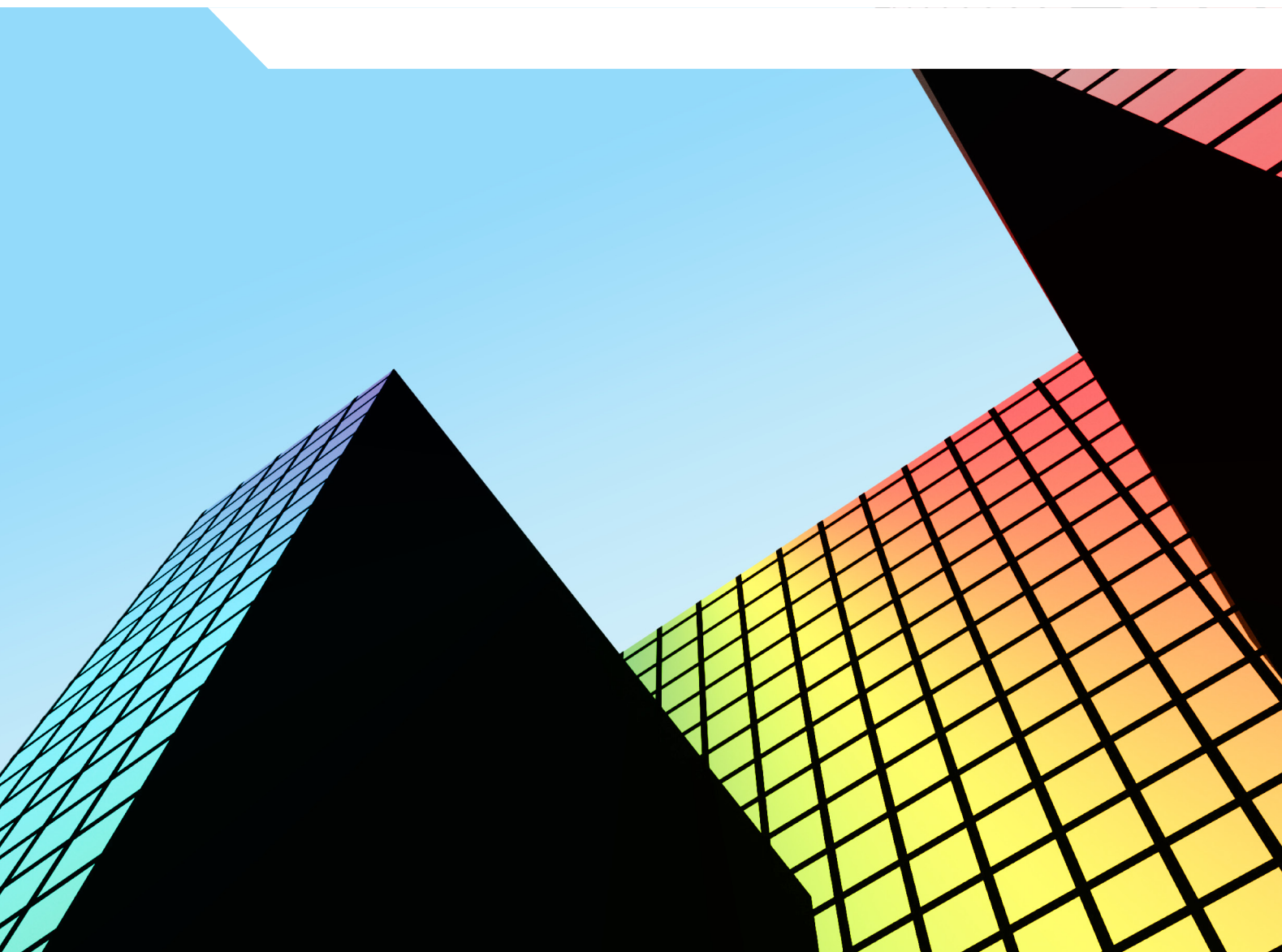




# Competitive Neutrality

## NATIONAL PRACTICES



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## EXECUTIVE SUMMARY

This report summarises the responses to a comprehensive questionnaire concerning national approaches to competitive neutrality. The questionnaire was sent to state ownership functions and competition authorities in all OECD member countries, the European Union (EU) and a small number of observer countries. Thirty countries have responded so far, many of which providing consolidated replies from various branches of government.

***National competitive neutrality frameworks.*** In all countries, public sector entities are providing goods and services in competition with the private sector – or in areas where private sector businesses could potentially compete. In specific jurisdictions, the degree to which aspects or elements of competitive neutrality are considered vary:

- In the case of all EU (including EEA) member States, specific provisions of EU law bearing on competitive neutrality apply to all undertakings regardless of ownership, including private companies entrusted with public service obligations (i.e. services of general economic interest) and companies benefiting from special and exclusive rights. The European Commission (EU Commission) is responsible for enforcing the EU rules on competitive neutrality.<sup>1</sup>
- In most countries, aspects or elements of competitive neutrality are dealt with through competition laws and policies. While most of these policies explicitly give public and private businesses equal rights and obligations, the extent to which competition policies and laws apply to different types of government businesses differ (e.g. general government activities may fall outside the scope for competition law, or exemptions from competition law may exist in statutory laws for state-owned enterprises (SOEs) in specific sectors, especially in the network sectors where universal service obligations are of importance). Among countries which are subject to certain EU rules, there may be national deviations for non-regulated aspects.
- A minority of countries have explicitly addressed and built-in the enforcement of competitive neutrality to their national policies. In a few countries, formal competitive neutrality frameworks have been established. In several others, competition law and other targeted policies are aimed explicitly at achieving competitive neutrality in mixed markets. In these cases, the application of such frameworks goes beyond traditional SOEs to include a broader definition of what constitutes government “business”.

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1. Across the document, national features of individual EU (including EEA) member States are described separately from the discussion of competitive neutrality provisions in the EU itself. However, given the specific features of the EU legal system, many national provisions originate from the EU provisions: all EU (including EEA) member States are subject to certain EU rules (e.g. EU rules on State Aid) and that for those aspects which are not regulated by the EU, there can be variations (e.g. on the implementation of EU Directives). The EC is entrusted with the task of monitoring member States’ compliance with the EU rules.

***Streamlining the operational form of government business.*** The trend across countries is toward a more complete corporatisation of SOEs and other commercial entities (established according to statutory legislation, public law, and/or company law). That said, a majority of countries retain general departments of government, agencies or other public institutions (at the national or sub-national level) delivering goods and services on a commercial basis.

Most countries have also sought to structurally separate commercial from non-commercial components of SOEs. However, practices vary depending on the company and sector. In cases where governments decide against structural separation, the reasons cited are mostly a technical infeasibility of separation, economic inefficiency and/or concerns about the ability to maintain public service obligations.

***Identifying the costs of any given function.*** Transparency and disclosure practices for incorporated SOEs are, to a large extent, similar as for private sector companies (e.g. annual/quarterly reporting according to internationally accepted reporting standards, subject to internal and external audit, and information is made available to the public). Some government businesses may be subject to more stringent reporting, especially where public budgets are directly affected. One area where incorporated SOEs may be subject to more lenient reporting requirements than private companies concerns the attribution of liabilities. A special case is often public pensions, which are usually reflected in the government's general balance sheets.

Separating commercial from non-commercial accounts may be particularly relevant in sectors where sectoral regulation exists (e.g. utilities and energy sectors) and/or where public service obligations are concerned. However, doing so is not a commonly applied practice. In EU countries accounting separation in principle applies to all undertakings (public or private) receiving public funds or benefiting from special or exclusive rights (the methods used to calculate costs are also subject to specific requirements).

***Achieving a commercial rate of return.*** It is not common practice to impose *ex-ante* rate-of-return (RoR) requirements on government businesses. Conversely, most incorporated SOEs have performance objectives which are benchmarked against industry comparisons. Among those countries that do impose RoR requirements, the requirements are market consistent and take into consideration benefits associated with public ownership (e.g. cost of capital, full costs, other economic conditions or pricing requirements set by the government). They are usually benchmarked according to government or sector risks.

***Accounting for public service obligations.*** Virtually all countries compensate undertakings (public or private) which deliver public service obligations alongside their commercial activities. Compensation mechanisms (e.g. direct transfers, capital grants, *ex-post* and *ex-ante* reimbursements, budget appropriations, and state aids/subsidies) depend on the service being delivered and entity delivering such services. Compensation for essential public services are often regulated according to sector-specific laws (e.g. in post, utilities, telecom, health, and transport sectors) and according to rules on state aids and subsidies [especially for EU (including EEA) member States].

In a minority of countries, compensation is not provided; public services are rather funded through user charges, directly factored into tariffs/cost structure. The adequacy of compensation is determined by sector regulators (or other public authorities) and in accordance with agreed standards in quality and price. Concerning cross-subsidisation practices, a majority of countries permit or tolerate cross-subsidisation from profit-making to loss-making activities to fund public obligations on a case-by-case basis. Conversely, a few countries have outright bans on cross-subsidisation across activity areas, but even they usually permit implicit transfers among client segments. To ensure that

public funds are not used to carry out commercially-oriented activities, some countries require that publicly-funded undertakings separate their commercial from non-commercial accounts.

**Tax neutrality.** In a majority of countries public undertakings are subject to the same or similar tax treatment as private enterprises, especially where public undertakings are conducted as legally incorporated businesses operating at arm's length from the government. Some exceptions apply to specific categories of SOEs which may be carrying out non-commercial objectives, such as universal service obligations (e.g. in postal sector), and which may be exempt from tax on income derived from such obligations in addition to being or exempt from VAT or charging VAT on these transactions.

In other cases, categories of public bodies may be afforded tax advantages through partial or entirely exempt status (direct or indirect taxes or a combination of the two). These undertakings are usually public bodies operating as part of general government plus in some cases statutory corporations. In some countries, unincorporated government undertakings may be subject to some other forms of taxation (depending on the public body and applicable tax laws). A minority of countries consider their SOEs to be at a tax *disadvantage* due to higher tax corporate tax rates or inability to benefit from tax write-offs.

Where differences in tax treatment exist, compensatory payments in lieu of taxation is not common practice in most countries, in fact only two countries report that some form of tax neutrally adjustments are made in order to compensate for differences between public and private business tax treatment. In the EU (and EEA) countries, any form of preferential tax treatment incompatible with EU rules on State aid is subject to enforcement by the EC.

**Regulatory neutrality.** In most countries, incorporated government businesses are subject to the same regulatory treatment as private sector businesses. Where exemptions apply, they are laid out in market regulation (e.g. where natural monopolies are concerned) or in the statutory/enacting legislation. Such exceptions usually concern competition laws. Where commercial activities are integrated with general government, some controversy may arise as to the applicability or exemption from regulations which may otherwise be applicable to private sector businesses.

State-owned businesses may in some cases/countries be afforded regulatory advantages such as: lower compliance costs (e.g. exempt or lower costs for permits, registration or licences); exemptions from zoning regulations; or preferential treatment due to their public sector status (e.g. quicker approval of projects). In other cases, public businesses may be subject to more stringent regulatory requirements than private sector companies, for instance regarding reporting requirements and the fulfilment of public service obligations.

**Debt neutrality and outright subsidies.** Sources of financing for state-owned companies differ depending on the level of incorporation. Incorporated SOEs are mostly financed through financial markets on the same terms as the private sector. In two exceptional cases state-owned businesses are not legally permitted to obtain financing from the market; financing is provided through national funds according to "commercial principles". Notwithstanding the widespread market financing, unintended advantages from government ownership do occur. More than half of the respondents report that government businesses are afforded preferential access to financing due to implicit guarantees or perceived government backing.

Where undue advantages are afforded to government-owned companies, a number of governments have put into place debt neutrality adjustments. These include compensatory payments factoring in competitive neutrality adjustment, adjustments of lending rates according to benchmarked rates, and/or disclaimers on loan documentation on perceived government backing.

**Public procurement.** In most countries, public procurement rules specify under which conditions state-owned businesses are allowed to participate as suppliers. National policies reflect World Trade Organisation (WTO) Principles [and in the case of EU (including EEA) member countries reflect EU directives] which seek to ensure equal treatment, non-discrimination, transparency and value for money.

A grey area which emerges from country practices concerns in-house procurement from unincorporated business units within general government. In a number of cases, in-house procurement is not subject to public procurement rules and competitive tendering may not be required. Some countries have very specific rules establishing the situations in which in-house procurement is permitted and when such practices may exempt from competitive tendering. Others report that all government bodies are treated the same in procurement processes regardless of whether transactions are intra- or extra-government.



## Chapter 1

### INTRODUCTION

#### 1.1. About this report

This report is a stocktaking of national practices concerning competitive neutrality. It is organised along eight priority identified by the OECD's Working Party on State Ownership and Privatisation Practices (WP SOPP) as having a bearing on the topic.<sup>1</sup> The factual information derives mainly from a questionnaire sent government representatives in OECD and other economies from state-owned enterprise (SOE) ownership/oversight entities and competition authorities. In total, 32 countries/jurisdictions have responded to the questionnaire; 27 of which provided a full submission on competitive neutrality practices: Australia, Austria, Chile, Czech Republic, Denmark, Egypt, Estonia, European Commission, Finland, Germany, Hungary, Iceland, Ireland, Israel, Italy, Korea, Mexico, New Zealand, Russia, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United Kingdom and United States. Five countries responded with partial answers to the questionnaire: Brazil, Greece, Japan, Lithuania and Poland.

The country responses also differ in respect of the parts of government that have contributed. This has ramifications for the completeness of answers since a whole-of-government approach (extending beyond either ownership/oversight entities or competition authorities) tends to offer information about a broader range of public activities than, for example, one agency is able to provide. The questionnaire approaches are summarised in Table 1.1.

**Table 1.1. Overview of country respondents**

<b>Respondent(s)</b>	<b>Country/Jurisdiction</b>
SOE ownership/oversight entities	Austria, Czech Republic, Estonia, Italy, Mexico and Slovenia.
Competition Authorities	Australia, Brazil, Egypt, European Commission, Ireland, Russia, Slovak Republic and Spain.
Whole of government approach	Chile, Denmark, Finland, Germany, Greece, Hungary, Iceland, Israel, Japan, Korea, Lithuania, New Zealand, Poland, Sweden, Switzerland, Turkey, United Kingdom and United States.

