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ROUNDTABLE ON COMPETITIVE NEUTRALITY IN COMPETITION ENFORCEMENT

-- Note by the Netherlands --

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More documents related to this discussion can be found at www.oecd.org/daf/competition/competitive-neutrality-in-competition-enforcement.htm.

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THE NETHERLANDS

1. Introduction

1. Competitive neutrality is about the role of government in the economy. The government can be active as entrepreneur, as contractor, as shareholder, and as a supporter of industry. The role of government as contractor is legislated for in public procurement rules. The role of government as shareholder, for example, in major energy and transport companies, is an important aspect of competitive neutrality that is governed by state aid law, competition law and sector-specific regulations. The Act that is currently being evaluated in the Netherlands, and which is the subject of this paper, relates solely to the role of government as entrepreneur. By entrepreneur we mean where government organizations, such as municipalities, become active economically in relatively local markets, for example in the provision of sports services, outside of the area covered by sector-specific legislation. Within this Act, a safe harbour has been put in place which gives municipalities the freedom to specify certain general interest that will subsequently fall outside the scope of this Act. We are fully aware that this particular Dutch Act covers only a part of the full picture. It supplements the existing framework of state aid law, competition law and sector-specific regulations.

2. The Netherlands tackles this specific aspect of competitive neutrality directly by addressing the government organizations (rather than the undertakings through which they are actively participating in the market).

3. The 2012 Act "Markets and governments" amends the Dutch Competition Act[1] by introducing rules regarding the conduct of government organizations.[2] The Act affects government organizations that either engage in economic activities themselves or via a government undertaking whose strategy may be set by those government organizations. [3] This Act provides clear rules on how government organizations engage in economic activities on markets where private undertakings are active. This is a supplement to existing general and sector-specific competition rules. The rationale is that government organizations may engage in such activities, but that they should not have an unfair advantage as defined in the legislation. As a result of this Act the ACM is able to take measures against unfair competition[4] by government organizations in this context. However, enforcement action by the ACM is not possible in cases where the democratically elected body in question has previously taken the decision that certain economic activities concern a public interest.

4. ACM's view of the working of this new legislation is cautiously positive. ACM's studies suggest that unfortunately, the Act helps achieve 'competitive neutrality' only to a limited degree. Nevertheless, we think on the balance that the Act delivers what it promises to deliver. In this paper

1 *De Nederlandse Mededingingswet* (Act of 22 May 1997, Providing New Rules for Economic Competition) (Competition Act) as amended.

2 In this paper, the term government organization as referred to in the Act, includes local councils, provinces, regional water authorities and quasi-autonomous administrative authorities.

3 A government undertaking is defined as a private undertaking which is controlled by (has its strategy set by) the government (as defined in footnote 3 above). Note that state-owned enterprises governed by sector-specific legislation fall outside this legislation.

4 In this paper the term unfair competition is used as a translation of the Dutch term *oneigenlijk* and refers to improper behaviour, this term does not necessarily confer any illegal status to the behaviour.

we set out the background to the legislation and explain our evaluation of its effectiveness. In the conclusion we address the questions of whether improvements to the legislation are necessary, and what other steps would promote competitive neutrality in this area.

2. Background to the legislation

5. In the 1980s, the Dutch government faced soaring budget deficits. In an attempt to address these deficits, it reorganized government finance sustainability by diminishing the budget allocated to government organizations, such as municipalities.[5] In response, many of these organizations began to expand their activities in the free market in an effort to compensate for the loss in income. As an expansion of their activities, government organizations started to supply goods and services that private market parties already offered, or could offer, on the free market. Examples include offering fire-safety trainings or providing local passenger transport services.

6. In principle, in the Netherlands, government organizations may act legally as a private undertaking. In such cases, the government organization could become a direct competitor of private undertakings. When government organizations started entering commercial markets, insufficient consideration was given to the possibility these government organizations would have an unfair advantage over private undertakings on the free market, thereby potentially causing market disruptions and an uneven playing field.[6] As the government's presence on the free market increased, so did the resistance regarding perceived inequalities.[7] Existing sector specific legislation as well as European rules on State Aid only go so far in alleviating these problems it does not tackle small undertakings.[8] In light of the above, the Dutch government came to the conclusion that a new legal framework was needed in order to prevent unfair competition from occurring when governments act as private companies. An ACM study has revealed that 83% of all local governments engage in commercial activities. Despite this fact, it took fifteen years of public debate in the Netherlands, before the new legislation was introduced.

