supreme Court to Rule on the Validity of Long-term Energy Supply Contracts], Press release, FCO, 7 November 2003, available at http://www.bundeskartellamt.de.

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FCO has recently changed its opinion with regard to railway services and has requested that railway concessions due to expire in 2005 are re-assigned via an EU-wide auction. This would open the market for railway services to more competition and would reduce the negative effects of an increasing number of mergers between domestic transport undertakings, which attempt to improve their market position in response to EU railway legislation of 2001.[188] We can only hope that other competition authorities eventually follow the German approach in order to introduce more competition in the internal market.

IV. Poor Responsiveness to Changes in Market Circumstances

After World War II, when governments were the only providers of such services as gas, electricity, water, transportation and telecommunications, emphasis was placed on the mere availability of these services.[189] Today it is not only easier to obtain private financing in comparison to the past allowing more undertakings to operate in these markets, modern technologies have also created substitutable products in response to changing consumer priorities. As a result, it has to be reconsidered whether privileges granted to undertakings for the performance of universal service obligations can still be justified.

1. Easiness to Obtain Private Financing in Comparison to the Past

The expansion of the financial sector has made it easier to obtain private financing in comparison to the past. Thus, undertakings are no longer dependent only on state finances, but can make use of different types of external financing such as bank loans, factoring, leasing and overdrafts, and can also apply for structural funds from the Community.[190] As providers of services of general economic interest are most likely going to be either medium or large undertakings due to the scale of operation required for the provision of services of general economic interest,[191] possibilities and conditions for obtaining financing are especially favourable. Banks are able to grant loans with more favourable interest rates and lower bank charges, as the scale of the loans is usually large enough to allow the bank to meet its profitability requirements. Moreover, the cost of a loan *per se* is lower, as administrative costs (gathering of information and application for a loan) do not grow proportionate to the size of

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[188] Decision of the FCO of 2 December 2003 in *Case B9-60 211-Fa-91/03 Deutsche Bahn AG and Others*, available at http://www.bundeskartellamt.de.
[189] *Cint*, *supra* note 8, at 161-162.
[190] Enterprises' Access to Finance [2001] SEC/1667, at 4-8; Green Paper on Services of General Interest, COM/2003/270 final, at 26.
[191] Small undertakings would neither be able to manage a network nor to provide services of general economic interest on a Community-wide basis, as less than 50 employees cannot perform all administrative and technical duties; see also Commission Recommendation 96/280/EC of 3 April 1996 concerning the definition of small and medium-sized enterprises, OJ 1996 L 107/4; Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises, OJ 2003 L 124/36.

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the loan. In addition, as large and medium-sized undertakings are the most important clients for banks, these enterprises have the possibility to 'shop' for the best financial services thereby obtaining considerable benefits for doing business.[192]

Nevertheless, Member States and the Community, as a result of extensive lobbying by the providers of services of general economic interest have chosen the most distorting way of external financing – state aid This should not be surprising because other types of external financing have to be repaid with interest and do not place undertakings in a similarly privileged position.

Even though Community law on state aids prohibits only overcompensation,[193] state aid *per se* puts the undertakings in a better position in the market in comparison to other undertakings, which do not receive similar aid.[194] As discussed in greater detail in Section III of this Chapter, the European Court has repeatedly decided that financing of universal service obligations does not constitute state aid. However, it not only exempted the actual costs of the performance of universal service obligations from the notion of 'state aid', it also exempted 'reasonable profit'.[195] Thereby, the Court not only failed to recognise that financing of universal service obligations does constitute state aid, but has indirectly permitted illegal state aid.

It is not complicated to establish that the financing of universal service obligations constitutes state aid. On numerous occasions the Commission, Advocates General and the Court itself have identified in their analysis that all four elements of state aid are present in these kind of cases. Since financing of universal service obligations (i) provides an economic advantage to selected undertakings or for the production of selected products; (ii) comes out of state resources; (iii) distorts competition; and (iv) affects trade between Member States, it should be regarded as state aid.[196] Furthermore, as already stated above, state aid generally has anti-competitive effects. The receiving undertaking obtains an economic advantage and, as a result, is able to operate under better market conditions than other undertakings. No matter how efficiently potential competitors operate, they cannot beat the providers of services of general economic interest receiving additional funding, because only the latter have

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[192] European Commission, SMEs and Access to Finance, Observatory of European SMEs (2003), available at http://www.europa.eu.int/comm, at 7-15; Enterprises' Access to Finance [2001] SEC/1667, at 8.

[193] Green Paper on Services of General Interest, COM/2003/270 final, at 26.

[194] Judgment of 24 February 1987 in *Case 304/85, Acciaierie e Ferriere Lombarde Falck v. Commission of the European Communities*, [1987] ECR 871.

[195] See operative part of Judgment of 24 July 2003 in *Case C-280/00, Altmark Trans GmbH and Regierungspräsidium Magdeburg v. Nahverkehrsgesellschaft Altmark GmbH, and Oberbundesanwalt beim Bundesverwaltungsgericht*, [2003] ECR I-7747.

[196] For example, see Commission Decision 2002/753 of 19 June 2002 on measures implemented by the Federal Republic of Germany for Deutsche Post AG, OJ 2002 L 247/27; Opinion of Mr Advocate General Tizzano of 8 May 2001 in *Case C-53/00, Ferring SA v. Agence centrale des organismes de securite sociale (ACOSS),* [2001] ECR I-9067; Judgment of 22 November 2001 in *Case C-53/00, Ferring SA v. Agence centrale des organismes de securite sociale (ACOSS)*, [2001] ECR I-9067. The four criteria of state aid are listed in Art. 87 (1) EC Treaty.

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guaranteed profit margins. Finally, trade between Member States is affected, as services of general economic interest produce spill-over effects on the rest of the economy, which can be illustrated by the consideration that costs for the production of services of general economic interest are passed on to producers of other goods and services potentially to be traded across national boundaries.[197]

Once it is established that the financing of universal service obligations constitutes state aid, it is necessary to determine whether one of the exceptions applies, thereby making it compatible with the internal market. However, neither Article 87 (2) and (3) EC Treaty provides an applicable justification, nor can the *de minimis* rule help out.[198] The financing of universal service obligations does not have purely marginal effects on competition because they are performed under oligopolistic conditions by undertakings with special rights. Furthermore, the competitive situation in the market of services of general economic interest produces adverse effects on the rest of the economy due to extensive interdependence of services of general economic interest and other goods or services.

Another exception to be considered is Article 86 (2) EC Treaty. In applying Article 87 EC Treaty in conjunction with Article 86 (2), the Court has taken the approach that the financing of universal service obligations is not only compatible with the internal market, but does not even constitute state aid because such financing supposedly produces neutral effects on the market.[199] This argumentation cannot be accepted, however. Firstly, as established above, the financing of universal service obligations constitutes state aid. Instead of declaring the opposite, the Court should have ruled that *it is state aid that may be declared compatible* with the internal market, because this would have helped to increase legal certainty. Secondly, the Court has mistakenly applied Article 86 (2). This article may only be invoked, if the prohibition of financing of universal service obligations would obstruct the performance of the entrusted task, thereby making the application of normal competition rules highly undesirable. However, since the Court excluded from the notion 'state aid' not only the costs for the performance of universal service obligations, but also 'reasonable

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[197] See also Chapter B, Section I.

[198] Commission Regulation (EC) 69/2001 of 12 January 2001 on the application of Arts. 87 and 88 of the EC Treaty to *de minimis* aid, OJ 2001 L 10/30; Judgment of 10 July 1986 in *Case 234/84, Kingdom of Belgium v. Commission of the European Communities*, [1986] ECR 2263.

Article 87 (2) EC Treaty provides that the following state aid is compatible with the internal market: (i) aid with social character; (ii) aid to compensate damage caused by natural disasters; (iii) aid granted to certain areas of the Federal Republic of Germany, which have been affected by the division of Germany.

Article 87 (3) EC Treaty provides that the following state aid may be considered compatible with the internal market: (i) aid to promote the economic development of areas with abnormally low standard of living or serious underemployment; (ii) aid for the execution of an important European project; (iii) aid facilitating the development of certain economic activities or areas, if this is not contrary to the Community interest; (iv) aid to promote culture and heritage conservation.

[199] Judgment of 22 November 2001 in *Case C-53/00, Ferring SA v. Agence centrale des organismes de securite sociale (ACOSS)*, [2001] ECR I-9067.

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profits', Article 86 (2) can no longer serve as a justification because only cost-coverage can be considered necessary for the provision of services of general economic interest under conditions of economic equilibrium. Only the cost-coverage serves as the "correction of market failure."[200] Profit-coverage is already hindering competition.