The purpose of this report is threefold. First, it provides government officials in OECD and other countries with an opportunity to synthesise and compare their recent experiences with policies enshrining the principle of competitive neutrality. Second, it aims to provide a number of good – or generally accepted – practices that may serve as a guidepost for countries that have only recently embarked on developing frameworks for competitive neutrality. Third, this report together with existing OECD recommendations<sup>2</sup> provides key inputs for a best practice report on competitive neutrality entitled, *Competitive Neutrality: Maintaining a level playing field between public and private business*.

## 1.2. Definition of competitive neutrality and priority areas

Most countries which have responded to the questionnaire agree that competitive neutrality is a sound idea and a majority of their governments consider aspects or elements of competitive neutrality in national policies. However, what constitutes competitive neutrality differs among relevant authorities of most countries covered by the survey. For the purposes of this report the following definition is adopted: *Competitive neutrality occurs where no entity operating in an economic market is subject to undue competitive advantages or disadvantages.*<sup>3</sup>

Indeed, if national authorities are committed to levelling the playing field and neutralise any advantages or disadvantages associated with public ownership, the following priorities have been identified and are covered by the questionnaire:

- The **operational form of government business** considers the organisational form and degree of corporatisation of entities that participate in commercial activities. It also considers the extent to which commercial and non-commercial objectives have been structurally separated. In practice, the level of corporatisation varies considerably from country to country depending on the type of business and whether the public body in question fulfils non-commercial objectives. Structural separation also depends on a number of factors which may be influenced by public policy functions (e.g. maintaining public service obligations) or economic considerations (e.g. infeasible).
- **Identifying costs** of commercial entities considers the level of transparency and disclosure surrounding a business' cost structure, whether costs of different functions are accounted for separately (e.g. commercial from non-commercial activities), and whether liabilities, including pension liabilities, are reported. It also examines how countries treat shared costs for commercial activities operating out of general units of government. In practice, transparency and disclosure are legal requirements in most countries' SOE policies, according to generally accepted accounting standards. While most countries report liabilities, they do not treat pension liabilities as a specific requirement. The degree of accounting separation between different functions varies from country to country and often depends on the type of business activity in question.
- Achieving a **commercial rate of return** considers whether government business activities are indeed operating like comparable businesses, and how they, or incumbents, co-exist with private competition, especially in regulated markets. In practice, roughly half of respondents report that their SOEs' commercial activities are required to earn market-consistent rates of return, employing a diverse range of methodologies to define these rates. SOEs and incumbents co-exist with private competition in a variety of regulated markets, most commonly in the utilities and network industries (e.g. post, telecommunications, electricity, and transport).
- **Accounting for public service obligations** considers the level of transparency and adequacy surrounding compensation for public service obligations, and how such compensation is disbursed by the government. In practice, a significant majority of respondents report that their SOEs are compensated from the public purse, via different disbursement channels defined by sector-specific laws and regulations. For what concerns European Union (EU) member states, transparency and adequacy is defined according to the Union's State aid rules and Transparency Directive.

- **Tax neutrality** considers whether government businesses are subject to the same tax treatment as similar businesses in the private sector. In practice, most incorporated SOEs are/should be subject to the similar treatment (tax or regulatory). A significant portion of respondents do not report whether unincorporated public entities are subject to tax exemptions, but report that there is no system of compensatory payments in lieu of taxation (with the exception of Australia).
- **Regulatory neutrality** considers the regulatory treatment of publicly-owned commercial bodies, and whether such treatment puts such bodies at a regulatory advantage or disadvantage as compared to similar businesses. In practice, most countries report that their SOEs are subject to no regulatory advantages due to their ownership; in a minority of cases, SOEs may be subject to regulatory disadvantages. Where regulatory advantages are reported, roughly half of respondents report that compensatory payments are made.
- **Debt neutrality** considers sources of financing for commercial undertakings and any advantages which may be afforded due to public ownership. In practice, financing emanates from a variety of sources from one country to the next, with almost all reporting that SOEs access financing at market rates from commercial banks (public or private banks or a combination of both). In a majority of countries, SOEs are reportedly subject to bankruptcy rules; whereas roughly half of countries which responded are backed in the form of explicit or implicit government guarantees.
- **Public procurement** considers whether government procurement rules take competitive neutrality into consideration and whether such rules apply to SOEs and in-house or intra-government procurement. It also considers whether incumbency advantages have been alleged, and if so whether compensatory payments have been made on the basis of these advantages. In practice, a majority of respondents report that general public procurement rules apply to government activities and in some cases also to SOEs; here are fewer countries that apply these rules to the provision of goods and services that are procured from in-house or intra-governmental suppliers.

Some national authorities apply competitive neutrality policies only to the activities of “traditional” SOEs (usually incorporated according to company law, charter or statutory authorisation).<sup>4</sup> Others apply competitive neutrality practices to all types of government activities that can be characterised as “commercial” in nature, regardless of their legal form. Activities which are commercial in nature can be characterised as a combination of the following: the entity intends to charge for the service; there are no restrictions on profitability; and there is actual or potential for competition.<sup>5</sup>

Non-commercial activities can be considered as public service obligations or other responsibilities that a public undertaking is required to undertake beyond its commercial activities (SOE Guideline I.C.).<sup>6</sup> These obligations (e.g. universal service, community service, or public service obligations) are often required in order to provide a service of a given quality at a “reasonable” price for consumers. While not all service obligations are non-commercial, most often such types of services are reported to involve provision of services to “economically identifiable” groups where costs exceed revenues from service those customers.

In most surveyed countries the boundaries between public and private, and commercial and non-commercial are sometimes blurred. Most obviously, some government businesses are requested to pursue jointly commercial and non-commercial objectives, such as public service obligations or industrial policy objectives. Further complications may arise from the level of incorporation of

state-owned commercial entities. There is immense variety in the types of government commercial activity that takes place across countries. For example, in some jurisdictions general units of government operating at the sub-national level may provide goods or services on a commercial or near-commercial basis (with actual or potential for private sector competition); whereas in others, commercial activities are carried out strictly by incorporated SOEs.

Some respondents also refer to the competitive position of entities that may not be directly controlled by the government (e.g. licensed operators, legacy rights or recently privatised companies). This is consistent with an enlarged EU concept which, in addition to the list above, includes:

- private companies entrusted with public service obligations (i.e. services of general economic interest); and,
- companies benefiting from special and exclusive rights.

Important issues may also arise from the commercial activities of the non-profit (or “third”) sector, but they fall outside the scope of the questionnaire and report.

### **1.3. Structure of the report**

The remainder of the report is organised as follows. Chapter 2 provides a brief overview of national policies and country experiences that consider aspects or elements of competitive neutrality, based on the first part of the questionnaire. Chapter 3 (subdivided into sections 1 to 8) reviews each of the eight priority areas identified and include case studies where relevant. These sections are based on the second part of the questionnaire exercise. Each section begins with an overview of main findings. It is followed by a number of sub-sections providing national details based on the individual questionnaire responses.

### **Notes**

1. The WP SOPP is an official body of the OECD focused on state ownership and privatisation practices. It is a multilateral body bringing together practitioners from government departments charged with the ownership and oversight of SOEs. It is also the custodian of the internationally-recognised OECD Guidelines on Corporate Governance of SOEs. The Working Party prepared the current report in concert with the OECD Competition Committee and its Working Party on Enforcement.
2. See report entitled, OECD (2012), *A compendium of OECD recommendations, guidance and best practices bearing on competitive neutrality*.
3. This definition slightly differs from the one used in the questionnaire. It reflects discussions involving relevant OECD bodies following subsequent revisions of the report.
4. For the purposes of this report, where SOE is mentioned it refers to incorporated state-owned enterprise under the relevant law (e.g. companies’ act, public or statutory law).
5. OECD (2005), *Journal of Competition Law and Policy*, Vol. 7, No. 3, OECD, Paris, p. 50.
6. The actual text of Guideline I.C. reads as follows, “Any obligations and responsibilities that an SOE is required to undertake in terms of public services beyond the generally accepted norm should be clearly mandated by laws or regulations. Such obligations and responsibilities should also be disclosed to the general public and related costs should be covered in a transparent manner.” (SOE Guideline I.C.)

## **NATIONAL COMPETITIVE NEUTRALITY FRAMEWORKS**

In most countries public sector entities provide goods and services in competition with the private sector – or in areas where private sector businesses could potentially compete. Insofar as markets are open and there is a level playing field among the public sector and private providers – which is both healthy and economically efficient – this is said to be competitively neutral. However, country experience illustrates that several sources of competitive distortions can arise because of advantages or disadvantages some public sector commercially-oriented activities face by virtue of their ownership. In order to tackle such distortions, policy-makers must address aspects or elements of competitive neutrality.

This section provides an overview of national competitive neutrality practices. The section considers whether authorities have expressed commitment to address aspects or elements of competitive neutrality in the presence of government-controlled businesses. It considers whether such policies are enshrined in laws and regulations and whether they apply beyond “traditional” SOEs, such as for unincorporated government business activities. Finally, it considers whether there are designated bodies responsible for the oversight, investigation and enforcement of competitive neutrality; and if so, whether remedies are made in cases of non-compliance.

### **2.1. Overview of findings**

In all surveyed countries, public sector entities provide goods and services in competition with the private sector – or in areas where private sector businesses could potentially compete. In these specific national contexts, the degrees to which aspects or elements of competitive neutrality are considered vary (Table 2.1):

- Over three quarter of responses indicate that explicit laws giving public and private businesses equal rights and obligations exist in national competition or other policy frameworks; for most countries the main framework for addressing any aspects or elements of competitive neutrality that arise out of public ownership are through competition laws and policies. Among these respondents, the extent to which the application and enforcement of such policies apply to the business activities of unincorporated public businesses, ring-fenced public businesses, actual state-owned enterprises, state or other public institutions, and recently privatized companies which maintain incumbency advantages varies.

**Table 2.1. Competitive neutrality frameworks and oversight**

Country/ Jurisdiction	CN Framework	Legal or Regulatory Framework and other Guidance	Application beyond “traditional SOEs”	Responsible institution(s) Oversight (O) Investigation (I) Enforcement (E)
	Yes (explicit), No, Other*			
EU (including EEA) member States	Yes	Treaty on the Functioning of the EU Transparency Directive SGEI Package State Aid, Anti-trust and Merger Rules Competition and Procurement Laws	Yes	EU Commission (EU cross-border or merger cases above a certain threshold) Union Courts
Australia	Yes	Competition Principles Agreement (1995) Commonwealth CN Policy Statement (1996) Australian Government Competitive Neutrality Guidelines (2004) <sup>1</sup>	Yes	Department of Finance and Deregulation(O, E); Treasury (O, E); Australian Government Competitive Neutrality Complaints Office (I)
Austria	Other	EU Legal Framework + Competition Law; Procurement Law; Rules on State Aid and liberalisation of markets	Yes	EU Commission; Austrian Court of Auditors (for SOEs); Public Procurement Agency (Bundesvergabamt)
Brazil	Other	Brazilian Federal Constitution, Art. 173 § 1	–	–
Chile	Other	Constitution Article 19 N°21	N/A	Congress Courts (Appeals, Supreme and Constitutional) (I, E) FNE (I) Competition Tribunal (E)
Czech Republic	Other	EU Legal Framework Protection of Competition Act Act on Public Procurement Act on Significant Market Power in the Sale of Agriculture and Food Products Guidance (State Aid, Public Procurement, Competition Act)	Yes	EU Commission; Office for the Protection of Competition
Denmark	Other/Yes	EU Legal Framework Competition Act	Yes	EU Commission; Competition Council (O, I) Public Prosecutor for Serious Economic Crime (I, E) Ministry of Economic and Business Affairs (E)
Egypt	Other	State Companies Law Competition law Corporate Governance Code for SOEs	No	Competition Authority Economic Courts
Estonia	Other	EU Legal Framework State Assets Act Competition Act Government of the Republic Act	–	EU Commission; Competition Authority Sector Regulators Ministry of Finance
Finland	Other	EU Legal Framework Policy lines Competition Act Local Government Act State Enterprises' Act Companies' Act National Procurement Rules	Yes	EU Commission; Finnish Competition Authority Ownership Steering Department Market Court
Germany	Other	EU Legal Framework Corporate Law Budget Law Stock Corporation Act Competition Law	N/A	EU Commission; Federal Cartel Office Other relevant bodies that enforce respective rules
Greece	Other	EU Legal Framework Competition Law	Yes	EU Commission; Hellenic Competition Commission
Hungary	Other	EU Legal Framework Constitution Competition Law	–	EU Commission; Competition Authority (GVH) (E)
Iceland	Other	Competition Act	Yes	Competition Authority (I, E) Sector supervisory authorities (O)