2.1 The competitive neutrality rules

7. The Act creates as level a playing field as possible for government organizations, while taking into account the government's specific public duties. Certain rules regarding the conduct of governments have therefore been incorporated into the Act relating to risks of disruption of competition.[9]

8. These rules cover the financing of economic activities, the sharing of information that has been collected whilst carrying out public duties, the separation of government and business roles, and preferential treatment of government undertakings. Given that these rules relate to competition, they are included in the Dutch Competition Act, and are enforced by the Authority Consumer and Markets (ACM). In principle, the Act covers all industries where the government acts as supplier of goods and

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5 Brief over Nader rapport inzake wetsvoorstel aanpassing Mededingingswet ter invoering van gedragsregels voor de overheid. http://www.ez.nl/dsresource?objectid=156104&type=PDF

6 Chapter 1.2 and 1.4.2 *Voorstel van wet tot wijziging van de Mededingingswet ter invoering van regels inzake ondernemingen die deel uitmaken van een publiekrechtelijke rechtspersoon of die hiermee zijn verbonden (aanpassing Mededingingswet ter invoering van gedragsregels voor de overheid)* Memorie van toelichting (15 februari 2008) (Tweede Kamer Vergaderjaar 2007-2008, 31 354, nr.3) (Explanatory Memorandum).

7 " *Onderzoek naar de problematiek Markt en Overheid"* PricewaterhouseCoopers, Den Haag, April 2005. (Investigation into the issue Markets and the Government).

8 See OECD-document *Roundtable on regulating market activities by the Public Sector*, background note by the Secretariat (Daf/COMP (2004) 18, Paris, 17 May 2004, p.19).

9 Chapter 6 Explanatory Memorandum.

services. However, as a result of political choices and other regulatory measures, some industries do not fall under the Act's scope, these include public education and research, public broadcasting, and, to a certain degree, sheltered workshops.[10] In addition, this Act does not apply to situations where European regulations on state aid are applicable.

9. Adopting legislation on competitive neutrality between public enterprises and private-owned businesses is sensitive because it impinges on the autonomy of governments to decide themselves what is beneficial for their citizens. It is therefore not surprising that the protracted political discussion about this law resulted in a compromise. The Act contains a major exception for activities that are in the public interest. The rules are as follows.

2.1.1 Obligation to include all costs

10. Government organizations are required to set the prices for their goods or services at such a level that they will at least cover the costs per good or service.[11] The obligation to include all costs means that all costs, both direct and indirect, need to be included in the product's price.

11. For example, a government organization must include all the costs of running a public swimming pool (exclusive the swimming pool profits) when determining the price to charge the consumer for the swimming facilities. All direct and indirect costs are to be included: for example, costs for making financial resources available, costs of utilizing means of production, labor costs and other personnel costs. By obliging government organizations to include all associated costs, the law enables private undertakings offering swimming pool activities to compete on a level playing field with a government organization active in the same market.

12. A more detailed set of rules, regarding the obligation of government organizations to include all costs has been drawn up in secondary legislation. This complementary set of rules serves as a benchmark for government organizations active on the free market, as well as for private undertakings and the ACM.

2.1.2 Inequality of access to information.

13. Government organizations may have an unfair competitive advantage if they have access to information obtained by governments when carrying out public duties using public funds.[12] The costs of gathering such competitively advantageous information are much lower for a government organization, as such bodies generally have free access to such information in their role as a public administrative body. The costs that a private undertaking would incur in order to obtain such information are generally calculated in the price to the consumer, with the result that the price of the product or service is much higher and can therefore not compete with similar products offered by government organizations. The Act therefore makes clear that information that has been collected within the context of a public duty may only be used for commercial purposes if that same information is also made available to third parties, under the same conditions as those that apply to the government organization.[13]

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10 Section 25h of the Act. There are some exceptions to this rule, see Chapter 4 Explanatory Memorandum.

