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Privatization and EC Competition Law

Mario Siragusa*

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Abstract

This Article will first review whether and how EC competition and state aid rules are applicable to privatizations, emphasizing issues peculiar to the privatization process. Other EC law principles that are relevant in the context of privatizations, such as freedom of establishment and investment, and public procurement rules will also be discussed.

PRIVATIZATION AND EC COMPETITION LAW

*Mario Siragusa**

CONTENTS

Introduction	1002
I. Competition Rules Applicable to Enterprises	1007
A. The Control of Concentrations: The Application of the Merger Regulation to Privatizations	1007
1. The EC Merger Regulation in a Nutshell	1007
2. Potential Impact of the Privatization Process on the Structure of Concentrations Involving Privatized Companies	1012
3. Different Forms of the Change in Control Brought About by Concentrations Involving Privatized Companies: In Particular, Concentrative Joint Ventures	1014
4. States' Public Power Prerogatives Do Not Confer a Decisive Influence over Privatized Enterprises.....	1020
5. Potential Impact of Statements Made by the Relevant National Privatization Authority on the Commission's Substantive Assessment of a Concentration	1021
6. Privatizations Carried Out Through the Public Flotation of a State-Owned Enterprise	1022
B. Application of Articles 85 and 86 of the EC Treaty to Acquisitions of Influence Short of Control.....	1027
1. Minority Shareholding Acquisitions Resulting in a Transfer of Control of the Acquired Company	1027
2. The Influence Threshold Triggering	

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	Application of Articles 85 and 86 of the EC Treaty Under the <i>Philip Morris</i> Judgment	1028
3.	The Expansion of the <i>Philip Morris</i> Influence Standard in the <i>Gillette</i> Commission Decision	1030
4.	Acquisition of Influence over an Enterprise To be Privatized by Way of a Minority Shareholding Acquisition or Other non-Joint Venture Arrangement: The Requirements for Application of Articles 85 and 86 of the EC Treaty	1034
C.	Special Issues Raised by the Privatization of Enterprises Holding a Dominant Position Prior to Privatization	1036
1.	Acquisition of Sole or Joint Control of a Monopoly to be Privatized: Substantive Assessment of the Transaction under the Merger Regulation	1037
2.	Acquisition of Limited Influence over an Enterprise to be Privatized: Substantive Assessment of the Transaction under the EC Treaty Rules	1044
a.	Article 85(1) of the EC Treaty	1045
b.	Article 86 of the EC Treaty	1048
3.	Creation of a True "Public Corporation" Through a Public Flotation of a Dominant Enterprise: Substantive Competitive Assessment	1050
4.	Liberalization of the Relevant Market as a First Step to Removing the Pre-existing Shield to the Dominant Position Held by a Publicly-Owned Enterprise to be Privatized . .	1051
5.	Does the Privatization of a Dominant Firm Without Concomitant Market Liberalization Infringe Articles 90 and 86 of the EC Treaty Within the Meaning of the <i>Corbeau</i> Judgment?	1053
6.	The Combined Impact of Privatization and Market Liberalization on Competition: Does the Privatization of a Dominant Firm "Create" a Dominant Position on a Newly-Created Market?	1058

D.	Application of Articles 85 and 86 of the EC Treaty to the Market Behavior of Undertakings Enjoying Exclusive or Special Rights After Privatization	1060
1.	Potential Recourse by Privatized Utilities to Unlawful Commercial Practices Directed at Reinforcing Their Market Power	1060
2.	Possible Issues for Review Under Article 85 of the EC Treaty	1061
3.	Possible Issues for Review Under Article 86 of the EC Treaty	1064
4.	Possible Issues for Review Under Article 5 <i>juncto</i> Articles 3(g) and 85 or 86 of the EC Treaty	1065
II.	Privatization and the European Union Rules Applicable to Public Undertakings	1068
A.	Liberalization and Privatization: Article 90, a Critical Overview	1068
B.	Article 90(1) of the EC Treaty	1070
C.	The Traditional Interpretation of Article 90(1) of the EC Treaty	1070
D.	The New Theory of Structural Abuse	1072
E.	The Public Service Defense	1074
F.	Article 90(3) of the EC Treaty: The Role of the Commission	1079
III.	Privatization and State Aid Rules	1081
A.	General Principles: An Overview	1081
B.	Reasons for Privatization of Public Undertakings	1083
C.	State Aid Rules: The Court and the Commission Approaches	1085
D.	State Aid to Public Undertakings	1089
E.	Constraints on Privatization Imposed by State Aid Rules	1093
F.	The Treuhand: The German Experience	1095
IV.	Freedom of Establishment, Investment, and Non-Discrimination	1098
A.	The Scope of the EC Rules and Their Impact on Privatization Programs	1098
B.	The United Kingdom Approach	1102
C.	The French Approach	1103
D.	The Italian Approach	1104

V. Public Procurement Issues	1105
A. The Scope of the EC Directives on Public Procurement	1105
B. The "General Directives" and the "Excluded Sectors Directive"	1106
C. The British Telecommunications Case	1108
Conclusion	1110

INTRODUCTION

The competition rules of the EC Treaty¹ ("Treaty") both protect competition as an economically desirable force and preserve individual economic freedom as one of the fundamental political freedoms guaranteed by a democracy.² These rules are based on the fundamental liberal belief that market forces should be the principal regulating factor in the economy and must be protected from improper interference: optimal economic efficiency is achieved when economic decision-making is left to businesses competing with one another in the marketplace, so that available resources are allocated to the most productive sectors and firms are stimulated to undertake risk, innovate, stimulate technical progress, and develop active market strategies.³

The Treaty competition rules also have a key role in ensuring that the establishment of a single market, through the opening of the Member States' national markets, completed in 1993, yields the expected economic and social benefits in terms of higher output, growth, and employment. These rules must ensure that existing regulatory barriers to trade are not replaced by market divisions, resulting from restrictive business practices or protectionist measures adopted by the Member States.

1. Treaty Establishing the European Community, art. 85, Feb. 7, 1992, [1992] 1 C.M.L.R. 573, 626 [hereinafter EC Treaty], *incorporating changes made by* Treaty on European Union, Feb. 7, 1992, O.J. C 224/1 (1992), [1992] 1 C.M.L.R. 719, 31 I.L.M. 247 [hereinafter TEU]. The TEU, *supra*, amended the Treaty Establishing the European Economic Community, Mar. 25, 1957, 298 U.N.T.S. 11, 1973 Gr. Brit. T.S. No. 1 (Cmd. 5179-II [hereinafter EEC Treaty], *as amended by* Single European Act, O.J. L 169/1 (1987), [1987] 2 C.M.L.R. 741 [hereinafter SEA], *in* TREATIES ESTABLISHING THE EUROPEAN COMMUNITIES (EC Off'l Pub. Off. 1987).

2. See LENNART RITTER ET AL., EEC COMPETITION LAW 9-10 (1991).

3. See COMMISSION OF THE EUROPEAN COMMUNITIES, EIGHTEENTH REPORT ON COMPETITION POLICY 1988 13-17, Introduction (1989); COMMISSION OF THE EUROPEAN COMMUNITIES, XXII^D REPORT ON COMPETITION POLICY 1992 13-16, Introduction (1993).

Therefore, companies must not be allowed to thwart market integration through the creation of cartels for the purposes of splitting markets, blocking exports or imports, by abusing existing local or Community-wide dominant positions,⁴ or by blocking new entrants or creating new dominant positions through anticompetitive mergers.⁵ Moreover, although it is true that the EC Treaty competition rules concern only the behavior of undertakings and do not apply to legal or regulatory measures adopted by Member States, these provisions, if read in combination with Article 5 of the EC Treaty,⁶ impose an obligation upon Member States to abstain from adopting or maintaining in force measures, including those of a legislative nature, that could render ineffective the EC Treaty competition rules.⁷ This may be the case, for example, where a Member State imposes or facilitates the conclusion of agreements contrary to Article 85,⁸ reinforces the effects of such agreements, or deprives its own legislation of its official character by delegating the responsibility for taking decisions affecting the economic sphere to private traders.⁹ It may also occur where a Member State extends an exclusive right granted to a monopolist to cover an ancillary activity, without objective justification,¹⁰ or structures such an exclusive right in a way that inevitably leads the monopolist to commit an abuse of that right contrary to Article 86 of the EC Treaty.¹¹

4. See EC Treaty, *supra* note 1, art. 86, [1992] 1 C.M.L.R. at 627-28.

5. See Council Regulation No. 4064/89, O.J. L 395/1 (1989) (setting forth control of concentrations between undertakings), *amended by* O.J. L 257/13 (1990) [hereinafter Merger Regulation].

6. EC Treaty, *supra* note 1, art. 5, [1992] 1 C.M.L.R. at 591.

7. GB-INNO v. ATAB, Case 13/77, [1977] E.C.R. 2115.

8. EC Treaty, *supra* note 1, art. 85, [1992] 1 C.M.L.R. at 626.

9. See Meng, Case C-2/91 (Eur. Ct. J. Nov. 17, 1993) (not yet reported); Bundesanstalt für den Güterfernverkehr v. Gebrüder Reiff, Case C-185/91 (Eur. Ct. J. Nov. 17, 1993) (not yet reported) [hereinafter Reiff]; Ohra Schadeverzekeringen, Case C-245/91 (Eur. Ct. J. Nov. 17, 1993) (not yet reported) [hereinafter Ohra]. See also Germany v. Delta Schifffahrts- und Speditionsgesellschaft, Case C-153/93, [1994] E.C.R. I-2517.

10. RTT v. GB-INNO, Case C-18/88, [1991] E.C.R. I-5941 (holding that state measure extending, without any objective justification, exclusive right granted to undertaking for establishment and running of public telecommunications network to adjacent but separate market for importation, marketing, bringing into service, and maintenance of equipment violate Articles 90(1) and 86 of Treaty).

11. See, e.g., Höfner v. Macrotron, Case C-41/90, [1991] E.C.R. I-1979 (stating that grant by German state to Federal Employment Office of exclusive right to provide recruitment services could result in violation of Articles 86 and 90(1) if mere exercise of right would oblige monopolist to abuse its dominant position, for example, where it

In addition, Member States must not be allowed to replace protectionism, abolished in the market integration process, with state aid.¹² The use of public funds by a Member State to give a national industry a competitive advantage over industry elsewhere in the European Union¹³ or to prop up inefficient businesses at the expense of those that are more successful, is as likely to distort competition in the EU market as the anticompetitive behavior of companies. It discourages the entry of new firms and prevents efficient players from increasing their market share through internal growth.¹⁴

Moreover, although Article 222¹⁵ of the EC Treaty leaves Member States free to adopt their own system of property ownership, which may include state-owned enterprises,¹⁶ they must refrain from acting in a manner contrary to the EC Treaty when they engage in commercial activity or influence the conduct of business enterprises.¹⁷ Pursuant to Article 90(1) of the EC Treaty, Member States may neither enact nor maintain in force, in relation to public enterprises and enterprises to which they grant special or exclusive rights, any measure contrary to the rules of the EC Treaty, including the principle of non-discrimination on grounds of nationality,¹⁸ and the rules on competition and subsidies.¹⁹ As a result, EC competition rules can also be used to open sectors, such as the markets for energy, telecom-

would be manifestly unable to satisfy market demand for placement services for business executives).

12. See EC Treaty, *supra* note 1, arts. 92-94, [1992] 1 C.M.L.R. at 631-32.

13. As of November 1, 1993, following the entry into force of the TEU, *supra* note 1, which substantially amended the EEC Treaty, *supra* note 1, the European Economic Community is referred to as the European Union. Deletion of the word "economic" reflects the broadening ambit of the Union from the purely economic objective of promoting the integration of the twelve (now fifteen) Member States' national markets into a unified "common market," which includes matters of social and monetary policy, education, international relations, defense and environmental concerns.

14. See EC Treaty, *supra* note 1, arts. 92(2), (3), [1992] 1 C.M.L.R. at 630-31. The EC Treaty does not declare the granting of aid per se incompatible with the common market, but provides for a number of exceptions either automatic or available at the discretion of the European Commission ("Commission"). *Id.*

15. *Id.* art. 222, [1992] 1 C.M.L.R. at 711.

16. *Id.* "This Treaty shall in no way prejudice the rules in Member States governing the system of property ownership." *Id.*

17. See *Italy v. Commission*, Case 41/83, [1985] E.C.R. 873, ¶¶ 21-23 [hereinafter *British Telecommunications*].

18. EC Treaty, *supra* note 1, art. 6, [1992] 1 C.M.L.R. at 591.

19. *Id.* arts. 85-94, [1992] 1 C.M.L.R. at 626-32.

munications, and postal services, that remain closed despite the establishment of the internal market, because Member States have entrusted management of those sectors to undertakings to which they have granted special or exclusive rights.²⁰

It may be interesting to note that, subject to the exception under Article 90(2) of the EC Treaty,²¹ the commercial activities

20. See *id.* art. 90(3), [1992] 1 C.M.L.R. at 629. Under Article 90(3), the Commission is to ensure the application of Article 90 and, where necessary, to address appropriate directives and individual decisions to Member States imposing upon them an obligation to abolish certain special or exclusive rights which conflict with the objectives of the internal market. In recent years, the Commission has more frequently used Article 90(3) of the Treaty as an instrument for attacking various state or private monopolies, in particular those that are fragmented along national lines or otherwise uncompetitive in the sectors of insurance, maritime transport, postal services, port services, airport services, and telecommunications. See Commission Decision 85/276/EEC, O.J. L 152/25 (1985) (Greek Insurance); Commission Decision No. 87/359/EEC, O.J. L 194/28 (1987) (maritime transport); Commission Decision No. 90/16/EEC, O.J. L 10/47 (1990) (Dutch express delivery services); Commission Decision No. 90/456/EEC, O.J. L 233/19 (1990) (Spanish international express courier services); Commission Decision No. 94/119/EC, O.J. L 55/52 (1994) (port services); Commission Decision No. 95/364/EC, O.J. L 216/8 (1995) (landing fees at Brussels National Airport); Commission Directive No. 88/301/EEC, O.J. L 131/73 (1988) (on competition in markets in telecommunications terminal equipment); Commission Directive No. 90/388/EEC, O.J. L 192/10 (1990) (on competition in the markets for telecommunications services); Commission Directive No. 94/46/EC, O.J. L 268/15 (1984) (amending directives 881301 and 901388 with regard to satellite communications). The distribution of gas and electricity, air transport and financial services are other areas in which the Commission indicated its intention to introduce greater competition by tackling existing monopolies. COMMISSION OF THE EUROPEAN COMMUNITIES, XXIVTH REPORT ON COMPETITION POLICY 1994, at 19, ¶ 6 (1994); COMMISSION OF THE EUROPEAN COMMUNITIES, XX-IIIIRD REPORT ON COMPETITION POLICY 1993, at 30-34, ¶¶ 36-42 (1994); COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIND REPORT ON COMPETITION POLICY 1992, at 29-31, ¶¶ 21-27 (1993). The Commission's powers to use Article 90 of the Treaty to prevent national governments from restricting competition by conferring monopoly or other special rights when it is not justified on genuine public-interest grounds of a non-economic nature were upheld by the Court of Justice in two judgments involving the Article 90(3), *France v. Commission*, and *Spain, Belgium and Italy v. Commission*. *France v. Commission*, Case C-202/88, [1991] E.C.R. I-223; *Spain, Belgium & Italy, Joined Cases C-271, 281, 289/90*, [1992] E.C.R. I-5833. And, in a ruling concerning an Article 90(3) individual decision that the Commission addressed to the Netherlands in order to impose the liberalization of the provision of express delivery services. *The Netherlands, Koninklijke PTT Nederland & PTT Bost v. Commission, Joined Cases C-48/90 and 66/90*, [1992] E.C.R. I-565.

21. EC Treaty, *supra* note 1, art. 90(2), [1992] 1 C.M.L.R. at 629. Article 90(2) provides that undertakings entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly are only subject to the Treaty competition rules insofar as their application does not obstruct the performance of the particular tasks assigned to them and where the development of trade is not affected to an extent contrary to the interests of the European Union. See *Corbeau*, Case C-320/91, [1995] 4 C.M.L.R. 621.

of public enterprises and firms granted special or exclusive rights are treated much like the commercial activities of private enterprises. Indeed, like Article 222,²² Article 90 is neutral as to the ownership of business enterprises²³ and makes only a functional distinction in favor of undertakings, public or private, that are required in the general economic interest to perform specific tasks on behalf of all consumers.²⁴ Although the privatization of utilities may increase the number of privately owned firms that enjoy special or exclusive rights, such firms will remain within the scope of Article 90.²⁵

At first sight, the process of privatization, that is, the transfer of the ownership of an enterprise from public to private hands, appears to raise no particular issues in relation to the competition rules of the EC Treaty. Ostensibly, privatizations should be treated no differently than the transfer of businesses between private parties.

There are cases, however, when privatization should be treated differently. The following analysis of the impact of competition rules on the privatization process starts from the intuitively appealing assertion, which has now become commonplace, that the privatization of enterprises enjoying special or exclusive rights must be accompanied by market liberalization measures to prevent private monopolies from replacing pre-existing public ones.²⁶ Indeed, the apparent neutrality towards public and privileged enterprises of the Treaty of Rome²⁷ establishing the Euro-

22. EC Treaty, *supra* note 1, art. 222, [1992] 1 C.M.L.R. at 711.

23. *See Sacchi*, Case C-155/73, [1974] E.C.R. 409, ¶ 14. As established by the Court of Justice ("Court"), nothing in the Treaty prevents Member States from removing certain activities from the field of competition by conferring on one or more establishments an exclusive right to carry them out, for considerations of a non-economic nature relating to the public interest. *Sacchi*, [1974] E.C.R. 409, ¶ 14. Moreover, the Treaty does not prohibit the creation of all state monopolies, since Article 37(1) only prohibits those "of a commercial character" (i.e., state monopolies having as their object transactions regarding a commercial product capable of being the subject of intra-Community competition and trade, and playing an effective part in such trade) and only insofar as they tend to introduce exclusive rights to import and export goods (not services) and thereby to discriminate against nationals of other Member States. *Costa v. ENEL*, Case 6/64, [1964] E.C.R. 585, 598.

24. *See DEWOST ET AL.*, 15 *LE DROIT DE LA COMMUNAUTÉ ÉCONOMIQUE EUROPÉENNE* 423 (1987).

25. Leigh Hancher & Piet Jan Slot, *Article 90*, 11 *EUR. COMPETITION L. REV.* 35, 36 (1990).

26. *See, e.g.*, PIERRE GUISLAIN, *LES PRIVATISATIONS* 71 (1995).

27. EEC Treaty, *supra* note 1, 298 U.N.T.S. 11, 1973 Gr. Brit. T.S. No. 1.

pean Economic Community seems to have been replaced in the Maastricht Treaty on European Union by a policy that clearly favors free markets over state planning.²⁸ The aim of this Article is to establish a firm legal basis for this concept, derived from the Commission's practice and the case law of the Court of Justice.

This Article will first review whether and how EC competition and state aid rules are applicable to privatizations, emphasizing issues peculiar to the privatization process. Other EC law principles that are relevant in the context of privatizations, such as freedom of establishment and investment, and public procurement rules will also be discussed.

I. COMPETITION RULES APPLICABLE TO ENTERPRISES

A. *The Control of Concentrations: The Application of The Merger Regulation to Privatizations*

1. The EC Merger Regulation in a Nutshell

EC antitrust law concerning merger control was, until recently, based on the concept of "structural" abuses of a dominant position under Article 86 of the EC Treaty.²⁹ The law was changed by the long-awaited Council Regulation 4064/89³⁰

28. TEU, *supra* note 1, O.J. C 224/1 (1992), [1992] 1 C.M.L.R. 719. Under Article 3(a) of the Treaty on European Union, "the activities of the Member States and the Community shall include . . . the adoption of an economic policy . . . conducted in accordance with the principles of an open market economy with free competition." *Id.* art. 3(a), O.J. C 224/1, at 8 (1992), [1992] 1 C.M.L.R. at 589. See generally Anthony Gardner, *The Velvet Revolution: Article 90 and the Triumph of the Free Market in Europe's Regulated Sectors*, 16 EUR. COMPETITION L. REV. 78 (1995).

29. *Europemballage Corporation and Continental Can Company Inc. v. Commission*, Case 6/72, [1973] E.C.R. 215, 244-45 ("Abuse may . . . occur if an undertaking in a dominant position strengthens such position in such a way that the degree of dominance reached substantially fetters competition, i.e., that only undertakings remain in the market whose behavior depends on the dominant one."). As first established by the *Continental Can* Court, mergers strengthening an existing dominant position held by one of the merging firms may amount to an "abuse" in violation of Article 86 of the Treaty. *Europemballage Corporation and Continental Can Company*, [1973] E.C.R. at 244-45. This case is solely of historical interest since Article 86 of the Treaty is no longer applicable to concentrations except by national courts, and only in case of transactions which do not create but *strengthen* a dominant position through concentration.

30. Merger Regulation, *supra* note 5, O.J. L 395/1 (1989). Firms are referred to as "undertakings" in EC law parlance. On the other hand, the Regulation uses the wider term of "concentrations" instead of mergers because it also applies to operations, such as concentrative joint ventures, which are not "mergers" in the strict sense. The Regulation has been supplemented. See Commission Regulation No. 3384/94, O.J. L 377/1 (1994) (notifications, time-limits, and hearings); Commission Guidelines, O.J. C 203/5

("Merger Regulation" or "Regulation") on the control of concentrations between undertakings, which came into force on September 21, 1990. The Merger Regulation established a "one-stop-shop" review procedure for all mergers having a "Community dimension."³¹

The concept of "concentration" in the Merger Regulation is based on a principle of "change in control."³² According to Recital 23 of the Merger Regulation,³³ the concept of "concentration" covers only operations that bring about a lasting change in the structure of the enterprises concerned. Such a structural change, under Article 3(1),³⁴ is brought about by either a merger between two previously independent undertakings or the acquisition of control over the whole or part of another business.

Under Article 3(5) of the Merger Regulation,³⁵ acquisitions of securities made by credit, other financial institutions, or insur-

(1990) (concerning ancillary restrictions in connection with notified concentrations); Commission Notice, O.J. C 385/1 (1994) (distinction between concentrative and cooperative joint ventures); Commission Notice, O.J. C 385/5 (1994) (articulating notion of concentration); Commission Notice, O.J. C 385/12 (1994) (notion of undertakings concerned); Commission Notice, O.J. C 385/21 (1994) (calculation of turnover). The notification form, known as Form CO, was published as an annex. Commission Regulation No. 3384/94, O.J. L 377/9, annex (1994).

31. Merger Regulation, *supra* note 5, arts. 9, 21, O.J. L 395/1 at 7, 11 (1989). In order to avoid overlapping review of mergers by the Commission and the enforcement agencies of the Member States, the Regulation gives the former exclusive jurisdiction over mergers having a "Community dimension" (with the possibility, however, for the Commission to refer the merger to national agencies in certain cases). *Id.* A merger, including a combination involving non-Community firms, has a Community dimension where the merging companies have combined worldwide sales in excess of 5 billion European Currency Units ("ECU") (equaling approximately US\$5850 million at the average 1994 exchange rate of 1.16982), at least two of the firms have a minimum of ECU250 million sales each within the European Union, and no more than two-thirds of each firm's sales in the European Union come from within one and the same Member State. *Id.* art. 1(2), O.J. L 395/1, at 3 (1989). Mergers above these turnover thresholds must be notified to the Commission in advance of their implementation and may not be consummated for three weeks after notification or until the Commission so decides. The time limits for Commission action are one month from notification for straightforward cases and five months for mergers which "raise[] serious doubts as to [their] compatibility with the common market" and thus require the opening of in-depth second-phase proceedings. *Id.* arts. 4-7, O.J. L 395/1, at 4-6 (1989).

32. See generally II BARRY E. HAWK, COMMON MARKET AND INTERNATIONAL ANTI-TRUST: A COMPARATIVE GUIDE 915 (2d ed. 1985 & Supp. 1992).

33. Merger Regulation, *supra* note 5, recital 23, O.J. L 395/1 (1989).

34. *Id.* art. 3(1), O.J. L 395/1, at 4 (1989).

35. *Id.* art. 3(5), O.J. L 395/1, at 4 (1989).

ance companies, whose activities include transactions for their own account or for the account of third parties, do not constitute "concentrations" if the securities are acquired for resale and are held only on a temporary basis. In this context, temporary basis means one year from the date of the acquisition, subject to extension where the acquired company can show that disposal of the acquired securities would not be reasonably possible within that period, and the acquiring company abstains from exercising the pertaining voting rights, or exercises them only with a view to preparing the disposal of the securities acquired and not in order to influence the competitive behavior of the undertaking involved.³⁶

Control is defined in Article 3(3)-(4) of the Merger Regulation as the ability to exercise a decisive influence on another undertaking through rights, contracts, or any other means, and may be acquired by one or more undertakings or persons, including public bodies,³⁷ acting alone or jointly.³⁸ A concentra-

36. *Id.* The acquisition by an investment bank, therefore, acting as global coordinator or underwriter in the context of the privatization of a state-owned enterprise, of a controlling interest in that enterprise for re-sale to institutional or retail investors does not normally involve a change in control and does not amount to a concentration. *Id.* On the other hand, the exception set forth in Article 3(5)(a) of the Merger Regulation does not normally apply to acquisitions of controlling interests by investment banks (e.g., in the context of rescue operations or buy-outs) in which, although the primary intention of the banks involved is a restructuring of the financing of the acquired company for its subsequent resale, the restructuring program requires the controlling banks to determine the company's strategic commercial behavior and makes it unrealistic to transfer a rescued company into a commercially viable entity and resell it within one year. *See, e.g.*, Commission Decision, O.J. C 223/38, ¶¶ 5-6 (1991) (Kelt/American Express) (finding concentrative joint venture in new entity formed by eight banks because strategic decisions on development of new entity would require unanimity). *See also* Commission Decision O.J. C 67/11, ¶¶ 6-7 (1994) (CWB/Goldman Sachs/Tarkett) (clearing management buy-out where joint control acquirers of newly-formed holding company would have certain rights conferred on them over acquired companies); Commission Decision, O.J. C 258/10, ¶¶ 5-9 (1992) (CCIE/GTE) (authorizing buy-out of IL by Edil, special purpose company set up and controlled by CCIE, which is wholly-owned subsidiary of Citicorp, where purchase constituted concentration since CCIE would continue to control Edil after completion of proposed transaction). In *Mediobanca/Generali*, the Commission apparently concluded that, under the surrounding circumstances, the Article 3(5)(a) exception was not applicable to Mediobanca's participation in the underwriting of an issue of new shares by Assicurazioni Generali, the largest Italian insurance company. *Mediobanca/Generali*, Case IV/M156, [1994] 4 C.M.L.R. M1, M3, ¶ 8.

37. *See, e.g.*, Commission Decision No. 94/449/EC, O.J. L 186/38 (1993), (*Kali+Salz/MdK/Treuhand*). "Persons" also include states. *Air France/Sabena*, Case IV/M517, [1994] 5 C.M.L.R. M1, ¶ 11.

38. *Air France v. Commission*, Case T-2/93, [1994] E.C.R. II-323, ¶¶ 62-65. In *Air*

tion may also occur where a transaction leads to a change in the structure of control, such as a change from joint to sole control or an increase in the number of shareholders exercising joint control.³⁹ Even the creation of a joint venture is a "concentration," pursuant to Article 3(2) of the Merger Regulation, if the new entity "perform[s] on a lasting basis all the functions of an autonomous economic entity, which does not give rise to coordination of the competitive behavior of the parties amongst themselves or between them and the joint venture."⁴⁰

In the Commission's assessment of mergers notified to it, the Merger Regulation is intended to determine whether the proposed combination is likely to increase the risk of the unilateral exercise of market power or the risk of coordinated interaction between players in the relevant market, i.e., the risk of the collective exercise of market power.⁴¹ Pursuant to Article 2(3)

France, the Court of First Instance ruled that where the holdings of shares in a controlled undertaking and the conferment of powers laid down by its statutes are such that major decisions can only be taken by mutual consent by the two undertakings involved in a concentration, the combined entity is jointly controlled in spite of the fact that one of them exercises a substantial influence over it. *Id.*

39. Commission Notice, O.J. C 385/1, at 1-2. *E.g.*, O.J. C 38/12 (1993) (Volkswagen AG/VAG UK); Commission Decision, O.J. C 165/26 (1992) (Solvay/Laporte/Interox) (finding that transaction, in which Solvay and Laporte would break-up and divide assets of jointly controlled Interlox group, gave rise to two separate concentrations through which both parties would acquire sole, as opposed to joint, control over two separate activities and sets of products); Commission Decision, O.J. C 204/12 (1991) (Eridania/ISI) (holding that new shareholder agreement, that came about because Eridania increased its shareholding enough to give it sole, instead of joint control, was not sufficient to confer on Finbieticola decisive influence over ISI); Commission Decision, O.J. C 163/9 (1995) (Nokia Corporation/SP Tyres) (finding that obligation of second largest shareholder fell short of indication of joint control, making Merger Regulation inapplicable).

40. Merger Regulation, *supra* note 5, art. 3(2), O.J. L 395/1, at 4 (1989).

41. Merger Regulation, *supra* note 5, O.J. L 395/1 (1989). Although the Merger Regulation appears to focus overwhelmingly on the former risk, the Commission has already accepted the concept of collective dominance. Commission Decision No. 92/553/EEC, O.J. L 356/1 (1992) (Nestlé/Perrier) (determining that oligopolistic dominance may result in restriction of competition, in particular, where relevant market is already performing anti-competitively prior to proposed merger and leading companies therein face no sufficient price-restraining actual or potential competition). *See, e.g.*, Kali+Salz/MdK/Treuhand, O.J. L 186/38, at 46-49, ¶¶ 51-68, 96 (1993) (finding that, absent agreement of parties to give several undertakings, acquisition would lead to duopoly because no effective competition would remain due to structural features of market, fragmentary nature of competition, and longstanding links between two companies). *See generally* HAWK, *supra* note 32, at 964.3; Derek Ridyard, *Economic Analysis of Single Firm and Oligopolistic Dominance Under the European Merger Control*, 15 EUR. COMPETITION L. REV. 255 (1994).

of the Merger Regulation,⁴² where the Commission finds that a concentration "creates or strengthens a dominant position as a result of which effective competition would be significantly impeded in the common market or in a substantial part of it," the Commission must declare the transaction "incompatible with the common market" and prohibit its consummation. Commission decisions under the Regulation have, thus far, endorsed the Court's established definition of dominance⁴³ as the Commission refers to the combined entity's power "to gain an appreciable influence on the determination of prices without losing market shares."⁴⁴

The privatization of an enterprise, by definition, implies one or more successive changes of control over it. Transition from public to private ownership of the business to be privatized often takes place in stages, with the national government or local entities selling significant minority stakes prior to transferring control to, or sharing control with, private investors.⁴⁵ A change in the control or in the structure of control of a public enterprise triggers the application of the Merger Regulation or, where the transaction does not fall within the Regulation's scope for lack of Community dimension, the national merger control rules

42. Merger Regulation, *supra* note 5, art. 2(3), O.J. L 395/1, at 3-4 (1989).

43. *See, e.g.*, *Nederlandse Bandenindustrie Michelin v. Commission*, Case 322/81, [1983] E.C.R. 3461, 3511. A dominant position relates to a position of economic strength enjoyed by an undertaking that enables it to prevent maintenance of effective competition on the relevant market by giving it the power to behave, to an appreciable extent, independently of its competitors, customers, and ultimately of consumers. *Michelin*, [1983] E.C.R. at 3511.

44. *See, e.g.*, *Re The Concentration Between Renault and Volvo*, Case IV/M4, [1991] 4 C.M.L.R. 297, 302-03, ¶ 14. *See also* Commission Decision, O.J. L 211/1, ¶ 105 (1995) (*Mercedes-Benz/Kassbohrer*); Commission Decision, O.J. L 354/32, ¶ 183 (1994) (*Procter & Gamble/VP Schickedenz (II)*); Commission Decision, O.J. C 68/5, ¶ 10 (1993) (*British Airways/Dan Air*); Commission Decision, O.J. L 334/1, ¶ 72 (1991) (*Aérospatiale-Alenia/de Havilland*) (referring to combined entity's "freedom of maneuver that escapes adequate competitive control" or power "to act independently of its customers and competitors"). *See also* COMMISSION OF THE EUROPEAN COMMUNITIES, XX-1ST REPORT ON COMPETITION POLICY 1991, at 85-86, ¶ 110 (1992) (stating that analysis of mergers is based on definition of dominant position under traditional case law of Article 86 of Treaty).