Country/ Jurisdiction	CN Framework	Legal or Regulatory Framework and other Guidance	Application beyond “traditional SOEs”	Responsible institution(s) Oversight (O) Investigation (I) Enforcement (E)
Ireland	Other	EU Legal Framework Competition Law Final Report by Review Group on State Assets and Liabilities	–	EU Commission; Competition Authority Sector Regulators Courts
Israel	Other	Restrictive Trade Practices Law	Yes	Antitrust Authority Sector Regulators
Italy	Other	EU Legal Framework Competition Law (Law 287) Civil Code Consolidated Act of Finance	Yes	EU Commission; Antitrust Authority
Japan	–	Antimonopoly Act	–	Japan Fair Trade Commission
Korea	No/Other	Monopoly Regulation and Fair Trade Act and subordinate rules Management of Public Institutions Act <sup>2</sup> Specific SOE laws	Yes	Korean Fair Trade Commission (O,I, E) Ministry of Strategy and Finance (O)
Lithuania	–	EU Legal Framework Law on Competition	–	EU Commission; Competition Council
Mexico	Other	Federal Law of Economic Competitiveness Constitution	Yes	Competition Federal Council Sector Regulators
New Zealand	Other	Commerce Act	Yes	Commerce Commission
Poland	Other	EU Legal Framework Act on Combating unfair Competition Act on Competition and Consumer Protection Competition Policy (government documents)	Yes	EU Commission; Office of Competition and Consumer Protection Local governments Consumer organisations
Russia	Other	Article 8 Constitution Federal Law on Protection of Competition (Antimonopoly law) Law on reduction of administrative barriers and improvement of accessibility of public and municipal services	Yes	Federal Anti-monopoly Service
Slovak Republic	Other	EU Legal Framework Act on Protection of Competition, General laws (e.g. budgetary rules) Policy frameworks within specific sectors	Yes	EU Commission; Anti-Monopoly Office specific regulatory authorities, other bodies according to specific laws
Slovenia	Other	EU Legal Framework Transparency of Financial Relations and Maintenance of Separate Accounts for Different Activities Act	–	EU Commission; Responsible ministries (O,I,E) Budget supervision Office (E)
Spain	Yes	EU Legal Framework Law on the Organisation and Functioning of the Central Administration of the State Public Administrations’ Wealth Act Royal Decree 1373/2009 Competition Act	Yes	EU Commission; Competition Authority Ministry of Economy and Finance (O)
Sweden	Other/Yes	EU Legal Framework Swedish Competition Act	Yes	EU Commission; Swedish Competition Authority
Switzerland	Other	Federal Constitution Cartels Act Sector market laws Financial Budget Act Public Procurement Act Specific SOE laws Guidelines on Corporate Governance	Yes	Swiss Competition Commission (Comco)
Turkey	Other	Competition Act	–	Competition Authority (O, I, E) Other relevant bodies that enforce respective rules

Country/ Jurisdiction	CN Framework	Legal or Regulatory Framework and other Guidance	Application beyond “traditional SOEs”	Responsible institution(s) Oversight (O) Investigation (I) Enforcement (E)
United Kingdom	Other/Yes	EU Legal Framework Competition and Procurement Laws Competition Act Public Contracts Regulation	Yes	EU Commission; Office of Fair Trading Relevant sector regulators
United States	No	U.S. Code Government Corporate Control Act	N/A (depends on the entity)	Individual government agencies Congressional committees

\*In the form of explicit laws giving public and private businesses equal rights and obligations. What constitutes public business differs greatly from one jurisdiction to the next. All EU (including EEA) member States must apply EU Rules on State Aid and CN to all types of undertakings, including government activity operating out of unincorporated units or undertakings entrusted with special or exclusive rights.

- The remaining quarter of responses are from countries which have explicitly addressed and built-in competitive neutrality to their national policies, either through comprehensive competitive neutrality frameworks (Australia and Spain) or through targeted policies that seek to achieve competitive neutrality in markets where public sector businesses compete (Denmark, Finland, Sweden and the United Kingdom). In these cases, the application of such frameworks goes beyond traditional SOEs to include a broader definition of what constitutes government “business” (Box 2.1).
- EU and European Economic Area (EEA) countries are subject to EU rules which explicitly address the issue of competitive neutrality, regardless of public ownership or the legal form of the “undertaking.” The rules also apply to private companies entrusted with public service obligations (i.e. services of general economic interest); and, companies benefiting from special and exclusive rights. Variations in EU Member States’ policies may exist where aspects of such rules are not regulated.<sup>3</sup>

## 2.2. Legal or regulatory frameworks and other guidance

Many governments express commitment to address aspects or elements of competitive neutrality in the presence of government-owned businesses. However, this commitment is usually not manifested explicitly in the form of policy frameworks, laws or regulations enshrining the principle of competitive neutrality. In fact, in most cases, such commitments are expressed implicitly through competition policy and a mosaic of other laws, regulations and guidance that apply to the activities of government-owned/controlled businesses and activities of general government.

According to the vast majority of questionnaire responses competition law is the main legal framework that applies to the competitive position of SOEs and other public undertakings *vis-à-vis* private enterprises. A few exceptions apply, where the competitive position of public undertakings is addressed in or under the constitution (Brazil, Chile, Mexico, Hungary and Russia) or in legislation that concerns the activities of public undertakings (Slovenia). Aspects or elements of competitive neutrality appear in a mosaic of other laws and regulations that apply in conjunction with competition policies. These include:

- Rules on State aid and transparency [as applicable to all EU (including EEA) member States<sup>4</sup>]
- Explicit policy statements on competitive neutrality (Australia,<sup>5</sup> Spain<sup>6</sup>) (Box 2.1)



### Box 2.1. Competitive neutrality frameworks and oversight

- **Australia:** The *Competition Principles Agreement* (1995) agreed among the Commonwealth and all the States and Territories to the overarching competitive neutrality principle that government businesses should not enjoy any net competitive advantages simply as a result of their ownership. The *Australian Competitive Neutrality Policy Statement* (2004) details the application of competitive neutrality principles in the Commonwealth; similar statements are available in all States and Territories. Implementation guidelines exist at the national and sub-national level to assist managers in enforcing the financial and governance framework of competitive neutrality.<sup>7</sup> The Australian Government Competitive Neutrality Complaints Office administers complaints mechanism intended to receive complaints, undertake complaints investigations and advise the Treasurer and responsible Minister(s) on the application of competitive neutrality to government businesses.
- **Denmark:** One of the main stated purposes of the *Danish Competition Act* is to achieve competitive neutrality. It applies to any form of commercial activity as well as aid from public funds granted to commercial activities (public or private). Government controlled businesses and public authorities exercising commercial activity are subject to the prohibitions laid down by the Act.
- **Finland:** Competitive neutrality is high on the agenda of government authorities to ensure by means of competition policy, equal preconditions for private and public service production as applicable in the *Finnish Competition Act*. In addition, the *State Enterprises Act* and the *Local Government Act* apply as respective “companies’ acts” stipulating the legal personality, organisation and basic functions of government enterprises. The former was recently amended (January 2011) to incorporate (to the extent possible) companies operating under this act; an amendment to the latter is currently being considered with a view to introduce a corporatisation obligation for municipally-owned economic operators engaged in competition with private operators on a market.
- **Spain:** In addition to the stipulations of the *Competition Act*, the *Royal Decree 1379/2009* introduces specific provisions oriented to reinforce competitive neutrality. (Box 2.3)
- **Sweden:** Since January 2010, the *Swedish Competition Act* includes a new rule which aims to overcome difficulties faced by anti-trust regulators where previous antitrust rules fell outside the scope of Competition Act and the Treaty on the Functioning of the EU. The rule encompasses all types of government commercial activities and prohibits public undertakings from operating (national and sub-national level) if it distorts or impedes competition. The aim is to avoid market distortions where government-owned businesses are present.
- **United Kingdom:** The *Competition Act* (1998), which is the main legislation that prohibits undertakings from engaging in anti-competitive agreements or by abusing their dominant position, applies to all undertakings, independently of ownership. The UK has undertaken a number of studies examining competitive neutrality namely through the Office of Fair Trading working paper on competitive neutrality in mixed markets (2010)<sup>8</sup> and the public sector industry review (*Julius Review*) which recommended competitive neutrality in competitive tendering.<sup>9</sup>

- Procurement laws and rules (Austria, Czech Republic,<sup>10</sup> Finland, Hungary, Russia,<sup>11</sup> United Kingdom<sup>12</sup>)
- Laws on trade or commerce (Israel,<sup>13</sup> New Zealand<sup>14</sup>)
- Rules or guidance on public administration, state assets, SOEs or other company laws (Egypt,<sup>15</sup> Estonia,<sup>16</sup> Finland,<sup>17</sup> Germany,<sup>18</sup> Ireland,<sup>19</sup> Korea, Slovak Republic, Spain<sup>20</sup>)
- Laws related to budget allocation or accounting (Slovak Republic, Slovenia<sup>21</sup>, Spain,<sup>22</sup> Switzerland<sup>23</sup>)

Complementary to the government institutions listed above, economic regulators play a role in regulating markets where government businesses may be competing with the private sector. In a

competitive neutrality context, where SOEs, incumbents or other public bodies compete with the private sector, market regulators ensure the terms under which public/universal service obligations are being delivered and may intervene to ensure a level playing field (see Table 2.2 for an overview of regulated markets where SOEs or other public bodies may be competing with the private sector).

**Table 2.2. Regulated markets where SOEs or other public bodies operate in competition with private sector**

REGULATED MARKETS <sup>24</sup>	COUNTRY
Telecom	Austria, Brazil, Egypt, Finland, Germany, Greece, Russia, Slovak Republic <sup>25</sup> , Spain, Switzerland, Turkey
Utilities (incl. electricity, water and water treatment)	Brazil, Chile, Egypt, Estonia, Finland, Greece, Hungary, Ireland, Israel, Korea, Lithuania, Slovak Republic, Spain, Switzerland (sub), Turkey, United States
Transportation (incl. ports, piloting, air traffic)	Brazil, Chile, Denmark, Egypt, Estonia, Finland, Germany, Greece, Ireland, Italy, Korea, Poland, Russia, Slovak Republic, Spain, Switzerland, Turkey, United States
Energy (incl. Oil, Gas, Coal, Nuclear)	Austria, Brazil, Chile, Denmark, Egypt, Estonia, Finland, Greece, Hungary, Korea, Lithuania, Slovak Republic, Spain, Turkey, United Kingdom, United States
Banking and Finance	Brazil, Chile, Egypt, Finland, Germany, Korea, Switzerland (+ sub), Turkey, United Kingdom, Russia, United States
Real Estate/Housing	Australia, Denmark, Finland, Korea, Spain, Turkey, United States
Postal Services	Austria, Brazil, Chile, Denmark, Estonia, Finland, Germany, Israel, Italy, New Zealand, Poland, Russia, Slovak Republic, Spain, Switzerland, Turkey, United Kingdom, United States
Sanitation (incl. waste, garbage)	Brazil, Chile, Finland, Spain, Turkey, United States
Media/Broadcasting	Chile, Denmark, Finland, Ireland, Poland, Slovak Republic, Spain, Turkey, United Kingdom, United States
Health	Chile, Brazil, Estonia, Finland, Russia, Sweden, Switzerland, Turkey, United States
Agriculture and Forestry	Chile, Estonia, Finland, Poland, Slovak Republic, Spain, Turkey
Other (incl. Meteorology, Education, Mining, Lottery, R&D)	Chile, Denmark, Estonia, Finland, Korea, Switzerland, Turkey, United States

### 2.3. Application to traditional SOEs and other public bodies

The majority of questionnaire responses indicate that national legislation, regulation and other guidance apply to the commercial activities of traditional SOEs and other “public bodies” (however defined). However, in some cases the application of such rules does not go beyond “traditional” SOEs (Egypt). Conversely, EU rules apply to traditional SOEs; other public bodies; private companies entrusted with public service obligations (i.e. services of general economic interest); and, companies benefiting from special and exclusive rights as applicable in all EU Member States.

There is a grey area between what actually constitutes a government business/undertaking and whether aspects or elements of competitive neutrality expressed in national legislation, regulations and guidance apply beyond “traditional” SOEs.<sup>26</sup> A number of countries define the scope for application as follows:

- In EU (including EEA) member States, EU competition rules apply to all “undertakings” which refers to any entity engaged in an economic activity, irrespective of its legal form and the way in which it is financed. Jurisprudence indicates that its application also extends to bodies (public or private) which have special or exclusive rights.
- In Australia, the national competitive neutrality framework applies to all “significant” government businesses, but only to the extent that benefits of the arrangements outweigh the costs. A number of thresholds apply: the activity must be considered to conduct “business” and the business must be determined to be “significant” (Box 2.2).

- In **Chile**, public sector undertakings are only allowed if authorized by law and if they fall under the same legal provisions as the private sector. The Chilean government response is limited to entities traditionally referred to as SOEs, however where public entities beyond SOEs operate on a commercial basis they are subject to operate in accordance with relevant laws ensuring aspects or elements of competitive neutrality (e.g. competition laws).
- In **Denmark** and **Sweden**,<sup>27</sup> neutrality provisions of the competition act apply to all “commercial” activity (any form of economic activity taking place in a market for product and services).
- In **Egypt**, applicable laws pertain only to corporatized SOEs with a number of such entities entirely exempt from the scope of applicable laws (e.g. public agencies, state departments’ public companies, and public holding companies).
- In **Estonia**,<sup>28</sup> **Finland**,<sup>29</sup> **Greece**,<sup>30</sup> **Hungary**, **Iceland**,<sup>31</sup> **Korea**,<sup>32</sup> **Spain** and **Turkey**, competition laws apply equally to private and state-owned “undertakings.”
- In **Mexico**, the economic competitiveness law is directed to all “economic agents”, in any form of participation in economic activity.
- In **Israel**, competition law applies to legal entities.<sup>33</sup>
- In **Poland**, the Combating Unfair Competition Act covers all entrepreneurs, regardless of ownership. This includes natural persons, legal persons and organizational units without legal personality, which by conducting (even only incidental) commercial or professional activity take part in a business.
- In **Russia**, antimonopoly laws apply to legal entities acting on the market place, irrespective of ownership; it also applies to the activities of authorities implementing state functions.
- In **Slovenia**, the Transparency law applies to all “public undertakings” where authorities exercise directly or indirectly dominant influence by virtue of their ownership, financial participation or rules which govern it. Threshold applies to activities with turnover above certain levels.
- In **Switzerland**, the Cartels Act also applies to non-incorporated government activities which compete with private businesses.<sup>34</sup>

Other countries report that aspects or elements of competitive neutrality apply to the commercial activities of public bodies, including non-incorporated government activities, but do not provide further details as to how such application is determined in practice (Austria,<sup>35</sup> Czech Republic, Ireland,<sup>36</sup> Italy, Japan, New Zealand, Slovak Republic, Turkey and United Kingdom).

As pointed out, in a number of cases, responses indicate that aspects or elements of competitive neutrality policies do not apply beyond “traditional SOEs”.

### **Box 2.2. Application of competitive neutrality framework to government business activity in Australia**

#### ***Is the entity conducting a business?***

Activities are classified as a business for the purposes of CN if they meet the following criteria:

1. There must be charging for goods or services (not necessarily to the final consumer);
2. There must be an actual or potential competitor (either in the private or public sector); and
3. Managers of the activity have a degree of independence in relation to the production or supply of the good or service and the price at which it is provided.