11 Section 25i of the Act. For the sake of clarity it is important to note that although the Act only directly regulates the behaviour of government organizations, that through such regulation, it also exerts an indirect affect on government undertakings.

12 Section 25k of the Act.

13 Section 25k of the Act.

2.1.3 Necessity to maintain a distinction between public duties and operating a government run economic business

14. The Act refers to the necessity of ensuring that duties and responsibilities regarding economic activities on the one hand, and the carrying out of administrative duties that are somehow related to those economic activities on the other hand, are not carried out by one and the same person. The fact that a government organization is engaged in economic activities in an industry in which the government also has statutory powers could result, for example, in suppliers assuming the government might be less strict in its assessment than for private undertakings competing on the same market.[14] When the government organization has a competitive advantage of that nature, other market players will be unable to maintain their position, no matter how trustworthy they are or how good their products appear to be. The Act therefore states that government organizations must ensure that in such situations the same individuals are prevented from being involved in the execution of the public duties and/or engaged in the economic activities related to those public duties.[15]

2.1.4 Prohibition of preferential treatment of government undertakings.

15. A government organization may establish or control an undertaking to conduct certain economic activities. Rather than requiring such an undertaking to include all costs, which may be unduly restricting, the Act prohibits preferential treatment by the government organization of such an undertaking.[16] Nor can the undertaking be allowed to profit from the reputation of being attached to or controlled by the government organization.[17]

2.2 Important exception: services of public interest

16. A government organization may at times carry out economic activities in the context of its public duties, which provide a service of public interest. These services are different from 'regular services' because certain public interests that are involved (eg. quality, accessibility and supply reliability).[18] Under certain circumstances, strict enforcement of the rules, and the obligation to include all costs in particular, may impede the execution of public duties. For example, in order to increase the penetration rate of a good or service, the government organization may offer economic activities below their cost price (e.g. offering swimming lessons or operating cultural events and/or businesses at or below cost price). The rules therefore do not apply insofar as a service/good of public interest is concerned. It is for the relevant government organization to judge whether the goods or services offered fall under a public interest, so that they are exempt from the Act. In order to make that judgment, the government organization will consider, firstly, whether the organization, or a part thereof, is charged with providing that service, and secondly, whether financing through public funds is vital to the provision of the service. The decision of whether or not an individual economic activity qualifies as an activity of public interest will be made by the relevant democratically elected public body, such as provincial councils, municipal councils and regional water authorities.[19] Interested parties may influence this decision-making process, using the normal public-inquiry procedures or other instruments. Furthermore, interested parties may file objections against such decisions before

14 In this instance, assessment refers to the regulatory role the government has in authorizing, for example, permits, certificates and clearances.

15 Section 251 of the Act.

16 Section 25j of the Act.

17 Secti0n 25j, second paragraph of the Act.

18 Section 25i of the Act which is based on articles 16 and 86 of the EC Treaty.

19 Section 25h, paragraph 6 of the Act.

the administrative court.[20] ACM is to follow that decision, and in practice steps back as regulator in such cases.

2.3 Enforcement of the Act

17. The Act adds several provisions to the Dutch Competition Act, which ACM is charged with enforcing. ACM is authorized to carry out enforcement activities at its own discretion, however it usually does so in response to complaints or tip-offs concerning alleged violations. For this reason it was very important to create a high awareness of the new rules.

18. When a violation of the rules has been established, ACM may issue a declaration stating that it has found a violation. Should the ACM believe that such a declaration is insufficient, it is able to impose an administrative order subject to periodic penalty payments, forcing the government organization involved to terminate the violation.[21] The Act does not grant the ACM the power to impose fines on government organizations. This power to fine was omitted from the Act as it was considered prudent to prevent one administrative body from having the ability to impose penalties on another.[22] The Dutch government believes that a public statement by the ACM in conjunction with the threat of imposing an order subject to periodic penalty payments will prove to be sufficiently effective in engendering compliance with the law. Awareness of the legislation therefore plays an important role in detecting possible transgressions, and is also crucial for self-regulation to succeed.