Thus, the Court has indirectly permitted illegal state aid with adverse consequences on the market. Excessive financial benefits to providers of services of general economic interest create entry barriers for potential competition. As a result, the choice of products remains limited and prices can be kept artificially high, which eventually indicates an inefficient operation of the market. Furthermore, the internal market cannot be completed but remains partitioned along national boundaries due to entry barriers created by the financial protection of selected undertakings. But the gravest problem is that the generous treatment of payments for universal service obligations may encourage large-scale aid from Member States in the future, thereby leading to more adverse distortions of competition.[201]

2. Existence of Substitutable Products as Provided by Investment and Innovation

An adequate discussion of the existence of substitutable products, as provided by investment and innovation, requires detailed expert knowledge and could be a topic for an independent research paper. Therefore, this sub-section will only give a brief introduction to this issue. As the Commission has acknowledged, modern technologies have created substitutable products in such areas as telecommunications, transport and postal services.[202] With technological advancement special rights are often no longer justified, as competitors can provide substitutable products and should be able to do so in a competitive environment, which must be provided by the state and guaranteed by legislation. However, the legislative framework has been fully adjusted to prohibit special rights only with regard to telecommunications services.

Note that the notion 'telecommunications services' goes beyond voice transmission. Much of traditional telephone use can now be effectively substituted by mobile telephony and the internet.[203] Especially the borders between fixed and mobile telephony have vanished. At the end of 2001 the number of mobile phone subscribers in the EU exceeded by 70 million the subscribers for fixed telephony, and also the density of mobile phones exceeded that for fixed lines.[204] The high degree of substitutability is further supported by

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[200] *A. Evans*, European Community Law of State Aid, 1997, p. 81.
[201] Id., at 90.
[202] Services of General Interest in Europe, OJ 1996 C 281/3, at paragraph 13.
[203] *N. Chryssanthou*, The EU's External Transactions in Telecommunication Services: a Mirror of the Dawning Information Society, 15 Statistics in Focus: Economy and Finance, 2001, pp. 1, 2-3 .
[204] The density of mobile phones and fixed telephone lines in the EU is 54 per 100 and 73 per 100 inhabitants respectively; see *M. Lumio & L.C. Sinigaglia,* Telecommunications in Europe, 12 Statistics in Focus: Industry, Trade and Services 1, 4-5 (2003).

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the annual price decrease of 30% for mobile telephony. The prices for mobile phone services have now reached theprice levels of fixed telephony.[205] All these developments have been taken into account in adopting the new legislative framework for telecommunications in 2002, which effectively covers all competitive concerns: universal service obligations, network access and the actual provision of services. Moreover, the new legislative framework has been adjusted to technological progress, and regulates not only telecommunications services but all electronic communications. Thereby, the risk that legislation soon becomes out of date because of rapid technological advancements, has been minimized.

However, the situation with regard to railway and postal services is not so promising, and the rest of this sub-section will address both of these services in turn.

In relation to railway services there has been little technological progress within the sector itself. Technological advancements relate mostly to other types of transport services, such as planes, cars and trucks. The main exception are high-speed trains, but they primarily provide substitutes for traditional passenger rail traffic.[206] Substitutability in the railway sector depends on the type of the targeted market. Business travellers require comfort and time-tables adjusted to business needs, but price plays a minor role. Thus, regular railway services can be substituted with scheduled air travel or high-speed trains. Leisure travellers, on the other hand, are mainly seeking favourable prices. Due to lower customer requirements, the choice of substitutes is larger and includes economy-class air travel, buses and personal vehicles. With regard to the transportation of goods, regular railway services can be substituted with trucks or to some extent with sea transport (as long as seller and buyer are located near waterways).[207] The existence of various substitutes for different types of target markets would presume that the changes in market circumstances have also led to adjustments of railway legislation by prohibiting special rights. Nevertheless, this is not the case. The current legislative framework for railways still supports railway services as 'public service obligations' of Member States, even though these services often do not really present the most efficient way for satisfying market needs due to the existence of substitutes. Similar as in the case of air transport, the ultimate goal of Member States is to secure that a local undertaking survives as a 'national symbol' even for the price of market inefficiency. In this context, it should not be forgotten that the increased use of railways is favourable for the environment, and decreases traffic congestion again reducing emissions. Since

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[205] *European Commission*, Price Levels and Price Dispersion in the EU, European Economy (July 2001), available at http://www.europa.eu.int/comm, at 13.

[206] *European Commission*, European Economy, 1999, pp. 211-212.

[207] Commission Decision 94/663 of 21 September 1994 relating to a proceeding pursuant to Article 85 of the EC Treaty and Article 53 of the EEA Agreement (IV/34.600 - Night Services), OJ 1994 L 259/20; Commission Decision 94/894 of 13 December 1994 relating to a proceeding under Article 85 of the EC Treaty and Article 53 of the EEA Agreement (IV/32.490 - Eurotunnel), OJ 1994 L 354/66; European Commission, European Economy 25 (1999).

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the protection of the environment is one of the EC objectives,[208] any policy changes with regard to railways should take due account of this.

With regard to postal services, technological advancements have provided substitutes for postal services currently treated as universal services obligations.[209] For example, such products as letters and other traditional mail can now be substituted, at least in party, by fax and e-mail, which are considerably cheaper than postal services.[210] Moreover, 12 % of the letter market has been lost by national postal monopolies to courier services, which is another form of substition.[211] In addition, certain developments in the financial sector have created substitutable services, for example, postal payment services are now frequently substituted by bank payment services.[212] However, postal legislation continues to permit anti-competitive special rights for national postal monopolies. It has not been adjusted to new market conditions and this is placing providers of substitute services in a disadvantaged position.

Furthermore, the Commission has identified in relation to packages that such multinationals as United Parcel Service and Federal Express are also active in the postal market.[213] Here the substitute is not the delivery of the packages itself, but additional services offered by these providers. For example, couriers are often in a position to provide cheaper and faster services than national postal monopolies.[214] However, as Member States may reserve the transportation of packages of up to twenty kilograms to their national postal monopolies, it is more difficult for potential competitors to operate in this market because package delivery services provided by them are similar to those reserved to national postal monopolies.

It has to be acknowledged, however, and this is true throughout this sub-section, that not all services for all users can be substituted. This means that not the entire population would have access to the full range of postal services in the absence of a universal service obligations, which, in turn, is contrary to the ieda of services of general economic interest. For example, elderly people in peripheral regions might not have the money and the knowledge to use the internet instead of sending a letter or making a telephone call. This cannot be permitted, as the Union is aiming not only at economic but also at social

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[208] EC Treaty, Arts. 174-176.

[209] Universal service obligations include various postal items not exceeding two kilograms, packages not exceeding ten kilograms (the weight can be extended to twenty kilograms), registered mail and insured items; see Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service, OJ 1998 L 15/14, Art. 3.

[210] *European Commission*, European Economy, 1999, pp. 200-201; *N. Chryssanthou*, The EU's External Transactions in Telecommunication Services: a Mirror of the Dawning Information Society, 15 Statistics in Focus: Economy and Finance, 2001, pp. 1, 2.

[211] *WTO Secretariat*, *supra* note 94, at 471.

[212] Commission Decision 2002/782 of 12 March 2002 on the aid granted by Italy to Poste Italiane SpA, OJ 2002 L 282/29, at paragraph 116.

[213] Commission Decision 2002/753 of 19 June 2002 on measures implemented by the Federal Republic of Germany for Deutsche Post AG, OJ 2002 L 247/27, at paragraph 100.

[214] *WTO Secretariat*, *supra* note 94, at 470.

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cohesion. Thus, as it can be seen in Chapter F, in my proposals for changing the current regulatory framework, I am not claiming that universal service obligations should be entirely abolished in order to promote more competition. Rather they should be limited to the essential minimum necessary to ensure that all EU inhabitants, regardless of their financial and technological sophistication, have access to services of general economic interest.

3. Changing Customer Priorities

To conclude the discussion on the satisfaction of consumer needs, it is important to identify that consumer priorities have changed with time. If right after World War II the main issue was the provision of services of general economic interest *per se*, nowadays the focus is on price, quality and added value.[215] In comparison to the past, the importance of price and choice of products has increased by 23% and 14% respectively.[216] Moreover, consumers demand increasingly more protection in case of a dispute in another Member State.[217] Therefore, consumers are no longer interested only in the mere availability of services of general economic interest or that the state performs its public service obligations, but they demand the provision of these services is based on conditions of an open market economy. There are many reasons for this shift, first and foremost, the increasing influence of the service sector on the economy overall, with services nowadays contributing three times more to Member States' GDP than manufacturing.[218]

However, while some success should be acknowledged, the current regulatory framework for services of general economic interest has only partially managed to keep up with changes in consumer priorities. As stated already in Section II of this Chapter, only 15% of EU consumers think that their interests in relation to price and quality are well taken care of by current Community policies on transport, energy, telecommunications and competition. To better demonstrate the reasons, the rest of this sub-section will look at how the results of the implementation of sector-specific legislation differ from consumer priorities.

Firstly, the implementation results of the current regulatory framework do not fully reflect changing consumer priorities in relation to price. It is true that in several sectors, e.g. telecommunications and electricity, prices have considerably decreased after the liberalisation. However, these prices have not yet attained the lowest possible level because the liberalisation process has been slow and has started only recently. In addition, the liberalisation has not been completed in

[215] Services of General Interest in Europe, OJ 1996 C 281/3, at paragraph 13.
[216] *G. Thornton*: Accountants and Business Advisors, Survey of Middle-Market Business Makers 2001, available at http://www.grantthornton.com (accessed on 27 Feb. 2004).
[217] *EOS Gallup Europe*, Consumer Survey, available at http://www.europa.eu.int (accessed on 27 Feb. 2004), at 9.
[218] Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee and the Committee of the Regions-Consumer Policy Strategy 2002-2006, OJ 2002 C 137/4.