#### ***Is the business significant?***

If it is determined that the entity is conducting a business, the business must be significant for CN to apply. The following business activities are considered significant for the purposes of CN:

- All government business enterprises (GBEs) and their subsidiaries: All GBEs are either companies or authorities which have been prescribed by Ministerial decision to be GBEs. They are the most commercialised group of legally separate organisations within the Commonwealth sector and can operate in markets which are open to competition.
- All Commonwealth Companies: Commonwealth Companies are statutory corporations, established in legislation as bodies corporate. They are governed both by their separate enabling legislation and by the *Commonwealth Authorities and Companies Act 1997 (CAC Act)*, which imposes reporting and auditing requirements on directors of these entities.
- All Business Units: Business units are established through administrative arrangements where an identifiable part of an agency or Department has a primary objective of trading goods and services in the market, for the purpose of earning a commercial return. Business units' management and accounting structures are separate from other parts of the overall organisation. Baseline costing for activities undertaken for market testing purposes.
- Baseline costing for activities undertaken for market testing purposes.
- Public sector bids over A\$10 million.
- Business activities not in these categories that are undertaken within (non-GBE) Prescribed Agencies or Departments with a commercial turnover of at least A\$10 million per annum.

(There are slightly different threshold questions at the sub-national level to determine whether CN arrangements should apply to a particular business activity.)

Source: Questionnaire response.

## **2.4. Oversight, investigation and enforcement of competitive neutrality**

Generally, government authorities responsible for the oversight, investment and enforcement of aspects or elements of competitive neutrality (as described above) correspond to the types of laws which apply and are in force. For the vast majority of countries, competition laws are the main legal frameworks that apply to aspects or elements of competitive neutrality; as such the corresponding institutions responsible for oversight, investigation and enforcement have generally been reported to be competition authorities. Other institutions which intervene in various aspects of oversight, investigation and/or enforcement can be characterised as follows:

- specific competitive neutrality complaints office (Australia);
- finance or Treasury ministries, budget oversight departments or agencies (Australia, Estonia, Germany, Korea, Slovak Republic, Slovenia);
- economic ministries (Denmark, Slovenia, Spain);
- sectoral regulatory authorities (Estonia, Iceland, Ireland, Israel, Mexico, Slovak Republic, United Kingdom);
- public procurement agencies (Austria, Slovak Republic);
- state auditors (Austria);
- parliament/Congress/sub-national legislatures (Chile, United States);
- local governments and consumer organisations (Poland); and,
- public prosecution and/or Courts (Chile, Denmark, Egypt, Finland,<sup>37</sup> Ireland).

Competition authorities and courts are generally responsible for intervening in cases of non-compliance in the majority of reporting countries. The types of remedies that are employed are often those that fall within the scope for intervention of competition authorities and those prescribed by national competition laws. Cited examples include financial penalties, sanctions, a combination of structural or behaviour remedies, or criminal liability in the most extreme of cases.

The scope for national competition law to address competitive neutrality challenges may be in some cases more limited than what policy makers would wish. Where this is the case, a number of different types of measures are employed by reporting countries in order to remedy non-neutrality.<sup>38</sup> These remedies include:

- In **EU (including EEA) member States**, it is the primary competence of the EU Commission to enforce EU rules on competitive neutrality. The EU Commission is under a legal obligation to act upon any complaint for non-respect of EU Rules on State Aid. If State Aid is deemed incompatible with the internal market, it will not be authorised, and if unlawfully granted, the EU Commission requires recovery.
- In **Australia**, any complaints concerning the advantages and disadvantages associated with ownership are made to a competitive neutrality complaints office; the remedy can be in the form of neutrality adjustments (by the responsible Ministers for a government business) or by other recommended courses of action (as overseen by the Treasury).
- In **Finland**, competition authorities have sought to promote competitive neutrality through awareness raising and advocacy; this method has worked in the past to remedy and prevent non-compliance.<sup>39</sup>
- In **Ireland**, sectoral commissions may take behavioural measures to cease or prevent contravention (e.g. holders of energy license or authorisations may be requested to construct or reconstruct a generating station); or impose a fine for non-compliance offences.

### Box 2.3. Remedying non-compliance in Spain

Beyond competition authorities the Ministry of Economy and Finance is entrusted to apply a number of neutrality adjustments in cases of non-compliance. It may exercise the below functions in order to enforce competitive neutrality:

- To determine the additional cost involved in the obligations and responsibilities associated to the public services that such entities are required to undertake.
- To estimate the extra cost of debt, bank guarantees, and safeguards, associated with being a public undertaking, as well as the impact of applying a specific regulatory framework to them.
- To estimate the income that the Treasury Department should receive as compensation for the capital invested in the public undertaking, as well as the corresponding dividends, taking into account the added financial responsibilities for ensuring public services, and the advantages that such undertakings enjoyed in terms of access to finance and of the regulatory framework applicable to them.

The Competition Authority is informed by the Ministry prior to the exercise of these functions.

Source: Questionnaire response.

- In **Russia**, administrative and regulatory barriers are being reformed with the aims of remedying any advantages associated with the special status of state and municipal institutions operating on a commercial basis.
- In **Spain**, the Ministry of Economy and Finance is entrusted to apply a number of neutrality adjustments in cases of non compliance (Box 2.3).

## Notes

1. There is also policy guidance at the sub-national level which conforms to the inter-governmental Competition Principles Agreement (1995).
2. Also referred to as the Public Entity Management Act (2007).
3. Across the document, national features of individual EU (including EEA) member States are described separately from the discussion of competitive neutrality provisions in the EU itself. However, given the specific features of the EU legal system, many national provisions originate from those of the EU. All EU Member States are subject to certain EU rules (e.g. EU rules on State Aid) and that for those aspects which are not regulated by the EU, there can be variations (e.g. on the implementation of EU Directives). The EU Commission is entrusted with the task of monitoring Member States compliance with the EU rules.
4. Treaty on the Functioning of the EU, Art.345, 101-102, 106-108; and secondary legislation: Transparency Directive and other State aid legislation in particular concerning Services of General Economic Interest.
5. Commonwealth Competitive Neutrality Policy Statement.
6. Royal Decree 1373/2009.

7. Commonwealth Competitive Neutrality Guidelines for Managers (1996-97) and revised update (2004).
8. [http://www.oft.gov.uk/shared\\_of/economic\\_research/oft1242.pdf](http://www.oft.gov.uk/shared_of/economic_research/oft1242.pdf)
9. <http://www.bis.gov.uk/files/file46965.pdf>
10. Guidance for companies prevented from competing in foreign markets because of discriminatory public procurement practices; Act on Public Procurement
11. Law on reduction of administrative barriers and improvement of accessibility of public and municipal services.
12. Office of Fair Trading working papers (e.g. *Competition in mixed markets: ensuring competitive neutrality* (2010), [http://www.oft.gov.uk/shared\\_of/economic\\_research/oft1242.pdf](http://www.oft.gov.uk/shared_of/economic_research/oft1242.pdf)) and the Julius Review (2008) (<http://www.bis.gov.uk/files/file46965.pdf>).
13. Restrictive Trade Practices Law.
14. Commerce Act.
15. State Companies' Law, Corporate Governance Code for SOEs.
16. State Assets Act, Government of the Republic Act.
17. Local Government Act, State Enterprises' Act.
18. Stock Corporations Act, Corporate Law.
19. Final Report by Review Group on State Assets and Liabilities.
20. Law on the Organisation and Functioning of the Central Administration of the State; Public Administrations' Wealth Act.
21. Transparency of Financial Relations and Maintenance of Separate Accounts for Different Activities Act.
22. Public Administrations' Wealth Act.
23. Financial Budget Act.
24. This table does not intent to provide an exhaustive list of regulated markets where SOEs or other public bodies may compete with the private sector. It intends to demonstrate some of the likely sectors concerned by competitive neutrality.
25. The company is not controlled by state but it is entrusted with public service obligations.
26. In Germany, public bodies beyond traditional SOEs do not perform commercial activities in competitive markets, thus do not fall within the scope of such laws. It is not clear whether applicable neutrality rules would apply if there were any unincorporated activities.
27. Regardless of its legal status or the way in which it is financed. Exceptions are provided where such activities are conducted in the public interest and which are compatible with law. The Swedish Competition Act was reformed in 2010 to provide further clarifications as to the scope of the Act, notably including provision clarifying that it is further applicable to state, county councils and municipalities engaging in offering goods or services; and companies controlled by the state, county councils and

municipalities. It should be noted that the definition excludes activities/conduct when the public entity in question engages in purchasing activities.

28. The provisions contained in the Competition Act and numerous sector regulations define “undertaking” to include SOEs and other public bodies participating in the goods market. The provisions also extend to persons who perform functions in public law and to the state and local governments if they participate in the goods market.
29. Finland is moving towards full incorporation of state-owned business activities; as such it has reformed its rules on State Enterprises and is moving towards an amendment of the Local Government Act (applicable to the national and sub-national level, respectively) which defines the roles of local authorities.
30. In practice, there is doubt as to under what circumstances government activities are acting as “undertaking” and therefore subject to competition law.
31. The competition act in Iceland also extends to undertakings operating under special or exclusive rights, with some exceptions as determined by special laws which may provide derogations for some public entities from such laws.
32. Unless the company’s conduct is considered justifiable under other laws.
33. The scope of this law extends to bodies which may perform public services in monopoly or restricted competition. In some types of cases (e.g. merger transactions) public bodies may be exempt from such rules as they apply to defined legal entities.
34. The answers provided apply to the federal level.
35. In Austria public procurement rules apply to public bodies and public entities are subject to audit from Austrian Court Auditors.
36. The issue has arisen in sectors such as household waste collection, leisure facilities and childcare. The competition authority has received complaints.
37. Enforcement of competitive neutrality in Finland is ensured by the FCA, which investigates such matters by its own initiative following a request by the contracting parties or following a complaint by a disturbed party. The court of application is the special Market Court whose decisions may be applied to the Supreme Court of Administration.
38. Respondents note that most CN problems are related to provisions of competition law that apply to the abuse of domination position. However, the threshold for finding a dominant position may not be exceeded. If this threshold is not exceeded, the competition authorities have no power to intervene, and thus remedy non-compliance.
39. Other roles for the competition authorities in remedying non-compliance are currently being considered by a draft parliamentary bill proposing an amendment of the Local Government Act.



## MAIN INDIVIDUAL ELEMENTS IN OBTAINING COMPETITIVE NEUTRALITY

### 3.1. Operational form of government business

In this section, broad comparisons have been drawn from the questionnaire results but should be interpreted “with a grain of salt.” Readers should bear in mind that different legal traditions and variations in the way respondents classify SOEs/public bodies make for a very diverse sample. Furthermore, the extent to which legal form determines the degree of corporatisation differs markedly from country, to jurisdiction, and company; hence, it should not be automatically assumed that incorporation also implies full corporatisation along the lines suggested in the *SOE Guidelines*. Lastly, respondents were not asked to provide detailed information on the size and composition of their SOE sectors;<sup>1</sup> therefore the comparisons drawn below are only intended to provide a rough picture of the types of public entities performing commercial activities which may be concerned by competitive neutrality; the results may also indicate where “grey” areas potentially exist. Finally, there is no indication of which organisational forms are most prominent in each national context.

#### *Overview of findings*

The reform trend among surveyed countries suggests that most countries have taken steps towards streamlining the operational form of government business activities, towards a more complete corporatisation of SOEs and other commercial entities. Despite this trend, a plethora of organisational forms exist among the surveyed countries which can roughly be grouped into three categories: (i) incorporated SOEs; (ii) unincorporated public bodies; and (iii) other forms of public institutions engaged in commercial activities.

In category (i) all countries report companies that are established according to special law; public law; company law; and sometimes combinations of the three. Roughly one-fifth of the respondents mention publicly owned enterprises at the sub-national level of government that may have a different corporate form from those owned by the central level of government.

In category (ii) over half of the reporting countries have such entities engaged in commercial activities. The majority of cases relate to government departments or independent agencies. The range of goods and services is very diverse and dependent largely on the national context. They range from local municipal services to energy and forest services. Conversely, a few responses state that, according to law in the respondent countries, commercial activities can *only* be carried out by incorporated public entities.

Category (iii) consists of other forms of public institutions which may be engaged in commercial activities. These include: include registered co-operatives, business associations, state budget funds, and foundations.

A trend among responding countries is to structurally separate commercial from non-commercial components of SOEs. The degree to which countries implement structural separation varies depending

on the company in question, the sector in which it operates and a number of public interest considerations that are determined by the government. The main reasons cited as rationales for non-separation are: infeasibility (e.g. intertwined production processes or dependence on the same physical or human capital); maintenance of public service obligations; and efficiency grounds (e.g. economies of scale reaped from joint provision of commercial and non-commercial activities). Other factors mentioned by some include risk, cultural factors, public pressures, a lack of adequate regulation, a need to maintain operational control.

Country practices concerning periodic review of government stake and commercial objectives of its business activities differ greatly. Almost two-thirds of the responding countries say that they conduct some form of regular or period reviews, although the processes are different for each country and type of business activity (e.g. commercial versus mainly operating in the public interest); the type of reporting also depends on who is responsible for its oversight and/or budget allocation. The majority of remaining countries conduct such reviews on a *vis-à-vis* basis. The only countries which do not report such review practices are Denmark and Italy.

### ***Organisational forms of publicly-owned corporate entities***

Public bodies operating on a commercial basis exist in a number of organisational forms depending on the national context; the main forms of incorporation for public companies are those established according to company law, special law or public law (Table 3.1):

- **Nearly all countries** which responded to the questionnaire have incorporated some of their SOEs according to company law (either as limited liability or joint stock companies).
- **Nearly all countries** have established statutory corporations through the enactment of special laws. Depending on the national context, these laws may apply for categories of SOEs or for specific SOEs. **Italy** is the notable exception.
- Most have established some categories of SOEs according to public law (Austria, Chile, Denmark, Japan, Mexico and Spain).
- Different corporate forms also exist at the sub-national level (Australia, Finland,<sup>2</sup> Mexico, New Zealand, Switzerland and United States).
- In a number of jurisdictions, commercial activities are reportedly *only* carried out by corporatised public entities according to the relevant law (including relevant State Enterprises' laws if applicable) (Czech Republic,<sup>3</sup> Germany, Hungary,<sup>4</sup> Iceland, Ireland,<sup>5</sup> Italy, New Zealand, Slovak Republic, Slovenia).