3. Evaluation

19. The Dutch Act came into force in July 2012. However a transitional regime was in place until July 2014 in order to give government organizations time to comply with the new provisions. This means that ACM has actually only been able to enforce the Act, as regards existing economic activities, since July, 2014. While ACM's practical enforcement experience has been relatively short, we are nevertheless already assessing the effectiveness of the Act because it contains a 'sunset clause'. This means that the Act will cease to exist from July 1, 2017, unless the legislature decides otherwise. In this light, the Dutch act on competitive neutrality is currently being evaluated by the Dutch Ministry of Economic Affairs, and ACM has evaluated the operation of the new rules, to determine whether they help to realise a level playing field.

3.1 Creating awareness

20. In May 2013, one year after the enactment became law, the Netherlands Competition Authority asked an external party to perform a baseline measurement concerning, inter alia the public awareness issue. At that point, the study found that almost 60% of government organizations were not engaged in activities aimed at compliance of the law. More strikingly 75% of those government organizations were not familiar with the goal of the new law. ACM needed to tackle this in order to achieve a high compliance rate.

21. In addition, the study researched where governments were seeking information concerning the law. There were several distinct information corridors that were used, for example, directly at ACM, branch organizations and the internet. Municipalities particularly expressed the desire for clarity on practical matters like calculation of costs. The information that was received from business owners was double-sided in that they perceived unfair competition by the government as a big problem but on the other hand the majority had no first-hand experience of unfair competition. Under business owners, 87% were ignorant of the law, so they could not signal transgressions. Furthermore

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20 The judge would likely use a marginal test in this judicial review, as such decisions involve a large measure of discretion on the part of the elected public body.

21 Chapter 3.2.2 Explanatory Memorandum.

22 Section B of the Act.

businesses were unaware that transgression could be notified to ACM. In all, this implied that the problem of government neutrality might be more severe than suggested beforehand.[23]

22. On the basis of the outcomes of this baseline measurement study ACM conducted a successful public awareness campaign. In March 2014, ACM launched the 'the Government and Free Markets Test'. This is an online test with which local governments, provinces, the central government and water authorities can see whether the rules of conduct laid down in the Dutch Act on Government and Free Markets applied to their situation. Furthermore, ACM collected several illustrative and practical examples of economic activities and published them in a book, titled 'If public employees become entrepreneurs'. Another achievement are our compliance and enforcement efforts of the Dutch Act on Government and Free Markets as explained above.

23. ACM's extensive guidance on this new legislation has seemed to pay off. Sector-studies, published in January 2015, show that the awareness of the legislation among government organizations has increased significantly. For example, the compliance by government organizations is far higher than was evidenced in the earlier baseline study. Also, most government organizations claim to have altered their behaviour in order to ensure continuing compliance with the new rules.

3.2 ACM's experience with the new rules

24. As mentioned above, ACM's baseline study revealed that many businesses consider unfair competition by governments as a huge problem. In the last four years, ACM received approximately 200 complaints. However, more than half of the complaints did not relate to commercial activities by governments. In fact, only 30 or so of the complaints related to issues that ACM could examine under the legislation. An often heard complaint is that businesses are of the opinion that the government carries out too many activities that could be more easily left to the market. For example, where police forces use their own vehicles to tow cars from collision scenes, or a municipality has its offices cleaned or protected by its own employees. However, these forms of insourcing fall outside the scope of the Dutch act on competitive neutrality between public enterprises and private-owned businesses.

25. Most complaints (that were considered admissible) concerned municipalities that offer products or services relating to:

- Sports facilities
- Marina berths
- Real estate
- Trainings and educational programs
- Commercial waste
- Motorhome campsites (or RV parks)
- Parking garages

26. The complaints relate mostly to relatively small commercial activities. However, the consequences of unfair competition for an individual business owner can be significant, and the collective impact on deterring innovation can be significant.

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[23] *"Nulmeting markt en overheid"* Kwink Groep, Den Haag, April 2013. (Zero measurement market and government), p 8-10.