45. Merger Regulation, *supra* note 5, O.J. L 395/1 (1989); EC Treaty, *supra* note 1, arts. 85, 86, [1992] 1 C.M.L.R. at 626-28. If the new private investors do not acquire decisive influence over the public undertaking individually or jointly (e.g., through a shareholders' agreement among themselves, or with the state), the transaction does not fall under the Merger Regulation but may be scrutinized under Articles 85 and 86 of the Treaty. *Id.*

of the relevant jurisdictions.⁴⁶

2. Potential Impact of the Privatization Process on the Structure of Concentrations Involving Privatized Companies

A review of the decisions adopted by the Commission pursuant to the Merger Regulation shows that the very structure of concentrations undertaken in the context of privatizations is often affected by the relevant national legislative framework, or by the vendor national government's need or desire to ensure a smooth transition from public to private ownership.

For example, in order to acquire Cokoladovny, a company manufacturing and marketing biscuits and chocolate sweets privatized by the Government of the Czech Republic, the agri-food groups BSN and Nestlé established a Dutch holding company in which they each owned 50%.⁴⁷ The holding company, in turn, acquired a 43% stockholding in Cokoladovny. Following a capital increase reserved to shareholders, this percentage would grow to 50.41%, with the rest of the capital divided among the European Bank for Reconstruction and Development, the Investicni Banka, the firm's employees, and the National Property Funds of the Czech Republic. This contractual structure was dictated by the Czech Government's decision that the privatized business could not be dismembered. Since Nestlé specialized in chocolate and BSN in biscuits, with neither having expertise in the other's sector, only a common project could enable them to pursue the economic policy objectives of privatization.⁴⁸ Interestingly, although the agreement relating to the structure of the ownership of Cokoladovny could be terminated after seven years, when the commitments entered into by BSN and Nestlé vis-à-vis the Czech Government would come to an end leaving

46. The latter situation may test the independence of the relevant national anti-trust authority from the national government in the assessment of a concentration involving the outright or partial privatization of a company owned by the same state.

47. BSN-Nestlé/Cokoladovny, Case IV/M90, [1992] 4 C.M.L.R. 441.

48. BSN-Nestlé/Cokoladovny, [1992] 4 C.M.L.R. at 441. The Commission eventually found that the transaction amounted to a cooperative joint venture, to be scrutinized pursuant to Article 85 of the EC Treaty, because of a risk of coordination between Cokoladovny and its parent companies. The Commission, however, expressly ruled out any risk of coordination between the parents. *Id.* It is submitted that if the Commission reviewed the same transaction now, it would conclude that it constituted a concentrative joint venture. Commission Notice, O.J. C 385/1 (1994).

the parent companies free to determine the future structure and development of the joint venture, the Commission found that Cokoladovny would perform all the functions of an autonomous economic entity on a lasting basis. The Commission's finding was presumably influenced also by the fact that the transaction was a privatization where the government vendor sought to provide for an initial period of stability and residual involvement.⁴⁹

Another example of a transaction whose structure was largely determined by the existing legislative framework concerning the privatization of the acquired entity was the acquisition of an important shareholding in Banco Totta & Açores ("Totta") by the Spanish banking and financial group Banco Español de Crédito ("Banesto") directly and indirectly through Valores Ibéricos ("VISA"), a holding company owned by Banesto, and certain Portuguese partners jointly operating through the holding company MSF.⁵⁰ The transaction was carried out by way of a staggered subscription of shares within the framework of the two-stage privatization of Totta's capital, which started in 1989. To avoid exceeding the 10% ceiling on share capital acquisitions by foreign investors in the Portuguese privatization law, Banesto directly acquired a 9.4% stake and, at the same time, set up a holding company, VISA, whose sole activity was the purchase of the highest shareholding in Totta allowed by Portuguese legislation. Since undertakings in which the majority interest was held by foreign persons were treated as foreign investors by Portuguese law, Banesto subscribed for only 49% of VISA's share capital, with the remaining 51% belonging to a group of Portuguese partners jointly operating through the holding company MSF. Following gradual direct and indirect acquisitions, the total shareholding of Banesto and its partners in Totta rose to 46.5%. Since the rest of the capital was spread among more than 40,000 shareholders, with the exception of a 16.6% stake held by the Portuguese state, Banesto, MSF and VISA held, in practice, more than 60% of the voting rights at Totta's shareholders' meeting. In addition, they were empowered to appoint twelve out of the thirteen directors of Totta's Board. It is interesting that the notification made to the Com-

49. See Jonathan Faull, *Case Note*, 2 EEC MERGER CONTROL REP. 684.1 (Kluwer 1992).

50. BANESTO/Totta, Case IV/M192, [1992] 4 C.M.L.R. 542.

mission concerned not the acquisition of joint control of Totta by Banesto and MSF, which had taken place a year before the notification, but the agreement entered into by the two companies to allow Banesto to consolidate Totta in its annual financial statements. To that end, it was agreed that seven out of the twelve directors would represent Banesto's interests in Totta, with only five representing MSF, and that Mr. Roquette, Chairman of Totta and VISA, would become a director of Banesto.

3. Different Forms of the Change in Control Brought About by Concentrations Involving Privatized Companies: In Particular, Concentrative Joint Ventures

A state's disposal of all or part of its interest in a company to be privatized may result, depending on the relevant factual and legal elements of each transaction, in the acquisition of sole control by the acquirer or one of the acquirers,⁵¹ in the acquisition of joint control by a number of undertakings or persons,⁵² or even in the acquisition of both sole and joint control, where a single notification is made in relation to several acquisitions by and between the same parties.⁵³

51. See, e.g., *Elf Aquitaine-Thyssen/Minol*, Case IV/M235, [1992] 5 C.M.L.R. 203; *DASA/Fokker*, Case IV/M237, [1993] 5 C.M.L.R. 18; *Nestlé/Italgel*, Case IV/M362, [1993] 5 C.M.L.R. 311; Commission Decision, O.J. C 162/7 (1994) (*GE/ENI/Nuovo Pignone (II)*); Commission Decision, O.J. C 185/3 (1994) (*Tractebel/Synatom*); Commission Decision, O.J. C 249/3 (1994) (*Tractebel/Distrigaz II*); Commission Decision, O.J. C 280/3 (1994) (*VAG/SAB*).

52. E.g., *BANESTO/Totta*, [1992] 4 C.M.L.R. at 542; *Air France/Sabena*, Case IV/M517, [1994] 5 C.M.L.R. M1; *Kali+Salz/MdK/Treuhand*, O.J. L 186/38 (1993); Commission Decision, O.J. L 158/24 (1994) (*Pilkington-Techint/SIV*); Commission Decision, O.J. C 189/5 (1994) (*PowerGen/NRG/Energy Morrison Knudsen/Mibrag*); *Thyssen Stahl/Krupp/Riva/Falck/Tadfin/AST*, Case IV/M484 (Eur. Comm'n 1994) (not yet reported); Commission Decision, O.J. C 181/17 (1995) (*DOW/BUNA*); Commission Decision, O.J. C 200/10 (1995) (*Swissair/Sabena*).

53. Commission Decision, O.J. C 23/13, ¶¶ 10-12 (1994) (*Fortis/CGER*). In analyzing the acquisition by the Group Fortis ("Fortis"), controlled by AG Group and AMEV, of a 49.9% shareholding in ASLK/CGER Bank and ASLK/CGER Insurance from ASLK Holding/CGER Holding ("Holding"), a Belgian state-owned public-interest banking holding company that also retained a 49.9% interest in each of the two companies, the Commission reasoned that after the transaction Fortis and Holding would have equal shareholdings and numbers of directors on the boards of ASLK/CGER Bank and ASLK/CGER Insurance. *Id.* The Commission, however, found that Fortis would have sole control over ASLK/CGER Insurance due to its right to a casting vote in case of deadlock, whereas Fortis and Holding would have joint control over ASLK/CGER Bank because Fortis, in proposing strategic decisions, was obliged to obtain the agreement of the members of the company's management committee, whose composition is subject to the approval by the Belgian Banking and Financial Commission. *Id.*

In the case of partial privatizations or privatizations carried out in stages, in which the entity concerned is subject to joint control, one of the persons exercising control may be the state itself, whose desire to retain a presence in the venture may be motivated by considerations of a financial, long-term strategy, or general interest nature rather than by a desire to maintain an effective role in its daily management. In such cases, the Commission has taken the view that, for joint control to exist, the state and its partners must be in agreement on the strategic decisions to be taken by the new entity and the state must retain a real possibility of contesting any decisions taken by the other parent company.⁵⁴

Moreover, the Commission has found that the acquisition of joint control of a privatized company does not give rise to the coordination of the competitive behavior of the state vendor and its partners, either among themselves, or between them and the joint venture,⁵⁵ where the state, which by definition lacks expertise in the joint venture's economic sector, exits the joint venture's market in circumstances in which it could not foreseeably re-enter it and, at the same time, gives preeminent weight in management decisions to the other parent company, which itself continues to operate on the joint venture's market: the "industrial leadership" principle.⁵⁶

54. See, e.g., *Kali+Salz/MdK/Treuhand*, O.J. L 186/38, at 39, ¶¶ 5-7 (1993). Treuhand retained 49% of the share capital and voting rights of MdK, but its approval was required for a number of market-related strategic decisions and it participated in drawing up a detailed five-year business plan for the joint venture together with the majority partner K+S. See Commission Decision, O.J. C 162/7, ¶¶ 6-9 (1994) (*GE/ENI/Nuovo Pignone (II)*). Since the veto rights conferred on the seller, the state holding company ENI, by the notified share acquisition agreement were temporary in nature and only concerned actions likely to have a social impact and not foreseen in the industrial plan put forward by the acquirer GE, the Commission found that ENI had no joint control over the combined entity. *Id.* See also Commission Notice, O.J. C 385/5, at 10, ¶ 36 (1994).

55. Merger Regulation, *supra* note 5, art. 3(2), O.J. L 395/1, at 4 (1989). The absence of any coordination of competitive behavior is one of the two requirements that must be fulfilled under Article 3(2) of the Merger Regulation for the setting up of a joint venture constituting a concentration. *Id.*

56. The Commission introduced the industrial leadership principle in a number of concentrations not involving a privatization. See, e.g., *Thomson/Pilkington*, Case IV/M86, [1991] 4 C.M.L.R. 897; *UAP/Transatlantic/Sun Life*, Case IV/M141, [1992] 4 C.M.L.R. 1; *Ericsson/Kolbe*, Case IV/M133, at 81 (Eur. Comm'n Jan. 22, 1992) (not yet reported); *British Airways/TAT*, Case IV/M259, [1993] 4 C.M.L.R. 7; *Linde/Fiat*, Case IV/M256, [1992] 5 C.M.L.R. 2987; Commission Decision, O.J. C 305/11 (1993) (*Arvin/Sogefi*). It is submitted that the industrial leadership principle "has links back to the

Applying the industrial leadership principle, the Commission decided that the acquisition by Air France's newly created subsidiary, Finacta, of a 37.58% stake in the national air carrier Sabena from the Belgian State, which retained a 62.11% interest, created a concentrative joint venture between Air France and the Belgian State.⁵⁷ Under the protocol of agreement, signed by Air France, Sabena, and the Belgian Government, that was notified to the Commission, Air France was granted rights that, the Commission stated, would go far beyond those ordinarily granted to minority shareholders for the protection of their financial investments. For example, not only would Finacta approve the designation of Sabena's President and Vice-President, but it would also, itself, appoint five out of the fourteen members of Sabena's Board. A three-quarters majority was required for Board decisions entailing substantial changes in the company's business strategy. Finally, Finacta would also appoint half of the members of Sabena's Executive Committee. On the other hand, the Commission noted that the protocol did not provide for any specific dispute resolution mechanism, so that the Belgian State, which remained the majority shareholder, had a preeminent position in the case of significant disagreements in Sabena's operation.⁵⁸

In relation to the competitive relationship between the parent companies, and between each of them and Sabena, the Commission decided that the Belgian State could be ruled out as an actual or potential competitor since it had no involvement in any other airline and was highly unlikely to establish a new airline in the future. On the other hand, in the Commission's view, the possibility of effective competition from Air France was rendered remote by the preeminent influence Air France would exercise

'single economic enterprise' approach in Article 85 cases involving parents and their subsidiaries." 2 *BUTTERWORTHS COMPETITION L.* VII/499 (Spearing & Brandeburger eds., 1994). For a critical view of this approach see Anand S. Pathak, *Case Note on Ericsson/Kolbe*, 2 *EEC MERGER CONTROL REP.* 656.1 (Kluwer 1992). The industrial leadership concept was apparently abandoned by the Commission since the 1994 Commission Notice on the distinction between concentrative and cooperative joint ventures, which replaced a previous notice published in 1990, makes no reference to it and clearly states instead that parent-to-venture coordination is relevant only insofar as it produces or reinforces parent-to-parent coordination. Commission Notice, O.J. C 385/1, at 3, ¶ 17 (1994).

57. Air France/Sabena, Case IV/M517, [1994] 5 *C.M.L.R.* M1, ¶¶ 7-11.

58. *Id.*

over Sabena's market behavior, particularly in light of the Belgian State's lack of technical expertise. The Commission pointed out that not only did Sabena's new industrial cooperation plan provide that the company would in many sectors be dependent on Air France's technology, installations, and equipment, but also that it was up to Sabena's President, who would be approved by Air France, and not the Belgian Government, to appoint one-half of the members of the Executive Committee and to coordinate with Air France on certain matters, such as Sabena's day-to-day management. Therefore, the Commission concluded that Sabena would integrate to a certain degree with Air France, although that integration would most probably not result in a complete harmonization of management policies at all levels.⁵⁹

Three years later, the Commission found that the acquisition of a 49.5% interest in Sabena by Swissair, which took place in July 1995, following a repurchase by the Belgian State of Finacta's stake in Sabena and a recapitalization of the air carrier, would result in Sabena being jointly controlled by Swissair and the Belgian State, which retained a 33.81% interest.⁶⁰ The issue of control was central to this transaction, because under EC law,⁶¹ Member States may only grant or maintain in force operating licenses to air carriers that are wholly or majority owned by, and are under the "effective control"⁶² of, Member States and/

59. *Id.* As noted, the Commission has ceased to apply the industrial leadership principle, since it is no longer concerned with the risk of collusion between the parents and the joint venture. See *supra* note 55 and accompanying text (discussing industrial leadership principle). For a joint venture to be considered concentrative it is now sufficient that one parent withdraw from the joint venture's market, regardless of whether the remaining parent is the "industrial leader."

60. In addition, a pool of Belgian institutional investors will hold a 16.5% stake in the acquired company, whereas the remaining 0.19% of Sabena's capital will be held by former or current employees of the company.

61. See Council Regulation No. 2407/92, art. 4(2), O.J. L 240/1, at 2 (1992). Pursuant to Article 3(3) of Council Regulation No. 2407/92, the grant of an appropriate operating license is a precondition for the provision of air transport services in the European Union's territory. An air carrier to which an operating license is granted pursuant to this Regulation enjoys free access to all intra-Community air routes. Commission Decision No. 93/347/EEC, O.J. L 140/51 (1993) (Viva Air).

62. Council Regulation No. 2407/92, art. 2(g), O.J. L 240/1, at 2 (1992). "Effective Control" is defined by Article 2(g) of Regulation 2407/92 according to the notion of control in Article 3(3) of the Merger Regulation. *Id.* The majority ownership and effective control obligations set forth in Regulation 2407/92 reflect, at the Community level, the restriction customarily imposed upon air carriers by international agreements

or EU nationals.⁶³ In taking the view that Sabena would be jointly controlled, the Commission emphasized that in light of its considerable expertise, Swissair would play an active role in the management and operation of the combined entity. At the same time, the Commission noted that, under the notified agreement, the Belgian State appeared to have the stronger influence over Sabena's board, which would have the primary responsibility for the company's management. Of the twelve board members, five would be appointed by Swissair, six by the Belgian shareholders, and one, the Chairman, by joint decision of the two groups of shareholders, or, in case of disagreement between them, on Swissair's proposal subject to approval at the shareholders' meeting. The new entity's board would make decisions by simple majority vote and would appoint, upon a joint proposal by Swissair and the Belgian State, a CEO who would be in charge of Sabena's day-to-day management. The Commission, however, found that the notified agreement included institutional mechanisms ensuring that Swissair and the Belgian

on air transport services. *Id.* These restrictions, which were originally based on national security justifications, are nowadays directed towards ensuring that the traffic rights exchanged in the framework of such agreements are effectively exploited by, or to the benefit of, the contracting parties and that third-country carriers are not allowed to take full advantage, on a non-reciprocity basis, either directly or through their subsidiaries, of the liberalization of the internal market for air transport services in the European Union. *Id.* Moreover, these restrictions prevent third-country carriers from providing services exclusively within the territory of one state or a group of states through subsidiaries. *Id.*

63. *Swissair/Sabena*, O.J. C 200/10 (1995). In a decision on a separate procedure relating to the application of Council Regulation 2407/92 on licensing of air carriers, the Commission reasoned that the first requirement was clearly satisfied as 50.5% of Sabena's voting shares will be held by the Belgian state and a pool of Belgian institutional investors, which will act as a single group pursuant to a shareholders' agreement between them, containing voting agreements. *Id.* With respect to the effective control requirement, the Commission found that both the corporate structure and the management organization of the combined entity would not jeopardize the ultimate decision-making power of the Belgian shareholders and would not be such as to confer on Swissair any prerogative incompatible with the effective control requirement. *Id.* In particular, Swissair would hold no veto rights at the board level, but only the power of creating a deadlock in the event that the Chairman voted against the Belgian shareholders. *Id.* Moreover, although as a matter of law Swissair will hold a veto right over certain decisions of the shareholders' meeting, that right would be limited to amendments to Sabena's articles of incorporation, capital increase or reduction, and winding-up, merger, or spin-off involving the company. *Id.* The Commission thus took the view that such a veto right amounted to an ordinary measure for the protection of minority shareholders of the same kind as those prescribed by the national company laws of most Member States. *Id.*

State would jointly exercise a decisive influence over Sabena.⁶⁴ Finally, in the Commission's view, the parties' intention to decide jointly the new entity's commercial policy was reflected in provisions in a concomitant cooperation agreement entered into between Sabena and Swissair, directed at achieving operational synergies in areas of strategic commercial importance. Under the agreement, all management action in such areas would require approval by the boards of Sabena and Swissair, which would define common planning and control processes in certain areas, harmonize their brand image, and set up a joint sales organization outside Belgium and Switzerland.⁶⁵

The Commission ruled out any risk of coordination of the competitive behavior between Swissair and the Belgian State, noting that all the latter's activities in the field of air transport were included in the joint venture, and decided that the new joint venture would be concentrative.⁶⁶

On the other hand, in the *DASA/Fokker* case,⁶⁷ which involved the acquisition by Daimler-Benz of a 51% interest in the Dutch group Fokker through its subsidiary Deutsche Aerospace ("DASA"), the second largest European aircraft manufacturer, the Commission decided that the Dutch State's 49% holding would not give it joint decisive influence over Fokker, in the absence of rights going beyond those normally granted to minority shareholders.⁶⁸ The Dutch State, DASA, and Fokker had concluded a primary agreement that would limit Daimler-Benz's control in some respects. While DASA would control a majority of seats on Fokker's management board, major decisions would need approval of the supervisory board, where a qualified majority would be required on some important business matters. Here, DASA would need the votes of two independent directors appointed by Fokker's labor unions, or one independent director and a director appointed by the State, in order to obtain the qualified majority. Nonetheless, the Commission determined that the transaction would result in Daimler-Benz acquiring sole

64. *See id.* O.J. C 200/10, at 6, ¶ 10 (1995) (noting new entity's board could neither appoint CEO without joint proposal of both parties, nor appoint or dismiss other members of executive management without CEO's recommendation).

65. *Id.* O.J. C 200/10, at 6, ¶ 11 (1995).

66. *Id.* O.J. C 200/10, at 6, ¶ 14 (1995).

67. *DASA/Fokker*, [1993] 5 C.M.L.R. at 18.

68. *Id.*

control of Fokker. The Dutch State's influence would be limited, the Commission noted, because it could not alone block business decisions in relation to Fokker, and, in any event, had agreed separately not to oppose the termination of troubled aircraft programs.⁶⁹

4. States' Public Power Prerogatives Do Not Confer a Decisive Influence over Privatized Enterprises

With respect to the notion of control, the Commission has also drawn an interesting distinction between the state's role as a shareholder and its role as public guarantor of the general interest. In the *Tractebel/Synatom*⁷⁰ and the *Tractebel/Distrigaz II*⁷¹ cases, the Commission decided not to oppose the acquisition by Tractebel of sole control over, respectively, Synatom, a supplier of uranium to nuclear power plants operated by Belgian electricity producers, and Distrigaz, the Belgian gas distribution monopoly. Prior to the notified concentrations, the Belgian State not only controlled the two companies, solely in the case of Synatom and jointly with Tractebel in the case of Distrigaz, but also enjoyed special public power prerogatives regarding the defense of the public interest in the continuity of the national energy supply and the definition of the state energy policy. Therefore, the Belgian State was represented on the two companies' boards by a government commissioner with the right to veto decisions deemed contrary to the public interest. As a result of the two concentrations, the Belgian State disposed of virtually its entire shareholding in both Synatom and Distrigaz, retaining only a "golden share" in each company, permitting it to appoint two board representatives without voting rights. In addition, the Belgian State retained the veto rights it formerly held as the public authority. In both privatizations, the Commission decided that the veto right was not sufficient to give the State joint control of the combined entities within the meaning of Article 3 of the Merger Regulation, since it had neither the object or effect of permitting the State to exercise a decisive influence on the activities of the companies concerned and, instead, reflected only the

69. *Id.* Compare Commission Decision, O.J. C 156/10 (1991) (Sanofi/Sterling Drug) (citing prior consultation right given to minority shareholder in a 70-30 venture as one of several factors establishing joint control).

70. Commission Decision, O.J. C 185/3 (1994) (Tractebel/Synatom).

71. Commission Decision, O.J. C 249/3 (1994) (Tractebel/Distrigaz II).

State's regulatory role, exercisable only in limited circumstances to protect the public interest.⁷²

5. Potential Impact of Statements Made by the Relevant National Privatization Authority on the Commission's Substantive Assessment of a Concentration

Finally, in *Elf Aquitaine-Thyssen/Minol*,⁷³ the Commission decided that a notified concentration effected in the context of a privatization would not create or strengthen a dominant position, in reliance, *inter alia*, on statements that the relevant national privatization authority had made in the course of the administrative procedure. In that case, the Commission gave conditional clearance to the acquisition by a consortium led by Société Nationale Elf Aquitaine ("Elf") of the assets of the former East German state oil-company, Minol, from the German Treuhandanstalt ("Treuhand"). As part of the transaction, Elf would have the right to manage two existing refineries in the new German Länder⁷⁴ until it built a replacement refinery. The Treuhand would, however, hold the old refineries in trust and bear their operating losses until they were dismantled. The Commission was concerned that the management agreement would give Elf an unfair advantage over its competitors by providing it with a service station network in the new German Länder under conditions more favorable than those available on the market generally and at the expense of the taxpayer.

The Commission was satisfied, however, with an undertaking by letter written by the Treuhand that it would use its inspection rights under the management contract to supervise the terms under which Elf would supply gasoline from the two refineries to its affiliates and competitors. The pricing and marketing policies of Elf would be certified by independent auditors.⁷⁵ Interestingly, the Treuhand's statements seem to have been relevant not so much to the issue of whether Elf would hold a dominant position in the German market for distribution of petroleum products, as to its opportunity to abuse that dominant position. Such potential abuse falls outside the scope of the sub-

72. *Tractebel/Synatom*, O.J. C 185/3, at 4, ¶¶ 12-14 (1994); *Tractebel/Distrigaz II*, O.J. C 249/3, at 3, ¶¶ 16-17 (1994).

73. *Elf Aquitaine-Thyssen/Minol*, [1992] 5 C.M.L.R. at 203.

74. A Länder is a German national State.

75. *Elf Aquitaine-Thyssen/Minol*, [1992] 5 C.M.L.R. at 203, ¶ 12.

stantive test in Article 2(3) of the Merger Regulation,⁷⁶ which relates only to combinations resulting in a lasting and substantial change in the structure of the market and, unlike Article 86 of the EC Treaty, is not a market behavior control instrument.⁷⁷

6. Privatizations Carried Out Through the Public Flotation of a State-Owned Enterprise

Finally, the sale of a state-owned enterprise to private investors may take place through a public flotation, that is, in a way that would not necessarily qualify as a concentration as defined in the Merger Regulation. Indeed, no concentration takes place when a privatization is carried out through the creation of a "public" corporation with a large number of small shareholders, as opposed to a corporation with closely held shares in which, by definition, nobody acquires control.

The public flotation of an enterprise to be privatized is occasionally combined with a private placement to create a "hard core" of investors with necessary technical, financial, or entrepreneurial expertise that will act as a single group in a voting or non-voting syndicate. The coordinated exercise of voting rights pursuant to some obligatory formula normally confers on this hard core of pooled investors, in which the state may also participate, joint control over the privatized company, not only where they hold a majority interest,⁷⁸ but often also where they have only a minority interest, since the remaining shares are usually widely dispersed.⁷⁹

76. Merger Regulation, *supra* note 5, art. 2(3), O.J. L 395/1, at 3-4 (1989).

77. Kurt Markert, *Case Note on Elf Aquitaine-Thyssen/Minol*, 2 EEC MERGER CONTROL REP. 872.4 (Kluwer 1993).

78. Commission Notice, O.J. C 385/5, at 8-10, ¶¶ 30-35 (1994) (stating that minority shareholders may obtain joint control if they have majority of voting rights and act together in exercising them by virtue of legally binding agreement or on *de facto* basis due to existence of strong common interests). *See, e.g., Kelt/American Express*, O.J. C 223/38, ¶¶ 5-6 (1991); *Costa Crociere/Chargeurs/Accor*, Case IV/M334, [1993] 5 C.M.L.R. at 206, ¶¶ 5-7 (voting syndicate among three shareholders holding 53.3% stake of acquired company found to exercise joint control over it); Commission Decision, O.J. C 132/12 (1991) (*Elf/BC/Cepsa*) (finding that Elf and Banco Central to jointly control CEPESA, in which they held 34% stake each).

79. *See, e.g.,* Commission Decision, O.J. C 225/2, (1993) (*Société Générale de Belgique/Générale de Banque*) (citing projections based on percentages of shares present at past shareholders' meeting of Générale de Banque and hypotheses about future behavior of small shareholders and concluding that SGB would acquire effective control over Générale de Banque since, by virtue of increase from its prior 20.94% shareholding of the company to 25.96%, it would have more than half of votes at future

Joint control by the syndicated investors may also come about via their acquisition of a "qualified minority interest." For example, the purchase of preferential shares linked to a majority of voting rights, or conferring other rights enabling the minority shareholders to determine the strategic commercial conduct of the company to be privatized, such as the power to appoint more than half of its supervisory or administrative board, may establish joint control over a privatized company.

Moreover, a hard core of investors acquiring a minority interest may obtain control of the company to be privatized in conjunction with other non-syndicated shareholders as a result of a binding agreement between them; in particular where veto rights conferred on the hard-core shareholders allow them to block strategic decisions relating to business policy of the enterprise to be privatized, including its budget, business plan, major investments, and the appointment of senior management.⁸⁰

On the other hand, syndicated shareholders do not nor-

shareholders' meetings and thus would be able to elect majority of Générale de Banque's board); Commission Decision, O.J. C 321/16 (1990) (Arjomari-Prioux/Wiggins Teape Appleton) (holding that 39% stake was sufficient to confer on Arjomari decisive influence over WTA because remainder of WTA's capital was widely dispersed and in light of attendance and voting patterns at annual general meetings). *See also Medibanca/Generali*, [1994] 4 C.M.L.R. at M3, ¶ 8 (stating that control over company may result from agreement among minority shareholders that either confers on syndicated shareholders majority vote at company's shareholders' meeting, or otherwise enables majority to exercise decisive influence on composition or decisions of company's management boards).

80. *See* Commission Notice, O.J. L 377/1, at 21-29, ¶¶ 14 (1994) (concerning notice of notion of concentration). *See also* Commission Decision, O.J. C 181/4 (1993) (Aegon/Scottish Equitable) (finding that Aegon initially acquired 100% of equity capital and 40% of voting rights of Scottish Equitable Life Assurances Society, whereas other partner (newly incorporated to safeguard rights of existing and future Scottish Equitable policy holders) held 60% of voting rights; joint control was established because strategic and business decisions and appointment of directors required parties' common agreement); Commission Decision, O.J. C 199/12 (1992) (Thomas Cook/LTU/West LB) (finding that acquisition by LTU and West LB of entire issued share capital of Thomas Cook, although two shareholders would acquire 90% and 10% shareholdings, respectively, West LB would obtain joint control because it could nominate 5 of 10 directors, including chairman of Thomas Cook's board, who had tie-breaking vote, and various strategic and ongoing business decisions would require consent of both shareholders); Commission Decision, O.J. C 203/14 (1991) (Elf/Enterprise) (finding that acquisition by Enterprise of one-third of the stock in subsidiary of Elf with proportional board representation found to confer joint control on Enterprise because of additional right to veto applications for petroleum licenses or exploration concessions as well as rights of budgetary approval; finding joint venture to be of cooperative nature on other grounds).

mally acquire control over a privatized entity where the shareholders' agreement between them is of a non-voting nature and only provides for consultation, a standstill or no-sale obligation, and/or a right of first refusal over the appointment of certain directors.

In the *Mediobanca/Generali* case,⁸¹ the Commission decided that a transaction where the Italian merchant bank Mediobanca underwrote part of the shares issued in the context of a capital increase of the insurance company Assicurazioni Generali ("Generali") did not constitute a concentration within the meaning of the Merger Regulation. As a result of the capital increase, Mediobanca brought its shareholding in Generali from 5.98% to 12.84%. The Commission reasoned that such a minority interest might itself confer control if a sufficiently poor attendance at Generali's ordinary shareholders' meeting could be demonstrated, but concluded that this was not the case. The Commission based its conclusion on the level of shareholder participation at such meetings in the five preceding years, which revealed that shareholders owning at least 33% of Generali's capital were present or represented and voted. Mediobanca informed the Commission of its agreement with Euralux, Generali's second largest shareholder, with a 4.77% holding, which provided for consultation between the two shareholders and included an undertaking from each not to sell its shares. This agreement did not, however, contain any provisions concerning the joint exercise of voting rights or any procedure intended to ensure that Mediobanca exercised a decisive influence on the composition and decisions of Generali's governing bodies. The Commission, therefore, concluded that the notified transaction would not give to Mediobanca joint or sole control of Generali and, as a result, did not constitute a concentration.

An unusual development in the *Mediobanca/Generali* case took place a few months after the adoption of the Commission's decision in December 1991, when an Italian financial newspaper published the text of a hitherto allegedly secret agreement signed in 1985 by Generali, Mediobanca, and Euralux's parent company, Lazard Frères. In addition to the bilateral no-sale clause already disclosed to the Commission, this shareholders' agreement provided, *inter alia*, for the creation of a three-mem-

81. *Mediobanca/Generali*, Case IV/M156, [1994] 4 C.M.L.R. M1.

ber steering committee comprised of representatives of Generali and its two main shareholders, with a view to examining problems suffered by Generali that were of common interest to the shareholders and proposing candidates for appointment to the company's administrative and senior executive positions, including the President, Vice-President, and Managing Director at the shareholders' meeting.⁸² The belated publication of this shareholders' agreement prompted a number of other minority shareholders in Generali to first ask the Commission to reopen the proceedings and, later, to attack the Commission's refusal to do so in the Court of First Instance. In their request to the Commission for the reopening of proceedings, three minority shareholders, which at that time represented less than 0.5% of Generali's share capital, submitted that the Commission's decision had been based on a misapprehension as to the essential facts of the case, attributable to manifestly incomplete or erroneous information on the terms and effects of the shareholders' agreement. The Commission rejected the applicants' request on the ground that it had been aware of the entire scope of the 1985 agreement and had taken it into account when adopting its decision on the case. The Court of First Instance declined to adjudicate on the interesting substantive issues raised by the appeal and dismissed the action on the grounds that the applicant shareholders lacked standing. In the view of the Court of First Instance, the shareholders could not establish that the contested decision that declared the Merger Regulation inapplicable to Mediobanca's increase of its stake in Generali was of direct and individual concern to them.⁸³

Although, in the absence of a shareholders' agreement concerning the joint exercise of decisive influence by a sufficiently powerful group of investors, a minority stock acquisition falls outside the scope of the Merger Regulation, it may, nonetheless, be subject to Article 85 of the EC Treaty if the stock acquisition

82. *Zunis Holding, Finan and Massinvest v. Commission*, Case T-83/92, [1994] 5 C.M.L.R. 154, 157, ¶ 3; *Ecco come è nato e cosa dice il patto tra Mediobanca, Lazard e Generali* [The New Agreement Between Mediobanca, Lazard and Generali: How It Was Born and What It Says], *Il Sole-24 Ore*, Mar. 19, 1992.