**Table 3.1. Organisational forms of publicly-owned corporate entities**

	Special Law		Public Law	Company Law		Not incorporated	Other	Different Sub-national	Comments**
	For categories of SOEs	For specific SOEs		Ltd Liability	Joint-stock				
	(1)		(2)	(3)		(4)	(5)	(6)	
Australia*	X	X		X	X	X		Y	(1): Categories: CAC Act entities classified statutory entity under 1999 Public Service Act; Specific: Act of Parliament, or CAC Act entity under own establishing legislation (3): CAC Act-Companies (4): Departments of state or statutory agencies, national Institutions
Austria*		X	X	X	X				(2): Incorporated public law institute
Brazil					X			N	
Chile		X	X	X	X	X			(1): <i>empresas creadas por ley</i> (2): Some companies organised by already known legal structure but contain a different organisation (3): <i>sociedades anonimas</i> (4): National health supply agency (CENABAST)
Czech Republic	X	X		X	X				(1): "state enterprises" according to Act. No. 77/1997 (2): Company specific (3): According to commercial code
Denmark		X	X	X		X			(2): Closely related to limited company but organised differently, often due to large number of public servants
Egypt		X			X	X		N	(1): Statutory corporations are also joint stock companies (4): Specific authorities not subject to public agencies law
Estonia	X	X		X		X		N	(1): Public legal entities, government institutions (3): Forms: AS, SA and OU (4): State profit agency
Finland		X		X		X		Y/N	(1): State enterprises' Act, specific law for each enterprise (3): Companies Act (also applicable at sub-national level) (4): Municipal enterprises and municipal/state agencies (6): Municipal enterprises and Municipal agencies
Germany		X		X	X		X	N	(1): Public Institutions (1%) (3): The majority of SOEs are LLCs (64%), 5% stock companies, 1% limited company/partnerships (5): Registered Co-operatives (29%) (6): With reservations
Greece*		X		X	X				(1): Charter law for SOE
Hungary*	X	X		X	X		X	N	(1): Commercial or quasi-commercial entities, generally under corporate law; in other cases there is an <i>ius specialae</i> with special legal requirements (5): Non-profit limited liability companies ; or according to the Business Associations act
Iceland	X			X				N	(1): Statutory corporations, co-owned agencies and joint enterprises
Ireland		X		X				N	(1): Created under special act of parliament
Israel		X		X					(1): Generally do not operated on a commercial basis with the exception of a few
Italy					X			N	
Japan*		X	X		X				Public corporation and quasi non-governmental organisations
Korea	X						X		(1): Public corporations.

	Special Law		Public Law	Company Law		Not incorporated	Other	Different Sub-national	Comments**
	For categories of SOEs	For specific SOEs		Ltd Liability	Joint-stock				
	(1)	(2)		(3)	(4)		(5)	(6)	
									**Comments are numbered as they correspond to the relevant column and organisational form cited to the left
									(5): Quasi-governmental institutions and other public institutions.
Mexico*	X	X	X	X	X			Y	(4): Trust funds, credit societies, insurance enterprises (6): Decentralised public organisations
New Zealand*	X	X		X	X			Y	(1): Crown statutory entities, limited liability companies, Crown Research Institutions; public finance act schedule four organisation (6): Local Authority Trading Enterprises (LLC aka Council Controlled Trading Organisations)
Poland					X	X			(3): Rare category for SOE (4): Special law can create special entities (e.g. state forests)
Russia		X			X	X	X		(1): State and municipal unitary enterprise (3): Public corporation (4): State and local government agencies (5): State budget fund,
Slovak Republic	X	X			X				(1): Enterprises established by specific Act on establishment of individual enterprise; state enterprises established by law on "state enterprise", budgetary or contributory agencies (national or sub-national)
Slovenia		X		X	X				(3): A special form of public enterprise according to the Law on Public Utilities
Spain	X		X	X	X	X	X		(1): Public trading entities provide goods and services of public interest subject to compensation. Governed by private law, except in their creation, their exercising of administrative powers, their statute and in respect of budgetary issues. (2): Public law entities. Governed by administrative law under Act 5/1996 (3): State corporations (4): Companies under law 30/2007 on public procurement
Sweden*	X		X	X	X	X			(1): Four statutory corporations organised as state bodies (3): All SOEs incorporated according to Company Law mainly as limited liability companies (4): Non-incorporated state agencies with commercial activities.
Switzerland		X		X	X	X		Y	(1): The Post, but to be transformed into joint stock company under company law. (4): Usually due to size, but there are exceptions (6): At the canton level and a number of municipalities
Turkey	X	X			X	X			(1): Categories: Some SOEs under law No. 233 on State Economic Enterprises and SOEs under privatisation portfolio, law 4046; Specific: Statutory corporations. (3): Some joint-stock SOEs under law 233
United Kingdom		X			X	X	X		(1): Statutory body (3): "Company Status" with full, majority or minority holding (5): Trading Fund, Non-departmental public body
United States		X						Y	(1): Federal government corporations (6): Municipal corporations, state chartered/owned corporations

\* Answers supplemented with data from: OECD (2005) Comparative Report on Corporate Governance of State-Owned Enterprises; and/or OECD (2011) Working Paper, The Size and Composition of the SOE Sector in OECD Countries.

### *Unincorporated public bodies operating in the commercial sphere*

Half of the countries which responded to the questionnaire indicate that in addition to the commercial activities of corporate entities, there are public bodies which operate in the commercial market as entirely unincorporated entities, usually through government departments or agencies. Other categories of public bodies performing commercial activities exist, but their forms vary considerably from country to country (Table 3.1). Details for each country, where reported,<sup>6</sup> are provided as follows:

- The **Australian** government engages in commercial activity through departments of state or departments of parliament, agencies, or national institutions. When they act in the marketplace, they act as the Commonwealth [with the exception of national institutions] and are conducted under the *Financial Management and Accountability Act 1997* (FMA Act)].
- In **Chile**, there are public entities at the state or municipal level offering services on a commercial basis (public hospitals and universities, medical centres, and national health supply agency).<sup>7</sup>
- In **Denmark** departments of general government may operate in the commercial market, under certain conditions; institutions must separate the production of goods or services from other tasks; prices must be set in a way which does not distort competition and in which costs are recovered; and commercial activity must be “natural offshoots” of the entity in question (e.g. Ministry of Foreign Affairs providing language classes for a fee).
- In **Egypt**, two government authorities operate on a commercial basis (e.g. Suez Canal Authority and Egyptian General Authority for Petroleum). Both conduct commercial and non-commercial activities which remain integrated.
- In **Estonia**, state institutions managed by the government (e.g. museums, theatres, educational establishments), state profit agencies (State Forest Management Centre), and public legal entities (e.g. libraries, foundations, and universities) may operate on a commercial basis in addition to “state” functions they provide.<sup>8</sup>
- In **Finland**, state agencies provide marketised services, but most of such types of activities have been transferred to state enterprises (e.g. in statistics, technical research and meteorological services). Municipal enterprises, established under the *Local Government Act* remain unincorporated, but nevertheless operate only on a commercial basis; these differ to some extent from municipal agencies which, only in some cases, operate on a commercial basis (providing welfare services primarily but also running energy power plants and harbours).<sup>9</sup>
- In **Mexico**, a number of finance and insurance commercial services are reportedly provided through non-incorporated credit societies and trust funds.
- In **Poland**, unincorporated state entities may perform commercial activities under special law (e.g. state forests entity supervised under Ministry of Environment).
- In **Russia**, public entities may only combine their public functions with economic activities if stipulated by law, presidential decrees, or government resolutions. A number of exceptions are listed, including those granted by the executive authority (e.g. Ministry of Internal Affairs’ police and other security functions).

- In **Spain**, a number of public entities provide goods and services on a commercial basis these may be attached to ministries and usually provide in-house services (e.g. export or foreign investment promotion, army housing, air traffic control) and in some cases external services in competition with the private sector (e.g. digital certification).
- In **Sweden**, a number of non-incorporated public entities operate on a commercial basis; in some cases through state agencies (e.g. in construction, consulting meteorological services, etc.) or in others through other public institutions (e.g. universities).
- In **Switzerland**, a limited set of public bodies provide commercial services (e.g. weather services or geo-information). At the municipal level, a number of commercial activities may also be operating through unincorporated entities (e.g. City of Zurich).

### Box 3.1. Case Study: Swiss Institute of Meteorology

The Swiss Institute of Meteorology (SIM, now called MeteoSwiss) is a non-incorporated business in the Federal Department of Home Affairs, which is obliged by the Act on Meteorology to execute certain sovereign tasks. The act leaves SIM the possibility to prepare meteorological data and exploit them; with prices set by ordinance and with some room for discounts. In 1996, the SIM entered into contract to supply weather data to the State-owned Swiss Broadcast Company (Schweizerische Rundfunk Gesellschaft, SRG). In July 1998, the SIM made an offer for similar services to Meteotest, a private weather forecasts enterprise, for a sum amounting to approximately twice the amount paid by SRG.

The Competition Authority prohibited the discrimination between trading partners as an abuse of a dominant position. The SIM lodged an appeal before the Swiss Supreme Court, arguing that the Swiss Cartels Act was not applying to the SIM in its quality of a state-owned enterprise, whose prices were set by ordinance. The Swiss Supreme Court upheld the appeal of the SIM and confirmed that the Act on Cartels did not apply to SIM.

As a consequence of this case, the Swiss Cartels Act was revised in 2004 in the following manner to ensure that the application of competition law is neutral to ownership and organisational form:

**Art. 2 para. 1bis ACart.** "(u)ndertakings are all consumers or suppliers of goods or services active in commerce regardless of their legal or organisational form". In brief:

*Source:* Questionnaire response.

- In **Turkey**, a number of units associated with line ministries operate on a commercial basis (e.g. food and agriculture, lottery administration, radio and television, housing development, etc.).
- In the **United Kingdom**, so-called non-departmental public bodies operate at arm's length from relevant government departments. In addition, a number of government departments directly offer products and services on a commercial basis (e.g. Trading Funds such as Ordnance Survey).
- In the **United States**, the federal government participates in regulated markets through federal agencies, departments or independent establishments (for example healthcare facilities, etc). Although these entities may compete with non-governmental facilities, they serve specific populations and are perceived more as complements rather than competitive substitutes.

Other categories of public bodies that engage in commercial activities include registered co-operatives (**Germany**), public institutions (**Germany**, **Spain**<sup>10</sup>), business associations (**Hungary**), state budget funds (**Russia**) and foundations (**Spain**).

### *Structural separation*

Structural separation implies the division of a formerly integrated entity into competitive and non-competitive parts. There are different degrees of separation ranging from accounting, functional or corporate separation, to ownership separation, club ownership and a separation of ownership from control. The type of separation may depend on the nature of the company and sector/industry. However, as mentioned earlier, dependent on technologies, capital equipment, human capital, etc. this is not always practically feasible, and sometimes where this is feasible it is not economically efficient. Country experiences with structural separation are different for these reasons, but some commonalities can be found as to reasons why structural separation may not be possible for certain government businesses (see Table 3.2).<sup>11</sup>

**Table 3.2. Structural separation**

Commonly cited reasons why structural separation has not been possible for certain government businesses	
Infeasible	Egypt, Korea, New Zealand, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States (9)
Maintain public service obligations	Estonia, Ireland, Italy, Mexico, Russia (5)
Efficiency grounds	Ireland, Italy, New Zealand, Switzerland (4)
Other	Australia, Egypt, Finland, Ireland, Russia, Slovak Republic, Switzerland, Turkey (9)
Industrial policy	Estonia, Russia (2)
Protect political or strategic interests	Estonia, Russia (2)
Costs outweigh benefits	Egypt, Sweden (2)

The country experiences with structural separation provided by respondents are described below:

- In **Australia**, most government entities operating in the market place are legally and financially separate from the Commonwealth, but remain part of the Australian government [e.g. entities established under the Commonwealth Authorities and Companies Act (CAC Act)]. Decisions around structural separation have typically been made having regard to the principles outlined in the Clause 4 of the Competition Principles Agreement 1995.<sup>12</sup>
- In **Denmark**, the production of goods and services offered on a commercial basis must be separated from other tasks where departments of governments are operating on a commercial basis. No further information is provided concerning other types of separation.
- In **Egypt**, state-owned companies and authorities do not structural separate commercial from non-commercial activities of SOEs. This is due to the fact that such separation is infeasible; costs outweigh the benefits; and cultural factors. As reported, the latter is due to a lack of awareness of the economic and consumer welfare benefits competitive neutrality may have.
- In **Estonia**, structural separation has been the case or is currently under way in a number of sectors (e.g. energy, gas, and rail) with separation of infrastructure from services in order to ensure competition in the service market. In other cases, the government has decided not to structurally separate in order to maintain public services, to pursue industrial policy objectives, and to protect strategic and political interests.