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any of the sectors of services of general economic interest. Therefore, as also identified by the Commission, there is still considerable potential for further price reductions. This finding is further supported by the fact that since the beginning of the liberalisation process, there have been price decreases in every year. Furthermore, in some industries, e.g. railway and postal services, the price level has not changed because the development of a Community policy for these services lags behind that in other sectors.[219] In both of these sectors little attention has been given to new consumer priorities.

Secondly, consumer priorities in relation to quality and choice of products are not fully taken into account either. European consumers by and large are dissatisfied with the quality and choice of services of general economic interest. This is a direct result of excessive protectionism in favour of current providers of these services, leading to market foreclosure for potential competitors.[220] If the markets were more liberalised, larger number of undertakings would provide more services of higher quality at lower prices, because higher competitive pressure would exist in the market. While the current legislative framework has brought some improvements, the main focus is still on the actual provision of services of general economic interest and not on changing consumer priorities demanding lower prices, better quality, and a larger selection of products and suppliers.

V. Decades of Failure of the Commission to Act

Article 86 (3) EC Treaty is a rather unique article, whose very existence is surprising. It gives the Commission a rare opportunity to adopt autonomous liberalisation directives without the need of prior consultations with the Parliament, the Council, or the Member States, depriving the latter of political influence on the Commission. In addition, it allows the Commission to adopt decisions addressed to Member States. The Commission has similar rights and duties under Articles 81 and 82 EC Treaty with the important difference that these decisions are addressed to undertakings. Therefore, it is the legislative and not the supervisory capacity of the Commission under Article 86, which is of particular significance.

From the wording of Article 86 (3) EC Treaty one might expect that the Commission uses its autonomous legislative capacity extensively in order to adopt liberalisation directives to increase competition in the internal market. In the same way one might expect that the Commission regularly take decisions against anti-competitive measures of Member States in its supervisory capacity. Unfortunately, the practice of the Commission has proven the opposite. Besides taking only a few decisions and adopting only a few directives under Article 86 (3), it was not until 1980 that the Commission acted at all; a full twenty years

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[219] *European Commission*, Price Levels and Price Dispersion in the EU, European Economy (July 2001), available at http://www.europa.eu.int/comm; see also Chapter D, Section II.
[220] See Chapter D, Sections II and III.

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after the adoption of the EEC Treaty.

1. Simplified Adoption Procedure for a Directive

Article 86 (3) EC Treaty provides a simplified adoption procedure for two types of liberalisation directives. Firstly, the Commission may adopt directives for the purpose of preventing future infringements of Community law by Member States, and secondly, it may adopt directives, which further clarify the Treaty obligations of Member States.[221] The simplicity of the adoption process lays in the fact that the Commission may act alone,[222] and that it may choose whether and how to address the issue in question.[223] Nevertheless, in an effort to avoid resistance from Member States, the Commission has always engaged in consultations with the Council, European Parliament, Member States and any third parties affected,[224] although this has slowed down the adoption procedure.

By failing to act even though Article 86 (3) EC Treaty provides a simplified tool to achieve a higher level of competition, the Commission violated one of its more important duties. It took the Commission more than twenty years after the adoption of the EEC Treaty until it adopted the first directive under Article 86 (3). The *Transparency Directive*[225] required Member States for the first time to ensure the maintenance of separate accounts for different activities of privileged undertakings and to provide transparency of cost allocation among different activities. This was seen as a necessary prerequisite for the elimination of illegal state aid and cross-subsidization that distort competition. However, these are not the only activities having anti-competitive effects.

Other directives adopted under the Article 86 (3) mainly cover the telecommunications sector.[226] However, this is not the only sector falling into

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[221] *Faull*, *supra* note 170, at 326-327; the Court has also ruled that the Commission may adopt directives and decisions under Art. 86 (3) EC Treaty only to condemn or prevent measures taken by Member States, which relate to undertakings falling under Art. 86 (1) or (2) EC Treaty; see Judgment of 19 March 1991 in *Case C-202/88, French Republic v. Commission of the European Communities,* [1991] ECR I-1223.

[222] Judgment of 19 March 1991 in *Case C-202/88, French Republic v. Commission of the European Communities,* [1991] ECR I-1223.

[223] Judgment of 20 February 1997 in *Case C-107/95 P, Bundesverband der Bilanzbuchhalter e.V. v. Commission of the European Communities*, [1997] ECR 947; however, the Commission has an obligation to observe all procedural requirements of the Community, such as providing the reasoning for the measures taken, observing the defence rights of parties and providing to Member States a complete statement of objections; see Judgment of 8 July 1999 in *Case T-266/97, Vlaamse Televisie Maatschapij NV. v. Commission of the European Communities*, [1999] ECR II-2329; Judgment of 12 February 1992 in *Joined Cases C-48/90 and C-66/90, Kingdom of the Netherlands and Koninklijke PTT Nederland NV. and PTT Post BV. v. Commission of the European Communities,* [1992] ECR I-565; Judgment of 6 July 1982 in *Joined Cases 188 to 190/80, French Republic, Italian Republic and United Kingdom of Great Britain and Northern Ireland v. Commission of the European Communities,* [1982] ECR 2545.

[224] Services of General Interest in Europe, OJ 1996 C 281/3, at paragraph 24.

[225] Commission Directive 80/723/EEC of 25 June 1980 on the transparency of financial relations between Member States and public undertakings, OJ 1980 L 195/35.

[226] For example, see Commission Directive 88/301/EEC of 16 May 1988 on competition in the

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the category 'services of general economic interest'. In this way, the Commission has left other services of general economic interest unregulated although anti-competitive effects in the markets for these services produce adverse spill-over effects on other markets due to significant interdependence. Altogether only a small number of directives have been adopted by the Commission under Article 86 (3) EC Treaty.

The current approach of the Commission is that it threatens Member States with the adoption of measures under Article 86 (3) EC Treaty, if the latter resist the completion of the internal market for different services of general economic interest.[227] Clearly the Commission should have taken this more affirmative approach much earlier. If it had not failed to fulfil its obligations under Article 86 (3), the current state of liberalisation would already be at a higher level, providing a more competitive market. The Commission not only should have acted but would have been perfectly able to do so, because it is experienced in making complex EU-wide economic evaluations, and it should have identified long ago that markets for services of general economic interest cannot be characterised as competitive. However, before criticising the Commission too much, we must not forget that if it had been up to the Council to adopt any liberalisation measures, "we should probably have seen no legislation at all."[228]

2. Negotiation Powers with the Council of Ministers

If the Commission did not want to adopt Article 86 (3) directives in order to avoid political resistance from Member States, which might have threatened the very existence of the Union, it could have negotiated with the Council and proposed the adoption of legislative measures under Article 95 EC Treaty. Nevertheless, it was not before the 1990s that the Commission used Article 95 for the adoption of legislative measures.[229] Its failure to act until then cannot be justified, even though these measures finally addressed several sectors: electronic communications, energy and postal services.

The Commission should have used Article 95 more extensively, as measures based on this provision are more credible. Under Article 95 not only the

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markets in telecommunications terminal equipment, OJ 1988 L 131/73; Commission Directive 90/388/EEC of 28 June 1990 on competition in the markets for telecommunications services, OJ 1990 L 192/10 (no longer in force); Commission Directive 95/51/EC of 18 October 1995 amending Directive 90/388/EEC with regard to the abolition of the restrictions on the use of cable television networks for the provision of already liberalized telecommunications services, OJ 1995 L 256/49 (no longer in force).

[227] European Commission Directorate-General for Competition, European Union Competition Policy: XXXIst Report on Competition Policy 2001, 29 (2002).

[228] *Lane*, *supra* note 18, at 242.

[229] For example, see the following legislative acts: Council Directive 90/387/EEC of 28 June 1990 on the establishment of the internal market for telecommunications services through the implementation of open network provision, OJ 1990 L 192/1 (no longer in force); Council Directive 90/547/EEC of 29 October 1990 on the transit of electricity through transmission grids, OJ 1990 L 313/30; Council Directive 91/296/EEC of 31 May 1991 on the transit of natural gas through grids, OJ 1991 L 147/37.

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Commission is officially involved in the legislative process, but also the Parliament and the Member States through the Council, which "gives to the relevant [measures] a democratic legitimacy."[230] Due to the political consensus generally underlying legislative measures on Article 95, there is usually less resistance from Member States. Finally, the adoption procedure provides for intensive cooperation on multiple levels, virtually assuring the achievement of the best-possible and acceptable result for everyone.

However, in sensitive areas like services of general economic interest, directives are not necessarily the ideal tool for the approximation of national legislation. While directives are a flexible tool to harmonise different legal systems and able to take into account different political and social values of different Member States which is always useful for complex changes,[231] they not only have to go through a lengthy adoption process, but they also have to be transposed into national law. This can lead to partial, incorrect or seriously delayed transposition, all of which, unfortunately, are quite common. Statistics indicate that the current transposition deficit of directives is at 2%. Although this is excellent compared to 20% ten years ago, it still deprives undertakings and consumers from fully enjoying the benefits of the internal market. In addition, open infringement cases have increased to 1,500 meaning that the directives have not been correctly transposed into national law, which distorts the functioning of the internal market almost as badly as total non-transposition.[232] As a result, different competitive conditions continue to prevail across the EU.[233] In the end, those Member States that have fully implemented the directives into national law are at a disadvantage, because undertakings operating in the foreclosed markets of less open Member States enjoy free access to more competitive markets, while being safe from competition in their national markets. Thus, the Commission should have either applied more restrictive wording in the directives or made more use of regulations that would have led to fewer violations due to the fact that they are directly applicable.