83. *Zunis Holding*, [1994] 5 C.M.L.R. at 157, ¶ 3. An appeal from this judgment is pending before the Court of Justice. On September 12, 1995, Advocate General Lenz presented his opinion on the appeal, recommending that the Court uphold the judgment of the Court of First Instance.

confers on the shareholders concerned the power to exercise a certain degree of influence over the commercial activities of a competitor.⁸⁴ Commentators have suggested that the Commission's broad interpretation of the "decisive influence" test under the Merger Regulation, through a gradual expansion of the concepts of sole and joint control, has extended the scope of the Regulation to acquisitions of minority interest that would have otherwise been eligible for review under Articles 85 and 86 of the EC Treaty.⁸⁵

Finally, a common feature of privatizations of public interest companies is the retention by the government, pursuant to a special clause to be inserted in the company's by-laws, of a "golden share" granting the state certain special rights and powers. In general, such powers include, for example, the power to prohibit acquisitions of significant holdings in the privatized company, to prohibit voting shareholders' agreements and no-sale clauses, to appoint one or more directors and statutory auditors, or to veto amendments to the company's articles of incorporation, capital increases and reductions, and any winding-up,

84. EC Treaty, *supra* note 1, arts. 85, 86, [1992] 1 C.M.L.R. at 626-28. Articles 85 and 86 of the Treaty are not applicable to concentrations falling within the scope of the Merger Regulation. Merger Regulation, *supra* note 5, art. 22(1)-(2), O.J. L 395/1, at 11 (1989) (disapplying enforcement powers under Council Regulation 17/62). Furthermore, the Commission has taken the policy position that, in general, it will not intervene under Articles 85 and 86 with respect to concentrations falling below the Merger Regulation's "Community dimension" turnover thresholds. The Commission, however, retains the right to take action according to the procedures laid down in Article 89 of the Treaty, in cases not provided for by Article 22 of the Merger Regulation, "where a very clear case of dominance is established that is not able to be dealt with by national competition authorities." Accompanying Statements Entered in the Minutes of the Council of the EU of December 19, 1989, Statement by the Commission at Article 22 of the Merger Regulation, 3 Butterworths Competition L. A/721B (Apr. 1995). See statement of then-Commissioner for competition matters Sir Leon Brittan, cited in Commission press release IP(92) 1048, Sir Leon Brittan Announces Preliminary Conclusions in relation to Proceedings in the British Airways/Dan Air Case (European Comm'n Dec. 15, 1992). On the other hand, concentrations, whether above or below the Merger Regulation's "Community dimension" turnover thresholds, remain subject to the application of Article 85(1), provided, however, that, in the absence of implementing legislation, there has been a ruling of infringement by the Commission or by the national competition authority having jurisdiction under Articles 88 or 89 of the Treaty, and Article 86 of the Treaty by national courts. *Ministère Public v. Asjes*, Joined Cases 209-13/84, [1986] E.C.R. 1425; *Ahmed Saeed Flugreisen and Silver Line Reisebüro v. Zentrale Zu Bekämpfung Unlauteren Wettbewerbs*, Case 66/86, [1989] E.C.R. 803.

85. Barry E. Hawk & Henry L. Huser, "Controlling" the Shifting Sands: *Minority Shareholdings Under EEC Competition Law*, 1993 *FORDHAM CORP. L. INST.* 373 (Barry Hawk ed., 1994).

merger, or spin-off involving the company. As discussed above, since these "golden share" powers reflect only the state's regulatory role and can only be exercised in limited circumstances to protect the public interest, they are normally insufficient by themselves to give the state joint control over privatized entities within the meaning of Article 3 of the Merger Regulation, unless the state is otherwise empowered to exercise jointly a decisive influence on the privatized companies' activities in its position as a shareholder.

B. Application of Articles 85 and 86 of the EC Treaty to Acquisitions of Influence Short of Control

1. Minority Shareholding Acquisitions Resulting in a Transfer of Control of the Acquired Company

As mentioned above, minority stock acquisitions and other commercial arrangements aimed at acquiring influence over an enterprise, such as cross-shareholdings, shared directors or managers, non-voting equity interests, and financing agreements may constitute concentrations for the purposes of the Merger Regulation to the extent that they involve an acquisition of sole or joint control and, in the latter case, to the extent that the joint venture established is of a concentrative rather than cooperative nature.⁸⁶ In addition, where the Merger Regulation does not apply,⁸⁷ such transactions may come within the scope of Articles 85

86. Merger Regulation, *supra* note 5, art. 3(1)(b), (2), O.J. L 395/1, at 4 (1989). See 2 BUTTERWORTHS COMPETITION L. VII/494 (Spearing & Brandeburger eds. 1994) (stating that "cross-shareholdings and reciprocal board representation may also fall within the [Merger] Regulation's scope, if a 'combined group' constituting a genuine economic unit is created through profit and loss sharing and joint liability to third parties").

87. *E.g., Renault/Volvo*, [1991] 4 C.M.L.R. at 302-03, ¶ 14. The acquisition of 45% crossholding in truck and bus/coach sector was found to be a concentration because it created a situation of strong common interest that forced parties to reach common decisions in the relevant joint management committee. The parties' positive commitments to make certain activities complementary pointed towards an irreversible reciprocal dependency. The acquisition of a 25% crossholding in the car sector was found to be cooperative because a joint management committee created by parties could adopt binding decisions only with an agreement between both parties and there was no concrete indication that the parties would proceed to irreversibly integrate the product ranges of respective car businesses. See also Commission Decision, O.J. C 259/3 (1993) (British Telecom/MCI) (finding that proposed purchase by BT of 20% of outstanding shares of common stock of MCI is not an acquisition of control because BT would have no veto power over MCI's competitive behavior and commercial strategy, and provisions enabling BT to block third party from acquiring control over MCI not considered

and 86 of the EC Treaty.⁸⁸

2. The Influence Threshold Triggering Application of Articles 85 and 86 of the EC Treaty Under the *Philip Morris* Judgment

In its *Philip Morris* judgement, the Court of Justice established for the first time that the acquisition of a minority shareholding in a competitor may fall within the scope of Article 85 to the extent that it may "serve as an instrument for influencing the commercial conduct of the companies in question so as to restrict or distort competition."⁸⁹ According to the Court, such a situation arises where one of the following conditions is met: (1) the shareholding confers on the acquiring entity legal or de facto control of the target, or a related agreement gives the ac-

to confer positive control except in extraordinary circumstances); Commission Decision, O.J. C 113/12 (1992) (*Eureko*). The holding company set up by four insurance companies or groups engaged in non-life and life insurance to whom they would transfer their business outside their respective home countries. The Commission was unable to establish the existence of joint control since none of the parent companies would have a veto right on the decisions of *Eureko* management board and changing their alliances in the decision-making process were allowed in all areas of commercial importance where their decisions could be approved by the supervisory board by simple majority or a super-majority. *But see* Commission Decision, O.J. C 258/9 (1992) (*Avesta/British Steel/NCC/AGA/AXEL Johnson*) (finding that newly formed joint venture combining stainless steel activities of British Steel and Avesta, which held stakes of 40 and 25.1%, exercised joint control because shareholders' agreement required approval of both two largest shareholders and one of two minority shareholders for strategic decisions, including approval of budgets and business plans, and despite risk of "shifting alliances").

88. EC Treaty, *supra* note 1, art. 85, [1992] 1 C.M.L.R. at 626-27. From a different standpoint, Articles 85 and 86 of the Treaty remain applicable to any agreements whereby the parties to a concentration, including the state or a public body disposing of its interest in a publicly-owned enterprise accept restrictions on their freedom of action in the market which are not directly related and necessary to the implementation of the transaction, whereas truly ancillary restrictions are to be assessed together with the concentration under the Merger Regulation. Merger Regulation, *supra* note 5, recital 25 O.J. L 395/1 (1989); *see supra* note 30 (listing Commission Notices regarding restrictions ancillary to concentration). *See also, e.g.*, *Kali+Salz/MdK/Treuhand*, O.J. L 186/38 (1993) (finding clause, by which K+S and Treuhand agreed not to compete with their joint venture MdK for period of ten years and to transfer non-compete obligation to third parties purchasing from them any assets or shareholdings that could be used to compete with MdK, did not qualify as an ancillary restraint since first obligation extended beyond five-year maximum duration for such clauses permitted by Commission).

89. *British American Tobacco Ltd and R.J. Reynolds Industries Inc. v. Commission*, Joined Cases 142 & 156/84, [1987] E.C.R. 4487, 4577, ¶ 37 [hereinafter *Philip Morris*].

quiring entity the option of reinforcing its position at a later time and thereby eventually taking effective control; or (2) acquisition of the shareholding requires the two companies to take account of each other's interests when determining their commercial policy, or the agreement in question provides for or creates a structure likely to be used for commercial cooperation between the parties.⁹⁰ The Court further indicated that an acquisition of a minority interest in a dominant undertaking by a competitor that "results in effective control of the other company or at least in some influence on its commercial policy" may amount to an abuse of dominant position in violation of Article 86 of the EC Treaty.⁹¹

The practical importance of the *Philip Morris* influence standard has been called into question following the Merger Regulation's entry into force, because, as mentioned above, the Commission appears to have progressively expanded the concept of "decisive influence" under the Merger Regulation so as to find sole or joint control in a variety of transactions involving minor-

90. See also Commission Decision No. 94/771/EC, O.J. L 309/24 (1994) (Olivetti-Digital) (declaring Article 85(1) of Treaty inapplicable to acquisition by Digital of 8% stake in Olivetti and to technical cooperation agreement between two companies). The Commission also granted an Article 85(3) exemption to Olivetti's purchasing commitment concerning Digital products based on Alpha AXP technology contained in the contribution. With respect to the share purchase agreement and the shareholders' agreement between the parties, which Olivetti and Digital terminated three months before the decision, the Commission noted that Digital's minority acquisition could not lead to a change in control over Olivetti because: (1) Digital was barred from acquiring an interest in excess of 10% and could not enter into voting arrangements with third parties; (2) Digital held no veto rights; and (3) Olivetti's controlling shareholder, CIR, held a right of first refusal as to any proposed sale by Digital of its Olivetti shares. Although Digital had a proportionate representation on Olivetti's board for so long as it owned at least 25 million shares of Olivetti's common stock, such representation could not lead to a coordination of competitive behavior or an exchange of information since Olivetti's board was not involved in any decisions on the development of new products or new product pricing, having delegated all of its operative functions to the company's President and General Manager).

91. See *Philip Morris*, [1987] E.C.R. at 4584, ¶ 65. The Court upheld the Commission's decision that declared Articles 85 and 86 inapplicable to the acquisition by Philip Morris of a 24.9% interest in the outstanding voting rights and the right to appoint one-half of the board members of Rothman's Holdings ("Rothman's"), the parent company of its competitor Rothmans International. Although the share transfer agreement between PM and Rothmans provided for the creation of reciprocal rights of first refusal in the case of subsequent share transfers and the acquisition by Philip Morris of 50% of the Rothmans International convertible bonds, the Commission and the Court took the view that the transaction at issue did not enable Philip Morris to control or influence Rothmans' conduct and did not allow the parties to coordinate their activities.

ity shareholdings that would have otherwise been subject to scrutiny under Articles 85 and 86 of the EC Treaty.⁹²

3. The Expansion of the *Philip Morris* Influence Standard in the *Gillette* Commission Decision

Not only did the Commission apply the *Philip Morris* doctrine again in the 1992 *Gillette* case,⁹³ but it appears to have also interpreted this standard quite extensively. First, it applied Article 86 of the EC Treaty to a seemingly passive investment made by the U.S. company Gillette in Eemland, a Dutch company which had become Gillette's leading competitor after buying out Wilkinson Sword. Gillette, which held a dominant position in the EU wet-shaving market, made the investment in Eemland by way of an acquisition of a minority shareholding and limited rights giving it no influence.⁹⁴ Second, the Commission applied Article 85 of the EC Treaty to a transaction constituting a concentration, i.e., the sale by Eemland of Wilkinson Sword's business outside of the European Union to Gillette, that was found to result in an artificial geographic break-up of the business subject to the change in control and an inevitable post-closing coordination between Gillette and Eemland.⁹⁵

92. HAWK & HUSER, *supra* note 85, at 393-94.

93. Commission Decision No. 93/252/EEC, O.J. L 116/21 (1993) (*Gillette*). Before *Gillette*, the Commission relied on *Philip Morris* to review a variety of acquisitions of minority shareholdings. Hudson's Bay/Finnish Fur Sales, COMMISSION OF THE EUROPEAN COMMUNITIES, NINETEENTH REPORT ON COMPETITION POLICY 1989, at 59, ¶ 42 (1990); Ibercobre/Outokumpu, COMMISSION OF THE EUROPEAN COMMUNITIES, NINETEENTH REPORT ON COMPETITION POLICY, 1989, at 80-81, ¶ 65 (1990); KLM/Transavia, COMMISSION OF THE EUROPEAN COMMUNITIES, XXIST REPORT ON COMPETITION POLICY 1991, at 72, ¶¶ 90-92 (1992). See also Commission Decision No. 87/100/EEC, O.J. L 41/31 (1986) [hereinafter *Mitchell Cotts/Sofitra*]. In all these cases, the Commission raised objections and the parties either abandoned the deal or restructured it along the lines of the *Philip Morris* case. *Id.*

94. HAWK & HUSER, *supra* note 85, at 398-400 (opining that sound policy basis exists for making minority acquisitions in competitors by dominant undertakings subject to lower influence threshold than minority acquisitions involving no dominant firm).

95. *Id.* at 402-07 (stating that application of Article 85 of the Treaty to concentrations beyond unique factual background of *Gillette* would have no policy justification and would run contrary to reduced transaction costs and legal certainty benefits created by "one-stop shop" principle underlying Merger Regulation). The agreements concerning *Gillette*'s investment in and relationship with Eemland were executed by the parties in December 1989 and notified to the Commission, for negative clearance or an individual exemption under Regulation 17/62, in February 1990. *Id.* These dates probably explain why, although the final decision was adopted on November 10, 1992, the Com-

In the context of a management buy-out of the Swedish company Stora, Eemland purchased the Wilkinson Sword razor and razor blade business worldwide, and re-sold the business outside the European Union and the United States to the market leader Gillette, while retaining the EU and U.S. activities. Rights to the Wilkinson Sword trademark were likewise divided between Gillette and Eemland. Gillette had provided substantial financing for the management buy-out, which was highly leveraged, so that it became a significant creditor of Eemland, its main competitor after the purchase. Although Gillette also acquired a 22% equity stake in Eemland, this participation did not include any voting rights, board or management representation, or access to any of Eemland's internal information. The Commission found that the pre-emption and conversion rights and options that Gillette obtained in connection with the acquisition of its shareholding in Eemland and its status as a major creditor enabled Gillette to exercise influence over Eemland's commercial policy, notwithstanding the lack of any direct means of control and a "Chinese Wall" undertaking given by Gillette to abstain from attempting to influence Eemland's board.⁹⁶

The Commission determined that the transaction's change in the structure of the wet-shaving market weakened competition in the market and created new barriers to entry by precluding other competitors from acquiring Eemland or cooperating

mission scrutinized the transaction at issue under Articles 85 and 86 of the Treaty instead of the Merger Regulation, which only entered into force on September 21, 1990.

96. Compare Gillette, O.J. L 116/21 (1993) with *CCIE/GTE*, O.J. C 258/10, ¶ 30 (1992). In *CCIE/GTE*, the Commission found: (1) a buy-out of GTE's non-American light bulb and lighting fixture business by Citicorp's subsidiary CCIE and simultaneous disposal by GTE of its North-American lighting division to Siemens' subsidiary Osram (the latter transaction falling outside the scope of the Merger Regulation); (2) that Siemens provided bridge financing for more than one-half of purchase price in the form of a loan to Edil, Citicorp's vehicle for the acquisition, but acquired no representation on Edil's board or access to its confidential information; (3) the Commission assessed the competitive impact of the links between Siemens and Edil created by the loan financing and various post-closing agreements with a view to both excluding Siemens' joint control of Edil and to appraising the compatibility of the concentration, of which they formed an integral part. In concluding that Siemens would not acquire a "permanent, long-lasting and decisive" influence over Edil, the Commission noted *inter alia* that the loan agreement was of limited duration, involved no shareholder rights and no traditional creditor's right prior to maturity, 75% of the loan would only fall due after a three-year "grace period," and the provision of an interest rate increasing over time would constitute an incentive for Edil to re-finance to loan earlier than would otherwise be the case. *Id.*

with it.⁹⁷ As a result, the Commission decided that Gillette's participation in the purchase of the Wilkinson Sword business from Stora constituted an abuse of its dominant position in the European Union razor market.⁹⁸ The Commission further held that, although the acquisition by Gillette of the equity interest in Eemland did not in itself amount to a *Philip Morris*-like violation of Article 85, the concomitant agreements for the geographic separation of the Wilkinson Sword business and trademark between the European Union and neighboring countries would necessitate commercial cooperation between Eemland and Gillette. Such inevitable cooperation would be reinforced by a two-year supply arrangement, under which Gillette would obtain Wilkinson Sword products from Eemland for sale outside the European Union, and by the parties' obligations to refrain from selling products under the Wilkinson Sword trademark outside their respective territories. According to the Commission, these agreements violated Article 85(1) and were not eligible for an individual exemption under Article 85(3).⁹⁹ This decision required Gillette to dispose of its interests in Eemland as both shareholder and creditor within a fixed period. Furthermore, to

97. Gillette, O.J. L 116/21, at 28, ¶ 26 (1993). Compare with *Philip Morris*, [1987] E.C.R. at 4580-82, ¶¶ 53-56 (ruling that similar preemption rights would not allow PM to influence Rothmans by enabling it to prevent any third parties from acquiring Rothmans and thereby improving its competitive performance).

98. The Commission distinguished the facts in the case at issue from the relevant facts in *Philip Morris*, and reasoned that in the latter case the Court considered a situation in which a dominant position was held not by the acquiring company, as in Gillette, but by the entity in which the minority interest was acquired. Gillette, O.J. L 116/21, at 27-28, ¶ 24 (1993).

99. Compare Gillette, O.J. L 116/21 (1993) with *CCIE/GTE*, O.J. C 258/10, ¶¶ 12, 31-32 (1992). In order to recreate the position of GTE's non-American business, which prior to the planned concentration had access to the Research and Development ("R&D") of the North-American business and to Osram's technical information and patents pursuant to certain reciprocal patent licenses and technical information exchange agreements with Osram, Edil and Siemens entered into a number of non-reciprocal commercial agreements aimed at ensuring Edil's access to Osram's R&D expertise for a transitional ten-year period. *Id.* Osram and Edil also executed non-exclusive supply agreements for bulb parts and, for maximum four-year periods, new bulbs and parts at a competitive price in order to enable Edil to fill any gaps in its product range while building up its own R&D capacity. *Id.* The Commission found that such post-closing agreements might afford Siemens a certain influence over Edil but not a permanent or decisive one, since they only represented a "safety net" for the buy-out during the time necessary for Edil to build up its own financial resources and in-house R&D and to develop new lines of supply. The firms had built-in economic incentives to encourage Edil to develop its own capacity for R&D as quickly as possible.

prevent coordination of the parties' commercial conduct in neighboring markets, Gillette was required to reassign the Wilkinson Sword trademark to Eemland in the former East Germany, certain Central and East European countries, and Turkey.¹⁰⁰

Similar anticompetitive concerns seem to have prompted the Commission to object recently to the proposed acquisition by Dresser-Rand, a joint venture between the U.S. companies Dresser Industries and Ingersoll-Rand, of a 24% stake in Nuovo Pignone ("NP"), a business active in the gas turbine and compressor sectors that General Electric ("GE") bought from the Italian State holding company ENI in 1994.¹⁰¹ As originally planned, the deal involved ENI transferring its 69.3% shareholding in NP to a GE-led consortium that included Dresser-Rand,¹⁰² NP's main competitor in the worldwide compressor market. The transaction was later restructured to exclude any participation in NP by Dresser-Rand, due to intense opposition by labor unions and in order to obtain approval from the Commission.¹⁰³ After the merger had been cleared under the Merger Regulation on May 6, 1994,¹⁰⁴ however, GE asked the Commission to clear the transfer of a minority shareholding to Dresser-Rand, as envis-

100. See HAWK & HUSER, *supra* note 85, at 397-400 (identifying only influence "plus factor" in Gillette, vis-à-vis *Philip Morris*, in existence of broader non-EU cooperation agreements between parties that were apparently more likely to produce effects within European Union, but opining that these facts did not justify application of either Articles 85 or 86 of Treaty under *Philip Morris* influence test).

101. Commission Notice No. 94/C162/04, O.J. C 162/7 (1994) (GE/ENI/Nuovo Pignone (II)).

102. *GE Group Wins Nuovo Battle*, INT'L GAS REP., Jan. 7, 1994; *General Electric Consortium Acquires Majority Share of Nuovo Pignone*, PR NEWSWIRE PREDICAST PROMT, Jan. 24, 1994.

103. *Anti-Trust Commission Blocks Dresser-Ingersoll's Participation in Nuovo Pignone/General Electric Deal*, IL SOLE-24 ORE, Apr. 1, 1994, at 25. Accordingly, a former notification lodged by GE with the Commission on February 24, 1994 was withdrawn and a new notification was submitted by GE and ENI on April 5, 1994. Commission Notice, O.J. C 105/7 (1994). On April 21, 1995, the Commission announced that GE agreed to drop its plan to sell a minority stake in Nuovo Pignone to Dresser-Rand and to terminate the shareholders' agreement it had entered into with Dresser-Rand, as a precondition for the GE/ENI concentration to be approved under the Merger Regulation. *GE Agrees not to Sell Two 12 Pct Stakes in Nuovo Pignone*, AFP-EXTEL NEWS, Apr. 21, 1995.

104. GE/ENI/Nuovo Pignone (II), O.J. C 162/7 (1994). GE later increased its stake in NP to 78.46%, following a public offer to purchase the NP shares still on the market in February 1995. *Anti-Trust Authority Blocks Acquisition of Nuovo Pignone Stock by Dresser and Ingersoll*, IL SOLE-24 ORE, Apr. 22, 1995, at 28.

aged in the original plan.¹⁰⁵ According to press reports, the Commission eventually decided to block the transfer of the minority shareholding, taking the view that any cooperation between the two largest players in the market for gas compressors would contravene the EC Treaty's competition rules.¹⁰⁶ Unfortunately, since the Commission published no formal decision or press release on this matter, the details of the proposed minority acquisition remain secret, including the existence and scope of any board or management representation, or related post-closing cooperation agreements requiring the exchange of sensitive information. It is thus impossible to ascertain precisely how the Commission applied the influence standard.¹⁰⁷

In the event that an acquisition of a minority shareholding or other corporate governance rights in a company to be privatized not involving a dominant firm raises any competitive concerns under Article 85(1) of the EC Treaty, the transaction in question may be notified to the Commission and an individual exemption may be obtained under Article 85(3) if it results in efficiencies or other pro-competitive benefits offsetting its restrictive effects.¹⁰⁸

4. Acquisition of Influence over an Enterprise To be Privatized by Way of a Minority Shareholding Acquisition or Other non-Joint Venture Arrangement: The Requirements for Application of Articles 85 and 86 of the EC Treaty

In light of the Commission's evolving policy, the following comments can be made in relation to the application of Articles 85 and 86 of the EC Treaty to minority stock acquisitions and other commercial arrangements aimed at acquiring an influence

105. *GE Says Still Wants to Sell Part of Nuovo Pignone*, REUTER NEWS SERVICE - WESTERN EUR., May 8, 1994; *GE Bids for Rest of Nuovo Pignone, Receives Formal Bid for Outstanding Shares from General Electric*, PR NEWswire PREDICAST PROMT, June 30, 1994.

106. *Brussels Blocks Pignone Plan*, INT'L GAS REP., Apr. 28, 1995; *Anti-Trust Authority*, *supra* note 104.

107. For example, whether under the restructured transaction plan, Dresser-Rand's investment was intended to be purely passive.

108. *E.g.*, Commission Decision No. 92/C333/03, O.J. C 333/3 (1992) (STET, Italtel-SIT, AT&T, AT&T-NSI) (notice pursuant to Article 19(3) of Regulation 17/62 informing any interested third parties of Commission's intention to grant an individual exemption to technological and commercial cooperation agreements among parties in field of telecommunications agreements).

over an enterprise to be privatized, such as cross-shareholdings, interlocking directors or managers, non-voting equity interests, and financing agreements.

First, the single investor or "hard-core" syndicate must be in a competitive relationship, or at least in a vertical seller-buyer relationship, with the business in which the minority shareholding or other corporate governance rights are acquired.¹⁰⁹ Second, since Article 85 only applies to agreements and concerted practices among undertakings, open market share purchases fall outside its scope; also, the acquisition of a minority interest by a dominant enterprise in a competitor to be privatized would seem more likely to result in effective control over the target, or at least some influence on its commercial policy, in violation of Article 86, than the acquisition of a minority shareholding by a competitor in a dominant enterprise to be privatized. Finally, the minority acquisition or commercial arrangement in question must not constitute a purely passive investment conveying no rights to exercise any influence over the target's commercial behavior. An investment may be defined as "passive" if all of the following "safe harbor" requirements are met: (1) no voting stock or other voting interest, no board or management representation, and no access to sensitive internal information of the enterprise to be privatized is acquired; (2) if the acquisition is carried out in the framework of a broader transaction in which the passive investor also provides substantial financing to the target, the investor does not obtain conversion or preemption rights potentially affecting the target's voting share capital, or creditor's rights beyond the usual creditors rights, such as the right to accelerate repayment or to place the debtor into bankruptcy for failure to make interest or principal payments; and (3) the investor and the undertaking to be privatized do not enter into cooperation agreements requiring post-closing performance, such as joint research and development, manufactur-

109. *Mediobanca/Generali*, [1994] 4 C.M.L.R. at M1-M3. The Commission decided not to review, under Articles 85 or 86 of the Treaty, the minority acquisition by *Mediobanca* in combination with the non-voting shareholders' agreement with *Euralux*. Presumably, however, the transaction conferred on *Mediobanca* at least "some influence" over *Generali's* commercial policy. *Id.* It may be argued that the Commission took the view that the Treaty competition rules were inapplicable in the absence of any significant horizontal or vertical relationship between the acquirer and the acquired entity. *Id.*

ing, distribution, cross product supplies, and exchanges or licensing of intellectual property rights that have significant effects within the European Union. By contrast, if one or more of these conditions are not met, including the "no voting stock" condition, notwithstanding the fact that the acquisition of voting stock below 25% was sanctioned in *Philip Morris*, it would seem that, depending on the legal and factual circumstances of the case, the investing company may be found to be in a position to exercise "some influence" over the undertaking to be privatized.

C. *Special Issues Raised by the Privatization of Enterprises Holding a Dominant Position Prior to Privatization*

Almost inevitably, the process of privatization will involve state-owned companies that, before their outright or partial transfer to private owners, hold a monopoly¹¹⁰ or a dominant position. It is submitted that, in such cases, market dominance will usually be the consequence of exclusive or special rights granted to the entity to be privatized by a national public authority rather than the result of internal growth in competitive conditions. Accordingly, a breaking-up of the dominant undertaking will often be the best means of ensuring that privatization does not lead to the replacement of a public monopoly with a private monopoly.¹¹¹

The mere transfer by the state of control over a monopolist or dominant enterprise to the private sector should not amount to a *per se* "creation of a dominant position" within the meaning of Article 2(3) of the Merger Regulation, since the dominant position existed prior to the privatization of the acquired company, the conduct of which was already subject to scrutiny under

110. *E.g.*, "Telemarketing", Case 311/84, [1985] E.C.R. 3261. According to the well-established case law of the Court of Justice, an undertaking that holds an exclusive right in a substantial part of the common market can be regarded as in a dominant position within the meaning of Article 86. *Id.* An exclusive right covering the whole territory of a Member State certainly covers a substantial part of the common market, and a part of a Member State's territory may amount to a substantial part of the Common Market. *E.g.*, *Merci Convenzionali Porto di Genova v. Siderurgica Gabrielli*, Case C-179/80, [1991] E.C.R. I-5009 (holding that port of Genova was substantial part of common market); *Accord*, *Corsica Ferries Italia v. Corpo dei piloti di Genova*, Case C-18/93, [1994] E.C.R. I-1783, ¶ 41.

111. Guislain, *supra* note 26, at 121; *see* Commission Decision, O.J. C 334/23 (1991) (Campsa).

Articles 86 and 90 of the EC Treaty.¹¹² If, in the framework of a concentration involving a monopolist or dominant firm, or a minority acquisition not conferring control, the acquirer is a competitor, a supplier, or a customer of the acquired firm or is an entity-holding conglomerate power, there may be a risk that the transaction will reinforce the acquired firm's pre-existing dominant position.

1. Acquisition of Sole or Joint Control of a Monopoly to be Privatized: Substantive Assessment of the Transaction under the Merger Regulation

As mentioned above,¹¹³ the Merger Regulation provides that a concentration must be declared incompatible with the common market and blocked if it either creates or strengthens a dominant position as a result of which effective competition would be significantly impeded in a relevant market within the Community. Indeed, if a high degree of dominance exists in the markets affected by a concentration, "the Commission must be particularly vigilant because in such circumstances even a very small increase in market power can have a disproportionately large negative effect on the competitive conditions on the market place."¹¹⁴ Accordingly, the Commission's policy is that a merger-to-monopoly or a concentration otherwise strengthening a dominant position already held by one or more of the combining entities may only be approved subject to structural or behavioral undertakings from the parties to the concentration,¹¹⁵ facil-

112. Conversely, it is possible that the privatization of a non-dominant firm results in the creation of a dominant position held by the combined entity on one or more of the markets affected by the concentration, irrespective of whether the acquirer was itself dominant before the transaction. The creation of a dominant position as a result of a concentration, however, does not necessarily imply that the transaction is incompatible with the common market.

113. See *supra* notes 29-46 and accompanying text (describing the Merger Regulation).

114. Commission Decision No. 91/535/EEC, O.J. L 290/35 (1991) (Tetra Pak/Alfa-Laval).

115. Merger Regulation, *supra* note 5, art. 8(2), O.J. L 395/1, at 6 (1989). The Commission may approve notified concentration conditional upon modifications to the original project and attach to its final, second-phase decisions, "conditions and obligations intended to ensure that the undertakings concerned comply with the commitments they have entered into vis-à-vis the Commission with a view to modifying the original concentration plan." *Id.*; see *supra* note 31 (discussing second-phase decisions); see, e.g., Kali+Salz/MdK/Treuhand, O.J. L 186/38 (1993). In order to resolve the Commission's concern that the acquisition by K+S of its ailing state-owned competitor MdK

itating entry by new competitors.

In light of the substantive analysis carried out by the Commission under the Merger Regulation,¹¹⁶ a tentative catalog of the factors to be taken into account in assessing the risk that a dominant position held by a privatized enterprise would be strengthened would include the following. First, with respect to the horizontal effects in concentrations involving competing firms: (1) the risk that the concentration would lead to an increase in a dominant undertaking's market shares or market power.¹¹⁷ One example would be the case where, through a tied

would lead to a situation of oligopolistic dominance by K+S and the French company EMC/SCPA in the Community market for agricultural potash outside of Germany, K+S and the new joint venture agreed: (1) to withdraw from Kali-Export, an export joint venture set up in Austria for the coordination of the sales of K+S and EMC/SCPA outside the European Union; (2) to terminate its distribution arrangement with EMC/SCPA and set up its own supply network in France; and (3) to use its best efforts to renegotiate the terms of an existing Canadian joint venture with EMC/SCPA to ensure that its parents could sell its potash production independently in the Community. These undertakings were challenged by EMC/SCPA before the Court of First Instance, which by interim order found that the withdrawal of K+S and the new entity from Kali-Export would cause irreparable injury to the applicant because it would lead to the dissolution of Kali-Export. The Court of First Instance, therefore, stayed the implementation of the relevant part of the Commission decision until it pronounces on the substance of the appeal. *Société commerciale des potasses et de l'azote and Entreprise Minière et Chimique v. Commission*, Case T-88/94 R, [1994] E.C.R. II-401 (Ct. First Instance). As of March 1, 1995, any proposed modifications to an original concentration plan must be submitted by the parties to the Commission within three months of the date of initiation of proceedings. Commission Regulation 3384/94 on the notifications, time-limits and hearings provided for in the Merger Regulation, Commission Regulation No. 3384/94, art. 18(1), O.J. L 377/1 (1994). In *Air France/Sabena*, the Commission accepted for the first time undertakings from a third party to a concentration (namely, the French Government). *Air France/Sabena*, Case IV/M517, [1994] 5 C.M.L.R. M1. Moreover, in a number of cases the Commission accepted commitments made by the parties in order to remedy clear-cut competition problems within the one-month initial examination with a view to avoiding the commencement of formal proceedings.

