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Towards a European recognition of public services at last? The potential impact of the Lisbon Treaty

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Séverine Picard

Séverine Picard is
Legal Adviser of the
European Trade Union
Confederation.

Policy implications

Public services, or Services of General Economic Interest, illustrate the tension between Social Europe and the requirements of the Internal Market. Whilst the European Union (EU) institutions and the European Court of Justice (EJC) do acknowledge the social dimension of the European Union, the economic dogma of the internal market has traditionally prevailed, admitting only limited exceptions. The Lisbon Treaty has introduced significant changes, bringing clear support to public services. However, it needs to be acted on. An ambitious reading of the new provisions could change a lot for the future of public services in Europe. But inertia on the part of the EU institutions is also possible. As the Lisbon Treaty will not by itself change the rules of the game, failure to promote a meaningful debate at European level will represent the waste of a formidable opportunity for Social Europe.

Introduction

Public services broadly cover everything from water, energy supply and waste disposal, to healthcare and social services, education and postal deliveries. Public services are at the heart of the European social model. Their functioning is based on the principle of solidarity, which guarantees universal access to essential public goods. In other words, entities carrying out public services are entrusted with a mission of general interest. While the forms, organisation and financing vary significantly from one Member State to another, the general characteristic of public services across the Union is that they exist to compensate for market failure to grant universal access to fundamental services simply because the market may not generate sufficient incentives to this end.

The idea that free market and undistorted competition can be overridden is only partially recognized by the European Treaties. Section 1 of this contribution provides an overview of the current legal situation, highlighting the conflictual relationship between EU internal market and competition rules on the one hand and public services on the other.

The greater the pressure on public authorities, the more the need for discussion of defences becomes pressing. There is an increasing recognition that the issue should be seen not so much

in terms of limits to the internal market but in terms of how to guarantee services which are more efficient and more responsive to social values. The second section of this contribution takes the view that an ambitious reading of the new provisions of the Lisbon Treaty could lead to a radical change of approach. The Lisbon Treaty offers the possibility to redefine the internal market concept in relation to Services of General Economic Interest (SGEI) and to define a new set of rules accordingly.

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What is at stake: the tension between public services and Treaty rules

Two main bodies of rules govern the functioning of public services in the Member States: EU competition law and the EU rules on freedom of movement. In both cases, an abundant ECJ case law circumscribes national discretion. In parallel, there is no transfer of 'public service considerations' at European level. This creates considerable tensions between internal market rules, which are economic in nature, and the organisation of public services, which require more intervention from the State.

The influence of EU competition law

Articles 101 to 109 of the Treaty on the Functioning of the European Union (TFEU) (ex Articles 81 to 89 EC) prohibit undertakings from behaving in such a way that competition would be restricted – for instance illegal agreement between undertakings leading to price fixing, abuse of dominant position through excessive pricing – and a general prohibition of state aid or measures equivalent to state aid. These provisions have been completed by an impressive volume of case law before the European Court of Justice.

The general thrust is free competition: avoiding undue manipulations of the market. Removing barriers to trade is not only of fundamental importance to the achievement of the internal market; it is also generally perceived as fulfilling a 'social function': the less efficient entities – in terms of productivity, pricing, innovation – are driven out. The rationale is that a free market is better for consumers, leads to higher productivity and more jobs.

However, society cannot rely on market forces alone to deliver public service obligations. The solidarity principle which is the *raison d'être* of public services implies that risks inherent in free competition are partly or entirely neutralised. For this, a certain amount of market distortion by the state is necessary and public authorities may deem it necessary to grant privileged status to an entity fulfilling a public service mission, protecting it from market failure. This is not prohibited per se by the EU treaties.

The principle of public undertakings and undertakings enjoying special or exclusive rights is acknowledged under strict conditions

The use of exclusive or special rights is frequent in relation to undertakings fulfilling a mission of general interest. The granting of such rights implies that the state authority has relieved the undertaking, partly or entirely, from the risks inherent in competition. Exclusive or special rights often presuppose the existence of an authorisation regime, whereby the public authority selects a limited number of undertakings which can provide the service in a given sector/ geographical zone. In case of exclusive rights, the existence of competitors is ruled out.

However, Article 106.1 of the Treaty on the Functioning of the European Union makes it very clear that there is no immunity from competition rules for such undertakings. This fits with the

general spirit of the EU Treaties. If the state were able to give unjustified preferential treatment to selected firms, barriers to trade would be erected and the very idea of a level playing field would be undermined.