- In **Finland**, most public service activities have been separated from commercial activities. Where such activities remain integrated this to ensure practical effectiveness and functionality. Furthermore, in some cases such services are considered “public” in nature, in which cases it may not serve a “particular purpose of strictly separating” such activities from the organisation of an entity.
- In **Ireland**, some sectors have been structurally separated more than others. For example, in the energy sector four components of the sector remain state-owned as natural monopolies; however they are subject to economic regulation to ensure fair access and competition. Irish authorities have chosen not to structurally separate components in the electricity sector due to risk associated with privatisation (assuming adequate prices, ensuring adequate regulatory structures). Whereas in the bus transport sector, public service obligations have been the main rationale in maintaining commercial and non-commercial services integrated.
- In **Iceland**, structural separation is mandatory in all instances where there is a risk that there could be potential competition distortions. Functional and corporate separation may be used as alternatives when necessary or more appropriate.
- In **Mexico**, generally public entities providing commercial and non-commercial services remain structurally integrated. This is to maintain public service obligations and to ensure public interest objectives.
- In **New Zealand**, most publicly-owned corporate entities have been structurally separated. In cases where non-commercial activities remain integrated (e.g. Public Trust, a provider of wills and estate administration services), this is justified on efficiency grounds (economies of scale reaped from existing personnel, networks and service capacities) and infeasibility (undesirable to separate interconnected services).
- In **Poland**, government entities which are under the purview of the State Treasury are generally not structurally separated. One exception is the Department of Research and Development which is funded entirely through public funds, and is structurally separated from the Ship Design and Research Centre (an SOE).
- In the **Slovak Republic**, structural (functional) separation was realised in several sectors such as electricity, gas, railways, accounting separation in postal services, telecom and broadcasting. In some cases the government has decided not to structurally separate due to infeasibility (e.g. News agency).
- In **Slovenia**, publicly-owned corporate entities are required to separate their accounting for public service and commercial activities.
- In **Spain**, structural separation depends on the legal status of the public undertaking to which public services have been entrusted. Some entities have not been separated due to infeasibility.
- In **Sweden**, over the last five years several commercial units operating from within general government have been structurally separated into incorporated entities. Where commercial activities remain structurally integrated, accounting and sometimes functional separation is ensured.



- In **Switzerland**, public bodies which carry out commercial activities do so under special legal entitlement. It is reported that commercial activities of such bodies remain minor; as such bodies have remained structurally integrated for feasibility considerations and on efficiency grounds. In some cases, integration is favoured in order to maintain direct control of the activities in question.
- In **Turkey**, the energy sector has been unbundled into a number of different components; however public service and commercial activities remain integrated. In cases where structural separation has not occurred, this is due to the fact that there is no clear separation (accounting separation) between commercial from non commercial activities, infeasibility and insufficient resources.
- In the **United Kingdom**, the government's aim is to maintain a clear separation between commercial and non-commercial public services. However, there are exceptions where separation would otherwise not be infeasible (due to the complexities of the organisation and the synergies that exist when remaining integrated).

### *Periodic review of government stake and commercial objectives*

Country practices concerning periodic review of government ownership and of the commercial objectives of its portfolio companies/entities can be categorised according to three groups: countries which conduct periodic/regular reviews; countries that conduct such reviews on an *ad hoc* basis; and countries which do not conduct such reviews (Table 3.3):<sup>13</sup>

- In the majority of countries periodic review of government stake in SOEs is conducted through annual reporting which also takes into consideration the relevance of the entity's commercial objectives. The frequency of such reviews depends on country practices, but generally governments report that for incorporated SOEs such reporting occurs on an annual, biannual, biennial or on a five-year basis. For SOEs which depend on public budgets, review of continued government stake and objectives are usually considered by government budget processes and/or the oversight bodies/sectoral ministries to which they are attached. Whereas other incorporated SOEs provide such reports to their ownership entities, boards and shareholders, and in some cases to parliament. (Australia, Czech Republic,<sup>14</sup> Estonia,<sup>15</sup> Finland, Germany,<sup>16</sup> Israel, Korea, Russia, Slovak Republic, Slovenia, Sweden, Switzerland,<sup>17</sup> Turkey, United States)
- In the second set of countries, there are reportedly no such review processes, however the government engages in *vis-à-vis* or periodic reviews where necessary (Egypt,<sup>18</sup> Chile,<sup>19</sup> Ireland,<sup>20</sup> Mexico,<sup>21</sup> New Zealand,<sup>22</sup> Spain, United Kingdom).
- Finally, the third set of countries report no known periodic review mechanisms that seek to review government stake or the commercial objectives of public commercial bodies (Denmark,<sup>23</sup> Italy).

**Table 3.3. Review of government stake and relevance of commercial objectives**

Periodic review of government stake/Review of relevance of commercial objectives	
Periodic Review (e.g. through annual reports, budget and planning processes)	Australia, Czech Republic, Estonia, Finland, Germany, Iceland, Israel, Korea, Russia, Slovak Republic, Slovenia, Sweden, Switzerland, Turkey, United States
<i>Ad hoc</i>	Egypt, Chile, Ireland, Hungary Mexico, New Zealand, Spain, Switzerland, United Kingdom
No such reviews	Denmark, Italy

Where specific details are provided on country practices they are highlighted below:

- In **Australia** there are both regular and periodic reviews of governance arrangements in commercial activities. Australian government businesses enterprises' (under the CAC Act) objectives, articulated in Statements of Corporate Intent, are considered on an annual basis by government ownership entities and Parliament. There are also periodic reviews evaluating government ownership in government businesses which evaluate the reasons for retaining government ownership and take into consideration each business' circumstances along with national priorities.
- Government bodies which are responsible for ownership steering in **Finland**, monitor the performance of SOEs, including the necessity for continued government stake. These assessments are also presented to the Ministerial Economic Council twice a year. At the municipal level review mechanisms may vary.
- In **Iceland**, it is the role of the Competition Authority to observe whether public entities do not restrict competition and to indicate where entry of new competitors to the market could be facilitated.
- In **Israel**, the Government Companies Authority periodically reviews the continued need for government stake in government companies; such reviews consider privatisation as an option. In 2011, the government began formulating an overall ownership policy that examines, *inter alia*, the public interest objectives in the State's retaining its holdings in existing government companies.
- In **Korea**, the Ministry of Strategy and Finance reviews plans for public institutions' functions every five years. The most review resulted in the Public Institutions Reform Plan which set objectives for privatisation and state divestiture of government assets.
- In **Russia**, the period review of the need to maintain government stake is conducted according to federal law on "Privatisation of the State and Municipal Property" which aims to privatise companies in which the state holds a stake with an overall goal of reducing the role of the public sector in the economy.
- In **Turkey**, performing regular reviews of continued government stake in public enterprises is, by law, one of the duties of the Privatisation Administration.
- In the **United Kingdom**, the government has conducted reviews to assess whether continued government support or oversight is necessary. In 2009, a specific review was carried out to this effect.<sup>24</sup> A Cabinet sub-Committee meets regularly to examine the government's involvement with each SOE with financial or political significance. The Shareholder

Executive also monitors the progress of each SOE through annual Investment Reviews to ensure that each business is fulfilling its stated objectives.

### **3.2. Identifying costs**

#### ***Overview of findings***

Transparency and disclosure practices concerning incorporated SOEs are fairly similar across the reporting countries. In most cases, SOEs are subject to similar annual/quarterly reporting requirements as private sector businesses, according to internationally/nationally accepted reporting standards; often accounts are subject to both internal and external auditing; and information on SOE performance is publicly disclosed. Where specific reporting requirements are set out for public sector businesses, these are often more stringent, especially where public funds are concerned. A number of public institutions may be involved in the oversight and monitoring of performance of SOEs, apart from regulatory bodies these include parliaments, supreme accounting institutions, line ministries and executive powers.

For what concerns identifying costs of public service obligations, a little over one-third of all countries covered by the survey respond that their government businesses separate commercial from non-commercial accounts for the purpose of identifying costs. Another third of the countries report that such practices are carried out on a case-by-case basis, for example in sectors where specific reporting requirements may exist (e.g. utilities and energy sectors). In a few countries no such accounting separation practices exist. Notable are practices in the EU (where accounting separation applies to all undertakings (public or private) receiving public funds or benefiting from special or exclusive rights;<sup>25</sup> methods used to calculate costs are subject to specific requirements.

The attribution of liabilities (including contingent and pension liabilities) differs from country to country, and to a certain extent, depends on the legal form of the government business. Most incorporated SOEs are subject to the same or similar reporting requirements as private companies, according to nationally/internationally recognised reporting standards. For what concerns pension liabilities specifically, most countries report that employees of state enterprises remain in the State public pension system and are therefore not reported separately. In these cases, pension liabilities are usually reflected in the general government's balance sheets. In other cases, pension liabilities may be reported separately, notable is the case of Ireland. A minority of respondents report of no known country practices in the reporting of liabilities.

#### ***Transparency and disclosure***

High standards of transparency and disclosure must be maintained among incorporated SOEs and unincorporated public business activities. Among other things, this is necessary to ensure that public service obligations (and often related subsidies) do not provide a conduit for cross-subsidising these businesses' competitive activities. In addition, the need for transparency around the operators' cost structure is further accentuated where compensation is provided through the public purse or where costs are shared with non-commercial activities of general government. Disclosure ensures that government businesses can be held accountable to their shareholders/oversight bodies/general public and to monitor their performance in meeting stated objectives.

Among surveyed countries, a majority report that transparency and disclosure of financial accounts is a legal requirement for SOEs.<sup>26</sup> Among this majority, financial and non-financial reporting takes place on an annual, bi-annual and/or quarterly basis. Roughly half of countries report that their SOEs are subject to transparency and disclosure reporting requirements above and beyond what is

requested of similar private sector businesses (as determined according to statutory laws or general government standards/guidelines). All EU Member States (and Iceland) are to comply with the Transparency Directive which sets out stringent transparency and disclosure obligations required for all undertaking (public or private, incorporated or unincorporated) benefiting from public funds or from special or exclusive rights.

In some countries, SOEs are subject to same reporting requirements as private companies; this usually depends on the legal form of the company (i.e. if it is subject to company law). In almost all jurisdictions, public undertakings are subject to financial reporting according to internationally/nationally recognised standards (e.g. IFRS or IPSAS), and most are subject to internal and external (independent) audit; and often such reporting is available to the public. For many SOEs, the government also plays an important oversight and monitoring role beyond the day-to-day corporate governance structures of the SOE in question (Table 3.4). Beyond competition authorities and regulators, relevant institutions which intervene in SOE oversight depend on the national context, these include:

- Line/sectoral ministries/council of ministers (Australia, Denmark, Egypt,<sup>27</sup> Finland, Israel, Turkey).
- Parliament/Congress/supreme audit institutions (Australia, Egypt, Israel, New Zealand, Sweden, Turkey, United Kingdom, United States).

**Table 3.4. Transparency and disclosure requirements**

Transparency and disclosure requirements	
Reporting according to internationally/nationally recognised accounting standards (Annual, bi-annual and/or quarterly reports)	All reporting countries
Reporting requirements for SOEs above and beyond similar private sector companies	Australia, Denmark, Estonia, Finland, Iceland, Israel, Korea, New Zealand, Slovak Republic, Spain, Switzerland, Turkey, United Kingdom, United States
SOE Reporting requirements similar to private sector (depending on legal form)	Austria, Chile, Finland (for limited companies), Germany, Israel (for some companies), Italy, Lithuania, New Zealand, Slovak Republic, Slovenia, Sweden

Country-specific transparency and disclosure practices include:

- In **EU (including EEA) member States**, the *EU Transparency Directive* provides for specific transparency requirements concerning the financial relations between public authorities and public undertakings (this directive also applies to the activities of companies carrying out services of general economic interest and companies benefiting from special or exclusive rights).. The Directive also requires undertakings which enjoy exclusive or special rights, as well as undertaking which receive public service compensation for the provision of a service of general economic interest while having activities outside the service of general economic interest, to maintain separate accounts between their different activities. The objective is to prevent those undertakings from cross-subsidising other activities with funds raised through activities reserved for them or from compensation to provide public service obligations. Notably, the Directive does not apply to public undertakings supplying services not liable to affect trade between EU Member States to an appreciable extent and to those whose turnover does not exceed a specific threshold (Box 3.3).

- In **Australia**, incorporated government bodies are expected to provide yearly financial reports (by law). Government businesses are subject to report and disclose their obligations according to the stipulations of the law with which they were established, and according to government guidelines *Governance Arrangements for Commonwealth Government Business Enterprises*. Government businesses' financial statements must be externally audited and are made available to the public and parliament. Government businesses also produce Corporate Plans on an annual basis; this confidential document prepared for the government, outlines the 3-5 year strategic financial and non-financial objectives for of the company.
- In **Denmark**, incorporated SOEs (public limited companies) are subject to special transparency and disclosure requirements which go above and beyond reporting requirements of private companies; such reporting is also made available to the general public. Although SOEs are not required to report according to IFRS standards on an annual basis, most SOEs adopt these standards according to statute or special laws (all listed companies are required to according to EU legislation).
- In **Egypt**, there are different accounting practices for incorporated versus unincorporated public businesses. For incorporated businesses, the Egyptian *Corporate Governance Code for SOEs* are the main guidelines followed by SOEs; these guidelines outline requirements of SOEs to report on their commercial objectives, any financial assistance received from the state, and financial reporting (on a quarterly basis and according to internationally recognised accounting practices) and internal and external audit requirements. Unincorporated businesses are subject to the parliamentary auditing office to ensure that any financial assistance received from the state is spent according to stated objectives.
- In **Estonia**, all SOEs final annual reports are sent to the commercial register (all are made available to the public) and reported according to international standards.<sup>28</sup> Companies held by the state (where the state has voting power) must provide an additional "good (or bad) business practices" activities report as part of the government's transparency requirements.
- In **Finland**, listed SOEs and larger SOEs (willing to maintain the standards of listed companies) follow the same financial reporting as private companies (annual reports following IFRS standards, external and internal audit). Small companies follow Finnish accounting standards (FAS). Notably, SOEs must report any state guarantees or financial assistance received under the same conditions as the private sector (all financial assistance must be approved by Parliament). At the municipal level, practices vary, although municipal enterprises' financial statements are required to give "a fair and true view" of their accounts.
- In **Hungary**, a variety of special laws regulate the transparency and disclosure practices of SOEs and municipally-owned companies. Notably, the *Accounting Act*, requires annual reports of undertakings, compulsory external audit of company books (internal audit is not mandated). These reports are made available to the public.
- In **Iceland**, annual accounts of SOEs (accompanied by reports from auditors and examiners) are to be submitted to the Register of Annual Accounts.
- In **Israel**, the Government Companies' Authority has issued specific transparency and disclosure directives for government-owned companies. Companies, depending on their legal form, report according to different accounting standards. Almost all companies are subject to the same transparency and disclosure practices private sector companies (annual financial

reports based on national/internationally recognised standards, subject to internal and external audit). Some may be required to provide further information concerning the company's performance (targets, objectives, deviations from approved budgets) when required by law.