116. *Air France/Sabena, Kali+Salz/Mdk/Treuhand and EniChem/Union Carbide* actually involve a total or partial privatization of the company subject to a change in control. *Air France/Sabena*, Case IV/M517, [1994] 5 C.M.L.R. M1; *Kali+Salz/MdK/Treuhand*, O.J. L 186/38 (1993); Commission Decision No. 95/C 123/05, O.J. C 123/3 (1995) (*EniChem/Union Carbide*). In *AT&T/NCR and Mannesmann/VDO*, however, a dominant undertaking was involved in the concentration as the acquired entity. Commission Decision No. 91/C 16/15, O.J. C 16/20 (1991) (*AT&T/NCR*); Commission Decision No. 92/C 88/10, O.J. C 88/13 (1992) (*Mannesmann/VDO*).

117. *E.g., Air France/Sabena*, Case IV/M517, [1994] 5 C.M.L.R. M1, ¶¶ 54-57. The Commission reasoned that the establishment by the two airlines of a jointly run "hub and spoke" network (i.e., a system of flights at least twice a day to and from 75 European destinations), centered on the Brussels National Airport, could strengthen the dominant position held by Air France and Sabena on all of the existing routes

sales policy, the product in relation to which dominance exists would be supplied as part of a comprehensive package to promote sales of the combined entity's other products,¹¹⁸ particularly regarding the conditions in the industry in question,¹¹⁹ and

between Belgium and France by making their flights the most practical for users in transit and making entry to the routes concerned by third-party competitors very difficult. *Id.* Eventually the transaction was approved in light of the commitment offered by the French government to allow, if any competing airline would so demand, the creation or development in Northern France of an integrated network comparable to the planned Brussels-based "hub and spoke" network. *See* *EniChem/Union Carbide*, O.J. C 123/3, ¶¶ 47, 52 (1995). The Commission authorized the formation of a joint venture by and between Union Carbide and Enichem, a subsidiary of the Italian state-owned holding company ENI, in which the parents pooled their polyethylene activities. *Id.* The Commission held that the proposed transaction would not strengthen the pre-existing arguably dominant position of Enichem in the upstream market for the production and supply of ethylene in Italy, because Union Carbide did not produce ethylene in Western Europe and would not contribute any ethylene facilities to the new entity. *Id.* *See also* Commission Decision No. 91/C5/04, O.J. C 5/7, ¶¶ 13-15 (1991) (*Mitsubishi/UCAR*). The Commission ruled out that the proposed joint venture would lead to a strengthening of UCAR's arguably dominant position on the EU markets for graphite electrodes and graphite specialties because Mitsubishi's pre-concentration share of these markets was negligible and its trading expertise would not significantly strengthen the dense and comprehensive distribution network of UCAR in Europe. Commission Decision No. 93/C104/06, O.J. C 104/10, ¶¶ 25-28 (1993) (concerning establishment of joint venture pooling parents' activities in fields of colors and coatings for ceramics and glass, including silver pastes). The Commission ruled out that the proposed transaction would strengthen Degussa's arguably dominant position in the EU markets for glass colors and silver pastes as the new entity's market shares would increase by less than 10% and 5%, respectively, Ciba/Geigy was active in only a few Member States before the transaction, and there was no indication that the concentration would reduce the alternatives available to industrial purchasers of the relevant products. *Id.*

118. *E.g.*, Commission Decision, O.J. C 37/3, ¶¶ 35-42 (1995) (*Akzo Nobel/Monsanto*). The Commission authorized the formation of a joint venture between Akzo Nobel and Monsanto to produce rubber chemicals, which are used principally in the production of tires. *Id.* The Commission ruled out the possibility that the transaction would strengthen Akzo Nobel's arguably dominant position in the EU market for insoluble sulfur, in which Monsanto had no interest prior to the transaction, and noted that despite the lack of product substitutability for insoluble sulfur due to its specific properties, Akzo Nobel had never in the past supplied it as part of a "package" with its other rubber chemical products, or offered discounts and rebates over a range of products including insoluble sulfur, and there was no reason to suppose that the new entity would start selling the product on a different basis. *Id.* Furthermore, the combined entity's market power would be restrained by actual or potential competition from several independent producers both within and outside of the European Union. *Id.*

119. *E.g.*, Commission Decision, O.J. C 59/13 ¶ 14 (1991) (*Aérospatiale/MBB*) (concerning creation of joint venture grouping civil and military helicopter business of two parent companies). The Commission took the view that the transaction would not strengthen the monopoly position held by Aérospatiale and MBB in their respective home markets for military helicopters because, in light of the national fragmentation

(2) the risk that a non-dominant party to the transaction that is a significant actual or potential competitor would disappear from the market as a result of the concentration,¹²⁰ or that the dominant undertaking would obtain access to competitively significant know-how in the possession of another party to the transaction.¹²¹ Second, with respect to the vertical effects of concentra-

peculiar to the defense industry, neither of the two parents was an actual or foreseeably potential competitor of the other. *Id.*

120. *E.g.*, O.J. C 65/3, ¶¶ 26-31 (1995) (Glaxo/Wellcome). Clearing Glaxo's public bid for the acquisition of its competitor Wellcome, the Commission reasoned that the proposed concentration would not strengthen Glaxo's arguably dominant position in some national markets for anti-migraine drugs because: (1) the removal of Wellcome's competing product, which has been off-patent for over 20 years and is supplied in generic or branded form by a number of other competitors, would have no significant impact on the competitive conditions of the market; (2) although both Glaxo and the acquired company have two new anti-migraine drugs in an advanced phase of clinical trials, Glaxo resolved any possible anticompetitive concerns by undertaking to grant an exclusive license to a third party to develop and independently market one of the two most promising new drugs; and (3) several competitors of the new entity also have anti-migraine compounds under research and development. *Id. See also* Union Carbide/Enichem, O.J. 123/3, ¶¶ 62-81 (1995). In Union Carbide/Enichem, the Commission stated that, although in the framework of the proposed combination Enichem would cease to offer its own polyethylene ("PE") technology for license within Western Europe, this would not result in a strengthening of Union Carbide's arguably dominant position in the worldwide PE technology market, founded on its proprietary gas-phase PE process. The Commission opined that Enichem had never been particularly active on the technology licensing market and its technologies are distinct from, or not comparable to, Unipol. The Commission further reasoned that, to the extent that there will still be demand in the high-pressure segment of the market, other technologies comparable to Enichem's are offered by certain competitors; in addition, no cross-fertilization was expected between Unipol and Enichem's low-pressure slurry technology, given the fundamental technical differences between the two processes. The Commission finally reasoned that the experiments made by Enichem in the area of gas-phase technology have never been developed to the level of commercial production. *Id. See* Mitsubishi/UCAR, O.J. C 5/7, ¶ 15 (1991) (holding that withdrawal of Mitsubishi as a trading company from UCAR's markets would not endanger possibility of other Japanese producers selling their products on EU markets as they already did).

121. *See, e.g.*, Commission Decision, O.J. C 88/13, ¶¶ 27-30, 36-37 (1992) (Mannesmann/VDO). The Commission noted that the acquisition by major German conglomerate Mannesmann of a majority of the voting shares of VDO, an important German manufacturer of mechanical, electrical and electronic information and control systems for the automobile industry, in concluding that the concentration would not strengthen either the arguably dominant position held by VDO in the German markets for (1) instrument panels; (2) liquid level sensors; or (3) Mannesmann's possible dominant position in the German tachography market, the Commission reasoned that Mannesmann could not be viewed as a significant potential competitor of VDO as, according to the industry expectation, in the long run existing technology would be substituted by new purely electronic instrument panels so that potential competitors would not consider it worthwhile to invest in old technology. Moreover, Mannesmann's disap-

tions between firms not competing on the market of the dominant undertaking, or in a supplier-to-customer relationship with each other: (1) the ability of the new entity to offer a fuller product range as a result of the combination of the complementary product ranges of the parties to the concentration, thereby limiting actual or potential competition, particularly if the market of the dominant firm is characterized by high entry barriers of a technical or commercial nature;¹²² (2) the ability of parties to the concentration with strong positions in upstream product markets to make access to their goods or services more difficult for non-integrated competitors of another party to the concentration active and dominant in a downstream market,¹²³ thereby

pearance as a potential competitor to new electronic products was not significant as a number of other independent potential competitors remained both within and outside the Community and the concentration would not allow VDO to get access to specific know-how belonging to Mannesmann. The Commission also relied on the absence of material barriers to entry of a technical nature with respect to the German market for liquid level sensors, which are relatively simple products, and the existence of potential competition existed since liquid level sensors do not represent significant vehicle components so that no consumer preferences, technical, or marketing reasons existed for car manufacturers not to purchase products produced captively by other car manufacturers. *Id.*

122. See, e.g., Tetra Pak/Alfa-Laval, O.J. L 290/35, at 39-41, ¶¶ 3.5-5.2 (1991). The Commission particularly noted the acquisition of the entire share capital of Alfa-Laval, a Swedish manufacturer of food processing equipment, by packaging equipment manufacturer Tetra Pak. The Commission found that Tetra Pak held a dominant position on the Community market for aseptic carton packaging machines, and in the separate but related market for carton blanks, but that the proposed concentration would not confer on the combined entity "an advantage of real significance that would be likely to further increase the difficulty of entry or penetration of actual or potential competitors" because historically there were very few simultaneous purchases of processing and packaging equipment from the same source, the interface between the two being relatively simple, there were a number of strong competitors in the processing equipment market, and the customers (diaries and juice processors) had significant buying power. See also, e.g., Akzo Nobel/Monsanto, O.J. C 37/3, ¶¶ 26-28, 42 (1995). In *Akzo Nobel/Monsanto*, the Commission held that the new entity's capability to provide a complete product range of rubber chemicals would not lead to a strengthening of Akzo Nobel's arguably dominant position in the EU market for insoluble sulfur because, despite tire manufacturers' tendency to conduct commercial negotiations on an across-the-board basis, certain competing manufacturers of single rubber chemicals had recently entered and obtained increasing shares in their respective market segments. *Id.* See *Mannesmann/VDO*, O.J. C 88/13, ¶¶ 28, 30 (1992) (finding that proposed concentration would not strengthen dominant position held by VDO and Mannesmann in German markets for instrument panels and tachographs, respectively, because combined sales of two products were possible only in one market segment representing less than 10% of total market and certain competitors were able to offer both products).

123. An example would be where A, enjoying significant market power in the upstream market for gypsum, combines with B, which is dominant in the downstream

strengthening the combined entity's position in the downstream market;¹²⁴ and (3) the ability of a dominant firm operating in an

market for plasterboard. As a result of this concentration, the new entity may make access to gypsum more difficult for its competitors in the plasterboard market that are not also integrated upstream.

124. See, e.g., Commission Decision, O.J. C 16/20, ¶¶ 15-16 (1991) (AT&T/NCR). The Commission cleared the contested takeover bid for NCR launched by AT&T. In analyzing whether the upstream integration of AT&T's activities, particularly its copyrighted UNIX open operating system software that is used *inter alia* in a number of workstation systems, could strengthen NCR's dominant position in the EU market for financial and retail workstations by restricting NCR's competitors' access to UNIX, the Commission put considerable emphasis on the continued availability to AT&T's competitors of UNIX through AT&T's policy of granting, usually irrevocable, paid-up licenses to all major computer manufacturers, who, moreover, were cooperating with each other to develop a competing open operating system software. *Id.* See also Commission Decision No. 04/022/EC, O.J. L 364/1, 16, ¶¶ 82-93 (1994) (MSG Media Service). In MSG Media Service, the Commission declared a proposed joint venture to provide digital pay-TV services incompatible with the Common Market. MSG was set up by and among Bertelsmann, the German telecommunications monopoly Deutsche Bundespost Telekom ("DBT") and the Kirch group. The Commission found, *inter alia*, that MSG's expected dominance on the market for pay-TV technical and administrative services would strengthen the already "extraordinarily strong," "leading" position of Bertelsmann and Kirch on the downstream pay-TV market because: (1) potential new entrants would be forced to use pay-TV services under terms, conditions and prices controlled by their strongest competitors via the new entity; (2) DBT would be able to favor the pay-TV programming of Bertelsmann and Kirch through its power over the input of competing pay-TV programs into its broadband cable network, especially in the first few years when transmission capacity for digital signals will be somewhat limited; and (3) Bertelsmann and Kirch would be in a position to influence consumers' choice of pay-TV programs through MSG's control of the decoder and the on-screen modulator, which gives the user guidance as to the various programs offered or through MSG's control over the "smart cards" that users will have to insert into the decoder in order to have access to programs. *Id.* The Commission also found that the creation of MSG would lead to a strengthening of DBT's dominant position resulting from its statutory monopoly on laying and operating cable networks in public road, by making it more difficult for private cable network operators to penetrate the market since they could not obtain their programs, which are required for attractive program packages, thereby slowing the competition that might occur after the expected liberalization and deregulation of the cable network market. *Id.* See also Commission Decision, Case IV/M490, Nordic Satellite Distribution, slip op. ¶¶ 113-132 (Eur. Comm'n July 19, 1995) [hereinafter NSD]. In *Nordic Satellite Distribution*, the Commission declared the setting-up of NSD incompatible with the Common Market. NSD was a joint venture to operate in the markets for the provision of transponder capacity to broadcasters, the operation of cable TV networks, and the transmission and distribution of satellite pay-TV and other encrypted TV channels to direct-to-home households in the Nordic region, by and between Norsk Telekom, a subsidiary of the state-owned Norwegian telephone and television service provider Telenor, Tele Denmark, the state-owned Danish telecommunications monopoly that also holds a legal monopoly on the ownership of commercial cable TV infrastructure and the transmission of TV signals by cable across municipal borders, and Kinnevik, a Swedish private conglomerate active also in the sector of satellite TV broadcasting and distribution. *Id.* The Commission took the

upstream market to acquire a substantial competitive advantage by combining its activities with those of another party to the concentration, which operates in a downstream market, thereby strengthening the combined entity's position in the downstream market.¹²⁵ Third, and finally, with respect to the conglomerate effects of the transaction, the risk that the market position of the dominant undertaking to be privatized will be strengthened by the know-how, manufacturing, or marketing capacity of the acquiring company or group, or its financial power.¹²⁶

Approval of a concentration that strengthens the dominant position held by the acquired company is unlikely to be permitted under the "failing company defense," since, by definition, a failing company is unlikely to be dominant. On the other hand, the Commission may apply this defense to transactions that strengthen a dominant position held by the acquirer com-

view, *inter alia*, that since the proposed joint venture would hold a dominant position in the transponder market in the Nordic countries, Tele Denmark's dominant position in the Danish market for the operation of cable TV networks would be strengthened by the proposed transaction because any competing independent cable TV operators would have henceforth to negotiate with NSD the terms, conditions and prices for obtaining the TV channels, and, therefore, NSD would be in a position to discriminate against them in favor of Tele Denmark. *Id.* See Mitsubishi/UCAR, O.J. C 5/7, ¶ 15 (1991) (finding that proposed joint venture would not lead to a strengthening of UCAR's arguably dominant position on EU markets for graphite electrodes and graphite specialties *inter alia* because Mitsubishi's position in upstream markets, in particular market for calcined needle petroleum coke, was not dominant and these markets were competitive so that new entity's competitors would be able to have unrestricted access to them).

125. See, e.g., MSG Media Service, O.J. L 364/1, at 17, ¶ 89 (1994) (finding that MSG's expected dominance on the market for pay-TV technical and administrative services would also strengthen the leading market position of Bertelsmann and Kirch on the downstream pay-TV market because, *inter alia*, Bertelsmann and Kirch could acquire via MSG substantial information on the pay-TV customer structure and viewer behavior, which would make it much easier to develop target-group-oriented programs or program packages, through their access to the subscriber data handled by MSG's subscriber management system).

126. See, e.g., AT&T/NCR, O.J. C 16/20, ¶¶ 23-31 (1991) (ruling out that NCR's dominant position in the market for workstations would be strengthened by its combination with AT&T's strength in the telecommunications and network processing businesses because, despite the important role played by networking in setting up workstation systems, AT&T had a limited presence on the Community telecommunications markets, synergies stemming from other combinations of computer and telecommunications business in the industry had proved hitherto "theoretical," and the new entity would face a number of important competitors), and *Mannesmann/VDO*, C 88/13, ¶¶ 28, 30 (1992) (finding that the possible strengthening of the combining parties' market position brought about by the proposed concentration would not affect their competitive position since certain competitors enjoyed even greater financial strength).

pany.¹²⁷

Interestingly, some of the above indicia of the strengthening of a pre-existing dominant position seem to relate to potential behavioral rather than structural aspects of the transaction, and thus seem to be more relevant to an assessment of abuse of dominant position under Article 86 of the EC Treaty than to an assessment under the Merger Regulation.¹²⁸ Some examples are: (1) the possibility that the concentration would enhance a dominant undertaking's market power through a tied sales policy operated by the combined entity; (2) the power of a party to the transaction operating in an upstream market to refuse to sell; and (3) the imposition of discriminatory prices or other discriminatory sales conditions on competitors of another party dominant in a downstream market.¹²⁹

2. Acquisition of Limited Influence over an Enterprise to be Privatized: Substantive Assessment of the Transaction under the EC Treaty Rules

A dominant undertaking may be partially privatized in a way that does not constitute a concentration, for example, through the transfer of a minority shareholding or other commercial arrangements, like cross-shareholdings, shared directors or managers, non-voting equity interests, or financing agreements that are intended to give a private acquirer limited influence, but not control, over the commercial conduct of the undertaking to be privatized. In such cases, the risk that the privatization, which

127. See *Kali+Salz/MdK/Treuhand*, O.J. L 186/38, at 45-53, ¶¶ 46-50, 70-90, 95 (1993) (approving the acquisition by K+S of the ailing company MdK, a company held in trust by the Treuhandanstalt which combined the potash and rock salt activities of the former German Democratic Republic, despite the fact that it would strengthen K+S' dominant position in the German market for agricultural potash; the Commission took the view that this would have happened even in the absence of the transaction as MdK would have ceased production and its market share would have been captured by K+S, which was the only other significant supplier on that market, since despite strenuous efforts by an investment bank no other company had made a competing offer for MdK).

128. See *Union Carbide/Enichem*, O.J. 123/3, ¶ 53, 84 (1995) (making this statement with respect to the possible concerns that the creation of the planned joint venture would create an incentive for either Enichem or the new entity to curtail their ethylene supplies to third parties in the future, or for Union Carbide to cease to make available for license to third parties in Western Europe the Unipol gas-phase PEE process technology, for which a non-exclusive license was granted to the joint venture).

129. *Id.*

the Merger Regulation is inapplicable to,¹³⁰ may lead, as a result of one or more of the factors discussed above, to the strengthening of a dominant position held by a state-owned firm would not seem to constitute an infringement of the prohibition of abuse of a dominant position in Article 86 of the EC Treaty.

Even in the absence of any abusive conduct by the dominant undertaking to be privatized, however, the sale by a Member State of a minority shareholding to one of its competitors, suppliers, customers, or an entity holding conglomerate power may constitute a violation of Article 86 of the EC Treaty. Indeed, where such a transaction leads to the strengthening of the acquired company's dominant position, the privatization may amount to a state "measure" violating Article 86 of the EC Treaty in conjunction with Article 90(1).

In addition, Article 85(1) will be applicable to the extent that the minority acquisition or other non-joint venture arrangement is capable of acting as an instrument for the coordination of the commercial conduct of the dominant company and its acquirer. The strengthening of a pre-existing dominant position will thus only be relevant under Article 85(1) if it is the result of such unlawful coordination.

a. Article 85(1) of the EC Treaty

As mentioned above, Article 85(1) focuses on whether an agreement or concerted practice¹³¹ between independent undertakings that is capable of affecting trade between Member states has as its purpose or effect an appreciable restriction or distortion of competition within the European Union. In other words, if the undertakings involved in the concerted action intend, or are led, to cease to determine independently their commercial policies in a manner that affects normal market conditions.¹³²

130. See *supra* notes 85-109 and accompanying text (examining application of Articles 85 and 86 of EC Treaty to acquisitions of influence short of control).

131. ICI v. Commission, Case 48/69, [1972] E.C.R. 619, ¶ 64. "Concerted practice" means "a form of coordination between undertakings which, without having reached the stage where an agreement properly so-called has been concluded, knowingly substitutes practical cooperation between them for the risks of competition." *Id.* See also, Coöperatieve vereniging Suiker Unie v. Commission, Joined Cases 40-48, 50, 54-56, 111, 113 and 114/73, [1975] E.C.R. 1663, ¶¶ 173-74; Rhône-Poulenc v. Commission, Case T-1/89, [1991] E.C.R. II-867, ¶ 121.

132. EC Treaty, *supra* note 1, art. 85(2)-(3), [1992] 1 C.M.L.R. at 627. Any agree-

As previously mentioned, even the acquisition by way of an agreement of a minority equity interest in a competitor, including a dominant firm, may fall within the scope of Article 85(1) of the EC Treaty to the extent that it could operate as an instrument for coordinating the commercial conduct of the companies involved. One example would entail allowing an acquirer direct access to sensitive information relating to the activities of a competitor.¹³³ The risk of coordination between the companies involved is particularly severe if they operate, or are the leading players in, an oligopolistic industry, in which such a minority acquisition might not only destroy the pre-existing balance between the businesses present in the market, but might also prevent competitors from acquiring financial control of the target. Moreover, the investing company cannot be expected to endanger its investment by competing strenuously with a firm in which it has a substantial shareholding.

Because the focus of Article 85(1) is the prohibition of anticompetitive cooperation, it has few implications in situations where a minority interest is acquired in a dominant undertaking by one of its competitors, suppliers, or customers, despite the risk that such an acquisition may result in a strengthening of the target's market power. Indeed, Article 85(1) is concerned not so much with structural changes in the market-place brought about by concerted action by independent operators as with its behavioral aspects, or the coordination of their commercial policies.

Article 85(1) of the EC Treaty thus applies to restrictive concerted action by independent undertakings even in the absence of market dominance. The scope of Article 85(1)'s substantive test is "the prevention, restriction or distortion of competition within the common market." The two-pronged test of Article 2(3) of the Merger Regulation, which is "the creation or strengthening of a dominant position as a result of which effec-

ments in violation of Article 85(1) are automatically void, unless granted exemption by the Commission. See generally ABA Antitrust Section, *Antitrust Law Developments* 921-49 (3d ed. 1992).

133. *Philip Morris*, [1987] E.C.R. at 4487. Philip Morris promulgated a test whereby such a restriction or distortion of the competitive conditions of the market may arise where the agreement in question gives the acquirer an opportunity to reinforce its position at a later time, thereby eventually taking effective control, or creates a structure likely to be used for commercial cooperation between the parties, or where the acquisition of the shareholding requires the two companies to take account of each other's interests when determining their commercial policy. *Id.*

tive competition would be significantly impeded in the common market or in a substantial part of it," is much less broad. Conversely, if a concentration involving a dominant state-owned undertaking results in "no creation or strengthening of a dominant position, the transaction must be authorized, without there being any need to examine the effects of the transaction on effective competition."¹³⁴

Moreover, the substantive test in Article 2(3) of the Merger Regulation focuses exclusively on the foreseeable structural effect of a proposed concentration, whereas no effect on competition is necessary for the application of Article 85(1), since its prohibition extends to agreements whose purpose is anti-competitive,¹³⁵ regardless of whether that purpose is in fact achieved.¹³⁶

In sum, an agreement for the purchase of a minority shareholding in a dominant enterprise to be privatized by one of its competitors, suppliers, or customers that would lead to a strengthening of the privatized entity's dominance, will violate Article 85(1) of the EC Treaty. That violation depends, however, on the surrounding circumstances and the precise context of the transaction, whether such strengthening is "the object or effect" of the parties' coordination of their commercial conduct. Violations of Article 85(1) may be found where the share purchase agreement creates a "two-way" flow of sensitive competitive information between the parties, enabling the dominant undertaking to access specific know-how, manufacturing or marketing capacity, or the financial power of its shareholder, or where the acquirer is a strong player in an upstream product market and starts making access to its goods or services more difficult for the non-integrated competitors of the dominant undertaking in a

134. *Air France v. Commission*, [1994] E.C.R. II-323, ¶ 79.

135. *E.g.*, *Compagnie Royale Asturienne des Mines v. Commission*, Joined Cases 29 & 30/83, [1984] E.C.R. 1679, ¶ 26. According to the case law of the Court of Justice, in order to determine whether an agreement has as its object a restriction of competition it is necessary to assess not the subjective intent of the parties at the time when the agreement was concluded, but rather the aims objectively pursued by the agreement as such, in the light of the economic context in which it is to be applied. *Id.*

136. *E.g.*, *Etablissements Consten and Grundig-Verkaufs v. Commission*, Joined Cases 56 & 58/64, [1966] E.C.R. 299, 342. "[T]he offense involved is a pure "conduct" offense so that it is not necessary to attempt to explain the actual effects of the agreement". *Rhône-Poulenc v. Commission*, [1991] E.C.R. at II-922. On the other hand, if the anticompetitive effect of an agreement between undertakings is established, proving that the agreement also has an anticompetitive object as well is unnecessary. *Id.* at 923.

downstream market. This is particularly evident through concomitant cooperation agreements requiring post-closing performance, such as supply or technical support agreements or licenses of intellectual property rights.

b. Article 86 of the EC Treaty

Article 86 of the EC Treaty prohibits abusive conduct by dominant undertakings, which include unilateral practices involving a direct exploitation of market power or otherwise result in a substantial reduction in competition on a relevant market within the European Union, or a substantial part thereof, to the detriment of customers or suppliers.¹³⁷ Where the abusive conduct takes place by way of concerted action or the execution of formal agreements, such as with non-dominant third parties on which the dominant firm imposes its will, either Article 85 or 86 of the EC Treaty, or both, will be applicable, "taking into account the nature of the reciprocal undertakings entered into and the competitive position of the various contracting parties on the market or markets on which they operated."¹³⁸

Market dominance, as such, is not prohibited by Article 86.¹³⁹ A dominant firm's strengthening of its market position through conduct that affects the structure of competition in the relevant market, reducing the opportunities for effective

137. See generally, ABA ANTITRUST SECTION, ANTITRUST LAW DEVELOPMENTS 949-57 (3d ed. 1992). "Abuse" for the purpose of Article 86 indicates "the behaviour of an undertaking in a dominant position which is such as to influence the structure of a market where, as a result of the very presence of the undertaking in question, the degree of competition is weakened and which, through recourse to methods different from those which condition normal competition in products or services on the basis of the transactions of commercial operators, has the effect of hindering the maintenance of the degree of competition still existing in the market or the growth of that competition". *Hoffmann-La Roche & Co. v. Commission*, Case 85/76, [1979] E.C.R. 461, ¶ 91.

138. *Hoffmann-La Roche*, [1979] E.C.R. at 550, ¶ 116. See also *Ahmed Saeed Flugreisen and Silver Line Reisebüro v. Zentrale Zu Bekämpfung Unlauteren Wettbewerbs*, [1989] E.C.R. 803, ¶ 37. The Commission applied Article 86 of the Treaty to the behavior of undertakings on an oligopolistic market which it also found to have indulged in concerted action contrary to Article 85(1). *Commission Decision No. 89/93/EEC*, O.J. L 33/44 (1989) (*Flat Glass*). This approach was upheld in principle by the Court of First Instance on appeal, although on the facts the Court quashed the Commission's finding of a collective dominant position and stated that in order to establish an infringement of Article 86 it was not sufficient to "recycle" the facts constituting an infringement of Article 85. *Società Italiana Vetro v. Commission*, Joined Cases T-68, 77 and 78/89, [1992] E.C.R. II-1403, ¶¶ 357-68.

139. E.g., *Società Italiana Vetro*, [1992] E.C.R. II-1403, ¶ 360.

residual competition by making it more difficult for rivals to compete and for potential competitors to enter the market, however, may constitute an abuse.¹⁴⁰

Since the principal focus of Article 86 is abusive conduct by one or more firms with market power, a scenario in which the acquisition of a minority shareholding in a dominant enterprise to be privatized by one of its competitors, suppliers, or customers that leads to a strengthening of its dominant position appears to raise few issues under Article 86 in the absence of an abuse by the acquired company. Indeed, the Commission's policy is that the acquisition of a minority shareholding in a competitor, which by conferring on the acquirer at least "some influence" over the target brings about a change in the structure of the market that adversely affects competition on it, is, *prima facie*, in violation of Article 86 only if the acquirer, and not the target company, is dominant.¹⁴¹ On the other hand, it is doubtful whether a dominant firm's sale of a minority holding in its own shares to a competitor, supplier, or customer, by which the commercial policy of the dominant firm becomes subject to the acquirer's influence, could constitute an abuse by the dominant firm, particularly in the context of a privatization process. Furthermore, it is doubtful whether an abuse would be recognized even where the participation of particular private investors in the capital of the dominant firm results in a strengthening of its market position, for example, by facilitating access to the financial, industrial, or technological resources of the new shareholders.¹⁴²

140. *E.g.*, *Continental Can*, [1973] E.C.R. at 245, ¶ 26 (holding that concentrations which strengthen an existing dominant position may be caught by Article 86 of Treaty); *see also* *Tetra Pak I* (BTG license), Commission Decision No. 88/501/EEC, O.J. L 272/27, at 40, ¶ 47 (1988); *Tetra Pak Rausing v. Commission*, Case T-51/89, [1990] E.C.R. II-309, ¶ 23 (Ct. First Instance) (upholding Commission decision declaring that acquisition by dominant Tetra Pak group of exclusive patent license for new technology that constituted key element to entering market, by means of take-over of former competitor and exclusive licensee, amounted to abuse of dominant position because it prevented or at least considerably delayed entry of new competitor (third player which had hitherto cooperated with target company in developing new product incorporating new technology) into a market where only minimal competition existed so as to considerably raise the barriers to entry therein).

141. *See* Gillette, O.J. L 116/21 (1993).

142. This was the view that the intervener Philip Morris took. *Philip Morris*, [1987] E.C.R. at 4530. The *Philip Morris* judgment is of no help on this matter since the cryptic language of its paragraph 65 refers ambiguously to the arguably dominant position of the target company Rothmans International and to the possibility that "an abuse of *such*

The acquisition of a minority shareholding in a dominant enterprise to be privatized may be abusive within the meaning of Article 86 of the EC Treaty in the marginal case in which the acquirer is itself dominant, because the relevant market is an oligopolistic one. An oligopolistic market is characterized by a high level of concentration, high barriers to entry and product homogeneity. Another aspect of abuse in the context of Article 86 is when strong enough economic links exist, like through agreements or licenses, between the acquirer and the acquired company, which is an abuse of a joint dominant position.¹⁴³

3. Creation of a True "Public Corporation" Through a Public Flotation of a Dominant Enterprise: Substantive Competitive Assessment

In order to resolve the anticompetitive concerns potentially raised by the privatization of a monopolistic or dominant enterprise, a Member State may decide to implement the privatization via its public flotation and the creation of a true "public corporation" with a large number of small shareholders. As indicated above, by definition, privatization by public flotation results in no acquisition of control or influence over the enterprise to be privatized and thus falls outside the scope of both the Merger Regulation and Articles 85 and 86 of the EC Treaty.¹⁴⁴ In addi-

a position . . . arise[s] where the shareholding in question [i.e., PM's shareholding in Rothmans International] results in effective control of the other company or at least in some influence on its commercial policy [i.e., arguably in PM's acquiring effective control or some influence over Rothmans International]" (emphasis added). The only possibly consistent reading of this statement of the Court of Justice is that a dominant firm may abuse its market power even by transferring to a competitor a minority equity interest which enables the latter to control it or influence its commercial policy. See EC COMPETITION L. REP. (CCH) 49, 153-54 (Ivo Van Bael & Jean-François Bellis eds., 1994) (suggesting that reduction in competition between acquirer and target company would have precisely same effect whichever of two were dominant).

143. See, e.g., *Società Italiana Vetro*, [1992] E.C.R. II-1403, ¶ 358 ("There is nothing, in principle, to prevent two or more independent economic entities from being, on a specific market, united by such economic links that, by virtue of that fact, together they hold a dominant position vis-à-vis the other operators on the same market.") A similar argument was submitted in the *Philip Morris* case by the applicant British American Tobacco, according to which the conclusion of the new agreements was an abuse of dominant positions held jointly by Rembrandt and Philip Morris in the Benelux market. *Philip Morris*, [1987] E.C.R. at 4526-27. As mentioned in the text, however, this case is of virtually no relevance in the context of the privatization of public utilities, which in general enjoy exclusive production and distribution rights.

144. See *supra* notes 28-85 and accompanying text (examining control of concentrations in context of application of Merger Regulation to privatizations). If, on the

tion, Article 86 will be inapplicable to the privatization of a dominant firm by means of its transformation into a "public corporation" owned by a large number of private investors, because no strengthening of a dominant position is likely to be involved in this process.¹⁴⁵

In the absence of a concomitant liberalization of the relevant market, however, the privatized "public corporation" will retain its exclusive or special rights and, thus, its monopolistic or dominant position. As a result, its future market behavior will remain subject to Articles 86 and 90 of the EC Treaty. Moreover, in order to avoid a replacement of the public monopoly with a private monopoly, and to guarantee consumer welfare and economic growth, privatization should go hand in hand with market liberalization.