Financing of public services is authorised under certain conditions (the Altmark ruling)

Article 107.1 TFEU sets out as a general principle that state aids to undertakings are incompatible with the single market. However, the ECJ has ruled in the Altmark case that, where assistance is granted to compensate for public service obligation, the measure is not caught by Article 107.1 TFEU. But strict conditions have to be fulfilled.

Breach of EU competition law may be justified on a case-by-case basis

Article 106.2 TFEU allows exemptions from EU competition law for "services of general economic interest" (SGEI) if it can be established that application of the Treaty rules would obstruct the performance of the particular tasks assigned to the undertaking.

The EU Treaty does not give a clear definition of what constitutes a SGEI. In the eye of the ECJ, a SGEI is entrusted by an act of a public authority. SGEIs are to be defined by specific characteristics such as universality, equality of access, availability and affordability. Utilities are usually considered as SGEIs.

Inevitably, instances of special status being granted to public services are perceived as business irritants and are often subjects of complaint by potential competitors. As a result of the ECJ-wide understanding of the concept of 'undertaking', entities fulfilling public services obligations will often have to abide by the prohibitions contained in Art. 101, 102 and 107 TFEU in the same way as ordinary commercial services. This means that an economic test will be applied to public service providers in order to determine whether competition rules have been breached. This is rather paradoxical, given that state intervention in those specific cases is designed precisely in order to compensate for market failure.

With regard to exclusive rights, the Court looks at whether a position of economic dominance could lead to abuse. In concrete terms, the ECJ will measure the efficiency of a public service using economic criteria, e.g. market demand, pricing not linked to the actual cost of the service, innovation, etc.

With regard to financing, the ECJ focuses on the amount of compensation which should not exceed what is necessary to cover the cost incurred in the discharge of the service and should be determined on the basis of the costs which a typical undertaking would have incurred (these are the Altmark criteria).

Article 106.2 TFEU is therefore essential, in that it allows the Court to take into account the characteristics inherent in public service obligations and which justify a restriction of competition. Art. 106.2 remains, however, a derogation to the competition rules and, as such, is interpreted strictly by the ECJ. Because

of the absence of clearly defined public service obligations at European level, assessment of SGEIs is performed by the ECJ on a case-by-case basis. Given the wide diversity of public services in the Member States, this leads to great legal uncertainty.

One may also question the need for such 'catch all' competition provisions, especially in the case of public financing. Some services, albeit fulfilling a general interest function, constitute local services with limited resources available. Whilst abiding by the Altmark strict criteria will prove costly and cumbersome for local authorities, the overall added value for the EU is questionable, given the limited impact of these services on cross-border trade.

Free movement – the specific case of health services

Articles 56 to 62 TFEU contain a general prohibition on national rules which might hinder cross-border trade. Consequently, the approach to free movement of services is essentially deregulatory in nature. Article 56 TFEU requires the elimination of all discrimination against a person providing services on the ground of his nationality.

Only services of a commercial nature are supposed to fall within Community law. The specific case of health services is rather confusing. Though it is not entirely clear whether health is a commercial service within the meaning of the Treaty, the rules on free movement may well be considered applicable. The ECJ seems unwilling to spend much time on the characterization of healthcare as a commercial service. Rather, it is the cross-border element – i.e. where the patient behaves as a 'consumer' by looking for health services outside his Member State of residence – that triggers the application of the free movement rules. The key question is under which conditions, if any, the cost of treatment received in another Member State can be reimbursed in the patient's Member State of residence.

The ECJ case law on health services is very favourable to patients because, overall, it offers European citizens broader choice. It may even be read as compensating for Member States' failure to invest in their own health care systems. At the same time, considering the ever increasing patient mobility, these judgments are bound to have an adverse impact on the organisation and the financial balance of healthcare services in certain Member States.

The ECJ has extended the rules on free movement to an area which traditionally was reserved to the Member States. Arguably, the stakes are too high and complex to leave the Court legislating in this area. It is undeniable that health care is an economic market with supply of goods and services. Nonetheless, the organisation of health budgets is inherently linked to specific values and principles across the Union. For instance, contrary to the provision of purely commercial services, access to health is not linked to ability to pay. Secondly, health care is not an ordinary market as it is the supplier who determines the demand and not the other way round. Patients cannot always be assimilated to consumers able to take a decision on their own and in their own best interests.

A combination of necessary patient mobility and Member States' primary responsibility with regard to the organisation and financing of healthcare requires a delicate balancing act; something that the ECJ should not be left to perform single handed. In 2008, the European Commission put forward a proposal for a Directive on the application of patients' rights in cross-border healthcare. This proposal seeks to ensure more legal certainty following the huge jurisprudence concerning the right of patients to benefit from medical treatment throughout the Union. Whilst it could indeed be useful to clarify exactly what rules are applicable, the legal base of such a Directive means that the question of healthcare in Europe is still approached under the 'free movement' angle.