3. The Possibility of Adopting a Decision under Article 86 (3) EC Treaty

A further possibility provided by Article 86 (3) EC Treaty is the adoption of decisions condemning anti-competitive measures of Member States. The Commission, however, has largely avoided this possibility. Since the adoption of the EEC treaty only fifteen decisions were adopted, of which one was declared void by the Court.[234] Not only are there few decisions, in addition, it took

[230] *Faull*, *supra* note 170, at 329.
[231] *P. Craig & G. de Burca*, EU Law: Text, Cases and Materials, 2003, p. 115.
[232] Cited in The Internal Market-Ten Years without Frontiers [2002] SEC/1417, at 10-11.
[233] See Chapter E and Section II of Chapter D.
[234] Judgment of 12 February 1992 in *Joined Cases C-48/90 and C-66/90, Kingdom of the Netherlands and Koninklijke PTT Nederland NV. and PTT Post BV. v. Commission of the European Communities*, [1992] ECR I-565.

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almost thirty years for the first one to be adopted.[235]

Moreover, the Commission has covered only three anti-competitive practices in its decisions. Firstly, the Commission has prohibited the extension of monopoly rights into markets for value-added services that are (potentially) competitive. Specifically, the Commission condemned state measures, reserving international express courier services and specified-time mail deliveries to national postal services.[236] However, neither of the Commission's decisions challenges national postal monopolies as such, even though it is well known that a sole supplier is often tempted to abuse its position by charging higher prices in relation to costs of production. In addition, monopolies usually enjoy strong bargaining power with the government, which can create or strengthen entry barriers for competitors through legislative or administrative measures. This has also been the case with services of general economic interest, putting consumers at a disadvantage not only in relation to choice between alternative products.

Secondly, the Commission has condemned financial benefits that were granted by the state to established public undertakings or undertakings with special or exclusive rights.[237] Thirdly, the Commission has prohibited the imposition of discriminatory network access fees.[238] By concentrating mainly on financial barriers to market integration (which are significant, as they can usually be classified as state aid having an over-compensatory nature, making it difficult for competitors who do not benefit from similar financial advantages to enter the market), the Commission has avoided addressing numerous other problems. In particular, the Commission so far has not even attempted to 'physically' separate network operators and providers of services of general economic interest, although this would be a significant pre-condition for establishing fair supply-side competition. Furthermore, the Commission has not seriously addressed network access restrictions, and a variety of other problems. Therefore, the Commission has failed to make use of its decision making powers under Article 86 (3) EC Treaty, although this would have been a time-efficient possibility to prohibit anti-competitive measures.[239] Similarly, the Commission

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[235] Commission Decision 85/276 of 24 April 1985 concerning the insurance in Greece of public property and loans granted by Greek State-owned banks, OJ 1985 L 152/25.

[236] For example, see Commission Decision 90/456 of 1 August 1990 concerning the provision in Spain of international express courier services, OJ 1990 L 233/19; Commission Decision 2001/176 of 21 December 2000 concerning proceedings pursuant to Art. 86 of the EC Treaty in relation to the provision of certain new postal services with a guaranteed day- or time-certain delivery in Italy, OJ 2001 L 63/59.

[237] For example, see Commission Decision 85/276 of 24 April 1985 concerning the insurance in Greece of public property and loans granted by Greek State-owned banks, OJ 1985 L 152/25; Commission Decision 97/181 of 18 December 1996 concerning the conditions imposed on the second operator of GSM radiotelephony services in Spain, OJ 1997 L 76/19.

[238] For example, see Commission Decision 87/359 of 22 June 1987 concerning reductions in air and sea transport fares available only to Spanish nationals resident in the Canary Islands and the Balearic Islands, OJ 1987 L 194/28; Commission Decision 2000/521 of 26 July 2000 relating to a proceeding pursuant to Article 86(3) of the EC Treaty (Spanish and Italian Airports), OJ 2000 L 208/36.

[239] *Faull*, *supra* note 170, at 322.

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did not makue use of its ability to address and solve a *specific violation*[240] – which would have allowed for a faster integration of the internal market through the establishment of more competition in the market for services of general economic interest.

Finally, the Commission is not confined to Article 86 (3) to condemn anti-competitive state measures. Article 226 EC Treaty provides for an effective alternative, which the Commission could have employed in addition or instead. As past experience demonstrates, measures under Article 86 (3) are frequently challenged in the Court for their validity.[241] Thus, it might have been more advantageous in some cases for the Commission to bring proceedings against a Member State under Article 226. This would have allowed the Commission to obtain binding rulings from the Court, which it could have used for subsequent development of Community policy and for gradually extending it further. This would not only have reduced disparities between the case law of both institutions, but would have also added judicial impartiality to measures taken under Article 86 (3), reducing political resistance of Member States.

E. Critical Analysis of Previously Suggested Remedies

Until the 1980s, Community action in the field for services of general economic interest was neither seen as necessary nor justified because these services were not considered an important element of the internal market. Little or no trans-national aspects of these services were identified due to the persisting opinion that markets for services of general economic interest were limited by national borders. In the beginning, nobody challenged the idea that Member States were not obliged to regulate services of general economic interest in accordance with the internal market requirements, and that national regulation in this field did not need to be compatible with EU competition rules. Rather, the focus was on core elements of a single European market: abolition of customs duties and charges having equivalent effect, abolition of quantitative restrictions and measures having equivalent effect, and prohibition of cartels. By and large, nobody even considered that commercially based provision of services of general economic interest would be advantageous for the effective functioning of the internal market and would contribute to faster economic integration of the Union.

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[240] Judgment of 12 February 1992 in *Joined Cases C-48/90 and C-66/90, Kingdom of the Netherlands and Koninklijke PTT Nederland NV. and PTT Post BV. v. Commission of the European Communities*, [1992] ECR I-565.

[241] For an example of a challenge to a Commission decision see the proceedings which led to the Judgment of 12 February 1992 in *Joined Cases C-48/90 and C-66/90, Kingdom of the Netherlands and Koninklijke PTT Nederland NV. and PTT Post BV. v. Commission of the European Communities*, [1992] ECR I-565; a challenge to a Commission Directive was concluded by the Judgment of 6 July 1982 in *Joined Cases 188 to 190/80, French Republic, Italian Republic and United Kingdom of Great Britain and Northern Ireland v. Commission of the European Communities,* [1982] ECR 2545.

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It took thirty years after the entry into force of the EEC Treaty, for the Community to identify that anti-competitive conditions in the market for services of general economic interest could produce spill-over effects in other markets for goods and services, which depend on the former due to their universal nature.Only after this link was understood, two proposals have been made to improve the functioning of the internal market. The Commission proposed in the 1980s, and also took action, to develop sector-specific regulation for services of general economic interest with clearly identifyable trans-national aspects. More recently, in May 2003, the Commission proposed to develop an autonomous 'Common European Framework' for services of general economic interest. Both proposals, and their respective advantages and disadvantages, are considered below.

I. Sector-Specific Regulation

Although sector-specific regulation has brought significant improvements in establishing competition in the market for services of general economic interest,[242] at present it still has substantial regulatory drawbacks. The main problem is that the Commission has tried to increase competition by addressing certain anti-competitive practices in one sector, while at the same time failing to address similar practices in other sectors. As a result substantial inconsistencies have appeared.

The main problem with a substantial part of the secondary legislation for services of general economic interest is the failure to adequately increase *supply-side competition.* For example, the Electricity Directive allows Member States to choose between the authorisation procedure and the tendering procedure when selecting providers. Only the tendering procedure must be conducted in accordance with principles of objectiveness, transparency and non-discrimination.[243] This approach is not unproblematic. While an open tendering procedure allows competitors to gain access to the market, the authorization procedure provides a possibility for Member States to continue anti-competitive practices. The authorization procedure simply does not guarantee an open and transparent selection process. Thus, the approach taken in the Directive does not secure genuine increases in competition in the market for electricity. If it were guaranteed that Member States chose the tendering procedure, a substantially higher level of competition could be achieved in the market. Unsurprisingly, Member States have by and large preferred to rely on the authorization rather than the tendering procedure,[244] thus continuing to foreclose their markets for

[242] See Chapter F.

[243] Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity, OJ 1997 L 27/20, art. 4-6.

[244] See Preamble to the Directive 2003/54/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in electricity and repealing Directive 96/92/EC-Statements made with regard to decommissioning and waste management activities, OJ 2003 L 176/37, at paragraph 22.

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competitors.

Furthermore, the criterion of 'technical, economic and financial capabilities' of the applicant undertaking has to be specifically mentioned, since it allows Member States to refuse permission for supplying electricity services. This criterion allows for a great deal of subjectivity in its application, and is generally difficult to satisfy for new entrants, as in many cases existing suppliers are well-established and stable undertakings that have received long-term state protection.