- In **Korea**, information on financial assistance from the government is included among transparency and disclosure requirements.
- In **Mexico**, the *Transparency Law*, requires all federal public entities (SOEs or general government activities), among other things, to provide financial and debt reports on a quarterly basis, to publish the results of financial audits, and to make transparent its assigned budget. Non financial information which should be made transparent includes the objectives and targets of the entity.
- In **New Zealand**, all state commercial entities are required to publicly disclose financial and non-financial information regarding their accounts (statements of corporate intent, annual reports, internal and external audits). Government entities are also subject to review by Parliament. The largest government SOEs are subject to the *Continuous Disclosure Regime* in which reporting requirements similar to listed companies.
- In **Russia**, different legal forms of enterprises are subject to specific sets of rules concerning transparency and disclosure requirements. Generally, all legal forms are required to submit annual financial statements subject to external audit. Notably, the Accounts Chamber of the Russian Federal is responsible for oversight and monitoring of the use of public funds made available to banks and other types of banking activity.
- In the **Slovak Republic**, state-owned stock companies are subject to the same transparency and disclosure practices as private stock companies where they earn above a specific turnover threshold. SOEs are subject to additional reporting when required according to specific law (annual reports, and financial statements verified by the state auditor). Moreover, enterprises established by state are also subject to general Act on Disclosure of Information.
- In **Slovenia**, SOEs are subject to the same transparency and disclosure requirements as private companies established under Company Law. Undertakings with special or exclusive rights are subject to audit the methods by which costs and revenues are assigned or allocated to different activities in separate accounts.
- In **Spain**, the Act 4/2007 imposes specific disclosure requirements to public enterprises and private companies granted with special or exclusive rights, or operating services of general economic interest. These practices are covered in Box 3.2. Notably, public undertakings excluded from the act are those which do not affect trade between EU member states and those whose turnover does not exceed a specific threshold (in line with the EU Transparency directive).

### Box 3.2. Supervising the use of public funds in Spain

In Spain the following supervisory controls are in place to ensure proper use of public funds in entities carrying out commercial activities:

- First, the undertaking's internal supervision which is carried out by its own governing body. This control enables the system to provide a truthful accounting for appropriate decision-making. In big companies, there is normally an internal audit department to ensure internal control and compliance with business objectives.
- Second, either the General State Comptroller or the Regional Comptrollers internally audit public undertakings since they also are Public Administration (national, regional or local).
- Public undertakings submit Action, Investing and Financing Programmes (the so called PAIF) together with their Annual Accounts, in order to justify the use of the public funds that they receive.
- Third, according to commercial law, undertakings' accountability implies financial statements complying with the principles set forth in the General Accounting Plan (mandatory in Spain) and Annual Accounts being subject to financial auditing.
- Fourth, the external supervision by permanent advisory bodies such as the *Tribunal de Cuentas* (the supreme supervisory body) and the regional external supervisory agencies. The existence of standardized financial statements allows for the financial or accounting auditing of the public undertakings that must be carried out annually through the General State Comptroller or through the Regional Comptrollers.

Finally, the Parliaments, as legal recipients of audit reports and of external audit services, exercise supervision through plenary sessions and commissions. Notably, public undertakings excluded from the Act are those which do not affect trade between EU (including EEA) member States and those whose turnover does not exceed a specific threshold (in line with the EU Transparency Directive).

Source: Questionnaire response.

- In **Sweden**, state-controlled companies are subject to disclose financial and non-financial information which is also made available to the public (following the same requirements as listed companies). State-controlled companies may be subject to external and internal audit, including by the State Auditor.
- In **Switzerland**, transparency and disclosure requirements vary depending on the legal form of the public business. For incorporated SOEs, reporting requirements are the same as for private sector companies (according to IFRS, annual reports available publicly). Whereas other government entities report according to the IPSAS. At the sub-national level, transparency standards are higher than for private companies, thus public business activities are subject to public scrutiny ("direct democracy"). Public statutory companies follow the provisions of the Swiss Code of Obligations.
- In **Turkey**, SOEs under the Treasury and Privatisation portfolio are required to make their annual reports public. Local government companies are not required to, but report on financial and non-financial information to the Undersecretariat of the Treasury. Specific sector regulations may also require additional reporting, for example in the natural gas, telecom and electricity sectors.
- In the **United Kingdom**, all state owned businesses are required to provide annual reports and accounts that disclose both financial and non-financial information. These accounts are generally audited by the National Audit office, are held accountable to the Public Accounts Committee and the House of Commons, and in some cases subject to the HM Treasury.

Above and beyond the *Financial Transparency Regulations* (which are in line with the EU Transparency Directive), specific sector regulations may impose additional reporting requirements (e.g. Royal Mail).

- In the **United States**, each federal government corporation may have varying practices depending on its statutory legislation. Companies registered under the U.S. Government Corporation Control Act are required to report according to standardised budget, auditing, debt management and depository practices. Additionally, annual reports to Congress may be required. Accounting standards are set according to the Federal Account Standards Advisory Board on Financial Reporting Requirements. Additional reporting requirements may be required of specific enterprises (e.g. U.S. Postal Service).

### *Identifying costs of commercial and non-commercial activities*

For government entities that perform both commercial and non-commercial activities, separate accounting allows to identify which costs and assets are attributed to non-commercial activities and to disclose which proportion are attributed to commercial activities. Separating such costs is important especially if financial assistance is received from the state. Country practices can be summarised as follows:

- Well over half of countries which answered this question, report that accounting separation is a requirement for government business activities. Among this group, a few countries stand out in terms the application of such requirements to all undertakings (public or private) that benefit from public funding or special/exclusive rights; whereas for other countries, the application of such practices are limited to incorporated SOEs. All EU Member States are obligated to comply with the EU Transparency Directive.
- The second set of countries report that accounting separation for the purposes of identifying costs is not a requirement for all SOEs or government bodies engaged in commercial activity. A majority of which note that sector laws and regulations determine whether such requirements exist (usually in energy or utilities sectors).
- The third set of countries does not report accounting separation for the purposes of identifying costs.

**Table 3.5. Identifying costs/income from commercial and non-commercial activities<sup>29</sup>**

<b>Separate Accounts, division in cost/income and budget structure between commercial and non-commercial activities</b>	
<b>Yes, specific rules on separate PSO accounts</b>	Australia, Czech Republic, Denmark, Estonia, Hungary, <sup>30</sup> Iceland, New Zealand, <sup>31</sup> Russia, Slovak Republic, Slovenia, Spain, Sweden, United Kingdom
<b>Generally, no specific rules on separate accounts</b>	Egypt, Italy, Mexico, United States
<b>Ad hoc, case-by-case</b>	Chile, <sup>32</sup> Ireland, Israel, <sup>33</sup> Korea, Lithuania, Poland, Switzerland, Turkey

Details on national practices are listed below:

- In **Australia**, financial statements of government business entities may separate accounts to detail purely commercial activities from public interest activities;<sup>34</sup> separate accounts may be held to evaluate the costs attributed to meeting public service obligations. According to the



*Australian Competitive Neutrality Guidelines* (2004), the pricing of goods and services must reflect full cost attribution for business activities.

- In **Denmark**, the production of goods and services must be separated according to commercial and non-commercial activities. Prices must reflect cost recovery, and should be set to avoid distortion *vis-à-vis* public or private competition.
- In **Estonia**, separating costs and revenues of public services is required by law (in Competition and other sector-specific acts). In addition, public bodies receiving funds from the state budget must keep additional records to monitor the use of budget allocation.
- In **Finland**, state enterprises are required to keep separate accounts and prepare separate financial statements for non-commercial activities (as specified by law for each enterprise). For municipal enterprises, there is also separate reporting for non-commercial activities (although further details concerning what should be reported is not provided), some examples of where this is enforced is in the production and distribution of electricity, natural gas, water and sewage services.
- In **Hungary**, the government's holding company requires its companies to report any public benefit activities separately in monthly/quarterly reports.
- In **Ireland**, commercial entities provide a breakdown, in their annual reports, of revenue received from the State and revenue generated commercially.
- In **Israel**, generally accepted accounting standards do not require specific reporting on public service obligations, however, where relevant sector regulation is concerned, additional reporting on companies' costs may be required in order to assess whether companies have met their public service/interest objectives.
- In **Korea**, some public corporations are required to separate accounts where public service obligations are of relevance.
- In **Lithuania**, specific provisions in sector laws (e.g. energy or communication companies) may require separate accounting.
- In **New Zealand**, public interest activities are only separately accounted for if public funding is explicitly provided to achieve them. If this is the case, the Statement of Intent for each entity outlines the goals and expected outcomes, and funding to be received. The use of such funds is reported in annual reports.
- In **Poland**, there is no general requirement to maintain separate accounts and not all public bodies are concerned in the same way. In some cases, special laws may determine whether accounting and budget separation is a requirement (e.g. the Press agency separates accounts).
- In **Spain**, the Royal Decree 1373/200 imposes an obligation to maintain separate accounts between commercial and non-commercial activities. The decree adopts the same requirements as the EU Transparency Directive, namely that costs and revenues associated with commercial and non-commercial activities must be reported, so to the methods by which such costs and revenues are associated and allocated to different activities.

### Box 3.3. The European Transparency Directive

The EU Treaty requires the Commission to ensure that Member States do not grant undertakings, public or private, aids incompatible with the internal market. However, the complexity of the financial relations between national public authorities and public undertakings tends to hinder the performance of this duty. A fair and effective application of the EU aid rules to both public and private undertakings is possible only if these financial relations are made transparent.

#### The Transparency Directive has two objectives:

- *Ensuring transparency of financial flows between public authorities and public undertakings.*

Some examples of financial flows existing between public authorities and public undertakings that have to be made transparent are:

1. the setting-off of operating losses;
2. the provision of capital;
3. non-refundable grants, or loans on privileged terms;
4. the granting of financial advantages by forgoing profits or the recovery of sums due;
5. the forgoing of a normal return on public funds used; and
6. compensation for financial burdens imposed by the public authorities.

- *Ensuring that public and private undertakings enjoying special or exclusive rights or receiving public service compensation for the provision of a service of general economic interest maintain separate accounts between their different activities.*

Such separate accounts should be available in relation to, on the one hand, products and services in respect of which the Member State has granted a special or exclusive right or entrusted the undertaking with the operation of a service of general economic interest, as well as, on the other hand, for each other product or service in respect of which the undertaking is active.

The objective is to prevent those undertakings from cross-subsidising other activities with funds raised through activities reserved for them or from compensation to provide public service obligations which would exceed the actual costs incurred in providing those obligations plus a reasonable profit.

For an undertaking to maintain separate accounts the Transparency Directive requires that:

- the internal accounts corresponding to different activities are separate;
  - all costs and revenues are correctly assigned or allocated on the basis of consistently applied and objectively justifiable cost accounting principles;
  - the cost accounting principles according to which separate accounts are maintained are clearly established; and,
  - the obligation of separation of accounts does not apply to undertakings whose activities are limited to the provision of services of general economic interest.
- Certain undertakings are excluded from the application of the transparency directive by virtue of the size of their turnover, in particular those public undertakings whose business is not conducted on such a scale as to justify the administrative burden of ensuring transparency.

Source: Questionnaire response.

### Box 3.4. Case Study: Lithuanian Police Department

In 2005 the Lithuanian Commissioner General issued an order applicable to selected security departments of the police. The order allowed these police departments to provide services on a commercial basis; however it did not distinguish specific provisions that apply when fulfilling public functions versus commercial activity. As such, the police were not prohibited from using the same equipment, including police cars and the possibility to use car lights, no matter which activity was carried out by them. Private sector competition operating in the area of personal and property security (and regulated under a different law than the police services), complained that given that public commercial security services are regulated under a different framework, certain advantages are afforded through their public ownership which are not afforded to private sector competition (rights and powers of police are regulated under the law on police activity). The claimants argued that private security firms could not compete at the same level with the police due to the fact that they operate under different legal conditions.

The Competition Council was asked to examine whether certain provisions of the Order were in compliance with Competition Law. The Competition Council found that :

- The problem was the legal regulation itself but not in the fact that the police pursued this commercial activity in general.
- The Competition Council could not apply the exemption placed in article 4 of the Law on Competition because the right to carry out such commercial activities was not regulated by any existing laws, but in the Order issued by the Commissioner General.
- Because the police are regulated under different provisions, the same license obligations required of private actors in the pursuit of security commercial services was not required (the licenses are provided by the police departments themselves).
- The Competition Council stated that it is unclear how the police commercial activities are financed, and from what financial sources. Therefore, the possibility that commercial activities of the police were financed from Police Department's general budget was high

In 2006 the Competition Council passed a resolution recognising that the provisions of the order of the Commissioner General contradicted the Law on Competition. The decision was affirmed by the Supreme Administrative Court. Consequently, the Commissioner General amended the Order which does not afford any rights to the police departments providing commercial services beyond those provided to the private sector. The Police Department has decided not to provide commercial services from January 2012.

Source: Questionnaire response.

- In **Switzerland**, accounts are separated insofar as sector regulations or ownership entities require (e.g. Swiss Post). According to public accounting and public management reforms at the sub-national level the separation of commercial and non-commercial activities is, reportedly, becoming commonplace.
- In **Turkey**, separate accounts are required for non-commercial activities specific sectors (e.g. in natural gas and electricity sectors).
- In the **United Kingdom**, the Financial Transparency Regulation (2009) requires that all government and private entities sufficiently report funding received from the state to avoid overcompensation and cross-subsidisation of commercial activities by state funds. Specific sectors may be subject to more stringent requirements as determined by sector regulation (e.g. postal market). Reportedly, some SOEs struggle with identifying such costs due to the difficulty of identifying what costs are attributed to commercial versus non-commercial activities.

### *Attribution of liabilities*

The attribution of liabilities is an important aspect in ensuring that government businesses' costs (and pricing) are fully identified and accounted for. Government businesses that are involved in both commercial and public interest activities may be afforded certain advantages, such as guarantees of their employees' pension liabilities; whereas other SOEs, may be put at a disadvantage, especially if former public-employees maintain special pension rights which may differ from the types of pension schemes found in the private sector.