4. Liberalization of the Relevant Market as a First Step to Removing the Pre-existing Shield to the Dominant Position Held by a Publicly-Owned Enterprise to be Privatized

In the event that, instead of creating a true "public corporation," a Member State intends to privatize a dominant enterprise by conferring on specified acquirers control or a more limited influence over it, and that acquisition of control or influence would lead to a strengthening of the acquired company's dominance, making the privatization subject to review under the Merger Regulation (or, for concentrations not having a Community dimension, the applicable national merger control rules) or the EC Treaty competition rules, the Member State concerned may find it desirable to resolve the possible anticompetitive concerns raised by the privatization by eliminating the dominant position before starting the privatization process. This can be done by liberalizing the relevant market and breaking-up the dominant enterprise.

For instance, the marketing assets of CAMPSA, the administrator of the former Spanish state monopoly for the distribution of certain petroleum products, which accounted for 90% of the

other hand, the public floatation is combined with a private placement to create a "hard core" of investors acquiring control or a more limited influence over the enterprise to be privatized, the Merger Regulation or the Treaty competition rules, respectively, will remain applicable. *Id.*

145. See *supra* note 116 and accompanying text.

national retail market, were divided into three separate legal entities to be run by the refineries REPSOL, CEPSA, and PETROMED, which were CAMPSA's main shareholders and suppliers. The Commission, acting pursuant to the Merger Regulation, established that the proposed transaction would increase competition, since three separate businesses would operate in the market instead of a monopoly, and noted that the proposed split-up would not substantially affect future access to the market by other important European refiners because the transaction did not relate either to primary distribution logistics or to independent petrol stations. Finally, in authorizing the concentration, the Commission favorably regarded the fact that the division of CAMPSA's assets was effected in a way that gave all three purchasers significant retailing premises throughout Spain and, as a result, regionally balanced positions.¹⁴⁶

As emphasized by the Commission, market liberalization by definition brings about an improvement in the competitive structure of a market by creating potential competition. One of the effects of the opening up of a regulated market to competition, however, may be to free a privatized monopoly from some of the constraints of Article 90, such as the ban on financing a predatory pricing policy through cross-subsidization between formerly reserved and other activities. On the other hand, market liberalization does not mean the end of regulation, since the privatized entity will normally be subject to regulatory agencies that will limit its opportunities to exercise unfettered market power on the market.

Moreover, according to the policy statements of the Commission,¹⁴⁷ the liberalization of a market in which, on the basis of public interest grounds of a non-economic nature, exclusive or special rights existed in favor of a public utility is consistent with both the maintenance in force of rules directed at safeguarding major public policy objectives in that sector¹⁴⁸ and with

146. CAMPSA, O.J. C 334/23, ¶¶ 27-31 (1991) (CampsA).

147. See COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIRD REPORT ON COMPETITION POLICY 1993, at 32, ¶ 39 (1994).

148. *Id.* "Thus, in transport, competition must not be to the detriment of passenger safety, and rules must be laid down to cover this. Similarly, in telecommunications and the postal sector, a universal service must be provided, without neglecting the social aspects of telecommunications, such as the help they provide for the elderly or the handicapped. In the energy sector, security of supply must be maintained, as must the universal service in the case of electricity." *Id.*

the continued reservation to the privatized enterprise, on a temporary basis, of certain activities, in order to guarantee it the economic resources necessary for the performance of its public-interest tasks and to avoid "cream skimming" by private competitors.¹⁴⁹

5. Does the Privatization of a Dominant Firm Without Concomitant Market Liberalization Infringe Articles 90 and 86 of the EC Treaty Within the Meaning of the *Corbeau* Judgment?

According to the traditional approach of the Court of Justice,¹⁵⁰ the mere creation a dominant position by granting exclusive rights within the meaning of Article 90(1) of the EC Treaty is not in itself incompatible with Article 86, unless the grant of such a right: (1) inevitably leads to or induces an abuse by the privileged undertaking;¹⁵¹ or (2) is liable to create a situation where the privileged undertaking is encouraged to infringe Article 86,¹⁵² either through active conduct,¹⁵³ or the passive exer-

149. *Id.* "If this were not the case, there would be a risk that firms acting on the basis of strictly commercial criteria would carry out only the most profitable activities at the expense of the public-interest task which the Member States wished to see performed." *Id.* See also *Corbeau*, [1995] 4 C.M.L.R. 621.

150. *E.g.*, *Sacchi*, [1974] E.C.R. 409, ¶ 14; *Merci Convenzionali Porto di Genova*, [1991] E.C.R. I-5009, ¶¶ 16-17 (stating that Member State infringes Articles 86 and 90(1) when undertaking in question is induced, by mere exercise of its exclusive rights, to abuse its dominant position, or when those rights are capable of creating situation in which undertaking is led to commit such abuses). See also *Corsica Ferries Italia*, [1994] E.C.R. I-1783, ¶ 42.

151. See, *e.g.*, *Höfner*, [1991] E.C.R. I-1979, ¶¶ 26-27; *Merci Convenzionali Porto di Genova*, [1991] E.C.R. I-5009, ¶ 19. This approach was followed most recently by the Court of Justice in *Centre d'Insémination de la Crespelle*. *Centre d'Insémination de la Crespelle v. Coopérative de la Mayenne*, Case C-323/93, [1994] E.C.R. I-5077, ¶¶ 18-22. The Court dismissed the argument that approved centers enjoying a statutory monopoly, which were legally empowered to require breeders requesting bovine semen from other production centers to pay the attending additional cost, could not avoid abusing their dominant position in exercising their exclusive rights by charging disproportionate costs simply because they were by the law given the task of calculating those costs.

152. *E.g.*, *Elliniki Radiophonia-Tileorassi v. Pliroforisis and Kouvelas*, Case C-260/89, [1991] E.C.R. I-2925, ¶37 (finding that grant by Greek state to national television monopoly of further exclusive right to retransmit television broadcasts from other Member States created risk that monopolist undertaking would adopt discriminatory broadcasting policy favoring its own programs in violation of Article 86 of Treaty). See also *Corsica Ferries*, [1994] E.C.R. I-1783, ¶¶ 43-45 (ruling that Articles 90(1) and 86 prohibit national authority from inducing undertaking holding monopoly for provision of compulsory piloting services, by approving tariffs adopted by it, to apply discriminatory tariffs to maritime transport undertakings depending on whether they operate

cise of its special or exclusive rights,¹⁵⁴ without any objective justification.

In addition, it has been suggested that, following the recent *Corbeau* ruling,¹⁵⁵ a Member State should be regarded as infringing Articles 90(1) and 86 of the EC Treaty by its inactivity in situations where, irrespective of the existence of any abusive conduct by the legal monopoly other than the foreclosure of competition inherent in the existence of a dominant position, the development of effective competition is restricted as a result of changes that have occurred in market conditions over time.

In other words, under certain circumstances, a Member State's failure to redefine and circumscribe, in light of the changing nature of market demands over time, the scope of a broad exclusive right lawfully granted to a privileged undertaking at some time in the past may constitute an infringement of Article 90(1).¹⁵⁶ According to the *Corbeau* judgment, the redefinition of the exclusive right must satisfy the two-prong test of Article 90(2), which focuses on: (1) the existence of a public service justification, of either an economic or a non-economic character, for maintaining a monopoly of such a scope,¹⁵⁷ and

transport services between Member States or between ports situated within national territory).

153. For example, through the implementation of a discriminatory policy, by charging unfair prices or conditions on final users or by illegally extending an existing monopoly into new related markets.

154. For example, through inefficiency, lack of innovation, poor product quality or inability to satisfy consumer demand for value-added services. Article 86(b) specifically mentions limiting productions, markets or technical development as a possible form of abuse of dominant position. EC Treaty, *supra* note 1, art. 86(b), [1992] 1 C.M.L.R. at 627.

155. *Corbeau*, [1995] 4 C.M.L.R. 621. The case concerned the issue of whether the Belgian postal law of 1956, which reserved all postal services involving the collection, transportation, and distribution of correspondence, including courier services, to the Belgian postal authorities, was compatible with Articles 90 and 86 of the Treaty. *Id.*

156. Leigh Hancher, *Case Note on Corbeau*, 31 COMMON MKT. L. REV. 105, 114 (1994); David Edward & Mark Hoskins, *Article 90: Deregulation and EC Law: Reflections Arising from the XVI FIDE Conference*, 32 COMMON MKT. L. REV. 157, 168 (1995). Inaction may also be considered an infringement of Article 90(1) where a Member State fails to exercise its supervisory powers in relation to an undertaking enjoying exclusive rights which abuses of its dominant position in using, on its own initiative, its margin of discretion. DERRICK WYATT & ALAN DASHWOOD, *EUROPEAN COMMUNITY LAW* 553 (3d ed. 1993). See also CLAUS-DIETER EHLERMANN, *Managing Monopolies: The Role of the State in Controlling Market Dominance in the European Community*, 14 EUR. COMPETITION L. REV. 61, 65 (1993).

157. In *Corbeau*, the Court of Justice noted that the Belgian postal authority is charged with the provision of basic postal services in Belgium and pointed out that,

(2) whether the elimination or restriction of competition inherent in maintaining the monopoly is proportionate with the proper performance of the tasks assigned to the monopolist.¹⁵⁸

Against this background, it may be argued, for at least three reasons, that the process of privatizing a public utility provides a Member State with an opportunity to reconsider whether to continue to allow exclusive or special rights enjoyed by an enterprise to be privatized and, thus, of discontinuing its "inaction" for the purposes of Article 90(1) of the EC Treaty.

First, the privatization and liberalization experiences of

pursuant to Articles 90(1) and (2), exclusive rights could be granted to the Belgian postal authority on public service grounds (i.e., for the provision of the basic postal services), provided that such exclusive rights were necessary to ensure the performance of the basic postal services in balanced economic conditions. *Corbeau*, [1995] 4 C.M.L.R. 621, ¶¶ 13-15. The Court defined "services of a general economic interest" as services that are provided to the benefit of all users, on the entire territory of a state, at uniform tariffs and similar quality, without regard to particular situations and the degree or profitability of each individual activity. *Id.* According to the case law of the Court of Justice, the provision of a telecommunications network for the use of the general public, the provision of employment placement services, the operation of regional public electricity supply and the operation of air routes that are not commercially viable but which are necessary for general interest reasons are also services of general economic interest. See *RTT v. GB-INNO*, [1991] E.C.R. I-5941; *Höfner*, [1991] E.C.R. I-1979; *Gemeente Almelo v. Energiebedrijf Ijsselmij*, Case C-393/92, [1994] 2 C.E.C. (CCH) 281 (Eur. Ct. J. Apr. 27, 1994); *Ahmed Saeed Flugreisen*, [1989] E.C.R. 803.

158. *Corbeau*, [1995] 4 C.M.L.R. 621, ¶¶ 16-19. The Court affirmed that, when examining the extent to which a restriction on, or even the exclusion of, competition is necessary to allow an undertaking entrusted with a service of general economic interest to perform its task under economically acceptable conditions, the starting point must be that the undertaking in question is obliged to perform its service in conditions of economic equilibrium and thus to offset less profitable sectors against the profitable ones. *Id.* Therefore, a restriction of competition from individual undertakings operating also in the profitable sectors, provided for by the applicable national legislation, may be justified lest these competitors be free to concentrate on such sectors and to offer more advantageous tariffs than the undertaking holder of the exclusive rights (so-called "creaming off"). *Id.* However, the exclusion of competition is not justified with respect to specific services, dissociable from the general interest service, which meet special needs of economic operators and call for certain additional services not offered by the traditional service, provided, however, that such specific services — by their nature and the conditions in which they are provided, including the relevant geographical area — do not compromise the economic equilibrium of the general economic interest service provided by the undertaking granted exclusive or special rights. *Id.* The question of whether the specific services at issue met these criteria was referred back to the Belgian court. See Luc Gyselen, *Anti-competitive State Measures Under the EC Treaty: Towards a Substantive Legality Standard*, 19 EUR. L. REV. CC55, CC82-83, CC96-97 (1994); Gardner, *supra* note 28, at 85 (suggesting that in recent jurisprudence of Court public monopolies are presumed to be incompatible with Treaty unless monopolist can prove that its exclusive right is permitted under specific circumstances, so that Article 90(1) has been practically subsumed into Article 90(2) inquiry).

some Member States may prompt other states to revise their traditional view regarding the existence of statutory monopolies in certain sectors, such as water, electricity, gas, and postal and telecommunications services, as justified on grounds of legitimate national objectives.

Second, the liberalization or deregulation of a public sector at the same time as the privatization of the related public sector monopoly has the advantage of removing any uncertainty as to the regulatory regime in which the privatized entity will operate. This works to the benefit of the public, of investors, and the state vendor, the latter being in a position to assess more accurately the revenues likely to be obtained through a total or partial disposal of its interest in the former monopoly.

Finally, combining the privatization of a public utility with market liberalization avoids the risks inherent in the creation of a private monopoly, particularly where it is likely to be very large and/or to operate in strategic economic sectors,¹⁵⁹ which may be difficult to effectively regulate and supervise, even where regulatory activities are limited to the setting of quality standards and tariffs to final users. Indeed, as the state withdraws from its role as market participant, retaining only its role as market regulator, its ability to pursue general objectives of efficient resource allocation and consumer protection may be seriously endangered by asymmetric access to relevant economic information, in particular, data concerning the structure and level of the cost of supplying the relevant product, and the consequent dependence of the state regulator on information provided by the privatized enterprise.¹⁶⁰

Accordingly, although Member States are not in all circum-

159. See Guislain, *supra* note 20, at 71, 121-22. It has been submitted that in such a situation the opening up to competition of a regulated sector if not accompanied by a re-organization or splitting-up of the monopoly or dominant firm or by other structural measures directed at removing the pre-existing dominant position of the state-owned enterprise granted exclusive or special rights, may be insufficient to establish conditions of effective competition in the marketplace if the market strength of the large privatized company or conglomerate operating in strategic economic sectors is such as to remove any likelihood of potential competitors entering the market for some time. *Id.*

160. *E.g.*, Autorità Garante della Concorrenza e del Mercato, *Nota informativa al Ministro dell'Industria, del Commercio e dell'Artigianato e al Ministro al Bilancio e della Programmazione economica in merito al riassetto strutturale del settore dell'energia elettrica* [Italian Antitrust Authority, *Memorandum for the Ministry of Industry, Trade and Crafts and the Ministry of the Budget and Economic Planning on the structural reorganization of the electricity sector*], 30 *BOLLETTINO DELL'AUTORITÀ GARANTE* 59, 66 (Aug. 1, 1995).

stances prevented by the EC Treaty from granting or maintaining a legal monopoly,¹⁶¹ a Member State's failure to withdraw the exclusive or special rights enjoyed by an enterprise to be privatized ("privatization without liberalization"), or otherwise to reorganize the privatized company in such a way as to ensure an immediate increase in the degree of competition in the market,¹⁶² may amount to a "measure contrary to" Article 86 of the EC Treaty, within the meaning of Article 90(1), where: (1) the exclusive rights enjoyed by the undertaking to be privatized are not justified by a legitimate national objective, such as the need to ensure universal service, or extend to a distinct market value-added services that meet emergent consumer demand and are not traditionally offered by the public monopolist; (2) the resulting restriction of competition exceeds that which is necessary to attain the required level of public service, i.e., to ensure the monopolist's financial viability, because, for example, the reserved general service activities are profitable and need not be subsidized by revenues from other non-reserved sectors,¹⁶³ or because such revenues are only a minor part of the monopoly's overall revenues and are thus not necessary to its financial equilibrium;¹⁶⁴ or (3) the monopolist enterprise to be privatized appears, for example, on the basis of indicators such as the productivity of its employees, price increases relative to the industry retail price index, the level of imported competing products or the number of customer complaints for poor product quality, to consider itself insulated from the need to maintain and improve its efficiency and the optimum use of resources, is unable to

161. Edward & Hoskins, *supra* note 131, at 164. This approach would above all be unacceptable in terms of an economic analysis since competition may be technically impossible or economically undesirable for certain economic activities constituting natural monopolies, in light, for example, of the scale and expense involved or the nature of supply. *Id.*. But see *supra* note 18 and accompanying text (explaining Member States' obligation to adjust progressively any state monopoly of commercial character pursuant to Article 37 of Treaty).

162. For example, by splitting-up or by unbundling its production, distribution, and transport functions, privatization and liberalization not immediately affecting the pre-existing dominance.

163. See Dutch Express Delivery Services, O.J. L 10/47 (1990).

164. See Spanish International Express Courier Services, O.J. L 233/19 (1990). See also Gyselen, *supra* note 158, at 97 n.1 (suggesting that loss-making services should also be open to competition and carried out by company agreeing to accept smallest subsidy, and noting difficulty inherent in determining exact scope of restriction of competition necessary to permit cross-subsidization).

meet demand or has failed to respond to new market developments, such as high quality or rapid value-added services, due to lack of innovation caused by the absence of competitive pressure.

6. The Combined Impact of Privatization and Market Liberalization on Competition: Does the Privatization of a Dominant Firm "Create" a Dominant Position on a Newly-Created Market?

The combination of the privatization of state-owned enterprises enjoying exclusive or special rights with market liberalization would seem to create the optimum conditions for the establishment of effective competition in previously regulated sectors. Since liberalization, in effect, creates a market that did not previously exist due to the presence of a statutory monopoly, it could be argued that liberalization coupled with simultaneous privatization of the monopolist or dominant enterprise would "create" a dominant position in that "new" market. In such a situation, if the privatization is carried out through a transfer of control of the dominant business there is a risk that the privatization would be blocked under the Merger Regulation, at least in so far as the dominant position created significantly impedes effective competition in the common market or a substantial part of it.¹⁶⁵

It may be argued in response, however, that, unlike the situation in which a truly new market develops as a result of technological innovation¹⁶⁶ or the state's withdrawal from the provision of a service traditionally constituting an activity *iure imperii*,¹⁶⁷

165. Merger Regulation, *supra* note 5, art. 2(3), O.J. L 395/1, at 4 (1989). On the other hand, the creation of a dominant position as such falls outside of the scope of Article 86 of the Treaty, which only prohibits structural strengthening of a pre-existing dominant position.

166. *MSG Media Service*, O.J. L 364/1, at 10-11, ¶ 55 (stating that "[a]lthough a monopoly in a future market [for technical and administrative services for pay-TV in Germany] that is only just beginning to develop should not necessarily be regarded as a dominant position within the meaning of Article 2(3) of the Merger Regulation, the assumption that no market dominance exists presupposes in such a case that the future market in question remains open to future competition and that the monopoly is consequently only temporary," and finding that this condition was not met in the case of the proposed transaction since the relevant market was foreseeably "being sealed off already in the development phase by the establishment of the joint venture and [MSG would] acquire a long-term monopoly").

167. Such as employment procurement, basic education, health care, or prison

even before liberalization, a market, in the sense of price-making forces directed at trading the relevant commodity or service, existed, albeit a monopolistic or quasi-monopolistic one, for the product supplied by the privatized enterprise, as did that enterprise's dominant position. Indeed, the dominant firm was not free to exercise unfettered market power, because its commercial conduct was subject to the restraints in Articles 86 and 90 of the EC Treaty.¹⁶⁸ Although the privatization of the dominant firm by way of a concentration may well result, therefore, depending on the market power of the acquirer and the effects of the transaction at the horizontal, vertical, and conglomerate levels, in a "strengthening" of the dominant position of the acquired company, technically, it cannot "create" such a position, other than in exceptional circumstances.¹⁶⁹

Moreover, as mentioned above, even if a dominant position was created by a concentration resulting from the privatization of a dominant enterprise operating in a newly-liberalized market, this finding would not be sufficient, *per se*, to make the privatization incompatible with the Common Market, at least where there is strong evidence that any such dominant position would only subsist for a limited period of time due to the likelihood of new entrants into the new market.¹⁷⁰ Of course this would de-

management (which in most Member states is a state activity *iure imperii* but in the United Kingdom has been farmed out to private undertakings on a trial basis).

168. A possible counter-argument is that, in the absence of competition in the relevant market, Article 86 applied to the former monopoly mainly as a consumer protection provision (for example, to bar unfair trading conditions, or excessive pricing or tie-in policies operating against the public interest), or in order to safeguard effective competition in a distinct but neighboring market (for example, to prevent the monopolist firm from refusing to give to interested third parties access to its essential facility without any objective justification).

169. See *supra* note 90 and accompanying text.

170. See *Eridania/ISI*, O.J. C 204/12, ¶¶ 26-27 (1991) (finding that ability of new entity to influence sugar price and market conditions in Italy would be strictly limited by threat of imports at lower price from neighboring areas of European Union given low transport costs); *Aérospatiale-Alenia/de Havilland*, O.J. L 334/1 (1991) (finding that the combined entity would face no realistic significant potential competition in the Union and worldwide regional aircraft markets in the foreseeable future as entry would require substantial fixed and sunk costs and six to seven years' lead time, market demand was declining, newly industrialized countries were unlikely to enter international markets and their products would not be sufficiently reliable, and finally that Japanese producers were not likely to participate in the commuter market because it lacks strategic and technical interest); Commission Decision, O.J. L 114/34, ¶¶ 112-14 (1993) (*Mannesmann/Hoesch*) (noting high incentives and opportunities for new entries in German market for gasoline pipes, in particular as result of on-going European Union

pend on the timespan necessary for potential new entrants to build a new plant of minimum efficient scale and the life span and amortization period of such a plant, the likelihood of recovering the initial investment through alternative use, the rate of technical change in the industry, and the ability of customers to shift from one supplier to another.¹⁷¹

D. *Application of Articles 85 and 86 of the EC Treaty to the Market Behavior of Undertakings Enjoying Exclusive or Special Rights After Privatization*

1. Potential Recourse by Privatized Utilities to Unlawful Commercial Practices Directed at Reinforcing Their Market Power

Article 90 of the EC Treaty is neutral as to the ownership, public or private, of business enterprises and makes only a functional distinction in favor of undertakings that are required to perform specific tasks on behalf of all consumers in the general economic interest. Accordingly, following their privatization, formerly state-owned undertakings holding exclusive or special rights remain subject to the EC Treaty competition rules.¹⁷² Even where privatization is accompanied by market liberaliza-

harmonization of technical standards and forthcoming entry into force of EU Directive 90/531 on public procurement in so-called excluded sectors); Commission Decision, O.J. L 217/35, ¶¶ 30, 65-70 (1993) (KNP/Bührmann-Tetterode/VRG) (finding that combined entity would control over two thirds of Belgian and Dutch markets for distribution and servicing of printing presses and that such dominant position was unlikely to be eroded quickly because, as availability and reliability of local maintenance service is key issue in decision to purchase printing press, customers would have no effective alternative; approval of transaction was ultimately made conditional on parties' agreeing to terminate by end of 1993 existing distribution and servicing agreements in Belgium and Netherlands with one of two major manufacturers of printing presses in European Union, and to transfer assets relating to terminated distribution and servicing agreements, including staff, to purchaser capable of continuing business); see NSD, slip op. ¶¶ 110-11 (finding that the combined entity would acquire a medium-to-long-term dominant position on the market for satellite TV transponder services suitable for Nordic viewers since the transaction would leave no sufficient capacity on the actual competitors Astra and Eutelsat or on other satellites not controlled by NSD, the additional capacity becoming available over time through digitalization was likely to be absorbed by NSD, and the combined entity would also have the power to define competition among its parent companies in their position as TV broadcasters).

171. See 2 BUTTERWORTHS COMPETITION L. VII/222 (Sufirin & Lowe eds., 1992).

172. This is similar to the Merger Regulation, *supra* note 5, O.J. L 395/1 (1989); See notes 109-71 and accompanying text (examining special issues raised by privatization of enterprises holding dominant positions prior to privatization).

tion, these rules still play an important role in ensuring that the pre-existing public monopoly is not merely replaced by a new private monopoly, since privileged undertakings undoubtedly *de facto* retain their market power for at least a certain period after privatization, and are thus in a position to use their strength to eliminate or restrict competition through restrictive practices, abusive conduct or concentrations,¹⁷³ on the relevant market or on other distinct but related markets, thereby depriving consumers of the benefits of demonopolization.¹⁷⁴

2. Possible Issues for Review Under Article 85 of the EC Treaty

The potential application of the prohibition in Article 85(1) on concerted action in restraint of competition to a privatized utility raises several specific issues. One such issue arises where a planned privatization involves the separation of the privileged enterprise, since, in such circumstances, it will frequently be necessary to formalize, prior to privatization, the internal practices of the enterprise concerned as agreements between the separate businesses created from it.¹⁷⁵ As with all activity taking place within a single enterprise, a privatized company's practices are not subject to Article 85 of the EC Treaty so long as they remain internal.¹⁷⁶ As a result, those practices may have restrictive as-

173. As discussed above, privatized undertakings enjoying exclusive rights or otherwise holding a dominant position may make recourse to acquisitions in order to strengthen their market power and create a situation in which competition from actual or potential rivals is not in fact possible. In the absence of structural or behavioral undertakings from the parties, aimed at maintaining conditions of effective competition and modifying the original concentration plan, concentrations resulting in a strengthening of a pre-existing dominant position are incompatible with the common market and must be blocked. *See supra* notes 91-93 and accompanying text. The Commission, however, "does not intend to oppose such regroupings where their real purpose is to allow firms to cope with the new competitive environment, which may sometimes be worldwide." COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIRD REPORT ON COMPETITION POLICY 1993, at 32-33, ¶ 40 (1994).

174. *Id.*

175. When one privatized utility is split into a number of separate businesses, they will deal at arm's-length with one another. Therefore, the pre-existing internal practices of the privatized utility must be formalized as new agreements.

176. *See, E.g.,* Béguelin Import v. GL Import Export, Case 22/71, [1971] E.C.R. 949, ¶ 8; Centrafarm v. Sterling Drug, Case 15/74, [1974] E.C.R. 1147, ¶ 41; Bodson v. Pompes Funèbres des Régions Libérées, Case 30/87, [1988] E.C.R. 2479, ¶ 19; Viho Europe v. Commission, Case T-102/92, [1995] 1 C.E.C. (CCH) 562. Article 85 does not apply to concerted action among connected undertakings belonging to a single economic unit, such as parent-subsidiary agreements, within which a subsidiary company,

pects, which, if incorporated in an agreement between independent undertakings, will, prima facie, amount to violations of Article 85 unless granted an exemption.¹⁷⁷ The Commission, however, can be expected to look favorably on agreements entered into pursuant to the reorganization of a national industry prior to its privatization.

For example, until March 31, 1990, Scotland's electricity requirements were met by two publicly-owned corporations, North of Scotland Hydro-Electric Board and South of Scotland Electricity Board. These companies generated, transmitted and distributed electricity in their assigned geographical areas, covering the northern and southern parts of Scotland, respectively. Prior to their privatization, two new companies were created to assume the non-nuclear activities of these Boards with respect to the north and south of Scotland, Scottish Hydro-electric ("Hydro-electric") and Scottish Power, respectively. The nuclear facilities, which would remain in public ownership, were taken over by Scottish Nuclear, formerly run by the South of Scotland Electricity Board. Under the terms of an exclusive sale agreement between Scottish Nuclear and the two new entities, Scottish Power and Hydro-electric would be obliged to purchase all the electricity generated by Scottish Nuclear on a take-or-pay basis, at an identical price and on the basis of quotas from which they could not deviate. Scottish Nuclear could not supply electricity to third parties without the consent of both Scottish Power and Hydro-electric. The Commission determined that the agreement met the conditions for an Article 85(3) individual exemp-

though having separate legal personality, enjoys no economic independence and no real freedom to determine its course of action in the market, as the agreement or concerted action in question is concerned merely with the internal allocation of tasks as between the undertakings involved. *Id.*

177. Commission Decision, O.J. L 45/34 ¶ 25 (1987) (Austin Rover Group/Unipart Group) (distribution agreement between vehicle manufacturer Austin Rover and wholesaler Unipart, which followed separation of ownership of two parties and provided that latter would continue to operate manufacturer's parts business). Under the Commission's policy, the applicability of Article 85(1) of the Treaty to a restrictive agreement between two businesses is not excluded merely because they were formerly fellow subsidiaries in the same group of companies and the agreement is connected with the privatization of one party, where the obligations imposed upon the parties (for example, to co-ordinate their purchasing, quality standards and controls, stockholding, ordering and invoicing, marketing and distribution) determine the competitive stance of the now independent businesses and are not a necessary and inherent part or condition of any such transfer of ownership. *Id.*

tion after the parties accepted the Commission's request that the agreement be limited to fifteen years instead of thirty. The Commission reasoned that the agreement formed an integral part of the electricity privatization scheme in Scotland and was necessary to allow transition from the previously monopolistic structure to a market-based electricity industry. The take-or-pay feature would allow the long-term planning necessary for reliable production, ensuring security of supply and an independent energy supply market. The agreement would also allow considerable economies of scale, induce Scottish Nuclear to maximize its output, and ensure the profitability of the nuclear power stations, including the offsetting of the high investment costs. In the Commission's view, the reorganization of the electricity industry, of which the agreement formed a part, and the gradual introduction of competition into the system would result in benefits to consumers, while the restrictions contained in the agreement did not limit competition any more than was necessary to achieve its goal of furthering the transition to a market-based structure. The quotas allocated to Scottish Power and Hydro-Electric did not reflect the market shares of the companies, since each would be free to determine its output individually, to allow the two new entities gradually to compete in their relations with customers. The Commission noted that, although the price set in the agreement was independent of the price at which Scottish Power and Hydro-Electric purchased electricity from other generators, particularly independent generators, that price should not be improperly used to justify a very low purchase price that would disadvantage independent generators and Scottish Nuclear's competitors. Given that the relevant market was defined as the market for the generation of electricity and that the agreement was confined to a part of that market, i.e., nuclear-powered generation, the Commission found that the market would remain sufficiently open and that there were real alternative sources of supply. Moreover, the agreement would gradually increase competition in the electricity industry. The Commission decided, therefore, to exempt the agreement until its expiration date of March 31, 2005.¹⁷⁸

178. *See also* Commission Notice, O.J. C 223/7 (1994) (Scottish Electricity Industry) (notice pursuant to Article 19(3) of Regulation 17 informing any interested third parties of the Commission's intention to grant an individual exemption to coal supply arrangements for electricity generation in Scotland entered into by Scottish Power,

3. Possible Issues for Review Under Article 86 of the EC Treaty

If a privatized utility manages and itself uses an essential facility,¹⁷⁹ and access to that facility is liberalized, other undertakings already operating on the market or planning to enter it, including value-added service providers, must be able to benefit from the essential facility on non-discriminatory terms. Using the strength of an essential facility in one market to protect or strengthen its position in another related market, by denying third-party access or granting it on less favorable terms than those it allows to itself, amounts to a violation of Article 86 of the EC Treaty.¹⁸⁰

Since the privatized enterprise owning the essential infrastructure will have incurred and will continue to incur certain costs in maintaining it and since it may also incur additional costs in fulfilling its obligation to provide public interest services not borne by its competitors, particularly if it retains exclusive or special rights, as in the case, for example, of national telecom-

Scottish Hydro-Electric and British Coal in preparation for the privatization of the coal industry in the United Kingdom); Commission Notice, O.J. C 191/4 (1990); Commission Notice, O.J. C 281/5 (1993); Commission Notice, O.J. C 15/9 (1994) (English and Welsh Electricity Industry) (notices pursuant to Article 19(3) of Regulation 17 informing any interested third parties of the Commission's intention to grant an individual exemption to the notified agreements implementing arrangements for the privatization of the electricity industry in England and Wales, namely (i) the coal supply contracts between British Coal Corporation and the fossil-fuel generators National Power and PowerGen, (ii) the option contracts or contracts for differences between the fossil-fuel generators and 12 regional electricity companies, and (iii) the coal supply contracts between National Power and 17 United Kingdom coal producers); Commission Notice, O.J. C 92/5 (1992) (Northern Ireland Electricity Industry) (notice pursuant to Article 19(3) of Regulation 17/62 informing any interested third parties of the Commission's view that there was no need for Commission action under Articles 85 and 86 of the Treaty in respect of the notified connection, power station and generating unit agreements forming part of plans to privatize the electricity industry in Northern Ireland).

179. An example of an essential facility is one without which, due to the absence of adequate alternatives, its competitors are unable to offer their services to customers.