Sector-specific legislation has also not been entirely successful in introducing *free access to networks,* which is a pre-condition for establishing fair competition. For example, the New Gas Directive sets a requirement that any derogation with regard to third-party access rights to the network must be notified to the Commission for individual exemptions.[245] This provision *per se* assumes the possibility not to grant access, although access is crucial for any competition to exist on the supply side. In addition, with regard to free access to networks, the secondary legislation allows both the authorisation and the tendering procedures for the distribution of additional network capacity, which might appear through investment and innovation.[246] Once again, there is a possibility for market foreclosure, as Member States are most likely going to prefer the authorisation procedure as they did in the case of the actual provision of services, thus again providing protection to existing suppliers.

Access problems also persist in the railway sector. Existing legislation provides that a railway undertaking may obtain a licence in the Member State of establishment, but the licence in itself does not guarantee access to the network. In addition, the railway undertaking has to prove that it operates under good financial conditions, has a good reputation and is competent to provide railway services.[247] The directive is contradictory in itself as its aim is to develop uniform rules for access to the railway infrastructure, but it states that mere possession of an access licence does not entitle the undertaking to use the network. Thus, the directive does not separate, but re-unites the infrastructure and the actual provision of railway services. Also the pre-conditions for the provision of services are rather subjective. While one can objectively prove financial solvency, 'reputation' is a broad and non-defined term. Especially unfair is the condition of 'competency'. On this basis, undertakings engaged in other transport areas and interested to expand their areas of operation may be refused access rights because they have no experience in the provision of railway services. Quite obviously this condition is difficult, if not impossible, to satisfy, as only existing railway undertakings have this kind of experience, and thus 'competency', in providing railway services.

Another problem, which is not adequately tackled by secondary legislation, is

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[245] Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC, OJ 2003 L 176/57, Art. 27.

[246] Directive 2003/54/EC, OJ 2003 L 176/37, Arts. 6 and 7.

[247] Council Directive 95/18/EC of 19 June 1995 on the licensing of railway undertakings, OJ 1995 L 143/70, Arts. 4-5.

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the *lack of independence of undertakings from national authorities*. Although it is a positive aspect of more recent secondary legislation that Member States are required to establish a regulatory body for the granting of licences in order to ensure transparency, non-discrimination and uniformity of decisions, the legislation still allows Member States to designate ministries to perform this duty.[248] If the aim of the legislative measures was to insulate the provision of services of general economic interest from political influences, this provision achieves the complete opposite – politicisation of the economic sectors. In its Green Paper of 2003, the Commission stated that allowing ministries to exercise regulatory functions leads to a lack of independence, especially if Member States have retained ownership or control over providers of services of general economic interest.[249] The Commission's concerns can be easily explained by looking at the main functions of regulatory bodies. Undertakings have to comply with standards set by national authorities. But if undertakings providing services of general economic interest and national authorities are one and the same person, these standards have neutral effects, as they can be adjusted to the needs of the undertakings, which would certainly prefer that the national market is foreclosed for (potential) competitors. Furthermore, if undertakings providing services of general economic interest and national authorities are one and the same person, deviations from standards may remain unpunished, as self-punishment is not likely.

A further problem is the *lack of separation between network operators and service suppliers*. For example, the Preamble to the New Electricity Directive states that vertically integrated electricity undertakings contribute to existing anti-competitive conditions in the electricity market. However, the same preamble reaffirms that this does not require Member States to break up the undertaking, as such a requirement would constitute interference with property rights, the regulations of which fall into the competences of the Member States. The mere legal separation is regarded as sufficient for introducing more competition in the internal market.[250] However, legal, account and management unbundling does not mean *de facto* separation, because undertakings separated in these ways are likely going to cooperate with each other, because they ultimately do not regard themselves as separate undertakings.[251] Thus, without full separation, it is not

[248] Directive 2001/14/EC of the European Parliament and of the Council of 26 February 2001 on the allocation of railway infrastructure capacity and the levying of charges for the use of railway infrastructure and safety certification, OJ 2001 L 75/29; Commission Directive 88/301/EEC of 16 May 1988 on competition in the markets in telecommunications terminal equipment, OJ 1998 L 131/73; Directive 96/92/EC of the European Parliament and of the Council of 19 December 1996 concerning common rules for the internal market in electricity, OJ 1997 L 27/20; Directive 98/30/EC of the European Parliament and of the Council of 22 June 1998 concerning common rules for the internal market in natural gas, OJ 1998 L 204/1; Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service, OJ 1998 L 15/14.

[249] Green Paper on Services of General Interest, COM/2003/270 final, at 46.

[250] Directive 2003/54/EC, OJ 2003 L 176/37; EC Treaty, at 295.

[251] The Commission has also identified that legally unbundled network operators, service

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possible to exclude anti-competitive behaviour. In addition, the practice of EC institutions, in particular the practice of the Commission, seems contradictory regarding property ownership. For example, under the Merger Regulation[252] the Commission can grant clearance subject to conditions, which often require undertakings to dispose of parts of their property.[253] This is also an interference with property ownership, but seems to be justified.

Furthermore, it is unfortunate that the secondary legislation contains *discriminatory provisions.* For example, the Postal Directive allows Member States to set up a 'compensation fund' to ensure economic equilibrium of the undertaking providing postal services. Any undertaking interested in providing postal services under the authorisation procedure may have to contribute to that compensation fund.[254] Because there is no indication that the postal monopoly is also required to make financial contribution to the fund, this is not only a discriminatory provision, but also a possibility to foreclose the postal market for potential competitors via the imposition of this additional financial burden on competing providers of universal or non-universal services. When the Postal Directive was amended, the EC institutions identified the mistake of the initial directive of 1997, and stated that financial support from such a fund should be treated as state aid requiring prior notification to the Commission. The provision itself however was not deleted, leaving considerable uncertainty.[255]

With regard to *procedural drawbacks* of current sector-specific legislation, two issues have to be highlighted. First, the existing secondary legislation tolerates extreme flexibility in the implementation of the directives.[256] Member states can delay the transposition of the directives into national law, which means that the market for many services of general economic interest will likely remain non-competitive for at least another decade. Secondly, while the Commission has generally preferred to use directives rather than regulations, it has to be mentioned that the Commission. Nevertheless, it has to be mentioned that the Commission has made a substantial step towards more competition in

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generators, transmitters, distributors and suppliers have a tendency to cooperate in order to delimit supply-side competition; see *European Commission Directorate-General for Competition,* European Union Competition Policy: XXXIst Report on Competition Policy 2001 27 (2002).

[252] Council Regulation (EEC) 4064/89 of 21 December 1989 on the control of concentrations between undertakings, OJ 1990 L 257/13, art. 6.

[253] For example, see Commission Decision of 13 October 2000 declaring a concentration to be compatible with the internal market (*Case No IV/M.2050 - VIVENDI/CANAL+/SEAGRAM*) according to Council Regulation (EEC) No 4064/89, OJ 2000 C 311/3.

[254] Directive 97/67/EC of the European Parliament and of the Council of 15 December 1997 on common rules for the development of the internal market of Community postal services and the improvement of quality of service, OJ 1998 L 15/14.

[255] See the Preamble to the Directive 2002/39/EC of the European Parliament and of the Council of 10 June 2002 amending Directive 97/67/EC with regard to the further opening to competition of Community postal services, OJ 2002 L 176/21, at paragraph 25.

[256] Directive 2003/55/EC of the European Parliament and of the Council of 26 June 2003 concerning common rules for the internal market in natural gas and repealing Directive 98/30/EC, OJ 2003 L 176/57, art. 27; Directive 2003/54/EC, OJ 2003 L 176/37.

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the internal market. with the recent adoption of the Electricity Regulation.[257] This is the first regulation in this sector, and its direct applicability excludes the possibility that Member States adopt anti-competitive legislation or that Member States do not implement EU law into national legislation, both of which hinder the effective functioning of the internal market.

II. Development of a 'Common European Framework' for Services of General Economic Interest

The Commission proposed the development of a 'Common European Framework' for services of general economic interest after the introduction of the new Article 16 EC Treaty. It concluded that a common framework could specify common characteristics of services of general economic interest and that it could include procedural articles for easier subsequent harmonisation.[258] The Commission is certainly right in assessing that it is necessary to simplify the completion of the internal market for services of general economic interest, as long-term resistance to take action has made rapid action necessary to finally introduce more competition in the internal market.

However, the creation of a common European framework for services of general economic interest is neither desirable nor possible. The current level of competition is not only different in various sectors of services of general economic interest, but also among Member States. The Eurostat has identified that Germany, Austria, Finland, Sweden and the UK have fully opened their electricity market to competition. However, Denmark, Greece and France opened their markets by only 33% on average. Similarly, in the gas market, Germany, Austria and the UK have a market opening of 100%, but Denmark and France have only an opening of some 27%.[259] The achievement of a common framework would be difficult, if not impossible, at the highest level of liberalisation – namely, the achievement of full open markets for all services of general economic interest. In the best case scenario, Member States might agree on a compromise, which would probably not exceed a market opening of some 70% across the EU, because of the high sensitivity in the area under consideration. Thus, a common framework might eventually be a step backwards in European market integration, because it would allow the reintroduction of anti-competitive practices in those Member States and in those areas with a current opening of 100%.