The Lisbon Treaty: towards a legal framework for public services?

With the entry into force of the Lisbon Treaty, the institutional context has significantly changed. Firstly, the Charter of Fundamental Rights, which recognises the fundamental nature of public service obligations has become legally binding with the Lisbon Treaty. Several articles of the Charter are directly linked to the notion of general interest. SGEIs have a crucial role to play in securing those rights. In fact, Article 36 of the Charter states that access to SGEIs is a fundamental right protected by the Union.

Secondly, the Lisbon Treaty has significantly amended ex-Article 16 EC. In the old Nice Treaty, ex-Article 16 EC recalled the role of SGEI and stressed the shared competence between the Member States and the Union in this area. The new provision now reads (changes introduced by the Lisbon Treaty in bold italics):

Article 14 TFEU (ex Article 16 EC)

Without prejudice to **Article 4 of the Treaty on European Union or to** Articles 93, 106 and 107 of this Treaty [ex Art 73, 86 and 87 EC], and given the place occupied by services of general economic interest in the shared values of the Union as well as their role in promoting social territorial cohesion, the Union and the Member States, each within their respective powers and within the scope of application of this Treaty, shall take care that such services operate on the basis of principles and conditions, particularly economic and financial conditions, which enable them to fulfill their missions. **The European Parliament and the Council, acting by means of regulations in accordance with the ordinary legislative procedure shall establish these principles and set these conditions without prejudice to the competence of Member States, in compliance with the Treaties, to provide, to commission and to fund such services."**

Article 14 TFEU paves the way for a new approach

Ex-Article 16 EC was not a legal base as such and did not grant the EU competence to act in this specific area. With the Lisbon Treaty, the EU's competence to take action in relation to public services is for the first time expressly recognised. In addition, annexed to the Lisbon Treaty is a "Protocol on services of

general interest" which reaffirms the shared values of the Union in respect of SGEIs within the meaning of Article 14 TFEU. The Protocol recognizes, in particular, the essential role and the wide discretion of public authorities at all levels, the diversity between various SGEIs, and the characteristics of SGEIs such as a high level of quality, safety and affordability, and universal access. The Protocol further stresses that the EU Treaties should not affect national competences to ensure the functioning of these services.

The Lisbon Treaty allows a redefinition of the internal market concept in relation to SGEIs. By introducing Community competence on SGEIs, Art. 14 TFEU does away with the derogation approach that has prevailed so far. The SGEI is no longer characterised by its economic viability but by its role in the Union social and territorial cohesion.

The EC Treaty offered a dualistic vision, with services on the one hand and non-services – or state prerogatives – on the other. Services are subject to free movement and competition rules. Article 106.2 TFEU allows derogations for SGEIs but it is market analysis that is used to establish to which services this is applicable. Article 14 TFEU is groundbreaking in the sense that it introduces a new sphere of regulation between market services and non-services. In this 'third sphere', market rules should no longer be in play and public services are to be governed by a different set of rules, to be devised in secondary legislation. This does not mean that the internal market rules would be totally excluded in relation to SGEIs – the Treaty must still be respected – but the internal market notion will have to be redefined in relation to SGEIs.

SGEIs have not become Community-exclusive competence and the Protocol reasserts that there should be plenty of room for national choices. However, a European legislation on public services should offer more than just an elaborate shield from competition law and economic freedoms. A set of core principles must be elaborated to secure respect of the shared values that are set out in the Protocol. The EU institutions need to develop a coherent approach to the rules governing the award and functioning of special or exclusive rights as well as the financing of public services. National public authorities at all levels should be able to enjoy more legal certainty. In this regard, it should be underlined that granting more flexibility to national authorities does not have to be incompatible with European rules, in particular concerning transparency and non-discrimination.

The form: Directive or Regulation? (and on which legal base)

Regrettably, Article 14 TFEU limits the Commission's usual discretion to decide on a case-by-case basis the most desirable level of harmonization. The institutions are to act "by means of Regulations". Regulations do not require transposition by the Member States; they are binding in their entirety and directly applicable into national legal orders. By contrast, Directives bind Member States only as to the result to be achieved and leave national authorities the choice of form and methods.

