A. Introduction

The provision of Article 86(2) EC Treaty[1] allows, under certain conditions, a deviation from the rules of the EC Treaty insofar as the application of these rules would obstruct the operation of services of general economic interest which have been entrusted to certain undertakings by the state. Thus, Article 86(2) is designed to strike a balance between the objectives of the Community in respect of market integration and national public service objectives. Against this background, Buendia Sierra described the meaning of Article 86(2) in the following manner:

> This provision is thus the main point of contact between two 'tectonic plates' moving in opposite directions. Regular 'seismic movement' is for this reason to be expected around Article 86(2) EC and its interpretation.[2]

In fact, from the 1980s on, the importance of Article 86(2) for litigations has steadily increased. This is primarily due to the fact that since then more and more public tasks have been outsourced to private undertakings in the course of liberalisation. In this context, the main legal problem is the very open wording of Article 86(2) which gives a huge bandwidth of possible interpretations to the European courts. Unfortunately, many questions concerning the interpretation of the provision were answered

[1] All following Articles without reference to a certain source are those of the EC Treaty.

[2] J L Buendia Sierra, 'An Analysis of Article 86(2)' in: M S Rydelski (ed), *The EC State Aid Regime – Distortive Effects of State Aid on Competition and Trade*, (London: Cameron May, 2006), p 543.

by the European Court of Justice (ECJ) or the European Commission without the formulation of general principles. This led to the development of several legal decisions on a case-by-case basis. These decisions are often unrelated to one another, overlap and have not dealt with several foreseeable issues which, because of accidents of litigation or the prudence or tactics of plaintiffs, have not been raised so far.[3]

With respect to its general scope, Article 86(2) does not only apply to competition rules but to any rules contained in the EC Treaty. The exemption can, for example, be invoked by undertakings in relation to proceedings based on Articles 81 or 82.[4] Furthermore, despite some doubts in the past,[5] it is now undisputed that Article 86(2) can also apply to state actions that infringe a Treaty rule addressed to Member States[6] or Article 86(1) in combination with provisions addressed to Member States.[7] The controversial issue of whether and under which circumstances Article 86(2) is applicable in the context of state aid will be dealt with further below.[8]

This paper addresses a critical analysis of the scope of Article 86(2) and its role between the poles of adequate provision of public services and

[3] See J Temple Lang, *European Union Law Rules on State Measures Restricting Competition*, http://www.gclc.coleurop.be/documents/288536_2.pdf, p 1 (accessed 1 January 2009).

[4] See for example Case C-393/92 *Almelo* [1994] ECR I-1477, paras 33 et seqq; Case 41/83 *British Telecommunications* [1985] ECR 873, paras 28 et seqq.

[5] See Case 72/83 *Campus Oil* [1984] ECR 2727, para 19.

[6] For instance Articles 28, 31, 43 or 49.

[7] J L Buendia Sierra (2006), p 543.

[8] See paragraph C.

undistorted competition as set out by the case law of the European courts and legislation. In a first step, the several requirements of the provision are examined. In the course of this, particular attention is paid to the definition of the term ‘services of general economic interest’ as well as to the meaning of ‘obstruction to the performance of the service’. Then, Article 86(2) is shown in its special role in the financing of services of general economic interest.

B. The requirements for the applicability of Article 86(2)

For Article 86(2) to be applicable an undertaking (I.) must be entrusted with the operation of services of general economic interest (II.) or have the character of a revenue producing monopoly (III.). Moreover, the application of certain rules of the Treaty must obstruct the performance of the particular tasks assigned to the undertaking (IV.). Finally, the derogation of the respective Treaty rule must not affect the development of trade to such an extent as would be contrary to the interests of the Community (V.).

I. The concept of 'undertaking'

The term 'undertaking' is not defined in the Treaty but has been widely construed by case law. As a general definition, the ECJ held in *Höfner and Elser v Macrotron* that 'the concept of an undertaking encompasses every entity engaged in an economic activity, regardless of the legal status of the entity or the way in which it is financed.'[9]

In *Commission v Italy*, the ECJ provided a basic definition of 'economic activity' by describing it as 'an activity consisting in offering goods and services on a given market.'[10] Moreover, the activity must be, at least in principle, pursuable by a private undertaking in order to make profits.[11]

[9] Case C-41/90 [1991] ECR I-1979, para 21.