Furthermore, the establishment of a common framework would be impossible, as long as it is in the competence of Member States to define services of general economic interest on the assumption that they are a reflection of each state's social, cultural and political values. In addition, although the Court has identified that services of general economic interest have such

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[257] Regulation (EC) No 1228/2003, OJ 2003 L 176/1, art. 3 and 4.

[258] Green Paper on Services of General Interest, COM/2003/270 final, at 13.

[259] *European Commission*, EU Energy and Transport in Figures, 2002, pp. 35-36.

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common elements as universality, suitability, necessity, continuity, equality of treatment and availability, the adoption of a common framework merely reflecting these elements would be too general and would produce no real progress in the legal framework.[260] Instead, it might further reduce legal certainty, which is already a significant shortcoming of the current regulatory framework for services of general economic interest.[261]

It would in any case be difficult to create a common framework for services of general economic interest, as technical requirements and characteristics of various sectors are different.[262] Different services of general economic interest have different requirements with regard to production, capital intensity, demand structure, etc.[263] Additionally, while there is potential competition in markets for electronic communications and postal services, the markets for electricity and gas, on the other hand, will always be oligopolistic. Furthermore, network operators are selected by the historic operator in the markets for electricity, gas and railway services. Only in the market for airline services, the network operator is chosen by open competition. Moreover, the railway industry is excessively subsidised, while electronic communication services are provided under normal commercial conditions (unregulated market). In addition, with regard to electricity, gas, electronic communications and railway services there is the problem of free access to the network.[264] This is not even an exhaustive list of examples of substantial differences in the current market conditions for providers of various services of general economic interest, but it clearly shows that a common framework would have to address difficult and varying issues, which are sector-related.

Moreover, it is not really necessary to establish a common framework with mere ‘symbolic value’, as desired by the Commission.[265] The simple adoption of a suitable framework directive, as identified by Eurocities, a network of European public authorities, would not be autonomous but supplementary to existing sector-specific legislation. This would not only increase legal certainty, but could also clarify existing definitions on services of general economic interest.[266] Moreover, an autonomous legislative framework, which would

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[260] See Chapter B. The Commission has also identified that a common framework would be too general if it merely concentrated on common elements of services of general economic interest; see Green Paper on Services of General Interest, COM/2003/270 final, at 13. See also Services of General Interest in Europe, OJ 1996 C 281/3, at paragraph 21. See also Electricité de France, Comments on Green Paper on Services of General Interest (19 Sept. 2003), available at http://www.europa.eu.int; *Deutsche Telekom*, Deutsche Telekom Comments on the Commission Green Paper on Services of General Interest (Sept. 2003), available at http://www.europa.eu.int.

[261] See Chapter D, Section I.

[262] Services of General Interest in Europe, OJ 1996 C 281/3, at paragraph 21.

[263] *Die Bahn*, Stellungnahme der DB AG zum „Grünbuch zu Dienstleistungen von allgemeinem Interesse“ der Europäischen Kommission [Comments of DB AG on the Commission’s Green Paper on Services of General Interest] (10 Sept. 2003), available at http://www.europa.eu.int.

[264] Green Paper on Services of General Interest, COM/2003/270 final, at 42-43.

[265] Id. at 13.

[266] See *Eurocities*, Eurocities’ Response to the European Commission’s Green Paper on Services of General Interest (15 Sept. 2003), available at http://www.europa.eu.int; *French Republic*,

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abolish existing sector-specific legislation, would mean that the Community acquires exclusive competence to regulate services of general economic interest. This could be problematic because the Commission would be confronted with considerable additional work load. Certainly in light of EU enlargement to twenty-five Member States and beyond, it seems more advantageous to continue with the adoption of sector-specific legislation, as a common framework will produce little or no significant added value.

F. Suggested Remedies

As the conclusions to previous chapters indicate, the current treatment of services of general economic interest under Community law creates legal uncertainty, obstructs the functioning of the internal market and damages the functioning of the market economy more generally. Furthermore, the conclusions drawn in Chapter E indicate that sector-specific legislation, the only remedy that has been implemented in practice until now to resolve shortcomings in the regulation of services of general economic interest, has significant regulatory drawbacks. It brings only moderate improvements because it gives considerable flexibility to Member States in the implementation of directives, Sector-specific legislation has also created considerable inconsistencies by addressing certain anti-competitive practices in one sector while, at the same time, ignoring similar practices in other sectors. Finally, as Chapter E indicates, the Commission's suggestion to develop a 'Common European Framework' for services of general economic interest is problematic, as it might not generate much added value and might even increase legal uncertainty.

In conclusion, and in spite of anticipated resistance from the Member States, the harmonization of sector-specific legislation should be fully deregulated by by deleting Article 86 (2) altogether from the EC Treaty. The rest of this chapter will provide an analysis of advantages and disadvantages of both proposals and will provide additional suggestions for the improvement of legislative framework for services of general economic interest.

I. Completing the Harmonization of Sector-specific Legislation

In order to decide whether the completion of sector-specific regulation is the best possible remedy, both its advantages and disadvantages should be identified. Continuing the adoption of sector-specific legislation has the following advantages:

- this type of regulation is supported by both Member States and undertak-

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Memorandum of the French Authorities: Answers to the Questionnaire in the Green Paper on Services of General Interest Presented by the European Commission (Sept. 2003), available at http://www.europa.eu.int.

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ings;[267]

- the most important sectors with cross-border effects are already regulated by secondary Community legislation, which has achieved rather positive but also incomplete and sometimes undesirable results; thus, it is particularly necessary to amend the existing legislation in order to increase competition in the internal market;
- through the implementation of directives into national legislation it is possible to adjust legislation for solving region-specific problems (this particularly refers to the availability of services of general economic interest in peripheral regions);
- it allows to take into account technical, industry-specific issues, when adopting legislation at the national level;
- it is possible to attack specific anti-competitive practices in individually reserved markets; and
- it provides more flexibility, as undertakings have time to adapt themselves to new market circumstances until the implementation deadline of a directive expires.

However, sector-specific regulation also has a number of disadvantages:

- the adoption process for directives is time-consuming and often leads to implementation problems;[268]
- it is not possible to achieve entirely fair competitive market conditions, as the internal market still remains to some extent 'regulated' because sectoral legislation is limited to the sectors and issues it addresses, but does not address the entire industry of services of general economic interest as a 'whole';
- as some Member States go beyond the requirements embodied in the directives, it creates different market conditions across the EU and perpetuates the partitioning of the internal market; ultimately, the European market integration is threatened; and
- poorly drafted directives as a result of the need to find a compromise that suits all or at least a large majority of Member States by allowing more flexibility at the Community level creates uncertainties, making violations of the directives more likely.

The above-mentioned disadvantages of sector-specific legislation can be eliminated or their negative effects can at least be minimized, if several

[267] For example, see French Republic, Memorandum of the French Authorities: Answers to the Questionnaire in the Green Paper on Services of General Interest Presented by the European Commission (Sept. 2003), available at http://www.europa.eu.int; Electricité de France, Comments on Green Paper on Services of General Interest (19 Sept. 2003), available at http://www.europa.eu.int.

[268] For details, see Chapter D, Section V.

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measures are taken: inconsistencies and other problems of secondary Community legislation distorting competition should be resolved and a new, effective institutional framework should be created to ensure effective implementation of sector-specific legislation. The rest of this sub-section will look at specific action that should be taken in order to resolve the problems of sector-specific legislation identified in Chapter E and beyond.

As stated in Chapter E, flexibility and poor drafting of directives has perpetuated the partitioning of the internal market. While past experience cannot be changed, there is a lesson for the future, namely that deadlines for the transposition of directives should be clearly set without allowing Member States to obtain exemptions considerably extending the time given for the implementation. The Commission seems to agree to this last point. In the recent regulatory framework for electronic communications a definite implementation deadline has been determined.[269] Furthermore, in order to avoid partial, incorrect or nonimplementation of the Community legislation, it would be preferable to adopt more regulations. Their direct applicability excludes the possibility that Member States adopt anti-competitive implementing legislation or that they do not implement the EU law into national legislation at all, both of which has hampered the effective functioning of the internal market. However, if Member States should turn out to be unwilling to accept legislation in the form of regulations, future directives should be drafted with more care as to the effects of their provisions. Furthermore, before even considering the adoption of additional legislation, the problems of current directives should be solved via amendments.

Required Amendments to Current Sector-Specific Legislation

The most important problem of current sector-specific legislation is inconsistency – different sectors address different anti-competitive actions, and a legal vacuum remains, as some anti-competitive practices seem to be addressed in one sector, but forgotten or differently regulated in another. Furthermore, in some cases sector-specific legislation fails to address the relevant issues. As identified in detail in Chapter E, this particularly refers to the procedure, by which network operators and suppliers of services of general economic interest are selected; the standard setting and the organisation of providers of services of general economic interest.