180. See Commission Decision No. 94/19/EC, O.J. L 15/8, ¶ 66 (1993) (*Sea Containers v. Stena Sealink*). The Commission has also found that the Danish Transport Ministry caused DSB, a public undertaking that managed the port of Rødby and jointly operated a ferry service from that port between Denmark and Germany, to abuse its dominant position by refusing access to the port, without any objective justification, to a Swedish group that planned to set up a competing ferry operation on the same route. Commission Press Release IP(95) 492, *Irish Ferries Access to the Port of Roscoff in Brittany: Commission Decides Interim Measures Against the Morlaix Chamber of Commerce* (Eur. Comm'n May 16, 1995).

munications operators in respect of voice telephony, third-party access to the essential facility will often be made conditional upon the payment of a fee to its owner. This, of course, raises the issue of how fairly to determine that fee.¹⁸¹

Finally, a privatized utility with exclusive or special rights may make use of its market power in the sector once, or still, reserved it to subsidize its activities in non-reserved markets, in which it faces fiercer competition, by allocating all or part of the costs of its non-reserved activities to its activity in the market in which it is dominant. Such cross-subsidization may amount to an abuse of dominant position contrary to Article 86 of the EC Treaty to the extent that it is instrumental in financing predatory pricing by the privatized utility in competitive markets. On the other hand, it is in principle unobjectionable for the monopolist or dominant firm to use part of its profits from non-regulated sectors, or other reserved activities, to comply with the universal service requirement.¹⁸²

The main difficulty as regards the prevention of predatory pricing via cross-subsidization between competitive and dominated markets appears to be establishing the existence of such cross-subsidization, not only because transparent accounting techniques have rarely been employed in the sectors traditionally reserved to state monopolies, but also because subsidies can be provided covertly in a variety of ways, for example, by not taking full account of the actual cost of access to the infrastructure, which is involved in providing a non-reserved value-added service, when setting the price charged for the latter and covering any resulting shortfall by increasing prices for the reserved service.¹⁸³

4. Possible Issues for Review Under Article 5 *juncto* Articles 3(g) and 85 or 86 of the EC Treaty

Finally, as noted above, one consequence of the withdrawal by a Member State of the exclusive or special rights previously

181. COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIRD REPORT ON COMPETITION POLICY 1993, at 32-33, ¶ 40 (1994).

182. Commission Guideline, O.J. C 233/2, ¶ 102 (1991) (clarifying the application of EEC competition rules in the telecommunications sector). *See also* COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIRD REPORT ON COMPETITION POLICY 1993, at 32-33, ¶ 40 (1994).

183. Edward & Hoskins, *supra* note 156, at 180.

granted to a privatized enterprise will be that the activities of the enterprise concerned will fall outside of the scope of Article 90(1) of the EC Treaty. The establishment of effective competition and the integration of markets in once-regulated sectors, however, could be jeopardized if Member States, after privatization and liberalization of such industries, were free to displace competition by creating regulatory regimes that might frustrate or undermine the attainment of such objectives.

Pursuant to Article 5 of the EC Treaty, Member States "shall abstain from any measure which could jeopardize the attainment of the objectives of this Treaty," including the establishment of "a system ensuring that competition in the common market is not distorted."¹⁸⁴ This objective is elaborated in several Treaty provisions, including Articles 85 and 86. Accordingly:

[W]hile it is true that [Articles 85 and] 86 [are] directed at undertakings, nonetheless, it is also true that the EC Treaty imposes a duty on Member States not to adopt or maintain in force any measure which could deprive th[ose] provision[s] of [their] effectiveness Likewise, Member States may not enact measures enabling private undertakings to escape from the constraints imposed by Articles 85 to 94 of the EC Treaty.¹⁸⁵

As previously mentioned in this Article, according to the case law of the Court of Justice, a Member State may infringe Article 5 in combination with Articles 3(g) and 85 or 86 of the EC Treaty where, after completion of the privatization and liberalization processes in a hitherto regulated industry: (1) it adopts or maintains in force national legislation that requires a privatized utility to enter into restrictive agreements, favors the adoption of such agreements,¹⁸⁶ to indulges in abusive exploitation of market power;¹⁸⁷ (2) it adopts or maintains in force national legislation that reinforces the effects of anti-competitive agreements entered into by a privatized utility by approving the agreement

184. EC Treaty, *supra* note 1, art. 3(f), [1992] 1 C.M.L.R. at 588-89.

185. *GB-INNO v. ATAB*, [1977] E.C.R. 2115, ¶¶ 31, 33.

186. *E.g., id.*; *Bureau National Interprofessionel du Cognac v. Clair*, Case 123/83, [1985] E.C.R. 391.

187. *E.g., Höfner*, [1991] E.C.R. I-1979, ¶¶ 26-27; *Merci Convenzionali Porto di Genova*, [1991] E.C.R. I-5009, ¶ 19; *Centre d'Insémination*, [1994] E.C.R. I-5077, ¶¶ 18-22.

or incorporating it into national legislation;¹⁸⁸ or (3) it deprives its own legislation of its official character by delegating to a privatized utility the responsibility for taking decisions affecting the economic sphere.¹⁸⁹

Even in industries that have been privatized and liberalized, Member States retain their power to regulate entrepreneurial activity to attain general economic or monetary policy objectives through the adoption of measures of a general character, such as the fixing of maximum prices to control inflation and the reduction of taxes or social charges to stimulate investment in depressed regions or to support employment. Although this type of public intervention in the national economy may restrict competition, that effect is insufficient to constitute an infringement of Articles 5, 3(g), and 85 or 86 if the restrictive national legislation or policy involves no form of delegation of regulatory powers to private economic operators.¹⁹⁰ For example, a Member State may lawfully fix the price, or minimum retail price,¹⁹¹ of a commodity or service following a decision-making process involving ad hoc tariff boards made up of industry representatives appointed by the public authorities, provided, first, that such representatives are not bound by orders or instructions from the undertakings they represent, including any privatized utility, and are required to take account of the public interest in setting prices, and, second, that the public authority retains the ultimate power to fix the price or tariff itself, regardless of the price set by the board, if it sees fit.

188. *E.g.*, *Bureau National Interprofessionnel du Cognac v. Aubert*, Case 136/86, [1987] E.C.R. 4789, ¶¶ 23-24; *Vereniging van Vlaamse Reisbureaus v. Sociale Dienst van de Plaatselijke en Gewestelijke Overheidsdiensten*, Case 311/85, [1987] E.C.R. 3801, ¶¶ 13-23.

189. *E.g.*, *Van Eycke v. ASPA*, Case 267/86, [1988] E.C.R. 4769, ¶ 19; *Meng*, slip op.; *Reiff*, slip op.; *Ohra*, slip op.; *Delta Schiffahrts*, [1994] E.C.R. I-2517.

190. *See Gyselen*, *supra* note 158, at 65-73 (advocating three-filter test according to which, where state measure distorts competition within meaning of Article 85 of Treaty without achieving genuine economic or monetary policy objective, it should be open to national authorities to demonstrate that measure serves other legitimate objectives such as, for example, protection of consumers or fairness of commercial transactions).

191. *Cullet v. Leclerc Toulouse*, Case 231/83, [1985] E.C.R. 305.

II. PRIVATIZATION AND THE EUROPEAN UNION RULES APPLICABLE TO PUBLIC UNDERTAKINGS

A. *Liberalization and Privatization: Article 90, a Critical Overview*

The European Union utilities liberalization program is another important factor in creating pressure for privatization. In its recent pronouncements on competition policy, the Commission has repeatedly emphasized that liberalization, through the restriction of state-created monopolies and the opening up of economic sectors so far characterized by high levels of state intervention, is one of its main priorities.¹⁹² To this end, the Commission is currently advocating liberalization in regulated sectors including gas, electricity, telecommunications, transport, and postal services.¹⁹³ As a result, certain authors have concluded that, in the Commission's view, "the restrictions of competition, which are inherent to legal monopolies, are, as a matter of principle, irreconcilable with the concept of the Single Market."¹⁹⁴

The Commission has been supported in its drive for liberalization by developments in the Court of Justice case law relating to Article 90, the Article of the EC Treaty that seeks to strike a balance between the existence of state-created monopolies, particularly those entrusted with the provision of public services and the requirements of free competition.¹⁹⁵ In a difficult set of recent cases concerning Article 90, the Court has limited the power of Member States to establish and maintain special and exclusive rights.

Despite the Commission's protestations that "the EC Treaty

192. See COMMISSION OF THE EUROPEAN COMMUNITIES, XXTH REPORT ON COMPETITION POLICY 1990, at 125-26, ¶ 169 (1991); COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIST REPORT ON COMPETITION POLICY 1991, at 25-38, ¶¶ 15-41 (1992); and COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIIRD REPORT ON COMPETITION POLICY 1993, at 30 ¶ 36 (1994).

193. Commission of the European Communities, Green Paper for a European Union Energy Policy, COM(94)659 (Feb. 1995); Commission of the European Communities, Green Paper on the Liberalization of Telecommunications Infrastructure and Cable TV Networks, COM(94)440 & COM(94)682 (Oct. 1994 & Jan. 1995); Commission of the European Communities, Draft Commission Notice on the Application of the Competition Rules to the Postal Sector, COM(95)830 (July 1995).

194. Erik Hordijk, *EC Law Versus Legal Monopolies: A Tense Relationship*, 5 INT'L BUS. L. J. 595 (1995).

195. See *id.*; Gardner, *supra* note 28; Maurits Dolmans, *Are Monopolies Compatible with the EC Treaty?*, Address at the 16th Annual Conference on Recent Developments on Competition Law (1993).

does not concern itself with the question of whether . . . enterprises enjoying such . . . exclusive rights are publicly or privately owned,"¹⁹⁶ it is clear that in almost all Member States the undertakings principally affected, such as post offices, telecommunications operators, and energy utilities, are publicly owned. Indeed, even the Commission concedes that "the entry of new competitors onto the market . . . will probably result in some privatization of these sectors."¹⁹⁷ In fact, the opening up of markets, which is also a result of EU deregulation initiatives, is creating a strong incentive for Member States to privatize previously monopolistic service providers. Once such undertakings are exposed to competition on a free market the arguments for continued state ownership are weakened. In such circumstances, privatization is both a means of raising revenue and of freeing public undertakings to compete fully in a deregulated market. Although the number of resulting privatizations may be small, their impact on the market is likely to be significant.

This new approach is a long way from that of the framers of the EC Treaty who, in 1957, tried to strike a balance between the free market and state planning through Treaty provisions such as Article 222, which provides that the EC Treaty will not prejudice national rules governing the system of property ownership, and Article 37, which calls on Member States to adjust only those state monopolies of a commercial character, i.e., non-production monopolies that discriminate between EU nationals. As one commentator puts it, these provisions "indicate that the framers of the Treaty of Rome wished to adopt a neutral position in the debate between state planning and free competition and that they preferred to leave to the Member States the liberty, within certain limits, to choose the appropriate model of economic organization."¹⁹⁸ In the European Union's new approach, characterized by the liberalization process, private undertakings have largely become the preferred business organizations of the EC legal order.

196. COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIRD REPORT ON COMPETITION POLICY 1993, at 30 ¶ 36 (1994).

197. *Id.* at 30 ¶ 41.

198. Gardner, *supra* note 28, at 78.

B. Article 90(1) of the EC Treaty

Article 90(1) obliges Member States not to enact or maintain measures contrary to the EC Treaty in relation to public undertakings¹⁹⁹ and undertakings entrusted with special or exclusive rights.²⁰⁰ Article 90(1) is thus infringed only in conjunction with other provisions of the EC Treaty.²⁰¹

Traditionally, the Court of Justice interpreted Article 90(1) narrowly, taking the view that the enactment or maintenance of an exclusive right could not, of itself, constitute a state measure contrary to Article 90(1).²⁰² More recently, however, the Court has developed a theory of structural abuse in relation to Article 90(1) that limits the power of Member States to establish and maintain exclusive rights.

C. The Traditional Interpretation of Article 90(1) of the EC Treaty

The traditional interpretation of Article 90(1) was estab-

199. Commission Directive No. 80/723, art. 2, O.J. L 195/35, at 36 (1980), as amended, defines public undertakings as:

any undertaking over which the public authorities may exercise directly or indirectly a dominant influence by virtue of their ownership of it, their financial participation therein, or the rules which govern it. A dominant influence on the part of the public authorities shall be presumed when these authorities, directly or indirectly in relation to any undertaking:

- (a) hold the major part of the undertaking's subscribed capital; or
- (b) control the majority of the votes attaching to shares issued by the undertakings; or
- (c) can appoint more than half of the members of the undertaking's administrative, managerial or supervisory body.

200. Commission Directive No. 90/388, art. 1, O.J. L 192/10, at 14 (1990). In Directive 90/388, special or exclusive rights are defined as "the rights granted through by a Member State or a public authority to one or more public or private bodies through any legal, regulatory or administrative instrument reserving them the right to provide a service or undertake an activity;" *see also* Telecom Services, ¶ 50, where Advocate General Jacobs states that exclusive rights are those granted to a single undertaking and special rights are those granted to a limited number of undertakings, but more than one.

201. Aurelio Pappalardo, *State Measures and Public Undertakings: Article 90 of the EEC Treaty Revisited*, EUR. COMPETITION L. REV. 29, 36 (1991). The Treaty provisions most commonly infringed in conjunction with Article 90(1) are Article 6 (non-discrimination on grounds of nationality), Articles 30 to 36 (free movement of goods), Article 48 (free movement of workers), Article 59 (free movement of services), Articles 52 and 53 (right of establishment), Article 85 (restrictive practices) and Article 86 (abuse of dominant position).

202. *See* Simon Taylor, *Article 90 and Telecommunications Monopolies*, EUR. COMPETITION L. REV. 322, 322 (1994).

lished by the Court of Justice in the *Sacchi* case.²⁰³ Under Italian law, Radio Audizioni Italiane enjoyed a monopoly over televised advertising. As part of that monopoly, other undertakings were prohibited from receiving audio-visual signals for the purpose of retransmission.

Mr. Sacchi, who had been fined for running an unauthorized cable television relay business, claimed that the Italian monopoly of television services contravened the rules of the EC Treaty on the ground that it infringed Article 90(1) in conjunction with Article 86. The Italian court referred the case to the Court of Justice under Article 177 for a preliminary ruling.

In his opinion to the Court, Advocate General Gerhard Reischl argued that the EC Treaty did not prohibit dominant positions *per se* and that "the dissolution of every kind of monopolistic structure cannot . . . be required by reliance on Article 86."²⁰⁴ He therefore concluded that the mere grant or extension of an exclusive right could not be contrary to Article 86 in the absence of "abuse" on the part of the undertaking benefiting from such rights. In the Advocate General's view, Article 86 could be infringed by an undertaking granted exclusive rights only where that undertaking made use of the dominant position that its exclusive rights conferred on it.

The Court of Justice followed the reasoning of the Advocate General. It held that "the interpretation of Articles 86 and 90 taken together leads to the conclusion that the fact that an undertaking to which a Member State grants exclusive rights has a monopoly is not as such incompatible with Article 86" and that "[i]t is therefore the same as regards an extension of exclusive rights following a new intervention by this State."²⁰⁵

Since only the abusive exercise and not the mere grant of an exclusive right could constitute an infringement of EC law, Article 90 could not be used in connection with Article 86 to dismantle legal monopolies. Either there was no abusive conduct on the part of the undertaking entrusted with the exclusive right, in which case Article 90 could not apply to the state measure that had established that right, or, the undertaking entrusted with the exclusive right engaged in abusive conduct, in

203. *Sacchi*, [1974] E.C.R. 409.

204. *Id.* at 441.

205. *Id.* at 441, ¶ 14.

which case Article 86 alone seemed applicable, since the infringement was not caused by the establishment of the right, but by the abusive behavior of the undertaking to which it had been granted.

This interpretation was systematically applied until the mid-1980's, when the Court of Justice and the Commission began to use Articles 90(1) and 86 to challenge the extension and, arguably, the very existence of monopoly rights.

D. *The New Theory of Structural Abuse*

In several recent cases, the Court of Justice adopted a much broader interpretation of Article 90(1), holding that, in conjunction with Article 86, it can apply to the existence of exclusive rights, conferring a dominant position on an undertaking in circumstances that inevitably lead to its abuse.²⁰⁶

In *Höfner*,²⁰⁷ a case referred by a German court, the Court of Justice was asked to give a preliminary ruling on issues relating to the exclusive right of the German national employment agency, Bundesanstalt für Arbeit, to provide recruitment and placement services and, in particular, on the rules prohibiting private companies from providing executive recruitment services.

A German company had engaged a private recruitment agency to assist in its search for an executive officer, but had ultimately decided not to retain the candidate suggested by the agency and had refused to pay its fees. Before the national court, the German company claimed that its contract with the recruitment agency should be annulled as it infringed the Bundesanstalt's monopoly of placement services. In response, the recruitment agency argued that the Bundesanstalt's monopoly violated Article 90(1) in conjunction with Article 86 and, as a result, was unenforceable.

Referring to the *Sacchi* case, the Court of Justice recalled that an undertaking entrusted with exclusive rights may be regarded as occupying a dominant position within the meaning of Article 86, but that the creation of such a dominant position by

206. See P. Manzini, *L'Intervento Pubblico Nell'Economia Alla Luce Dell'Art. 90 Del Trattato CE*, RIVISTA DI DIRITTO INTERNAZIONALE 379 (1995).

207. See *Höfner*, [1991] E.C.R. I-1979; see Piet Jan Slot, *Case Note*, 28 COMMON MKT. L. REV. 964 (1991).

granting exclusive rights within the meaning of Article 90(1) was not, as such, incompatible with Article 86.

The Court added that a Member State is in breach of the prohibition contained in Articles 90(1) and 86 "if the undertaking in question, merely by exercising the exclusive rights granted to it, cannot avoid abusing its dominant position."²⁰⁸ The Court indicated that this would be the case where an undertaking granted exclusive rights by a Member State to provide executive recruitment services is "manifestly not in a position to satisfy the demand prevailing on the market for activities of that kind" and "the effective pursuit of such activities by private companies is rendered impossible by the maintenance in force of a statutory provision under which such activities are prohibited and non-observance of that prohibition renders the contracts concerned void."

By identifying this new category of exclusive rights whose exercise necessarily leads to an abuse of dominant position, the Court of Justice established a bridge between what had appeared to be two mutually exclusive provisions and made Articles 90(1) and 86 applicable to the very existence of inefficient legal monopolies.

In *ERT*²⁰⁹ and *Porto di Genova*,²¹⁰ the Court confirmed this doctrine of structural abuse. In *ERT*, the Court held that Article 90(1) prohibits the establishment of a television broadcasting monopoly if establishing such a monopoly is "liable" to create a situation in which the undertaking enjoying the monopoly is led to infringe Article 86.

Similarly, in *Porto di Genova*, the Court considered that Article 90(1), taken together with Article 86, is infringed when an undertaking "merely by exercising the exclusive right granted to it cannot avoid abusing its dominant position or when such rights are liable to create a situation in which that undertaking is induced to commit such abuses."²¹¹ In the *Porto di Genova* case itself, the Court identified a number of Article 86 infringements

208. *Höfner*, [1991] E.C.R. at I-1987, ¶ 28.

209. *ERT*, Case C-260/89, [1991] E.C.R. I-2925, ¶ 37; see D. Chalmers, *Television and the Court of Justice*, 17 EUR. L. REV. 248 (1992).

210. *Merci Convenzionali Porto di Genova*, [1991] E.C.R. I-5889; see L. Gyslen, *Case Note*, 29 COMMON MKT. L. REV. 1229 (1992).

211. See e.g., *ERT*, [1991] E.C.R. at I-2946, ¶ 39 (providing example where Treaty is violated because undertaking cannot avoid abusing its dominant power); *Höfner*, [1991]

that the port companies were led to commit by reason of their exclusive rights, including requiring payment for services that had not been requested, charging unfair or discriminatory prices and failure to use modern technology.

In the *RTT* case,²¹² the Court of Justice went even further, taking the view that the extension of a legal monopoly through state measures to a separate but neighboring market also constituted a violation of Article 90(1) in combination with Article 86. The Court's reasoning was based on its established case law to the effect that an abuse within the meaning of Article 86 is committed when a dominant position on one market is used to monopolize a separate but neighboring market.²¹³ Referring to that case law, the Court held that Article 90(1) obliges Member States not to put public undertakings and undertakings entrusted with special or exclusive rights "in a position which the said undertakings could not themselves attain by their own conduct without infringing Article 86."²¹⁴ This holding implies that any state measure extending the dominant position of a public or privileged undertaking constitutes an infringement of Article 90 in conjunction with Article 86.

In sum, it is now settled case law that state measures creating or maintaining inefficient legal monopolies as well as those extending existing legal monopolies are, in principle, unlawful pursuant to Article 90(1) when taken together with Article 86.

E. *The Public Service Defense*

Article 90(2) provides that undertakings entrusted with the operation of services of general economic interest or having the character of a revenue-producing monopoly are subject to the rules of the EC Treaty, in particular the rules on competition, insofar as the application of those rules does not obstruct, in law or in fact, the performance of the particular tasks assigned to them.

As well as creating a public service defense for the undertakings to which it applies, Article 90(2) limits the application of

E.C.R. 1979 (providing example where Treaty is violated because undertaking is induced to commit abuses).

212. *RTT v. GB-INNO*, [1991] E.C.R. I-5941; see Gyselen, *supra* note 158.

213. *RTT v. GB-INNO*, [1991] E.C.R. I-5941.

214. *Id.*

Article 90(1) to state measures granting exclusive rights to such undertakings. As the Court of Justice's interpretation of Article 90(1) has become increasingly hostile to state monopolies, this aspect of Article 90(2) has become more important. The Court's recent case law, however, makes it clear that Article 90(2) provides only limited protection to public monopolies. Despite the fact that Article 90(2) is phrased expansively, applying the rules of the EC Treaty to undertakings performing public service duties only where this does not obstruct, in law or in fact, the performance of their tasks, the Court has applied it as a narrow exception to Article 90(1).

In *Corbeau*,²¹⁵ the Court of Justice was asked by a tribunal in Liège to give a preliminary ruling on the compatibility with Article 90 of a law imposing penal sanctions for infringement of the Belgian postal monopoly. The issue arose as a result of the prosecution of Mr. Corbeau for operating a private postal service in and around Liège.

Mr. Corbeau would collect mail from the homes of his customers in the evening and deliver it within the Liège area before noon the next day. He would put mail to be delivered outside the Liège area into the ordinary post.

In responding to the tribunal's question, the Court began its analysis by referring to Article 90(1), reiterating that the grant of an exclusive right does not of itself violate Article 86 and adding, citing *ERT*, that Member States are nonetheless obliged not to enact or maintain in force measures threatening the "effet utile" of that article. The Court gave no analysis, however, of the way in which the Belgian postal monopoly might violate Article 90(1) in conjunction with Article 86 or any other rule of the EC Treaty.

Instead, the Court moved directly to an examination of whether the Belgian postal monopoly could be justified under Article 90(2), which, according to the Court, permits Member States to:

[C]onfer on undertakings' to which they entrust the operation of services of general economic interest, exclusive rights which may hinder the application of the rules of the EC Treaty on competition insofar as restrictions on competition,

215. *Corbeau*, [1995] 4 C.M.L.R. 621. See Dolmans, *supra* note 166; Gardner, *supra* note 28; Gyselen, *supra* note 158; Taylor, *supra* note 173.

or even the exclusion of all competition, by other economic operators are necessary to ensure the performance of the particular tasks assigned to the undertakings possessed of the exclusive rights.²¹⁶

The Court accepted that the collection, transport, and distribution of mail is a service of general economic interest, since it is a service benefiting all users in the territory of the state, provided at "uniform tariffs and similar quality conditions, irrespective of the specific situations or the degree of economic profitability of each individual operation."²¹⁷ Consequently, the Court stated that it was necessary to examine whether restrictions on competition were necessary to allow the provision of that service on acceptable economic conditions. The Court recognized that this presupposed the possibility of cross-subsidizing less profitable aspects of the service with revenues from more profitable activities. Private enterprises should not be able to "cherry-pick" profitable parts of a service as they are under no obligation to undertake its loss-making aspects.

The Court concluded, however, that this did not mean that the exclusion of competition could be justified in relation to:

[S]pecific services dissociable from the service of general interest which meet special needs of economic operators and which call for certain additional services not offered by the traditional postal service . . . insofar 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.²¹⁸

The decision in *Corbeau* has two important aspects. First, while the Court refers to the "effet utile" of Article 86, it makes no express finding that either Article 86 or any other provision of the EC Treaty was breached in conjunction with Article 90(1). This has led some commentators to suggest that Article 90 must now be understood to permit state monopolies only where they can be justified under Article 90(2).²¹⁹ Others suggest that the

216. *Corbeau*, [1995] 4 C.M.L.R. 643, ¶ 14.

217. *Id.* at 643, ¶ 15.

218. *Id.* at 643, ¶ 19.

219. *See, e.g.* Gyselen, *supra* note 158.

case involves an implicit application of the structural abuse doctrine described above, i.e., a finding that the Belgian mail company had abused its dominant position by failing to develop new "value added" postal services for which a demand existed.²²⁰ This latter reading of the case is preferred, since it conforms better with previous case law and the wording of the EC Treaty.

Even if *Corbeau* does invoke an implicit finding of breach of Article 90(1) in combination with Article 86, the fact that the Court felt able to deal with the point so briefly underscores the extent to which public monopolies are now regarded as incompatible with EC law. Indeed, whatever the correct legal interpretation of *Corbeau*, in practice, the burden of proof may now be on state monopolies to justify their own continued existence.

The second important aspect of the *Corbeau* decision is the narrow interpretation given to Article 90(2), the scope of which was restricted in two ways. First, the Court defined services in the general economic interest narrowly, as services provided at a uniform tariff and similar quality without regard to profitability or particular circumstances. Second, the Court held that Article 90(2) limits the application of competition rules to a provider of a service of special economic interest only to the extent necessary to allow provision of the service on economically acceptable conditions. In particular, an exclusive right to provide services may not be extended to "dissociable" services, the provision of which by private operators does not threaten the economic equilibrium of the public monopoly.

This restrictive interpretation of Article 90(2) has now been confirmed by the Court's decision in *Almelo*,²²¹ a case concerning standard terms that breached Article 85 and, potentially, Article 86 in agreements between a Dutch regional electricity distributor and local distributors prohibiting the local distributors from importing electricity. In examining whether the import restriction could be justified under Article 90(2), the Court first determined that the supply of electricity was a service of general interest since it was provided at a uniform tariff and on terms that did not vary other than in accordance with objective criteria applicable to all customers. The Court then went on to state that the restriction on importing electricity was compatible with

220. See, e.g., Gardner, *supra* note 28, at 82; Taylor, *supra* note 173, at 329.

221. *Gemeente Almelo*, Case C-393/92, [1994] 2 C.E.C. (CCH) 281.

Article 90(2) insofar as it was necessary to allow that service to be carried out.

In examining the extent to which restrictions of competition, and in particular exclusive rights, are likely to be found necessary to ensure the provision of public services, it is interesting to note recent developments in the legislation concerning the liberalization of the telecommunications sector. Both the Council and Commission have recognized that the universal service obligation to provide a basic voice telephony service may involve the provision of services at a loss.²²² Traditionally, such services have been provided by national monopoly telecommunications undertakings that cross-subsidized them with revenues from other telecommunications services. Current proposals, however, for interconnection in telecommunications and the implementation of full competition in telecommunications markets envision that Member States should provide for the fulfillment of the universal service obligation either through supplementary infrastructure charges imposed on all telecommunications operators in the liberalized market, or through direct contributions levied on such operators.²²³ The implication of these proposals is that, at least in the eyes of the Commission, there are sectors in which exclusive rights cannot be justified by the need to provide public services. If that view were accepted by the Court of Justice, the public service defense of Article 90(2) would, in practice, provide no protection to monopoly rights granted in such sectors.

Article 90(2) must now, therefore, be understood as a narrow exception to the EC Treaty rules. Indeed, in light of the position now apparently taken by the Commission, it may be that, in practice, exclusive rights cannot be justified under Article 90(2).

222. Council Resolution of 7 February 1994, O.J. C 48/01 (1994) (concerning Universal Service Principles in the Telecommunications Sector); Green Paper on the Liberalization of Telecommunications Infrastructure and Cable Television Networks, *supra* note 164, § 5.

223. See Proposal for a European Parliament and Council Directive on Interconnection in Telecommunications, COM (95) 379, art. 5 (Eur. Comm'n July 1, 1995); Commission Notice, O.J. C 263/07 (1995) (concerning full competition in telecommunications markets).

F. *Article 90(3) of the EC Treaty: The Role of the Commission*

Article 90(3) gives the Commission the task of ensuring the application of Article 90, and grants it the power, where necessary, to address appropriate directives or decisions to Member States.

While the theory of structural abuse under Article 90(1) has challenged the existence of state measures creating or extending exclusive rights and the restrictive interpretation of Article 90(2) has limited the public service defense, the Commission has begun to use its powers under Article 90(3) to introduce legislation to break up traditional state monopolies.²²⁴ The importance of Article 90(3) is that it allows the Commission to act independently of the Council and Parliament. Other Treaty articles under which legislation of this sort might be adopted, such as Article 100a, which allows the adoption of harmonization legislation, grant the power to finally adopt legislation to the Council rather than the Commission, although the Commission initiates the legislative process.

The Commission first used Article 90(3) to enact legislation abolishing monopoly rights in 1988 when it adopted Commission Directive No. 88/301 on Terminal Equipment,²²⁵ which opened up the market for telecommunications terminal equipment. This new exercise of power by the Commission was immediately challenged.

In *Terminal Equipment*,²²⁶ France, supported by a number of other Member States, argued that rather than adopting the Terminal Equipment Directive under Article 90(3), the Commission should have proceeded individually against Member States whose telecommunications laws breached Article 90(1) under Article 169 and that the Commission's power to issue directives under Article 90(3) was restricted to situations in which it was unclear what action Member States were required to take in order to comply with the EC Treaty. France also argued that since the directive had the effect of restructuring the market for termi-

224. Gardner, *supra* note 28, at 84; Pijnacker Hordijk, *supra* note 194, at 603-11.

225. Commission Directive No. 88/301, O.J. L 131/73 (1988).

226. [1991] E.C.R. I-1223; see S. Wheeler, *Competition in the Telecommunications Sector*, EUR. L. REV. 67 (1992); J. Naftel, *The Natural Death of a Natural Monopoly: Competition in EC Telecommunications After the Telecommunications Terminals Judgment*, 14 EUR. COMPETITION L. REV. 105 (1993).

nal equipment, the appropriate basis for such legislation was Article 100a.

Despite suggestions in the opinion of Advocate General Giuseppe Tesouro that the use of Article 90(3) had indeed been improper, the Court rejected the challenge to the Commission's authority, finding that the purpose of Article 90(3) is different from that of Article 169 in that it gives the Commission the power to define the obligations imposed on Member States by Article 90(1) without the need to find that Member States are in breach of it. In addition, the Court held that the use of Article 90(3) was appropriate as its scope was more specific than Article 100a, since it expressly related to state measures as defined in Article 90(1).²²⁷

The Court's endorsement of the Commission's jurisdiction to attack public monopolies has allowed the Commission to continue to adopt legislation under Article 90(3) breaking up legal monopolies,²²⁸ particularly in the telecommunications field where technological progress has undermined the concept of "natural monopoly." The Court's support also appears to have "persuaded" Member States, through the Council, to enter actively into the liberalization process in order to retain some control over it.²²⁹ As a result, current legislative proposals for liberalization in the fields of electricity and gas relate to Council directives to be adopted under the Article 100a process.²³⁰

Article 90(3) has, therefore, both allowed the Commission to take action against state monopolies and, indirectly, led to the expansion of the liberalization process to include the Council and the Member States.

The developments in the law in relation to Article 90 all

227. However, in "Terminal Equipment" and "Telecom Services," the Court annulled the Commission Directives at issues insofar as they purported to apply to the grant of special (as opposed to exclusive) rights without defining such rights or explaining how they might infringe the treaty.

228. See, e.g., Commission Directive No. 90/388, O.J. L 192/10 (1990) (concerning Competition in the Markets for Telecommunication Services); Commission Directive No. 94/46, O.J. L 268/15 (1994) (concerning Satellite Communications Services); Commission Notice, O.J. C 263/07 (1995) (concerning full competition in telecommunications markets).

229. Gardner, *supra* note 28, at 85.

230. See e.g., Commission Communication, O.J. C 65/4 (1992) (concerning proposed Council Directive on internal market in electricity), amended by O.J. C 123/1 (1994); Commission Communication, O.J. C 63/14 (1992) (concerning proposed Council Directive on internal market in gas), amended by O.J. C 123/1 (1994).

move in a single direction, against state monopolies. The new theory of structural abuse under Article 90(1) and the gradual expansion of its scope, means that, in principle, state monopolies may now in many cases be unlawful, while the narrow interpretation given to the public service defense in Article 90(2) has reduced the circumstances in which otherwise unlawful monopolies can be justified on public interest grounds. Meanwhile, the volume of legislation actively dismantling legal monopolies has increased as the Commission, with the support of the Court, has made use of its powers under Article 90(3) and the Council has been persuaded to take part in the process.