[10] Case C-35/96 [1998] ECR I-3851, para 36.

[11] Cases C-180-184/98 *Pavlov v Stichting Pensioenfonds Medische Specialisten* [2000] ECR I-6451, para 201.

However, it is not necessary that an actual profit was made[12] or that the entity was established for an economic purpose.[13]

The courts took a functional approach in order to define the notion of an undertaking, which means that the focus lies on the nature of the activity carried out by the entity in question. It is therefore 'a relative concept in the sense that a given entity might be regarded as an undertaking for one part of its activities while the rest fall outside the competition rules.'[14]

The concentration on the activities or functions of the entity also leads to the situation that its legal personality is irrelevant, with the consequence that natural persons, legal persons and administrative bodies of the state are potentially covered.[15]

However, the usual activities of employees,[16] trade unions[17] and agents[18] are principally excluded from the definition of 'undertaking'. Moreover, the courts have set up two categories of activities which cannot be

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[12] Case 96/82 *IAZ International Belgium SA v Commission* [1983] ECR 3369.

[13] Case 155/73 *Italy v Sacchi* [1974] ECR 409.

[14] Case C-475/99 *Ambulanz Glöckner v Landkreis Südwestpfalz* [2001] ECR I-8089, Opinion of AG Jacobs, para 72.

[15] Commission Decision No 90/456/EEC *Spanish Courier Services*, OJ 1990 L233/19; D G Goyder, *EC Competition Law* (Oxford: University Press, 4th edition, 2003), p 60.

[16] Case C-22/98 *Criminal Proceedings against Becu* [1999] ECR I-5665, para 26; Case C-67/96 *Albany International BV v Stichting Bedrijfspensioenfonds Textielindustrie* [1999] ECR I-5751, Opinion of AG Jacobs, para 217.

[17] *Albany* (ibid), para 227.

[18] D G Goyder (2003), p 63.

considered to be economic.[19] First, activities concerning the essential prerogatives of the state are excluded from the competition rules. This category includes traditional *ius imperii* activities, such as the conduct of the judiciary, diplomacy, the representation of the state and foreign relations[20] and a number of public control and regulatory functions of the state, for instance granting concessions for funeral services,[21] the maintenance and improvement of air navigation safety[22] and the performance of services relating to the protection of the environment.[23] Second, certain social protection systems have not been found to be encompassed as long as they were based on the principle of solidarity.[24]

[19] See G Monti, *EC Competition Law* (Cambridge: University Press, 2007), pp 486 et seqq.

[20] J Gonzales-Orus, 'Beyond the Scope of Article 90 of the EC Treaty: Activities Excluded From the EC Competition Rules' (1999) 5 EPL 387.

[21] Case 30/87 *Corinne Bodson v Pompes Funèbres des Régions Libérées SA* [1988] ECR 2497.

[22] Case C-364/92 *SAT Fluggesellschaft mbH v Eurocontrol* [1994] ECR I-43.

[23] Case C-343/95 *Diego Cali e Figli SrL v SEPG* [1997] ECR I-1547.

[24] Cases C-159-160/91 *Poucet et Pistre v Assurances Générales de France* [1993] ECR I-637; Case C-244/94 *Fédération Française des Sociétés d'Assurance and Others v Ministère de l'Agriculture et de la Pêche* [1995] ECR I-4013; Case C-218/00 *Cisal di Batistello v INAIL* [2002] ECR-691.