In order to increase supply-side competition, providers of services of general economic interest should always be selected on the basis of the tendering procedure. As stated in Chapter E, past experience with widespread use of the the authorisation procedure is negative, as this has allowed Member States to foreclose national markets. Tendering allows the selection of the provider of services of general economic interest based upon transparent, objective and economic (but not political) criteria. Another possibility would be to follow the approach taken in the electronic communications legislation, which has been the most successful so far, in establishing fair competitive conditions for economic

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[269] Directive 2002/22/EC, OJ 2002 L 108/51, art. 38.

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operators in this sector. This means that the tendering procedure could be substituted by a quasi 'authorisation procedure' whereby undertakings interested in providing services of general economic interest merely have to inform national authorities that they have established themselves as 'competitors' in the market. The actual provision of the services does not depend on an administrative act or some other form of permission.[270] This alternative could prove to be very effective, as there is no artificial regulation of the market meaning that fair competition can be established by the forces of supply and demand in an open market economy. Nevertheless, the selection procedure *per se* is not the gravest problem.

The most troublesome issue is that sector-specific legislation has failed to introduce entirely free access to networks[271] thereby hindering the establishment of effective supply-side competition. Therefore, the tendering procedure should be required also with regard to network access, which means that the permission to distribute network capacity based on the authorisation procedure should be deleted from the directives. Moreover, the requirements of licensing in the railway sector, as the procedure for selecting network operators and suppliers of services of general economic interest, should be further developed. It is not acceptable that the legislation foresees licensees for railway undertaking, but that these licences in themselves do not guarantee access to the network. This very possibility nullifies the purpose of the licensing procedure. Rather, an amendment should clarify that possession of a license entitles an undertaking to provide railway services.

Moreover, as the Commission has identified, as long as a single network operator may obtain exclusive rights for the provision of services of general economic interest, priority will continue to be given to the historical network operator in case of electricity, gas, postal and railway service sectors.[272] This has to be changed. The abolition of the authorisation procedure would help here as well, since it would permit the tendering of the network operator function. It seems crucial that the most efficient economic operator should be granted the rights to operate the network, rather than the 'politically preferred undertaking'.

Next, standard setting has to be done at the European and not any more at the national level. As stated in Chapter E with regard to potential providers of services of general economic interest, current sector-specific legislation refers to criteria such as 'technical, economic and financial capabilities of undertakings', 'good financial conditions', 'good reputation' and 'competency'. These are broad conditions permitting great subjectivity, which allows Member States to apply the conditions in a manner that is consistent with political and not economic conditions. Therefore, it would be desirable that the Commission

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[270] Directive 2002/20/EC, OJ 2002 L 108/21, art 3.

[271] See Chapter E, Section I on 'Free Access to Networks' to learn about main network access problems. Electricité de France is one of the undertakings, which considers that network access should be improved; see Electricité de France, Comments on Green Paper on Services of General Interest (19 Sept. 2003), available at http://www.europa.eu.int.

[272] Green Paper on Services of General Interest, COM/2003/270 final, at 43-44 (N.A.-no information available).

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adopts guidelines clarifying these concepts in order to avoid interpretation by Member States in favour of domestic industries. Without European standards it will be difficult to end the current partitioning of the internal market.

Another issue that has to be addressed via amendments is the vertical integration of undertakings. The current state of Community law requires account, management or legal unbundling, but not the separation of the network provider from the provider of services of general economic interest. Such a separation supposedly would constitute interference with property ownership, which is beyond the competence of the EU (as stated in Article 295 EC Treaty). However, as identified in Chapter D, mere legal separation, which is the highest form of unbundling besides ownership separation, does not lead to more competition in the internal market, as the respective undertakings tend to continue to cooperate (exclusively) with each other because they do not regard themselves as separate undertakings. Moreover, ownership unbundling would be preferable because mere legal, management or account separation from the state does not ensure that the provision of services of general economic interest is without political interference.[273] As it is unlikely that Member States will agree to delete Article 295 from the EC Treaty, the Commission should at least adopt a recommendation suggesting ownership unbundling due to its beneficial effects on competition in the internal market.

Financing of Public Service Obligations

Another problem that has to be resolved is the inconsistency created by the Court with regard to financing of public service obligations. There are three approaches to address the financing issue:

- to identify the entire compensation as state aid;
- to identify the financing as compensation for performing universal service obligations; or
- to determine whether or not such compensation constitutes state aid on a case-by-case basis.

The first option automatically implies that every financing scheme has to be notified to the Commission, whose analysis would then establish whether or not the aid is compatible with the internal market. This makes it possible to condemn illegal state aid (overcompensation) and to ensure fair competitive conditions in the EU. The second approach excludes the possibility of Commission interference, which leaves too much discretion to national authorities. This type of approach is not acceptable because it permits Member States to partition the internal market. The third approach is time-efficient because notifications are required only when the aid can influence suppliers in

[273] *C. Scott*, Services of General Interest in EC Law: Matching Values to Regulatory Technique in the Public and Privatised Sectors, 6/4 ELJ 310, 316 (2000); *OECD*, Recommendation of the Council Concerning Structural Separation in Regulated Industries (6 June 2003), available at http://www.oecd.org, at 3.

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other Member States. The negative side of this approach is legal uncertainty because the undertaking receiving compensation cannot be sure whether or not this financing influences economic operators in other Member States. Eventually this might lead to a situation, where all aid would have to be notified to the Commission in order to avoid repayments in the future. Thus, from a substantive point of view the first and the third approaches are nearly identical.

From these analysis and conclusions in Chapter D, it is clear that the entire compensation should be classified as state aid in order to ensure the highest possible level of competition in the EU. However, Member States might not agree to this approach, which is the complete opposite of the Court's current case law. If we should be stuck with the current rulings, which identify the entire state financing as legitimate compensation for the performance of universal service obligations, it would be necessary, at the very least, that the Court clarifies its judgment in *Altmark*[274] and that the Commission amends the 'Community Framework' adopted in 2004[275] to reduce current uncertainties. The following issues should be addressed in order to increase legal certainty, transparency and stability of investments in the internal market:

- either the Commission or the Court should specify the boundaries of public service obligations, excluding from these all services which have substitutes;
- the Commission should further develop the Community method for calculating costs for the performance of public service obligations (and the method should be based on market prices);
- the Commission should set clear conditions of accountability for national authorities to exclude hidden protection of domestic providers of services of general economic interest;
- the Court should overrule the part of its judgement, where it allows 'reasonable profit' as permitted compensation: this is illegal state aid because it functions as overcompensation; and
- either the Commission or the Court should explain the cost calculation method for cases, where the provider of services of general economic interest is not chosen in a public procurement procedure; costs of a 'typical, well-run undertaking' is a broad and unclear term allowing overly broad discretion on the part of Member States, which can easily lead to the partitioning of the internal market.

New Institutional Framework

A further problem that has to be solved is the dependence of providers of

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[274] Judgment of 24 July 2003 in *Case C-280/00, Altmark Trans GmbH and Regierungspräsidium Magdeburg v. Nahverkehrsgesellschaft Altmark GmbH, and Oberbundesanwalt beim Bundesverwaltungsgericht*, [2003] ECR I-7447.

[275] Community Framework for State Aid in the Form of Public Service Compensation (2004), *supra* note 175.

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services of general economic interest on national authorities, which leadd to the politicisation of these economic sectors. In this regard the Commission has suggested the development of a European regulator or the establishment of a network of national regulators.[276] Before assessing which institutional changes are better, it is necessary to restate that impartiality of the regulator should be achieved. As identified in Chapter E, the authorisation of national ministries to perform the duties of National Regulatory Authorities [hereinafter NRA] has invited inefficiency, corruption, irresponsiveness to changing market circumstances and excessive control of the market. This has damaged the functioning of the open market economy,[277] and cannot be accepted. Thus, it is clear that the institutional framework for the supervision of providers of services of general economic interest must be improved in a way that it is independent from public administration.

In addition to ministerial supervision, there are at present several Europe-wide associations dealing with individual sectors of services of general economic interest, e.g. CERP attempts to establish a common approach for addressing problems in postal regulation,[278] and CEER tries to improve cross-border trade of gas and electricity.[279] In addition, the Commission has set up Madrid and Florence Regulatory Processes consisting of national authorities, the Commission itself, suppliers, consumers and network operators etc., which have the aim to improve cross-border trade of gas and electricity, allocation of network capacity and tariff setting.[280] Without a doubt it is beneficial that all interested parties work together to improve competitive conditions in the internal market. In particular, the involvement of consumers in consultations with national authorities and undertakings providing respective services of general economic interest promotes a balance of interests of all parties involved. However, this type of a regulatory framework has more disadvantages than advantages. The main problem is that these bodies act only in an advisory capacity, meaning that specific distortions of competition cannot be directly addressed. Since the outcome of the negotiation process is non-binding, its consistent application in all Member States is doubtful. Moreover, the Madrid and Florence Regulatory Processes meet only twice a year, which does not allow them to address regulatory problems on a continuous basis.