This process of limiting and even eliminating national monopolies through EC competition rules is bound to speed up the pace of privatization, in particular of public utilities. Provided that universal service in public utilities is safeguarded, the new regulatory environment makes it easier for Member State governments to justify to public opinion disengagement from previously monopolistic undertakings, thus freeing up state resources without cutting spending and realizing revenues without raising taxes. In addition, successful publicly owned undertakings are likely to exert pressure to be freed from state interference to compete in liberalized markets. Consequently, in sectors previously characterized by state intervention through state-owned undertakings, private companies are likely to become, over time, with the encouragement of EC law, the typical market participants.

III. *PRIVATIZATION AND STATE AID RULES*

A. *General Principles: An Overview*

Article 92(1) of the EC Treaty²³¹ provides that any aid granted by a Member State or through state resources, in any form whatsoever, which distorts or threatens to distort competition by favoring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be deemed incompatible with the common market. Article 92(1) together with the other Treaty rules relating to state

231. Similar provisions are contained in Articles 4(c), 54-56 of the ECSC Treaty; not, however, in the EAEC Treaty. This Essay focuses on the provisions of the EC Treaty and only refer to the ECSC Treaty in so far as privatization of undertakings covered by the latter Treaty are affected.

aid, do not prohibit all state aid, but only aid that may distort competition and affect trade between Member States. Rules on state aid were, at least originally, seen not so much as an instrument for reducing subsidies in general, but as a mechanism for ensuring that the establishment and development of the common market was not undermined by the granting of state aid to national producers in a way that would give them an unfair competitive advantage and delay necessary structural change.²³² Thus, in contrast with the ECSC Treaty,²³³ the EC Treaty does not impose an absolute ban on state aids. Indeed, Article 92(2) creates various mandatory exceptions to the general prohibition of aid for certain categories of state support, and the Commission may, at its discretion, authorize: aids in particularly depressed regions;²³⁴ aids to promote important European projects or to remedy a serious disturbance in a Member State,²³⁵ and, sectorial and regional aids which do not adversely affect trading conditions to an extent contrary to the common interest.²³⁶ Although these exceptions are to be construed in a restrictive manner,²³⁷ the Commission enjoys broad discretionary powers as to their definition and application.²³⁸

Although it has been suggested that the EC rules on state aid have indirectly had a profound effect on privatization,²³⁹ those rules do not, and pursuant to Article 222 cannot, specifically address privatization issues. Article 222 stipulates that the EC Treaty shall in no way prejudice the rules in Member States governing the system of property ownership. The EC Treaty is neutral as between public and private ownership. Member States are, therefore, fully entitled to establish and maintain public undertakings, to nationalize entire sectors of the economy, and to acquire or increase shareholdings in companies.²⁴⁰ While

232. See COMMISSION OF THE EUROPEAN COMMUNITIES, TWELFTH REPORT ON COMPETITION POLICY 1982 109-10, ¶ 158 (1983).

233. Treaty Establishing the European Coal and Steel Community (ECSC), Apr. 18, 1951, 261 U.N.T.S. 140.

234. EC Treaty, *supra* note 1, art. 92(3)(a), [1992] 1 C.M.L.R. at 630.

235. *Id.* art. 92(3)(b), [1992] 1 C.M.L.R. at 630.

236. *Id.* art. 92(3)(c), [1992] 1 C.M.L.R. at 630.

237. *Philip Morris* [1987] E.C.R. at 4577, ¶ 37.

238. Fritz-Harald Wenig, Artikel 92-94, in Groeben, Thiesing, Ehlermann, Kommentar zum EWG-Vertrag ¶ 39 (4th ed. 1991).

239. Abate, *Droit Communautaire, Privatisations, Déréglementations*, in *REVUE DU MARCHÉ UNIQUE EUROPÉEN* 69-71 (1994).

240. HANCHER ET AL., EC STATE AIDS 12.2 (1993).

the Commission has always been cautious in referring to this principle of neutrality,²⁴¹ it has constantly stressed, following the jurisprudence of the Court of Justice, that pursuant to Articles 3(f), 5, and 90(1) of the EC Treaty private and public undertakings must be treated equally and that the EC rules on competition, and in particular those relating to state aid, apply equally to public and private undertakings.²⁴²

B. *Reasons for Privatization of Public Undertakings*

While some public undertakings are involved in commercial activity, most pursue non-economic goals, such as providing basic and universal services, maintaining an adequate level of employment, or furthering regional development. As a consequence of their non-economic functions, and, occasionally, lax management, public undertakings have frequently encountered financial difficulties and have often been able to survive only as a result either of being sheltered from competition or being granted state aid. The adverse effect that such protective measures may have both on competition and trade between Member states is obvious. The problem is aggravated by the fact that a state's role as the protector of the public interest may become confused with its economic role as the owner of public undertakings. The potential magnitude of this problem becomes apparent when the role played by the public sector in the economies of most Member States is considered. In the Member States of Southern Europe, in late 1991, public undertakings represented an average of 20% of the national economy. In other Member States the figure was approximately 12%.²⁴³

241. Commission Communication, O.J. C 307/3, ¶ 4 (1993) (to Member States on Application of Articles 92 and 93 of the EEC Treaty and of Article 5 of Commission Directive 80/723 to Public Undertakings in the Manufacturing Sector); COMMISSION OF THE EUROPEAN COMMUNITIES, XXIST COMPETITION REPORT 1991, at 126-27, ¶ 168 (1992).

242. *See, e.g.*, France, Italy and UK & N.I. v. Commission, Joined Cases 188 to 190/80, [1982] E.C.R. 2545.

243. This data is based on statistics provided by the European Center for Public Undertakings. *Les Entreprises à Participation Publique dans l'Union Européenne*, ANNALES DU CEEP (1994). The public sector accounted, at the end of 1991, for 19% in Italy, 18% in France, 23% in Portugal, and 20% in Greece. For the purpose of these statistics, by the term "public undertakings" reference is made to those entities engaged in manufacturing and services, excluding agriculture, which are under the control of a State either through its shares or its voting rights. Central and local governments, as well as social security administrations, are not taken into account. Abate, *supra* note 239, at 15.

Public undertakings have come under pressure as a result of several interrelated developments. First, the gradual process of European integration, and in particular the creation of the Single Market as envisaged in the Single European Act in 1986,²⁴⁴ has led to the progressive dismantling of trade barriers. This process has gradually exposed public undertakings to competition and has, as a result, increased their reliance on state aid. At the same time, the significance of the distortion of competition and intra-Community trade resulting from the grant of state aid to public undertakings, much of it illegal, has become increasingly apparent. After its first comprehensive survey of state aid,²⁴⁵ the Commission concluded that, with the completion of the internal market in 1992, state aid would be one of the few remaining mechanisms by which Member States could pursue protectionist policies in intra-Community trade.²⁴⁶ A stricter enforcement of state aid rules was, therefore, seen as an important means of protecting the benefits generated by the Single Market.²⁴⁷ The White Paper on growth, competitiveness, and employment²⁴⁸ emphasized that part of the reason for the European Union's recent poor record of growth and job creation was its resistance to structural adjustment caused, *inter alia*, by an artificially large public sector and unwarranted state aid to public undertakings. The control of state aid was, therefore, regarded as "part of the essential regulatory framework which will underpin and facilitate achievement of the objectives of the White Paper."²⁴⁹

As the importance of controlling state aid has grown, Community institutions have gradually developed, from the principles enshrined in the EC Treaty, a detailed and comprehensive set of both substantive and procedural rules governing state aid. This development, and in particular the policies and rules adopted by the Commission and the Court of Justice in dealing with state aid granted to public undertakings, merit in-depth

244. SEA, *supra* note 1, O.J. L 169/1 (1987), [1987] 2 C.M.L.R. 741.

245. First Survey on State Aids in the European Community, Brussels-Luxembourg (EN ISBN 92-825-9535-8, 1988).

246. COMMISSION OF THE EUROPEAN COMMUNITIES, NINETEENTH COMPETITION REPORT 1990, at ¶ 119 (1990).

247. *Id.* at ¶ 169.

248. Com (93) 700 Final.

249. COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIrd COMPETITION REPORT 1993, at ¶¶ 27-30 (1993).

analysis to assess their influence on the privatization process in the Member States of the European Union.

In many cases, public undertakings are privatized because they have become a financial burden that Member States can no longer can afford, for either legal or budgetary reasons. The privatization of public undertakings usually involves substantial injections of capital to attract private buyers or investors. EC rules on state aid do not expressly promote privatization, although they have in a number of instances been used to that end. That the granting of state aid in the context of a privatization is subject to the same substantive rules and procedures as any other form of state aid is confirmed by the Commission's approach to the approval of both the Greek and Portuguese privatization programs, as well as the Commission's approach to the privatization by the Treuhand of the companies formerly owned by East Germany following German reunification.

C. State Aid Rules: The Court and the Commission Approaches

A comparison of the papers on state aid presented to the Fordham Corporate Law Institute by Manfred Caspari in 1983,²⁵⁰ and Claus-Dieter Ehlerman in 1994,²⁵¹ both at the time responsible for the Commission's competition policy, clearly indicates that state aid rules have undergone considerable development, leading to stricter enforcement by the Commission, supported by the Court of Justice.

Articles 92 to 94 of the EC Treaty set out only the basic principles of state aid law. Thus, only the Article 92(3) duty to notify has been found to be directly applicable by the Court of Justice.²⁵² As a result, Articles 92 to 94 give the Commission broad discretion to determine the legal status of state aid. Indeed, the Commission was obliged to determine the forms of state assistance that qualify as aid within the meaning of Article 92(1)²⁵³ on

250. Manfred Caspari, *State Aids in the EEC*, in 1983 FORDHAM CORP. L. INST. 1 (Barry Hawk ed., 1984).

251. Claus-Dieter Ehlermann, *State Aids under European Community Law*, 1993 FORDHAM CORP. L. INST. 55 (Barry Hawk ed., 1994).

252. *Lorenz v. Germany*, Case 120/73, [1973] E.C.R. 1471, ¶ 8.

253. There have been many attempts to define the concept of State aid. See, e.g., DESPINA SCHINA, *STATE AIDS UNDER THE EEC TREATY* arts. 92-94 (1987). Rather than establishing abstract definitions the Court as well as the Commission have so far relied on descriptions of State Aid as working definitions, Wenig in Groeben, Thiesing, & Ehlermann, *KOMMENTAR ZUM EWG-VERTRAG*, art. 92, ¶ 4.

a case by case basis before the state aid rules could have a substantial impact.²⁵⁴ This approach was necessitated by the fact that state aid rules are a unique feature of Community law, so there were no models to guide their development. A case by case approach was necessary not only in relation to the rules governing the application of the discretionary exceptions in Article 92(3), but also as regards the procedural rules set out in Article 93. Gradually, a jurisprudence evolved around the core of Articles 92 to 94, through a dialogue between the Commission and the Court of Justice. During the 1960's the Court rendered only five cases, only twenty-three during the 1970's. In the early 1980's, the Court started to produce judgments of major importance in this area.²⁵⁵

The worldwide recession triggered by the oil crisis in the early 1970's, and the resulting desire of Member States to give financial support to their national economies, led to a greater appreciation within the Commission of the harmful effects of such support on intra-Community trade.²⁵⁶ This, in turn, led to an increased focus on the economic impact of state aid law.

The 1970's also saw the introduction of policy guidelines, the so-called frameworks, dealing with the problems raised by state aid in various industrial sectors including textiles, synthetic fibers, and, somewhat later, motor vehicles.²⁵⁷ There was a general perception at that time, that as "sensitive" economic sectors, these industries should be protected and might therefore legitimately be granted some degree of state aid, provided that the aid could be controlled in a way that would avoid a surge in counter-productive measures. In any event, in the view of some scholars, these frameworks were "more a damage limitation exercise than an expression of policy driving for a reduction of aid and the attainment of the EC Treaty's system of undistorted

254. The wealth of Commission Directives, Notices and frameworks has been collected in the second volume of: *Competition Law - Compendium of the Commission of 1989*. See also Della Cananea, *Administration by Guidelines: The Policy Guidelines of the Commission in the Field of State Aids*, in HARDEN, *STATE AID: COMMUNITY LAW AND POLICY* [page number] (1993).

255. See, e.g., *Philip Morris v. Comm'n*, Case C-730/79, [1980] E.C.R. 2671; *France v. Commission*, Case C-301/87, [1990] E.C.R. I-307.

256. Abate, *supra* note 239, at 31.

257. See Frank Rawlinson, *The Role of Policy Frameworks, Codes and Guidelines in the Control of State Aid*, in HARDEN, *STATE AID: COMMUNITY LAW AND POLICY* 52 (1993).

competition."²⁵⁸

The 1980's saw significant development in EC state aid rules. In its *Phillip Morris* decision,²⁵⁹ which was upheld by the Court in 1980,²⁶⁰ the Commission developed the concept of compensatory justification, i.e., that aid can be allowed only if it furthers the objectives and interests set out in Article 92(3). The national interest of a Member State and the benefit to the recipient of aid are not in themselves sufficient.²⁶¹ The concept was further elaborated in the Twelfth Competition Report,²⁶² which set out its requirements that the aid should promote development that is in the interest of the European Union as a whole, that the aid should be necessary for the achievement of that development, and that the modalities of the aid, such as its intensity, duration, and impact on competition, should be commensurate with the importance of its purpose.²⁶³

In relation to aid for the restructuring of ailing companies, which is often a first step towards privatization, the Commission has introduced the additional concept of compensatory contribution.²⁶⁴ This requires that the company receiving aid implement a restructuring plan that will enable it to become viable within a short period; aid that merely maintains the status quo is not, therefore, acceptable.²⁶⁵ Furthermore, the aid recipient makes a contribution to the Community interest, which in the case of companies operating in industries suffering from structural over capacity will comprise a reduction in production capacity.²⁶⁶

Parallel to the development of increasingly stringent criteria

258. Ehlermann, *supra* note 251, at 6.

259. Commission Decision No. 79/743/EEC, O.J. L 217/17 (1979).

260. *Phillip Morris*, [1980] E.C.R. 2671.

261. COMMISSION OF THE EUROPEAN COMMUNITIES, XTH REPORT ON COMPETITION POLICY 1980 ¶ 216 (1980).

262. COMMISSION OF THE EUROPEAN COMMUNITIES, TWELFTH REPORT ON COMPETITION POLICY 1982 (1983).

263. *Id.* at 110-11, ¶ 160.

264. Community Guidelines on state aid for rescuing and restructuring firms in difficulty, 94/C 368/05, O.J. C 368/12 (1994).

265. *See, e.g.*, Alfa Romeo v. Commission, Case C-305/89, [1991] E.C.R. I-1616.

266. *See* Commission Decision No. 89/58/EEC, O.J. L 28/1, at 92 (1989) [hereinafter Rover]. *See also* Commission Notice, O.J. C 6/92, at 4 (1995) [hereinafter CMF Decision]. In CMF Decision, the Commission cleared the aid granted by the Italian authorities in the form of financial contributions in favor of two construction companies. *Id.*

for the exercise of the Commission's discretion under Article 92(3), procedural developments have made the control of state aid more effective. Prior to 1980, the Commission had repeatedly noted²⁶⁷ that the control of state aid was greatly hindered by the fact that many state aids were not reported to it, in breach of the requirements of Article 93(3). As a result, in 1980, the Commission sent a letter to the Member States reminding them of their obligation to notify planned aid before granting it.²⁶⁸ Despite this very public reminder, Member States continued to fail to notify aid. This led the Commission to announce, in 1983, that it would systematically order the recovery of state aid that did not meet the exemption requirements.²⁶⁹ At the same time, the Commission warned undertakings receiving aid of the risk that non-notified aid would have to be paid back. As well as controlling new state aid more rigorously, the Commission began to review existing aid schemes more systematically under the Article 93(1) procedure.²⁷⁰

The procedural powers of the Commission were greatly enhanced by the Court's ruling in *Boussac*.²⁷¹ Although the Court rejected the Commission's argument that failure to comply with the notification requirement of itself justified a finding that aid was unlawful,²⁷² it found that the Commission was entitled, after giving the Member State an opportunity to submit its comments, to require the suspension of payment of non-notified aid while it

267. Commission Communication, O.J. C 318/3 (1983) (to Member States and potential recipients of State aid on application of Articles 92 and 93 to the refund of illegal State aid); *see, e.g.*, COMMISSION OF THE EUROPEAN COMMUNITIES, XTH REPORT ON COMPETITION POLICY 1980, at ¶ 162 (1980).

268. Commission Information, O.J. C 252/2 (1980) (to Member States on failure of Member States to respect their obligations pursuant to Article 93(3) with respect to the notification of State aids).

269. Commission Communication, *supra* note 267, O.J. C 318/3 (1983).

270. *See, e.g.*, COMMISSION OF THE EUROPEAN COMMUNITIES, NINETEENTH REPORT ON COMPETITION POLICY 1989, at 127, ¶ 119 (1990).

271. *France v. Commission*, Case C-301/87, [1990] E.C.R. I-307.

272. In *Fédération nationale du commerce extérieur des produits alimentaires et syndicat national des négociants et transformateurs de saumon v. France*, Case C-354/90, [1991] E.C.R. I-5505 (the "French Salmon" case), the Court of Justice stated, however, in a referral for preliminary ruling from the French Conseil d'Etat, that Member States courts are entitled to declare unnotified aid unlawful. *Id.* The notification and prior authorization of an aid, before it is granted, are strict requirements for its validity. *See* Community Guidelines on State Aid for Rescuing and Restructuring Firms in Difficulty, 94/C 368/05, O.J. C 368/12 (1994) [hereinafter State Aid Guidelines]; Commission Communication, *supra* note 267, O.J. C 318/3 (1983).

examined the aid's legality. Where a Member State failed to comply with such an interim decision the Commission could refer the matter directly to the Court, seeking interim measures under either the second subparagraph of Article 93(2) or Article 169. The Commission has since made systematic use of this procedure and recently informed Member States that in appropriate cases it may, after giving the Member State concerned the opportunity to comment, order the recovery of aid paid out in breach of procedural requirement.²⁷³

D. *State Aid to Public Undertakings*

It is in the context of these general developments in state aid law that the Commission's increasing scrutiny of the aid granted to public undertakings must be understood. As early as its first Competition Report in 1971,²⁷⁴ the Commission expressed its concern over state intervention to support ailing public undertakings. The main obstacle faced by the Commission in policing such state intervention was a lack of transparency. Often the Commission had no way of discovering financial transactions taking place between the state and public undertakings. In order to ensure the effective application of state aid rules to public enterprises, in 1980 the Commission issued Directive 80/723 on the transparency of financial relations between Member States and public undertakings under Article 90(3).²⁷⁵ In essence, the Directive requires Member States to ensure that information concerning financial relations between public authorities and public undertakings is available to the Commission. In 1985²⁷⁶ and again in 1993,²⁷⁷ the scope of the Directive was extended to sectors not originally covered, namely: water, energy,

273. Commission Communication, O.J. C 156/05 (1995) (to member States advising that the Commission may order recovery of illegal rescue aid to undertakings to counteract infringements of Article 93).

274. COMMISSION OF THE EUROPEAN COMMUNITIES, FIRST REPORT ON COMPETITION POLICY 1971, at ¶ 192 (1972).

275. Commission Directive No. 80/723, O.J. L 195/35 (1980), *amended by* O.J. L 229/20 (1985) (Transparency of Financial Relations Directive) (concerning transparency of financial relations between Member States and undertakings).

276. Commission Directive No. 85/413, *amending* Commission Directive No. 80/723, O.J. L 229/20 (1985).

277. Commission Directive No. 93/84, *amending* Directive No. 80/723, O.J. L 254/16 (1993). An earlier Commission Communication had been annulled by the Court, because it was based on the wrong legal basis. Commission Communication, O.J. C 273/2 (1991); *France v. Commission*, Case C 325/91, [1993] E.C.R. I-3283. The pres-

postal services, telecommunications, transport, credit institutions, and manufacturing. The Directive defines both public undertakings and state aid broadly. Thus, not only the setting-off of operating losses but also the provision of capital and the foregoing of a normal return on funds invested may be regarded as state aid, and may, as a result, require prior investigation by the Commission.²⁷⁸ This has enabled the Commission to extend the application of the state aid rules to areas that were previously exempt from them. The Directive's validity has been confirmed by the Court,²⁷⁹ which, while acknowledging that the situations of public and private undertakings are not necessarily comparable, upheld the Directive, *inter alia*, on the basis that public undertakings may compete directly with private ones and should, therefore, be treated in the same way.

In a communication to the Member States, the Commission summarized the so-called market economy investor principle by which the Commission determines whether a Member State's assistance of a public undertaking, for example, by way of capital injection, involves state aid.²⁸⁰ To apply the principle, the Commission examines whether a private investor seeking a reasonable return and ignoring all social, regional, and sectorial policy considerations would have been willing to make a similar investment. If not, the state assistance is deemed to be aid. This approach, which the Commission has applied consistently since it was announced, has been upheld by the Court in a number of cases.²⁸¹ Indeed, in *Alfa Romeo*, the Court developed the market economy investor principle, making a distinction between short-term private investors and private holding groups with a longer term perspective.²⁸² Public holding companies injected significant amounts of capital into Alfa Romeo, despite the fact that the company had been accumulating losses for twelve years and had not been restructured. The Court found that while the

ent Directive was subsequently issued together with the Commission Communication 93/C307/03, O.J. C 307/3 (1993) (to Member States).

278. Commission Directive No. 80/723, art. 3, O.J. L 195/35, at 36 (1980).

279. France, Italy and UK v. Commission, Joined Cases 188 to 190/80, [1982] E.C.R. 2545.

280. 7 EC BULL., no. 9, at 94 (1984).

281. Belgium v. Commission, Case 234/84, [1986] E.C.R. 2280; Belgium v. Commission, Case C-142/82, [1990] E.C.R. I-959 [hereinafter *Tubemeuse*].

282. Italy v. Commission, Case C-305/89, [1991] E.C.R. I-1603 [hereinafter *Alfa Romeo*].

holding company of a private group might take investment decisions at the group level and in a wider economic context that would take into account the negative impact of short-term decisions on the group's reputation, the Commission had nonetheless been correct in deciding that the capital injected into Alfa Romeo qualified as state aid, since, even in the long term, no acceptable rate of return on the capital could be expected.²⁸³

The Commission, with the support of the Court, has applied the market investor principle and ordered Member States to recover aid, even where this has resulted in the public undertaking involved ceasing all economic activity.²⁸⁴ *Boch*²⁸⁵ is a typical case. In *Boch*, the Court held that the Belgian Government was in breach of EC law for failing to recover state aid granted to Boch. The Court rejected the Government's submission that Boch's financial position was such that it could not repay the aid, indicating that the objective of abolishing the aid could be achieved by winding up the company, a process which the Belgian authorities could institute in either its capacity as shareholder or as creditor.

The Commission's application of Directive 80/723 on transparency and the market economy investor principle, together with the systematic recovery of illegal state aid, has forced public undertakings to compete with private undertakings on equal terms. Consequently, Member States have been effectively prevented from pursuing non-economic goals through public undertakings. This has meant that much of the incentive for Member States to bear the economic burden of owning public undertakings has been removed. It has been suggested that this has led Member States, even if indirectly, to begin or to accelerate the process of privatization.²⁸⁶ While, in Italy, budgetary constraints were also an important factor, the pressure exerted by state aid rules is seen as one motive for the Italian privatization programs of the 1990's.²⁸⁷ The Agreement reached between the Commission and the Italian Government in 1993 on the indebt-

283. Commission Guidelines, O.J. C 368/19 (1994).

284. *Tubemeuse*, Case C-142/87, [1990] E.C.R. I-959.

285. Commission v. Belgium, Case 52/84, [1986] E.C.R. 100, 104.

286. Abate, *supra* note 239, at 35.

287. *Id.* For further reference to Gobbo-Cazzola, see *Privatizzazioni e concorrenza*, in ACQUISIZIONI FUSIONI CONCORRENZA 64 (1993).

edness of Italian public enterprises clearly reflects this.²⁸⁸ Under the Agreement, the debts of Italian public enterprises are to be frozen at the level reached at the end of 1993, and are to be gradually reduced between 1994 and 1996. Thereafter, the Government is to sell at least part of its interest in those enterprises wholly owned by it, so as to terminate the automatic state guarantee of their indebtedness.

As illustrated by the compensatory contribution concept described above, the approval of aid, in particular in the context of restructuring, can be conditional on significant commitments from the aid recipient, such as closing excess capacity, reducing market share, or abandoning certain business activities.²⁸⁹ The principle of neutrality in Article 222 means that the Commission cannot officially seek a commitment to privatize a public undertaking as a precondition to approving state aid. Nonetheless, the Commission's approval of aid is often preceded by lengthy and intensive negotiations between the Member State granting the aid and the Commission. It is perhaps not uncommon during such negotiations for Commission officials to suggest that the donor state formally propose the privatization of the recipient public undertaking. This allows the Commission to avoid stating publicly that its decision to approve the aid was conditional on privatization. Although it is difficult to produce hard evidence that this occurs, the Commission's decision to approve aid to the French electronics group Bull²⁹⁰ suggests that it does. In its decision, the Commission first referred to an independent consultants report finding that privatization was the only way for the Bull group to survive, the Commission then endorsed this view and stated that it was shared by the French Government, which then proposed to privatize the group.²⁹¹

288. Commission Press Release Memo/94/67 of November 10, 1994 on Community State Aid Policy. *See also* Commission Notice, O.J. C 349/02 (1993) (agreement of aid from Italy to EFIM).

289. *See* Commission Guidelines, O.J. C 368/19, ¶¶ 3.2 *et seq.* (1994).

290. Commission Decision No. 94/1073/EC, O.J. L 386/1 (1994) (Bull).

291. *Id.* at 10 ("the Commission also recognizes the effect of Article 222 . . . and, therefore, the Commission appreciates that it cannot request or oblige the privatization of Bull. However it is also apparent that the French Government itself wishes to privatize the group and has made this fact known to the Commission.").

E. Constraints on Privatization Imposed by State Aid Rules

In recent years, the Commission has repeatedly stressed²⁹² the importance of liberalizing key sectors of the economy, which more often than not involves the privatization of those sectors. Aid that facilitates privatization is not exempt from the basic principle that state aid is incompatible with the common market, pursuant to the principle of neutrality in Article 222. Privatization aid can give the recipient an unfair competitive advantage that may prevent competition from developing, thereby defeating the purpose of liberalization.

While Member States may chose to privatize public undertakings for policy reasons, in most cases, public undertakings are privatized because they have become a political or financial burden that the Member State can no longer bear. Where this is the case, the public undertaking involved will likely require some form of financial assistance in order to attract buyers. Such assistance, whether it is provided by the writing off of debts or by the conversion of debt into capital, will in most cases constitute state aid within the meaning of Article 92(1) and is, therefore, subject to investigation by the Commission. Because it may be difficult to determine whether the measures taken during a privatization constitute state aid, the Commission has established guidelines in a number of its decisions for determining when notification under Article 93(3) is necessary.²⁹³ Where a public undertaking is sold on the stock market or is subject to an unconditional public offer involving non-discriminatory and transparent procedures the Commission considers that no aid is involved. If the sale is made via a restricted procedure, however, and is preceded by a debt write-off or is subject to conditions that would not be acceptable in a transaction between market economy investors, the sale must be notified as it may contain elements of state aid. The latter criterion is of particular interest in that it clearly implies that Member States should consider the winding up of an ailing public undertaking as an alternative to privatization, where this would be a cheaper alternative. In as-

292. COMMISSION OF THE EUROPEAN COMMUNITIES, XXIIIRD REPORT ON COMPETITION POLICY 1993, at 31, ¶ 37 (1994).

293. Commission Notice, O.J. C 253/3, at 4 (1993) (Portugal decision) (advising other Member States and interested parties concerning Law No 11/90 of 5 April 1990 on the program for the reprivatization of enterprises nationalized after 25 April 1974 in Portugal).

sessing the alternatives, the Commission disregards the costs a Member State may ultimately incur through the payment of unemployment or other social benefits.

Since the *Rover*²⁹⁴ decision of 1988, the Commission has conditioned its consent to privatization aid on the establishment of a detailed and realistic restructuring plan enabling the undertaking to improve its long-term profitability, while at the same time reducing its production capacity. While the Commission will in most cases review privatization aid in accordance with the restructuring guidelines,²⁹⁵ it will generally accept business plans drawn up by private investors without review, on the grounds that, unlike a Member State, a private investor will neither be tempted to bail out the privatized undertaking if the restructuring fails, nor have the financial capacity to do so. The Commission will not, however, clear privatization schemes that grant the private investor an unfair competitive advantage through overgenerous terms of sale, as was the case in *Rover*.²⁹⁶ On the same basis, the Commission held that the unlimited guarantee granted to the buyer of a joint-stock company from the state holding group EFIM was unlawful aid in the context of the privatization of public undertakings formerly owned by the state holding group EFIM.²⁹⁷ Although the Italian Government did not write off the debts of all privatized companies, Article 2362 of the Italian Civil Code²⁹⁸ made the state holding company liable for all debts incurred by companies to be privatized.²⁹⁹ In 1993, a political agreement was reached between the Commission and the Italian Government imposing a strict ceiling on the debts of Italian State holding companies, thereby ensuring the effective application of EC rules to future Italian privatizations.³⁰⁰

The Commission also applied these criteria to the recent

294. *Rover*, O.J. L 28/1, at 92 (1989).

295. Commission Guidelines, O.J. C 368/19 (1994).

296. *See Rover*, O.J. L 28/1, at 100 (1989). The Commission decided that £331 million out of an envisaged aid of £800 million was incompatible with the Treaty and could therefore not be granted. *Id.*

297. Commission Notice, O.J. C 349/02 (1993) (agreement of aid from Italy to EFIM).

298. Art. 2362 C.c. (Italy).

299. *Id.* Article 2362 of the Italian Civil Code reads: "Sole Shareholder. For obligations of the company which arose during the period in which the shares are shown to have belonged to one person only, such person is liable without limitation in the case of insolvency of the company." *Id.*

300. *Id.*

privatization programs of Greece³⁰¹ and Portugal.³⁰² Due to the severe economic situation in Greece during the privatization of the 208 undertakings owned by the Business Reconstruction Organization, the Commission approved certain state aids under Article 92(3)(b) as part of the privatization process. In doing so, the Commission may have adopted a generous approach to applying state aid rules, in the hope that privatization would mean that no further aid would be granted to undertakings involved.

F. *The Treuhand: The German Experience*

As well as creating problems for the Government of the Federal Republic, German unification raised a number of difficult issues concerning the extent to which the Commission could or should approve aid linked to the privatization of the undertakings formerly owned by the East German Government. At the moment of German reunification on October 3, 1990, the geographical scope of the EC Treaty was extended to cover the former East Germany. Although interim measures in relation to East Germany were granted in certain areas of Community law,³⁰³ state aid rules were applied with immediate effect. This point is worthy of note, since, in the accession treaties of most new Member States, transitional periods for the application of state aid rules were granted. In relation to East Germany, only two legislative changes were made, in relation to shipbuilding and the steel industry.

A few months prior to reunification, the acting Government of East Germany set up the Treuhand, in cooperation with the West German Federal Government, as a holding company for all the undertakings previously controlled by the state, which were converted into either joint-stock companies or limited liability companies. After restructuring, the Treuhand held, at its peak, almost 10,000 companies and was the world's largest holding

301. See Panayotis Bernitsas, *State Aids and Public Undertakings*, in Harden, *STATE AID: COMMUNITY LAW AND POLICY* (1993).

302. See Commission Notice, O.J. C 253/3 (1993). On October 10, 1995, the Commission decided not to raise objections on the privatization of the Companhia Nacional Petroquímica ("CNP"), the publicly held Portuguese petrochemical company, to be achieved through a direct sale from the Portuguese government to Borealis, a Danish petrochemical company. CNP, created in 1972, has been a public sector company since 1982. *Id.*

303. Commission Regulation No. 2761/90, O.J. L 267/1 (1990); Council Regulation No. 3569/90, O.J. L 353/7 (1990).

company. The law establishing the Treuhand³⁰⁴ stated that its aim was to restructure the economy of eastern Germany by privatizing formerly state-owned undertakings and financing necessary infrastructure investment with the proceeds of privatization. It soon became clear, however, that the rapid transition from a planned to a market economy, together with the loss of markets in the former COMECON³⁰⁵ states, meant that virtually none of the companies then held by the Treuhand could survive without substantial investment. Thus, a number of measures, often including the financing of ongoing business operations, were necessary to prevent the economic collapse of entire regions and to prepare for a massive privatization program. The Commission indicated that the write-offs of debt incurred under central planning and exemptions from liability for environmental damage caused before July 1, 1990, would not be regarded as aid, since such measures did not confer any competitive advantage on the beneficiary.³⁰⁶ Furthermore, while credits and guarantees provided by the Treuhand to companies that remained under its ownership generally involved aid, the Commission decided to examine such cases flexibly, in view of the need to develop the economy of the former East Germany.³⁰⁷ Although the Commission insisted on being notified of all measures that might potentially involve state aid, it announced that it would adopt a sensitive and flexible approach in the application of state aid rules.³⁰⁸ In addition, the Commission unilaterally decided to speed up the procedure for reviewing notifications, reducing the time required from two months to fifteen or ten working days.³⁰⁹

Interestingly, the Commission cleared state aid under Article 92(2)(c) in only two cases.³¹⁰ This mandatory exemption, which permits aid that compensates for economic disadvantages

304. Beschluß zur Gründung der Anstalt zur treuhänderischen Verwaltung des Volksvermögens (Act on the Establishment of the Institute entrusted with managing the peoples assets) of March 1, 1990, Gbl. (DDR) I Nr. 14, p.107.