II. The entrustment of the operation of services of general economic interest

1. Services of general economic interest ('SGEI')

a. Definition

The term 'services of general economic interest' finds expression in the Articles 16 and 86(2) but is not expressly defined. What amounts to an SGEI is the subject of a considerable body of case law and legislation. As a starting point, it has to be emphasised that the word 'economic' does not relate to the word 'interest' but to the word 'service'.[25] This is also implied by the Commission which defined the notion as

> … market services which the Member States or the Community subject to specific public service obligations by virtue of a general interest criterion. This would tend to cover such things as transport networks, energy and communication.[26]

A similar description can be found in the White Paper with the exemption of using 'services of an economic nature' instead of 'market services'. Moreover, it clarifies that the term encompasses any economic activity subject to public service obligations.[27] Therefore, SGEI can be seen as

[25] A Jones/B Sufrin, *EC Competition Law* (Oxford: University Press, 3rd edition, 2007), p 621.

[26] Communication on Services of General Interest, OJ 2001 C17/4, Annex II.

[27] White Paper on Service on General Interest, COM (2004) 374 final, Annex 1.

services which belong to the market but which are also influenced by other, ie non-market, values.

The Commission's Green Paper points out that the existing sector specific Community legislation on SGEI 'contains a number of common elements that can be drawn on to define a useful Community concept of services of general economic interest. These elements include in particular: universal service, continuity, quality of service, affordability, as well as user and consumer protection.'[28]

The concept of 'services' in Article 86(2) has a broad meaning. In this respect, the Court, inter alia, decided that the administration of major waterways,[29] the operation of airlines,[30] the provision of electricity,[31] the provision of postal service,[32] mooring services in ports,[33] the treatment of waste,[34] the provision of emergency ambulance services[35] and the supply of telecommunication equipments[36] are encompassed by the notion. It

[28] Green Paper on Services of General Interest, COM (2003) 270 final, para 49.

[29] Case 10/71 *Ministère Public of Luxembourg v Muller* [1971] ECR 723.

[30] Case C-66/86 *Ahmed Saeed Flugreisen and Silver Line Reiseburo GmbH v Zentrale zur Bekämpfung Unlauteren Wettwerbs eV* [1989] ECR 803.

[31] Case C-157/94 *Commission of the European Communities v Kingdom of the Netherlands* [1997] ECR I-5699.

[32] Case C-320/91 *Corbeau* [1993] ECR I-2533.

[33] Case C-266/96 *Corsica Ferries France SA v Gruppo Antichi Ormeggiatori del Porto di Genoa* [1998] ECR I-3949.

[34] Case C-203/96 *Chemische Afvalstoffen Dusseldorp BV and Others* v *Minister van Volkshuisvesting, Ruimtelijke Ordening en Milieubeheer* [1998] ECR I-4075.

[35] *Ambulanz Glöckner* (see footnote 14).

[36] Case C-18/88 *RTT v GB-INNO-BM SA* [1991] ECR I-5973.

follows that not only the provision of services in the sense of Article 50 but also the provision of goods in terms of Article 23 is included.

The notion of 'economic' makes clear that the services concerned have to be of a market nature.[37]

The word 'general' shall ensure that the respective service serves the interests of society as a whole and is not limited to a special category of people.[38] Principally, SGEI should be mainly directed at private citizens although undertakings may also take advantage of them. It has been doubted whether services that are directly addressed only to undertakings can be considered to be SGEI.[39] Allowedly, it could be argued that such services are mainly in the interest of the respective undertakings and not in the general interest. However, as Buendia Sierra has set forth, it can sometimes be the best way to provide services or infrastructure to undertakings in order to create a benefit for the whole society indirectly.[40] This approach can also be found in a number of cases.[41] Moreover, the term 'general' cannot mean that every citizen or every geographic part must benefit from the service. Regional developments and actions favouring certain disadvantaged groups of people can be

[37] This issue was already explained in paragraph B.I. in the context of the notion 'undertaking'.

[38] J L Buendia Sierra, 'Article 86 - Exclusive Rights and Other Anti-Competitive State Measures' in: J Faull/A Nikpay (eds), *The EC Law of Competition* (Oxford: University Press, 2nd edition, 2007), para 6.142.

[39] Liyang Hou, 'Uncovering The Veil Of Article 86(2) EC', available at SSRN: http://ssrn.com/abstract=1025407, p 5 (accessed 1 January 2009).

[40] See J L Buendia Sierra (2006), p 551.