In this context, it is noteworthy that there is already one sector-specific EU regulator, namely EASA, which is responsible for the certification of

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[276] Green Paper on Services of General Interest, COM/2003/270 final.
[277] *C. Scott*, Services of General Interest in EC Law: Matching Values to Regulatory Technique in the Public and Privatised Sectors, 6/4 ELJ 310, 318 (2000).
[278] See *European Committee for Postal Regulation*, Annual Report 2002, available at http://www.cept-cerp.org (accessed on March 9, 2004).
[279] See *Council of European Energy Regulators*, Annual Report 2003, available at http://www.ceer-eu.org (accessed on March 9, 2004).
[280] See *European Commission*, The Florence Regulatory Process, available at http://www.europa.eu.int (accessed on 9 March 2004); European Commission, The Madrid Regulatory Process, available at http://www.europa.eu.int (accessed on 9 March 2004).

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aeronautical products, licensing of air crews, setting of safety standards etc.[281] The question is whether the creation of this type of regulator would be beneficial for other sectors and whether a European regulator brings any enough added value to justify the effort.

For example, Electricité de France has identified that different aspects of various sectors have a Europe-wide dimension, e.g. access to networks, tariff setting and safety standards. A European regulator could address all these problems at the European level and reduce market partitioning caused by standards set at the national level. French authorities have also stated that a European regulator would bring a definite advantage – the consistent application of Community sector-specific legislation throughout the EU. However, the problem that a European regulator would face, is the implementation of these rules in a manner consistent with different market conditions across the EU.[282] Therefore, the new institutional framework should also take into account the interests of peripheral regions.

Furthermore, as the Commission is already overloaded with work, I do not agree with the proposal of Eurocities that, in addition to DG Competition and DG Internal Market, DGs such as Environment, Employment, and Health and Consumer Protection should also take part in the supervision of providers of services of general economic interest.[283] The latter have no direct interest in ensuring fair competition in the internal market, but concentrate on the supervision of specific, separate areas. In addition, if five DGs were to be involved in the supervisory process, this would undermine the effective application of sector-specific legislation because there would not be a sufficiently clear division of competences.

Therefore, the best option would be to create a combined regulatory model with one EU regulatory authority divided into departments related to sector-specific legislation (including one general department for other services of general interest). It also means that this regulator would absorb EASA at a later stage. In addition, special departments in the National Competition Authorities [hereinafter NCAs] should be created, which would deal with sector-specific issues at national level. This would mean that either existing NRAs are abolished or incorporated (when possible) into NCAs as separate departments. This would keep the institutional framework simple and ensure, via the effective application of competition rules, that the market is no longer partitioned alongside national boundaries through the effective application of competition rules. Furthermore, NCAs would be able to ensure that region-specific matters are not forgotten. This institutional framework would be especially effective if

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[281] For more information, see *European Aviation Safety Agency*, About Us, available at http://www.easa.eu.int (accessed on 9 March 2004).

[282] *Electricité de France*, Comments on Green Paper on Services of General Interest (19 Sept. 2003), available at http://www.europa.eu.int; *French Republic*, Memorandum of the French Authorities: Answers to the Questionnaire in the Green Paper on Services of General Interest Presented by the European Commission (Sept. 2003), available at http://www.europa.eu.int, at 3.

[283] *Eurocities*, Eurocities' Response to the European Commission's Green Paper on Services of General Interest (15 Sept. 2003), available at http://www.europa.eu.int, at 7.

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the EU regulator is established as a separate Commission DG (or as a department under DG Competition), as it would have larger enforcement powers than a mere EU agency.

Furthermore, to ensure that NCAs are consistently applying sector-specific legislation, the Commission should adopt guidelines based on the following principles:

- intervention by NCAs is allowed only, when competition is distorted;
- proper market analysis should be conducted meaning that they must be the same as under Articles 81 and 82 EC Treaty and the Merger Regulation; therefore, the product market definition should be based on demand and supply-side substitutability; the geographic market should cover the area with sufficiently homogeneous competition conditions, where goods or services are demanded and supplied; a dominant position must be established considering such aspects as market share, technological superiority, efficiency, vertical integration, potential competition etc.[284]

II. Deregulation Through the Removal of Article 86 (2) from the EC Treaty

With regard to the second suggested remedy – deregulation by deletion of Article 86 (2) from the EC Treaty – several advantages and disadvantages can again be identified. Advantages of this remedy would be the following:

- it is time-efficient, as it does not require the adoption of multiple sector-related legal acts;
- it achieves a higher level of competition in the internal market because the market would be exposed to entirely free competition; there would be a higher level of protection for economic operators and consumer interests would be better satisfied; and
- fair competitive conditions would achieve that the market is operating efficiently, prices are decreasing, there is a greater choice of products, and the quality of products is higher.

The disadvantages of this remedy are the following:

- this solution will most likely be rejected by Member States, as they do not want to give up further areas of competences;
- it would increase legal uncertainty because the EC Treaty contains contradictory articles. If this remedy was chosen in addition to deleting Article 86 (2) from the EC Treaty, contradictions between Articles 157 and 295 EC Treaty should also be resolved.

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[284] For more information, see *Korah*, *supra* note 120, at 35-140, 301-323.

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The problem with regard to Article 295 and Article 157 is that the former safeguards "the rules … governing the system of [national] property ownership," which means that Member States are free to impose public service obligations upon undertakings and to regulate them in a manner that ensures the security of supply. Article 157 on the contrary, stipulates a need for "open and competitive markets," which means that any type of interference into the functioning of the market is prohibited.[285] As a result, two entirely different directions for practical application of the rules are conceivable; (i) Article 157 would be invoked by competition-oriented Member States, which are going to avoid practices partitioning the internal market; but (ii) Article 295 would be invoked by more conservative Member States holding on to the opinion that an entirely open market cannot provide services of general economic interest on satisfactory terms;

- deletion of Article 86 (2) would also create uncertainties in the short-term with regard to the application of competition rules on services of general economic interest; national authorities in particular might misunderstand the new regulatory framework, and create further inconsistencies; this would require the adoption of Commission guidelines to ensure that competition law is correctly applied; these guidelines should also outline a clear separation between economic and non-economic services of general interest;
- further legal uncertainty would be created because of current inconsistencies in the Court's case law; thus, clarification of the financing of public service obligations and how the proportionality test is applied would be necessary despite the removal of Article 86 (2) from the EC Treaty; and
- as the deletion of Article 86 (2) from the EC Treaty would increase the Commission's work load, further changes in the institutional framework would also be required (for the proposed institutional framework, see previous sub-section).

The analysis of advantages and disadvantages of deleting Article 86 (2) from the EC Treaty shows that this remedy might lead to further inconsistencies and uncertainties. Furthermore, subsequent action in the form of further Treaty amendments and explanatory guidelines would nonetheless be required, which is time-consuming. Therefore, the continuation of sector-specific legislation would be more advantageous at least in the short-term, and once national authorities, undertakings and consumers have adapted themselves to the new market circumstances, and the problems of current legislative framework have been resolved, a further step could be taken by deleting Article 86 (2) from the EC Treaty.

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[285] EC Treaty, Arts. 157 and 295. See also *Craig*, *supra* note 231, at 1122-1123; *C.O. Lenz & K.-D. Borchardt*, EU- und EG-Vertrag 1571, 2003, p. 298.

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G. Conclusions

As I have stated, the current treatment of services of general economic interest under Community law obstructs the functioning of the internal market and damages the functioning of the market economy in general. Several arguments support my statement. First, the regulation of services of general economic interest is characterised by substantial legal uncertainty, whose practical implications are rather serious, as market uncertainty increases commercial risks for economic operators. Second, the current regulatory framework is not achieving such Community objectives as fair competition, market integration, efficient production and the satisfaction of customer needs to a satisfactory degree and hinders the completion of the internal market. Third, the Community Court and the national judiciary have produced inconsistencies and have excessively protected existing providers of services of general economic interest, which has led to considerable legal uncertainty and a certain loss of trust in the impartiality of the judiciary. Finally, the Community legislation has not been sufficiently adjusted to changing market circumstances. The focus of interest is no longer on the mere availability of services of general economic interest. Overall, there is little doubt that because of the politicisation of economic sectors, the main aims of the Community – market integration through the completion of the internal market and effective operation of free forces of supply and demand – have been forgotten.

Thus, as "it is impossible for any country to prosper today under the burden of an inefficient and expensive services structure,"[286] it is necessary that the Community takes a further step in the liberalisation process of services of general economic interest, and completes the adoption of sector-specific legislation. This approach has a number of advantages, for example it enjoys relatively strong support by Member States and undertakings. While the existing rules have had positive results, they are incomplete. Therefore, the shortcomings of existing sector-specific legislation should be addressed via further action on the part of the Community, in particular, effective amendment of current sector-specific legislation and the introduction of a new institutional framework extensively involving both the Commission and National Competition Authorities. At the very least, this would minimize negative effects of current exemptions of services of of general economic interest from the full application of competition law.

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[286] *WTO*, GATS: Facts and Fiction (29 Oct. 1999), available at http://www.wto.org.

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In conclusion, I dare to say that the future with regard to the treatment of services under Community law seems to be promising. As a result, the EU economy will grow and the Community will become yet more competitive in world markets.

> The ejection of the state from the market in pursuit of the integration imperative always runs the risk of throwing the baby out with the bathwater," but nevertheless, it is worth trying, as long-term 'profits' are larger that short-term losses.
>
> Malcolm Ross, Professor of Law at the University of Sussex[287]

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[287] *Ross*, *supra* note 24, at 35.