305. Council for Mutual Economic Assistance.

306. COMMISSION OF THE EUROPEAN COMMUNITIES, XXIST REPORT ON COMPETITION POLICY 1991, at 157, ¶ 249 (1992).

307. *Id.*

308. The Community and German Unification, Communication presented by the Commission to the Council on August 22, 1990, *in* E.C. Bull. Suppl. 4/90, at 27.

309. COMMISSION OF THE EUROPEAN COMMUNITIES, XXII^D REPORT ON COMPETITION POLICY 1992, at 212, ¶ 349 (1993).

310. Commission Regulation No. 2611/92, O.J. L 263/9 (1992) (Potsdamer Platz); Commission Press Release, IP (94) 300 (1994).

caused by the division of Germany, was not removed in the revision of the EC Treaty by the Maastricht Treaty, although the revision postdates reunification. In most cases, the Commission based its clearance of aid on Article 92(3)(c). Although it has by and large fulfilled its pledge to apply the state aid rules in a sensitive and flexible way, aid to sensitive sectors such as the automobile and textile industries was only permitted where privatization involved a reduction in the capacity of the undertaking concerned.³¹¹

The Commission's approach to privatization in eastern Germany may not, due to the particular problems associated with the transition from a planned to a market economy, accurately reflect the Commission's approach to state aid granted in connection with privatizations in other regions of the European Union. It may indicate the Commission's approach, if other countries in transition, like Hungary, Poland, or the Czech and Slovak Republics, were to join the European Union before having fully converted to a market economy.³¹² At the same time, the accession of such states is unlikely to raise as many state aid issues as German unification since they do not have the same financial resources as the Federal Republic of Germany.

While the rules on state aid impose constraints on privatization, they are not intended to inhibit the privatization process, but to ensure that privatization does not distort competition. Moreover, the Commission perceives privatization as an important means of achieving greater efficiency and competitiveness and has used state aid rules effectively. Thus, while Article 222 declares the European Union to be neutral as regards public ownership, the structure of the EC Treaty and, in particular, the provisions concerning state aid mandate an economic environment conducive to private undertakings and a market economy. Article 222 must be understood in the light of these provisions.

311. Peter Schütterle, Die Rechtsgrundlage für Beihilfen zur Überwindung der wirtschaftlichen Folgen der Teilung Deutschlands, *Europäische Zeitschrift für Wirtschaftsrecht* 715 (1994).

312. See Michael Schütte & Jan-Peter Hix, *The Application of the EC State Aid Rules to Privatizations: The East German Example*, in 32 *COMMON MKT. L. REV.* 215 (1995). The Europe Agreement, concluded between the European Union and Hungary, Poland, and the Czech and Slovak Republics, provides for state aid rules analogous to Article 92 of the EC Treaty. *Id.*

IV. *FREEDOM OF ESTABLISHMENT, INVESTMENT, AND NON-DISCRIMINATION*

A. *The Scope of the EC Rules and Their Impact on Privatization Programs*

Measures taken by a Member State in relation to the ownership of public enterprises earmarked for privatization, such as the creation of special governmental powers, may be of such a nature as to imply the scope of Article 222 of the EC Treaty. According to Article 222, the EC Treaty will in no way prejudice the rules in Member States governing the system of property ownership.³¹³

Nevertheless, to the extent that such measures are applicable to EU nationals, they should comply with Articles 52, 58, 73(b), and 221 of the EC Treaty on the freedom of establishment and investment and the free circulation of capital.³¹⁴ The

313. See also, EC Treaty, *supra* note 1, art. 223(1)(b), [1992] 1 C.M.L.R. at 711 ("any Member States may take such measures as it considers necessary for the protection of the essential interests of its security which are connected with the production of or trade in arms, munitions and war material; such measures shall not adversely affect the conditions of competition in the common market regarding products which are not intended for specifically military purposes").

314. EC Treaty, *supra* note 1, art. 52, [1992] 1 C.M.L.R. at 613-14. Article 52 reads:

Within the framework of the provisions set out below, restrictions on the freedom of establishment of nationals of a Member State in the territory of another Member State shall be abolished by progressive stages in the course of the transitional period. Such progressive abolition shall also apply to restrictions on the setting-up of agencies, branches or subsidiaries by nationals of any Member State established in the territory of any Member State. Freedom of establishment shall include the right to take up and pursue activities as self-employed persons and to set up and manage undertakings, in particular companies or firms within the meaning of the second paragraph of Article 58, under the conditions laid down for its own nationals by the law of the country where such establishment is effected, subject to the provisions of the Chapter relating to capital.

Id.; see *Steinhauser v. City of Biarritz*, Case 197/84, [1985] E.C.R. 1819 (the right of establishment implies the equal treatment of nationals and citizens of other Member States, and thus any discrimination based on national laws, regulations, or practices should be forbidden); *Micheletti v. Delegacion del Gobierno en Cantabria*, Case C-369/90, [1992] E.C.R. 4239 (the EU rules prevent a Member State from denying the right of establishment to a national of another Member State, who was also a national of a third non-EU country); EC Treaty, *supra* note 1, art. 58, [1992] 1 C.M.L.R. at 616 ("Companies or firms formed in accordance with the law of a Member State and having their registered office, central administration or principal place of business within the Community shall, for the purposes of this Chapter, be treated in the same way as natural persons who are nationals of Member States."). "Companies or firms" means companies or firms constituted under civil or commercial law, including cooperative socie-

EC Treaty rules on non-discrimination and the freedom of establishment and investment in other EU Member States may exercise a significant influence on the national privatization programs of the Member States.

The prohibition of discrimination on grounds of nationality is set out in Article 6 of the EC Treaty, formerly Article 7 of the EEC Treaty, and has been enforced consistently in a large and well established body of case law.³¹⁵ In the 1963 *Refrigerators* case,³¹⁶ the Court established the principle that differing treatment of non-comparable situations is not automatically discriminatory. Instead, material discrimination consists either of treating similar situations differently or of treating differing situations identically.

As the principle of non-discrimination is of a general nature, it affects the whole spirit and scope of the EC Treaty. As a result, both in relation to privatizations and in other circumstances, the principle of freedom of establishment for European Union nationals within the Union, in Article 52, extended by Article 58 to legal entities, must be interpreted in light of the non-discrimination principle. EU natural and legal persons have the right to establish themselves in Member States other than their own in order to engage in economic activity under

ties, and other legal persons governed by public or private law, save for those which are non-profit-making." EC Treaty, *supra* note 1, art. 73(b), [1992] 1 C.M.L.R. at 621. Article 73(b) reads:

1. Within the framework of the provisions set out in this Chapter, all restrictions on the movement of capital between Member States and between Member States and third countries shall be prohibited.
2. Within the framework of the provisions set out in this Chapter, all restrictions on payments between Member States and between Member States and third countries shall be prohibited.

Id.; *id.* art. 221, [1992] 1 C.M.L.R. at 711. Article 221 reads:

Within three years of the entry into force of this Treaty, Member States shall accord nationals of the other Member states the same treatment as their own nationals as regards participation in the capital of companies or firms within the meaning of Article 58, without prejudice to the application of the other provisions of this Treaty.

Id.

315. See, e.g., *Italian Republic v. Commission*, Case 13/63, [1963] E.C.R. 165, 177 (*Refrigerators Case*); *Wilhelm v. Bundeskartellamt*, Case 14/68, [1969] E.C.R. 1, 13; *Sotgiu v. Deutsche Bundespost*, Case 152/73, [1974] E.C.R. 153, 162; *Knooks v. Secretary of State for Economic Affairs*, Case 115/78, [1979] E.C.R. 399, 407; *Oebel*, Case 155/80, [1981] E.C.R. 1993, 2005.

316. *Italian Republic*, [1963] E.C.R. at 177, ¶ 4.

the same conditions as nationals of the Member State of establishment. In relation to privatizations, these rules imply that national provisions that limit the ability of EU investors to establish themselves in another EU Member State by acquiring sole or joint control of a company to be privatized in that Member State violate Article 52 and/or Article 58, at least to the extent that they discriminate between nationals and non-nationals.³¹⁷

It follows that restrictions on foreign ownership, if applicable to EU nationals, infringe Article 52 and/or Article 58 and may only be justified under the public policy and public security exceptions in Article 56 of the EC Treaty,³¹⁸ which are restrictively interpreted.³¹⁹

317. The relationship between privatization and non-discrimination has not, to date, generated a substantial amount of case law. In *Commission v. France*, Case 270/83, [1986] E.C.R. 273, the Commission argued that the French Republic failed to grant to branches and agencies of insurance companies from other Member State set up in France the benefit of the shareholders' tax credit known as "avoir fiscal" from which corresponding French undertakings benefit. This omission, and the discrimination resulting from it, was alleged to be a breach of Article 52 of the Treaty. In upholding the Commission's argument, the Court of Justice stressed that Member States are obliged to grant EU nationals equal opportunities to participate in foreign undertakings, and held that establishment in a Member State may be achieved via the acquisition of a company.

318. EC Treaty, *supra* note 1, art. 56, [1992] 1 C.M.L.R. at 615-16.

1. The provisions of this Chapter and measures taken in pursuance thereof shall not prejudice the applicability of provisions laid down by law, regulation or administrative action providing for special treatment for foreign nationals on grounds of public policy, public security or public health.

2. Before the end of the transitional period, the Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament, issue directives for the coordination of the afore-mentioned provisions laid down by law, regulation or administrative action. After the end of the second stage, however, the Council shall, acting by a qualified majority on a proposal from the Commission and in cooperation with the European Parliament, issue directives for the coordination of such provisions as, in each Member State, are a matter for regulation or administrative action.

Id.

319. G. AMORELLI, *LE PRIVATIZZAZIONI NELLA PROSPETTIVA DEL TRATTATO ISTITUTIVO DELLA COMUNITÀ ECONOMICA EUROPEA* 257 (1992). In *Commission v. Luxembourg*, a case concerning Luxembourg legislation requiring that EU nationals be resident in Luxembourg before being entitled to Luxembourg maternity allowances, the Court stated that the national legislation at issue failed to comply with the Treaty provisions concerning the freedom of movement of workers and with Article 52, explaining that all forms of discrimination, whether overt or implicit, are illegal and, therefore, prohibited. *Commission v. Luxembourg*, Case 111/91, (Eur. Ct. J. Mar. 10, 1993) (not yet reported). In *Marguerite Johnston v. Chief Constable of the Royal Ulster Constabulary*, which concerned a request for a preliminary ruling relating to the equal treatment between men and women as regards job opportunities, the Court held that the ability of Member States to impose restrictions in the name of public safety must be interpreted nar-

In addition, Article 221 on the freedom of investment makes it unlawful for a Member State to restrict the ability of natural or legal persons established in another Member State to acquire minority interests in companies that it is privatizing.³²⁰

In attempting to maintain domestic control of privatized undertakings, states generally adopt one of the following devices: (1) fixing a ceiling on the proportion of corporate capital that can be held by foreign investors, whether individuals or companies controlled by foreign nationals; and/or (2) stipulating that the board of directors and management must include a given proportion of nationals. These systems have been adopted with a number of slight variations in the privatization programs of several Member States. The conformity of such systems, however, and in particular those adopted by the United Kingdom and France, with the EC Treaty rules on non-discrimination and freedom of establishment has been questioned.

An in-depth survey of the legislation of all Member States on this issue would clearly be beyond the scope of this Article. It may, nonetheless, be worthwhile to describe some of the principal features of the national legislation whose consistency with

rowly, and that it would not be correct to conclude that the Treaty creates any reservation in favor of measures motivated by the protection of the essential interests of state security. *Marguerite Johnston v. Chief Constable of the Royal Ulster Constabulary*, Case 222/84, [1986], E.C.R. 1684. In particular, the Court held that:

the only articles in which the Treaty provides for derogations applicable in situations which may involve public safety are Articles 36, 48, 56, 223 and 224 which deal with exceptional and clearly defined cases. Because of their limited character those articles do not lend themselves to a wide interpretation and it is not possible to infer from them that there is inherent in the Treaty a general proviso covering all measures taken for reasons of public safety.

Id. ¶ 26.

320. EC Treaty, *supra* note 1, art. 221, [1992] 1 C.M.L.R. at 711. Commentators have taken the view that the right to make investments, in Article 221, is part of the right of establishment, and thus implies the right to make investments abroad. *Id.* The principle of freedom to make direct investments is confirmed by a Directive of June 1988. Council Directive 88/361, art. 1, O.J. L 178/5, at 6 (1988). This Directive implemented Article 67 of the EEC Treaty (now Article 73(b) of the EC Treaty), which reads in relevant part, "Member States shall abolish restrictions on movements of capital taking place between persons resident in Member States." EC Treaty, *supra* note 1, art. 73(b), [1992] 1 C.M.L.R. at 621. See also R. Kovar, *Nationalisations — Privatisations et Droit Communautaire*, in J. SCHWARZE, DISCRETIONARY POWERS OF THE MEMBER STATES IN THE FIELD OF ECONOMIC POLICIES AND THEIR LIMITS UNDER THE EEC TREATY 100 *et seq* (1988); E. DEL CASALE, LE PRIVATIZZAZIONI IN EUROPA 151-52 (1987); G. AMORELLI, *supra* note 319, at 256.

the EC rules on freedom of establishment and non-discrimination has come under scrutiny.

B. *The United Kingdom Approach*

The United Kingdom has introduced a form of indirect control through the "golden share" system. This system is intended to ensure that some degree of domestic and governmental control is maintained over the governing bodies, shareholder base, and principal decisions of privatized companies. The U.K. "golden share" rules are not statutory provisions, being instead contained in the privatized companies' articles of association; a golden share is, in effect, a special share held by the Government or its nominee. Certain decisions, as specified in each company's articles of association, can only be put into effect with the golden shareholder's written consent.³²¹

The powers allowing the Government to control the proportion of foreign ownership of capital include veto rights, which allow the Government to limit the proportion of the privatized company's capital held by foreign investors, as well as to prevent transfer of the company's business or its liquidation.³²² It may be worth mentioning that, at the time of their privatization, the articles of Britoil and Enterprise Oil contained golden share provisions aimed at protecting these companies from hostile takeovers. In particular, they provided that, in given circumstances, the golden share holder would have the right to exercise voting majority.³²³

In addition, the golden share rules may also grant the Government the right to monitor the composition of the board of directors. In the case of certain strategic privatized companies,³²⁴ British citizenship is a requirement for appointment to a

321. J. Flynn, British Report to the XVI FIDE Congress on Competition Law Implications of Deregulation and Privatisation 175-77 (1994). See generally C.D. FOSTER, *PRIVATISATION, PUBLIC OWNERSHIP AND THE REGULATION OF NATIONAL MONOPOLY* (1992); see C. VELIANOVSKY, *SELLING THE STATE: PRIVATIZATION IN BRITAIN* (1988) (describing, specifically, privatization of services in Britain); R. FITZGERALD, *WHEN GOVERNMENT GOES PRIVATE: SUCCESSFUL ALTERNATIVES TO PUBLIC SERVICES* (1988).

322. See Kovar, *supra* note 320, at 100; J. Vickers & V. Wright, *Special Issue on the Politics of Privatisation in Western Europe*, WEST EUR. POLITICS, Oct. 1988, at 29; DEL CA-SALE, *supra* note 320. See generally Flynn, *supra* note 321, n.4 (describing UK legislation).

323. Flynn, *supra* note 321, at 170-71.

324. E.g., Rolls Royce and British Aerospace, cited after Flynn, *supra* note 321, at 176.

top executive position.

C. *The French Approach*

The limits on foreign investment in privatized companies originally enacted by French law were of an even stricter nature. The French law of 1986³²⁵ created the "action spécifique,"³²⁶ a variant of the U.K. golden share, which was intended to grant the Government a number of special powers to protect the national interest. These powers included: a requirement that the Ministry of the Economy approve any purchase of shares in the privatized companies in excess of certain statutory thresholds; the right to appoint one or two members of the board of directors or of the surveillance committee of such companies; and the power to veto any transfer of the company's business that could be deemed to jeopardize the national interest. In response to objections raised by the EU Commission, the French law was amended in 1993. The 1993 amendments repealed, as regards EU nationals, the prohibition on the purchase by foreign investors of more than 20% of the shares of privatized companies, although they maintained the requirement that the Ministry of Economy approve purchases by foreign investors, including EU nationals, of more than 5% of the corporate capital of companies operating in strategic sectors.

Commentators³²⁷ have questioned the legality of both the U.K. and French legislation to the extent that they discriminate between national and foreign investors on the grounds that they may potentially be inconsistent with the principles of freedom of establishment and investment. One commentator³²⁸ has suggested that, whereas the U.K. legislation could be regarded as a legitimate protection of national interests, the amendments of 1993 to the French law of 1986 were necessary, even in the absence of any formal challenge to it, because the original legislation differentiated, without apparent public policy justification, between national and foreign investors in a manner inconsistent

325. Law No. 86-912 of August 6, 1986 (Fr.), amended by Law No. 92-923 of July 19, 1993 (Fr.).

326. Law No. 86-912 of August 6, 1986, art. 10 (Fr.).

327. See, e.g., Abate, *supra* note 239; Amorelli, *supra* note 319, at 256; TURRINI, PRIVATISATIONS ET DROIT COMMUNAUTAIRE, IN REVUE DES AFFAIRES INTERNATIONALES 823 (1993).

328. AMORELLI, *supra* note 319, at 256.

with the wording of Article 52 of the EC Treaty. Even after the 1993 amendment, it is questionable whether the French privatization law can be regarded as in full compliance with the EC Treaty.

D. *The Italian Approach*

A somewhat different approach has been taken by the recent Italian legislation on privatization.³²⁹ Law No. 474 provides that the sale of shares held by the State or by public entities must normally take place by public offering, through direct negotiations, or through a combination of the two.³³⁰ If a sale is carried out by direct negotiation, the Government can select certain investors with adequate entrepreneurial capacity to establish a core group of strategic shareholders.³³¹ As to public interest companies, such as those in the sectors of defense, transportation, telecommunications, energy sources, and other public services, Law No. 474 stipulates that, before the State transfers control in them, they must adopt in their by-laws a golden share clause, the precise contents of which is to be defined in a governmental decree, granting the Minister of the Treasury a number of special powers, including requirements that the Minister approve significant capital participations, certain shareholders' agreements regulating voting, and the transfer or purchase of shares, as well as powers to veto transfer of the business or dissolution of the company, and powers to appoint at least one director and one auditor.³³²

The Italian law on privatizations appears not to contain any provisions with overt or indirect discriminatory intent or effect.³³³ In particular, Law No. 474 does not discriminate on grounds of nationality nor does it hinder foreign investment. The principal objectives of the Law include the prevention of "creeping acquisitions" after the Government has relinquished control through a public offering of shares, which may disadvan-

329. Law No. 474 of July 30, 1994 (Italy).

330. *Id.* art. 1.2.

331. *Id.* art. 1.3.

332. *Id.* arts. 2.1a-2.1d.

333. Same conclusions can be drawn as to the German privatization law. According to § 3 of the Treuhandanstalt by-laws, the Treuhandanstalt should let both national and foreign investors participate in the shareholdings of the companies to be privatized.

tage small investors and avoid paying any premium to the State. To this end, the Law provides that equity ownership limits introduced in the by-laws of privatized companies may be exceeded only through a public offering for the purchase of the majority of the company's shares. Law No. 474 also attempts to enhance "shareholders' democracy" in privatized companies, for instance, by creating the possibility of voting by mail and reserving at least one-fifth of the seats on the board of directors for minority shareholders.³³⁴

Prominent Italian legal scholars³³⁵ have nonetheless criticized certain aspects of the Law that appear not to be fully consistent with established principles of Italian corporate law. The Commission for its part, appears to have taken the view that, since the Law reserves a significant margin of discretion to the Government in its implementation, there is a risk that the Law might be applied in a discriminatory manner. If that were to occur, however, the infringement of EC law would clearly result from the Italian Government's application of the Law, rather than from the Law itself.

V. PUBLIC PROCUREMENT ISSUES

A. *The Scope of the EC Directives on Public Procurement*

The adoption of measures intended to establish Community-wide competition in the public procurement sector constitutes an important part of the completion of the internal market.³³⁶ Community legislation in the field of public procurement is specifically designed to prevent government authorities, other bodies subject to public law, and public and private undertakings carrying out services of public utility from discriminating

334. Law No. 474 art. 4 (1994) (Italy).

335. See G. Rossi, *Privatizzazioni e Diritto Societario*, RIVISTA DELLE SOCIETÀ 390 (1994). Criticism has been directed at the Italian "golden share" system. *Id.* See also R. Costi, *Privatizzazione e Diritto delle Società per Azioni*, GIURISPRUDENZA COMMERCIALE I 77 (1995).

336. See Commission of the European Communities, *Completing the Internal Market: White Paper from the Commission to the European Council*, COM(85) 310 Final, at 23 (June 1985). See also L.A. CARSWELL, & X. DE SARRAU, *LAW & BUSINESS IN THE EUROPEAN SINGLE MARKET* (1993); I. Van Bael, *Public Procurement and the Completion of the Internal Market: Law and Practice*, 1 LEGAL ISSUES EUR. INTEGRATION 21 (1989); Laurence Gormley, *Some Reflections on Public Procurement in the European Community*, EUR. BUS. L. REV. 63 (Nov. 1990); J. Winter, *Public Procurement in the EEC*, 28 COMMON MKT L. REV. 741 (1991).

against contractors from other Member States.³³⁷

The Commission's 1985 White Paper acknowledged the need for amendment of the public procurement directives then in force and the extension of their limited scope. The White Paper identified specific problems in opening up procurement in the utilities sectors, however, such as water, energy, transport, and telecommunications, since the entities involved in awarding contracts in such sectors included not only bodies organized under public law or otherwise government-owned, but also private companies with special or exclusive rights. The approach adopted by the Council in a new set of directives governing public procurement³³⁸ was to apply the public procurement rules to both types of organization.³³⁹ The public procurement directives apply to contracts for pecuniary interest concluded in writing between a provider of supplies, services, or construction works and a contracting authority.³⁴⁰ When awarding public service, public supply, and public works contracts, bodies and authorities to which the public procurement directives apply are, in principle, obliged to follow the procedures set out in the directives, which are intended to ensure that public contracts are awarded in a non-discriminatory and pro-competitive manner.

B. *The "General Directives" and the "Excluded Sectors Directive"*

A distinction should be drawn, however, between the scope

337. *Commission v. Ireland*, Case 249/81, [1982] E.C.R. 4005. The Court of Justice confirmed that buy-national policies that partition markets are incompatible with the free movement of goods and Community law in general. *Id.*

338. Council Directive No. 92/50/EEC, O.J. L 209/1 (1992) (relating to the coordination of procedures for the award of public service contracts); Council Directive No. 93/36/EEC, O.J. L 199/1 (1993) (coordinating procedures for the award of public supply contracts); Council Directive No. 93/37/EEC, O.J. L 199/54 (1993) (concerning the coordination of procedures for the award of public works contracts); and Council Directive No. 93/38, O.J. L 199/84 (1993) (coordinating the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors).

339. See E.M.F. Temple & P.F. Clarke, *Public Procurement Contracts*, IRCL, 1995, at 32 (Explaining that, as to utility sectors, "there were two choices, either an approximation of the two types of organization within the directives, or an approach via Articles 85, 86, and 90, the competition Articles of the EC Treaty. In the event, the EC Commission chose the former").

340. Council Directive No. 92/50, art. 1(a), O.J. L 209/1, at 3 (1992); Council Directive No. 93/36, art. 1(a), O.J. L 199/1, at 2 (1992); Council Directive No. 93/37/EEC, art. 1(a), O.J. L 199/54, at 55 (1993); Council Directive No. 93/38/EEC, art. 1(4), O.J. L 199/84, at 88 (1993).

of Directives 92/50, 93/36, and 93/37 ("general directives"), and that of Directive 93/38 concerning procurement in the utilities sectors ("excluded sectors directive").

The main difference, for our purposes, between the two sets of provisions concerns the definition of the contracting authorities to which the directives apply. In the general directives, this includes the state, regional and local authorities, bodies governed by public law, and associations formed by one or more of such authorities or bodies governed by public law, regardless of the sector in which they operate. A body is considered to be governed by public law where it is established for the specific purpose of meeting needs in the general interest, meaning needs not of an industrial or commercial nature. All other legal entities, even if wholly or partly owned by private shareholders, established to meet general interest needs that are ultimately financed by or controlled by governmental authorities, are regarded as bodies governed by public law.³⁴¹

Article 1(b) of the general directives excluded from their scope of application the bodies having an "industrial or commercial character." It seems, therefore, that public procurement rules will not play a role in the privatization of state-owned manufacturing or commercial companies.

It cannot be ruled out, however, that Member States will resolve to privatize a number of entities performing functions of general interest, currently organized as public bodies, such as the postal or the health services. Were this to happen, the companies in charge of providing such services to the public would no longer be subject to public procurement rules following privatization, unless they continue to rely on the state or local authorities as their main source of funding.

The excluded sector directive covers the water, energy, transport, and telecommunication sectors and applies not only to public authorities and public undertakings,³⁴² but also to pri-

341. Council Directive No. 92/50, art. 1(b), O.J. L 209/1, at 3 (1992); Council Directive No. 93/36, art. 1(b), O.J. L 199/1, at 3 (1992); Council Directive No. 93/37/EEC, art. 1(b), O.J. L 199/54, at 55 (1993).

342. Council Directive 93/38, art. 2, O.J. L 199/84, at 89 (1993). According to Article 1.1, " 'public authorities' shall mean the State, regional or local authorities, bodies governed by public law, or associations formed by one or more of such authorities or bodies governed by public law." *Id.* art. 1(1), O.J. L 199/84, at 87 (1993). Article (1)2 defines "public undertaking" as "any undertaking over which the public authorities may

vate undertakings that operate on the basis of special or exclusive rights granted by the competent authorities of the Member States.

To the extent that undertakings earmarked for privatization are not already organized in the form of a corporation, such reorganization is normally effected before privatization takes place. This implies that, even if undertakings entrusted with such activities were to be privatized, the fact of privatization would not affect the application of the excluded sectors directive, provided and to the extent that, the special or exclusive rights referred to under Article 2.1(b) and described under Article 2.3 of the excluded sectors directive remain unaffected.³⁴³

An exception to the rules described above in the telecommunications sector is contained in Article 8.1 of the excluded sector directive.³⁴⁴ Public procurement rules do not apply to contracts that contracting entities operating public telecommunication networks or providing telecommunication services award for purchases, intended only "to enable them to provide one or more telecommunications services, where other entities are free to offer the same services in the same geographical area and under substantially the same conditions."³⁴⁵ Thus, to the extent that the provision of such services is liberalized, the public procurement rules should cease to apply.

C. *The British Telecommunications Case*

Guidance as to the precise meaning of Article 8.1 of the excluded sectors directive, the effects of which are potentially far-reaching, is likely to be offered by the *British Telecommunications* case,³⁴⁶ which is currently pending before the Court of Justice.

exercise directly or indirectly a dominant influence by virtue of their ownership of it, their financial participation therein, or the rules which govern it." *Id.* art. (1)2, O.J. L 199/84, at 87-88 (1993) The existence of a dominant influence exercised by a public authority may be presumed, if the latter holds the majority of the undertaking's capital, controls a voting majority or has the right to appoint more than half of the board of directors. *Id.*

343. *Id.* art. 2.3, O.J. L 199/84, at 90 (1993) ("For the purpose of applying paragraph 1(b), special or exclusive rights shall mean rights deriving from authorizations granted by a competent authority of the Member State concerned, by law, regulation or administrative action, having as their result the reservation for one or more entities of the exploitation of an activity defined in paragraph 2.").

344. *Id.* art. 8.1, O.J. L 199/4, at 92 (1993).

345. *Id.*

346. *Italy v. Commission*, Case 41/83, [1985] E.C.R. 873, ¶¶ 21-23. Reference for

British Telecommunications ("BT") was privatized in 1984, and only 22% of its corporate capital is now held by public entities.³⁴⁷ BT's privatization was immediately followed by the liberalization of telecommunications services, including voice telephony, in the United Kingdom. In the *British Telecommunications* case, BT is seeking judicial review of the application of the U.K. regulations implementing the excluded sectors directive. The regulations at issue deny BT the benefit of the "liberalization" exception, while extending it to all other licensed U.K. telecommunications operators but one.

The central issue to be addressed by the Court is the interpretation and definition of the notion of freedom to offer the same services on equal conditions. Two interpretations of this notion may have been suggested, with opposite consequences as to the impact of public procurement rules on privatization. A more formalistic but straightforward reading of Article 8.1 is that the freedom to provide services refers only to the legal freedom introduced by EC directives and/or domestic legislation enacted in connection with the privatization of the local telecommunications operator, to offer competitive telecommunications services. A more sophisticated interpretation, but also one likely to be more difficult to apply, is that the concept of freedom to provide services requires *de facto* equality of competitive conditions. This is the interpretation supported by the Commission and the U.K. Government, which rely for support on recitals 9, 11, and 13 of the Directive.³⁴⁸ Were the Court of Justice to uphold this

a Preliminary Ruling, *The Queen v. the Secretary of State for Trade and Industry*, ex parte: *British Telecommunications plc*, Case C-302/94, O.J. C 380/3 (1994).

347. See R. Arrigoni, *Regolazione e Gestione nelle Public Utilities: Principio di Separazione e Libera Concorrenza nell'Applicazione di Principi Costituzionali e Comunitari*, *RIVISTA TRIMESTRALE DI DIRITTO PUBBLICO*, 1995, at 96; see also Flynn, *supra* note 321, at 183.

348. See Council Directive 93/38, O.J. L 199/84, at 84-85 (1993). Recital number 9 reads: "[W]hereas the need to ensure a real opening-up of the market and a fair balance in the application of procurement rules in these sectors requires that the entities to be covered must be identified on a different basis than by reference to their legal status." *Id.* Recital number 11 reads:

Whereas, among the main reasons why entities operating in these sectors do not purchase on the basis of Community-wide competition is the closed nature of the markets in which they operate, due to the existence of special or exclusive rights granted by the national authorities, concerning the supply to, provision or operation of, networks for providing the service concerned, the exploitation of a given geographical area for a particular purpose, the provision or operation of public telecommunications networks or the provision of public telecommunications services.

latter interpretation, privatization and liberalization of the utilities sectors would not terminate the applicability of public procurement legislation, if the former state-owned monopolist continued to enjoy a dominant position.

CONCLUSION

The neutral stance originally enshrined in the EC Treaty between public and private ownership has given way to an environment more conducive to privatization in Europe, a movement that raises issues primarily under two sets of Treaty rules. The first, Articles 90(1) and 86 of the EC Treaty have significantly influenced most of the processes of liberalization in the Community. Secondly, the rules on state aids, applied with renewed vigor, have become a powerful force driving the Member States toward privatization.

The existing competition rules of the Community, especially the Merger Regulation and Articles 85 and 86 of the EC Treaty, can potentially be used to control the entire privatization process. If these rules are strictly enforced, that process offers a historic opportunity to modernize and render more dynamic the structure of the European market.

In sum, liberalization and privatization are two different aspects of the same complex process and EC competition rules may serve as a means of strengthening the link between them. In particular, while liberalization has been made possible in Europe thanks to the application of the competition rules, via Article 90, privatization should be shaped both by applying competition rules and, above all, by the need to ensure the complete and effective liberalization of markets.

Id. Recital number 13 reads: "Whereas this Directive should not extend to activities of those entities which either fall outside the sectors of water, energy and transport services or outside the telecommunications sector, or which fall within those sectors but are nevertheless *directly exposed to competitive forces in markets to which entry is unrestricted.*" *Id.* (emphasis added). According to the United Kingdom and the Commission, the terms "free" and "conditions" in Article 8.1 of the excluded sectors directive refer not only to freedom and conditions of a regulatory nature but also to *de facto* freedom and conditions, since the purpose of the directive is to open the market in the services concerned to Community-wide competition. *See* Schmidt v. Spar-und Leihkasse der fruheren Amter Bordschholm Kiel and Cronshagen, Case C-392/92, I-12, (Eur. Ct. J. Apr. 24, 1994) (not yet reported). This interpretation of Article 8.1 was recently upheld by the Court of Justice. *The Queen v. H.M. Treasury, ex parte*, Case C-392/93 (Eur. Ct. J. Mar. 26, 1996) (not yet reported).