[41] For example *Ministère Public of Luxembourg v Muller* (footnote 29), para 11.

viewed as in the general interest. The essential point is that such actions are founded upon deliberations of general nature even though their concrete application may be addressed to certain groups.

b. Community law or national law concept?

An important issue concerning SGEI is the question whether it lies within the competence of the Community or the Member States to define what amounts to an SGEI. Formerly, the Court took the approach that SGEI is solely a Community concept.[42] However, it has been argued that the inclusion of Article 16 into the Treaty seems to alter this finding, since the provision could be interpreted as establishing shared and horizontal competences of the Community and Member States for the definition of this concept.[43] In contrast, some authors submit that Article 16 changes nothing of the case law by the Court.[44] Obviously, the biggest problem of a shared horizontal approach is that the powers of the Community and the Member States overlap where both pursue common interests with the provision of services. There is no specification in Article 16 in respect of the boundary of the Community's shared competence. Some guidance as to this issue was provided in the Commission's Green Paper on Services of General Interest which tries to concretise the respective powers of the Community and its Member States.[45] However, the following White Paper did not continue such an attempt but expected a reconstruction of

[42] Ibid, paras 14-15.

[43] See Liyang Hou, p 3.

[44] See M Ross, 'Article 16 EC and Services of General Interest: From Derogation to Obligation' (2000) 25 ELR 22.

[45] Cf footnote 28, paras 27 et seqq.

Article 16 in the European Constitution in order to give surveillance power on the operation of SGEI by Member States to the Community.[46]

In the author's view, a hierarchical surveillance model would be a better solution to the problem than a horizontal or shared approach. There are many cultural, economic and political differences among Member States, which makes it very difficult or even impracticable for the Community to establish a uniform system of SGEI appropriate for the whole Common Market. Thus, Member States need adequate discretion to perform what they traditionally view as SGEI. One good example for a wide discretion for Member States and, at the same time, a controlling function of the Community is the electronic telecommunications sector. The respective regulatory framework of 2002 allows Member States to include more universal service obligations at their will with the requirement to report these to the Commission for monitoring.[47] Another supportive argument for this solution is the fact that the concept of SGEI is a very dynamic one, capable of changing in time according to factors such as technological advances, the state of Community integration or variations in society's perception of the needs that have to be covered by the state. Hence, services which are categorised as in the general interest today can fall out of this category at a later date; on the other hand, new services can be added.[48] Member States can deal with this alteration more flexibly

[46] Cf footnote 27, p 6.

[47] Directive 2002/22/EC of the European Parliament and of the Council of March 7, 2002 on universal service and users' rights relating to electronic communications networks and services, OJ 2002 L108/51.

[48] *RTT* (footnote 36), para 16; see also Communication on Services of General Interest, OJ 1996 281/3, p 4, para 29.

than the Community could do it by finding a common solution for all members.

Nevertheless, it is apparent that the Member States' power to define what an SGEI is should not be absolute but subjected to control by the Community. A developed control already exists in certain sectors which are harmonised in respect of market access and competition, for example the electronic communications, energy, transport and postal sector. Community legislation in these areas has introduced limits on Member States' discretion to define what is meant by SGEI.[49] In addition, the ECJ already pointed out that Article 86(2) cannot be invoked when the public interest in question has been subject to Community harmonisation.[50] But even if a sector is not harmonised, the discretion of Member States is not unlimited, since it is widely accepted that the Community has the competence to prevent manifest errors.[51] So, the Community law concept of SGEI works as a maximum standard beyond which Member States cannot go. In this way, it shall be prevented that Member States abuse their freedom by artificially extending their definition of SGEI to give excessive protection to certain operators. This follows from the Court's judgments in *Port of Genoa*[52] and *BRT II*.[53]

[49] See J L Buendia Sierra (2006), p 549 with references to the sector-specific legislation.

[50] Case C-206/98 *Commission v Belgium* [2000] ECR I-3509, para 45.

[51] Case T-17/02 *Fred Olsen* [2005] ECR II-2031, para 216.

[52] Case C-179/90 [1991] ECR-I 5889, para 27.

[53] Case 127/73 [1974] ECR 318, para 23.