27. ACM recently looked into the effect of the Dutch act on competitive neutrality in three of these sectors. We focused specifically on sport facilities, car-parks and company waste disposal. The studies revealed that municipalities do comply with the law, but that this compliance has helped realize equal competitive positions only to a limited extent. One of the main reasons for this is that, in many cases, governments decided that their activities are public interests, rendering the Dutch act on competitive neutrality inapplicable. Furthermore, we have observed that, in other sectors too, the public-interest exception is used extensively. More than 90% of municipalities have decided that they carry out one or more public-interest activities.

3.2.1 Definition of public interest

28. The question is whether it is right that the government organization itself decides when an activity qualifies as an activity of public interest. This is an issue that we expect to arise in the upcoming parliamentary debates on this legislation. It is ACM's view that the democratically elected public representative body (be that a council, a municipality or a provincial board) is best placed to make this decision. Having a definition of what amounts to a public interest would unlikely have a major effect. It is not our experience that municipalities are in fact involved in major economic interests outside of their public tasks. We simply have no evidence that this is the case. There are at most, a couple of instances, a yacht harbor here, a sports facility there. Most of the decisions made by municipalities relate to swimming pools and sports facilities.

29. What is striking is that private businesses hardly object to such public-interest decisions. However, it could be that private companies are becoming more alert to the legal possibilities created by the new legislation, because the first lawsuit has recently been filed against a municipal public-interest decision.

3.2.2 Assessing costs

30. Assessing the costs incurred by the municipalities has proven difficult. In reality, ACM's assessments are complaint-driven. We only assess the costs where we have complaints. The burden of proof lies with the municipality to prove that costs are included in the price. This has proven more difficult in reality than we had foreseen. Not all municipalities calculate their costs in the same way, and it can be difficult to encourage them to detail their costs, rather than allocate high-level costs, which is what they are used to doing.

31. To give an example, a municipality may have a sports facility, which is used during the day by local schools, but is available for hire in the evenings. The municipality allocates budget annually to cover energy costs. However, it does not automatically split the energy costs related to the day-use of the sports facility from the energy costs related to the evening, commercial use of the sports facility.

32. Another problem arises where for example, the sports facility includes tanning booths. The municipality charges a standard tariff for entrance all of its sports facilities. In this particular sports facility, that entrance fee automatically includes the use of the tanning booths. The competitor active in the tanning booth market, facing competition from the municipality in this market, may complain about the level at which costs should be aggregated.

3.2.3 Prioritisation

33. It is important for ACM to manage expectations in relation to what the legislation can achieve. The success that has been booked with the implementation of this new Act relates primarily to the compliance that has been achieved by ACM through promoting awareness.

34. The actual cases that emerge from the enforcement of the legislation seem largely to relate to small markets. This does not take from their importance but the question must be posed to what

degree such cases should be prioritized by the authority in the long term. Where choices have to be made between spending resources on investigating a cartel, or on assessing a cost-benefit analysis on the sponsoring by local government of a swimming pool in a small village, the question is whether the cartel should win priority. Is it fair, in that context, to expect local government to engage in an elaborate cost-allocation exercise in relation to marginal economic activities?

4. Conclusion

35. In conclusion, we would argue that the Dutch Act on competitive neutrality has had a positive effect. Firstly, the Act ensures that the topic of 'competitive neutrality' is present on the political agenda. Secondly, there are examples of local governments that have changed their practices, either voluntarily or after ACM had urged them to do so. So the first steps have been taken. The first ACM decisions enforcing the legislation are soon to be published. The evaluation of the Ministry will probably reignite the debate. Employers' organizations are already calling on lawmakers to revise the law.

36. ACM's view is that this law is good as far as it goes, but that its scope is limited. Municipalities are complying with the legislation. We have made it clear what is permitted by the law, and what is not allowed. We will have some decisions implementing the rules, but municipalities are largely compliant now. So if more changes are desired then other types of rules will be needed. A very real question is, whether a sharpening of the current rules, would really solve the remaining problems as companies see them. These are more problems relating to insourcing, and state aid issues. There are also problems, when it comes to the government as shareholder, relating to perceptions and expectations of the government's role in defending national interests. These are not covered by this Act.