Because they are directly applicable, Regulations are usually very detailed, with hardly any room left for national variations. Due to the subsidiarity principle, Directives are largely preferred to Regulations

In an area as controversial and diverse as public services, where national orientations correspond to well matured socio-economic and cultural choices, detailed Regulations may be perceived as an infringement of domestic sovereignty. Even though the new Article 14 TFEU will benefit from qualified majority voting in the Council, adoption of framework Regulations will prove to be a real challenge for the institutions. The risk is that quality of legislation will suffer from a lengthy and ideological legislative procedure.

In theory, it would still be possible to adopt a Directive on public services but this would have to be done in accordance with a legal base specifically allowing such an instrument. Arguably, Article 114 TFEU (ex-Art. 95 EC) would constitute an acceptable legal base. In fact, the proposed Directive on healthcare is based on this. This provision allows the adoption of measures which have as their purpose the establishment and functioning of the internal market. However, it should be kept in mind that any instrument adopted on this legal base will be interpreted by the Courts in the light of internal market principles. In other words, a Directive based on free movement principles would not solve all the tensions between public services and economic freedoms. On the other hand, a Regulation on the basis of Art. 14 TFEU, whilst challenging, could potentially widen the perspectives towards a constructive approach to public services.

The choice of a Regulation over a Directive has direct consequences on the scope of the instrument: it will have to be more narrowly defined.

The scope of an Art. 14 Regulation

Confusingly, several terms are used in relation to public services: services of general economic interest, services of general interest, non-economic services of general interest, etc. The accurate labeling of a service is fundamental as it conditions the degree of application of Treaty rules on free movement and competition. Depending on the status of the service in question, three possibilities can be envisaged:

1. exclusion from Treaty rules (e.g.: police, justice, education when it is not a profit-making activity, etc.)
2. application of Treaty rules with enhanced consideration for the general interest (see for instance case law on Art. 106.2; health services would also fall under this category)
3. unconditioned application of Treaty rules (purely commercial services)

Another point is whether an EU instrument should be expected to cover all public services (a horizontal approach) or whether sectoral approaches would be preferable. A Regulation will, by definition, leave little room for manoeuvre to the Member States. As a result, the EU institutions might find it more productive in political terms to legislate sector by sector. For instance,

consensus may be found on the organisation of health services but not on local transport. A narrow scope may therefore help to achieve ambitious instruments in certain sectors.

In addition, a sectoral approach would be of considerable help with regard to definitions, as a legal presumption of general interest could be extended to a whole category of activities. On the other hand, an instrument with a wide remit would inevitably leave open the issue of how to characterise a SGEI. In case of conflict, the ECJ will decide on the basis of the existing case law, bringing back the uncertainty.

Nonetheless, the major disadvantage of a sectoral approach would be that it will inevitably entail some gaps. Some services – possibly the most problematic ones – will be left out. This is the reasoning of the services Directive (2006/123/EC). The services Directive covers a wide range of activities because the legal obstacles to the achievement of the internal market are often common to a large number of services and have many features in common. This horizontal instrument is not intended to lay down detailed rules or harmonise all rules applicable to services. A similar reasoning should logically apply to SGEIs, especially since the services Directive provides for a general exclusion of non-economic services of general interest and a derogation for SGEIs. A horizontal Regulation would allow the legislator to lay down a set of core principles, inspired by the guidelines set out in the Protocol of the Lisbon Treaty, and which would need to be respected in all sectors.

The debate is therefore open. In any case, horizontal and sectoral approaches need not be exclusive. Art. 14 TFEU uses the plural in referring to 'Regulations'. A possible compromise would be to call for a framework Regulation which would set out a core of principles applicable to all SGEIs. Specific sectors would then be dealt with in more detail in separate instruments. For instance, one could envisage a sectoral Regulation on health services, dealing in particular with the complex issues of reimbursement and patient mobility. This would not be a new exercise in Community law. For instance, a Framework Directive on health and safety adopted in 1989 was explicitly intended to serve as a basis for additional specific Directives, without prejudice to more stringent and/or specific provisions contained in those individual instruments.

Conclusion

The Lisbon Treaty may well be the beginning of a new reality for public services. The creation of a specific legal base means that the Union now has the means to define a coherent European

approach to public services. This exercise requires a voluntary approach as Article 14 TFEU will not in itself trigger any significant change. Only the European legislator can change the rules of the game by adopting a specific instrument on SGEIs. This will not be an easy exercise. In particular, a delicate balance will have to be found between the need for the Union to recognise the role and place of public services and the subsidiarity principle that is implicitly enshrined in the Protocol. The Commission has not yet expressed the intention of taking action on the basis of Article 14 TFEU. It is, however, essential to launch a debate on the future of public services in the Union. Legislative inertia would be tantamount to the waste of a formidable opportunity for Social Europe.

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