The attribution of liabilities (including contingent and pension liabilities) differs from country to country, and to a certain extent depends on the legal form of the government business. Most incorporated SOEs are subject to the same or similar reporting requirements as private companies, according to nationally/internationally recognised reporting standards. For SOEs performing both commercial and non-commercial activities, practices may vary from country to country: some countries split the attribution of liabilities according to the commercial or non-commercial activities to which they correspond (e.g. Italy); whereas other countries do not differentiate the attribution of liabilities between commercial versus non-commercial activities (e.g. New Zealand).

As for pension liabilities, most countries report that employees of state enterprises remain in the State public pension system and are therefore not reported separately. In these cases, pension liabilities are reflected in the general government's balance sheets. In other cases, pension liabilities may be reported where special benefits remain for former state employees and where such benefits are guaranteed by the state. Pension liabilities may also be reported where they are covered by private pension schemes (e.g. Finland and Spain). Notable are practices in Ireland where SOEs report pension liabilities according to specific cost-allocation methodologies.

**Table 3.6. Attribution of liabilities**

Reporting of liabilities <sup>35</sup>	
<b>Reporting liabilities is a requirement (in accordance with national accounting standards)</b>	Australia, Chile, <sup>36</sup> Czech Republic, <sup>37</sup> Estonia, Israel, Italy, Korea, Mexico, New Zealand, Poland, Slovenia, Sweden, Switzerland, Turkey, United States
<b>Specifically Report Pension Liabilities</b>	Czech Republic, <sup>38</sup> Ireland, Israel, Italy, New Zealand, <sup>39</sup> Spain, Switzerland, United States
<b>None of the above</b>	Egypt, Russia

Where details concerning country reporting practices are provided, they are described below:<sup>40</sup>

- In **Australia**, government business enterprises ("GBEs") report liabilities (pension or other) according to Australian Accounting Standards, however no distinction is made between those attributed to commercial versus public interest objectives of the businesses. For other types of government businesses, superannuation (pension) liabilities for government employees are not reflected in the balance sheets of the business activity (they are instead reflected in the Australian government's balance sheet). Interestingly, where the government considers entering into an arrangement which may result in liabilities or contingent liabilities, government businesses (covered by the *Financial Management and Accountability Act 1997*) must have regard to the government's policies contained in the *Guidelines for Issuing and Managing Indemnities, Guarantees, Warranties and Letters of Comfort*. These Guidelines outline that government business should only accept liabilities if costs outweigh the risks.<sup>41</sup>

- In **Chile**, the *Report of Contingent Liabilities of the State*, published on an annual basis comprises of reporting on SOEs which have received state debt guarantees; other SOEs are not covered by this report. Public bodies do not reflect pension liabilities in their balance sheets.
- In **EU (including EEA) member States**, the reporting of liabilities is pursuant to the Transparency Directive. Specifically such reporting should reveal public funds being made available via public authorities, via intermediaries and/or financial institutions. No specific rules relate to the reporting of pension liabilities; however rules of State Aid would be concerned by any advantages associated with the treatment of pension liabilities that are afforded to public businesses.
- In **Estonia**, SOEs' liabilities are reported according to the same accounting standards as private companies (based on IFRS or IAS Regulation).
- In **Finland**, employees of state enterprises remain in the public pension system of the state and are therefore not reported as a specific liability concerning the government business. In some cases, for SOEs which employ former state-employees, special benefits remain and are covered by private pension insurance.
- In **Ireland**, attribution of liabilities is not separately reported. However, pension liabilities are generally reflected in SOE balance sheets (Box 3.5).

#### **Box 3.5. Actuarial calculations for Bord Gáis in Ireland**

***Bord Gáis* (gas networks and supplier) has defined pension benefit and contribution arrangements as follows:**

- Each of the defined benefit pension scheme assets are measured using fair values;
- Pension scheme liabilities are measured using the projected unit method and discounted at the rate of return of a high quality corporate bond of a comparable duration to the benefit flows.
- Pension schemes' surpluses, to the extent that they are considered recoverable, or deficits are recognised in full and presented on the face of the balance sheet net of related deferred tax.
- The current service cost and gains and losses on settlements and curtailments are charged to operating profit or provisions as appropriate. The interest cost and the expected return on assets are included as other finance income/expenses. Actuarial gains and losses are recognised in the consolidated statement of total recognised gains and losses in the period in which they occur.

The contributions payable by *Bord Gáis* under the defined contribution schemes are charged to the profit and loss account in the period in which they become payable.

*Source:* Questionnaire response

- In **Israel**, government companies are required to report liabilities, including contingent liabilities and pensions, according to generally accepted accounting standards in company financial statements.
- In **Italy**, liabilities, including pension liabilities are reported according to the government business activity they are related to. In other words, liabilities associated with public interest activities will be reported separately from purely commercial activities.

- In **Korea**, public institutions with assets above a certain threshold are required to submit a five year debt management plan. The plan is assessed by the National Assembly.
- In **New Zealand**, there is no distinct treatment of liabilities between those attributable to public interest objectives and those attributable to commercial objectives; liabilities are reported according to national IFRS standards. Where public sector pension liabilities are concerned, public bodies performing commercial activities report these obligations on their balance sheets. Reportedly, this practice is rare.
- In **Poland**, liabilities are recognised in company financial statements in accordance with national accounting standards. There are not specific guidelines concerning reporting of pension liabilities.
- In **Spain**, public undertakings do not report pension liabilities which are covered by the state (as they are reported under the Public Social benefits Registry); for undertakings which cover pensions according to private pension schemes, there is reporting of liabilities.
- In **Sweden**, corporatized SOEs report liabilities according to the same reporting requirements as private companies. Public sector pension liabilities are not reflected in public bodies' balance sheets.
- In **Switzerland**, incorporated SOEs and statutory corporations report their liabilities according to accounting standards set out in IFRS or Swiss GAAP FER. The remaining public bodies (national or sub-national level) report according to IPSAS. Pension liabilities are included in the federal and sub-national governments' balance sheets as applicable.
- In the **United Kingdom**, liabilities are reported according to the general reporting requirements of SOEs (as set out under the Transparency and Disclosure section).<sup>42</sup> Reporting of pension liabilities depends on the legal form of the government business. In the case of limited liability SOEs, pension liabilities are reported according to international accounting standards. However, where public bodies employ civil servants, such pensions are reported according to the governments wider pension scheme; annual contributions to the pension scheme and pension arrangements are reported.
- In the **United States**' Office of Management and Budget (OMB) provides guidance for government-wide financial reporting requirements, including for government corporations.<sup>43</sup> Liabilities and contingent liabilities are to be reported in financial statements and are classified as liabilities either covered or not covered by budget resources. Actuarial liabilities are to be reported under federal employee benefits. Specific accounting for liabilities standards are set forth by the OMB, although their applicability varies according to the entity.<sup>44</sup>

### 3.3. Commercial rate-of-return

#### *Overview of findings*

Concerning rate of return (RoR) requirements, over half of responding countries report that there are no imposed requirements for SOEs and/or other public bodies performing commercial activities, but report that SOE performance is benchmarked *ex-post* against industry comparisons. A number of responding countries report that their SOEs/public bodies are required to earn market-consistent rates of return on commercial activities according to specified methodology/policy. Methodologies for

defining such requirements vary; notable are the cases of Australia, Hungary and Turkey which have set out specific guidelines for rates of return. A number of countries do not define specific return requirements for their SOEs, and in more rare cases, SOEs may not be expected to earn market-consistent ROR.

### *Commercial rate of return requirements for government businesses*

Among the responses received, eight countries report that commercial rate of return requirements are imposed on the goods and services offered by SOEs and other public bodies; among these respondents rate of return requirements are defined differently. In Australia, Hungary, Sweden, Switzerland and the United Kingdom guidelines concerning rate of return requirements are provided as recommendation for SOEs on how to calculate ROR targets.

**Table 3.7. Commercial ROR policy for public undertakings**

<b>Guidelines on how to calculate rate of return targets for <i>commercial</i> activities of SOEs</b>	
<b>Yes, according to guidelines recommended by the state</b>	<b>Australia, Hungary, Sweden, Switzerland, United Kingdom</b>
<b>No guidelines or recommended methodology, based on a company-by-company assessment</b>	<b>Austria:</b> ROR and prices take into consideration public interest objectives <b>Chile:</b> Board sets ROR targets, benchmarked against industry comparisons <b>Denmark:</b> ROR depends on market risks <b>Estonia:</b> SOEs are profit-oriented, ROR benchmarked against industry comparisons <b>Finland:</b> according to comparable performance of privately held companies active in the same business <b>Germany:</b> where applicable ROR is dependent on the decision regarding profit use made by the relevant body <sup>45</sup> <b>Ireland</b> <b>Israel:</b> ROR benchmarked against industry comparisons <b>New Zealand:</b> SOEs are expected to produce a commercial return that reflects their cost of capital over the medium-term <b>Slovak Republic</b> <b>Slovenia</b> <b>Turkey</b> <b>United States:</b> varies according to the entity
<b>Guidelines are generally not defined or recommended.</b>	<b>Czech Republic</b> <b>Egypt:</b> government does not set ROR, against the law <b>Italy</b> <b>Korea:</b> except in the electricity and gas sector where prices must cover costs of production and service provision. <b>Mexico:</b> SOEs do not earn market-consistent ROR <b>Russia</b>

Among countries which report no specific recommendations for guidelines on rate of return requirements, country practices vary. Most countries report that rate of return requirements are set according to benchmarks comparable with what is earned by the majority of firms within the same industry. A number of countries report that equity and price considerations are factored into rate of return requirements, especially where public interest objectives are being met by the SOE/public body in question. This raises an important issue: while the SOE Guidelines recommend on-budget compensation, from a competitive-neutrality perspective a selective lowering of RoR requirements (assuming it is accurately calibrated) can be equivalent.<sup>46</sup>

Country practices where market-consistent rate of return practices are reported are described as follows:

- In **Australia**, all government businesses are required to earn a commercial rate of return on the goods and services offered. Full costs of resources employed, including the cost of capital (calculated according to credit risk of the Australian government), must be recovered. Government businesses are expected to manage their performance objectives to recover costs, as such prices should reflect this principle (taking into account economic “forces” and pricing conditions which may be imposed). The *Australian Competitive Neutrality Guidelines* (2004) sets out standards in this regard.
- In **Hungary**, SOEs are subject to commercial rate of return requirements (Box 3.6).

### Box 3.6. ROR calculations in Hungary

#### *Rate of Return Requirements for Hungarian SOEs*

- In line with private equity standards, sophisticated planning guideline is prepared by HSHC. It specifies the principles and basic requirements for next year’s business planning practice.
- The planning guideline has a macro outlook part that defines the premises and the owner’s requirements for the upcoming year’s business planning. All the majority-owned HSHC portfolio shall use the planning guideline accepted by HSHC.
- The main features of the guideline are the followings:
  - Gives an overview about external macro premises
  - Draws expectations for capital efficiency and dividend yield policies
  - Demonstrates the owner’s resource allocation possibilities
  - Defines the formal minimum standards of business plans
  - Defines salary increase ceilings
- One of the main goals of SOE asset management is efficiency and increasing the rate of return. Therefore, capital effectiveness is monitored thoroughly. Minimum expected yield is defined individually for major SOEs. As for homogenous portfolios and other state-owned enterprises, yield requirement (HSHC uses return on equity) is defined for the group as a whole.
- As a general principle, the minimum target is positive earning before tax and earnings cannot be lower than the previous years’ one.

HSHC benchmarks yield requirements to average yields of the Hungarian Treasury bonds with 5 years maturity auctioned in 2010.

Source: Questionnaire response.



### Box 3.7. Case study: The Australian Valuation Office

In November 2003, the AGCNCO received a complaint from Herron Todd White Pty Ltd concerning the activities of the Australian Valuation Office (AVO), an Australian Government business unit operated by the Australian Taxation Office (ATO).

The AVO provides a range of valuation services, on a fee for service basis, to government departments and agencies and the private sector. These services include: appraisals of property and other assets for government housing and welfare agencies (examples include large scale valuations for State and Territory housing authorities and the valuation of the assets of applicants for social security benefits); special purpose valuations of property for capital or rental value, connected to acquisitions, disposals, leases or financial statements; plant and equipment valuations; and corporate valuations for consolidation and taxation purposes.

Herron Todd White Pty Ltd is one of Australia's largest Independent Property Advisory groups. The complainant alleged that the AVO was not complying with competitive neutrality and that the pricing regime used by the AVO in tendering situations systematically fails to adequately reflect the full costs of service provision. The complainant claimed that the AVO's pricing failed to adjust for a number of key cost advantages which accrue from its position within the ATO, including: access to resources such as IT and telecommunications at reduced rates; reduced commercial rents, accommodation search costs and fit-out costs as a result of being co-located with the ATO; and diminished search and compliance costs in relation to professional indemnity insurance, given AVO's 'government' status. The complainant further alleged that the pricing regime employed by the AVO fails to include a tax equivalence component, and that the AVO cannot be earning a rate of return which accords with normal commercial standards.

The issue was addressed through a complaint made to the Commonwealth Government complaints office, AGCNCO, who undertook an investigation of the issues and provided a report, along with recommendations, to the relevant Australian Government Ministers and the Treasurer. The AGCNCO found that the AVO:

- operated as a stand alone business and did not receive a competitive advantage through access to ATO resources at non-commercial rates;
- appeared to gain no material advantages in the areas of taxation, regulation or debt financing, as a result of it being government owned;
- met competitive neutrality obligations in relation to payments for insurance costs in the areas of public liability, property loss and fraud, fidelity, workers' compensation and third party motor vehicle coverage; and
- generated a rate of return in the last five years, based on current levels of expenditure consistent with competitive neutrality principles.

However, in the area of professional indemnity insurance, the AGCNCO found that an increase was required, on competitive neutrality grounds, in the professional indemnity insurance premium paid by the AVO. The AGCNCO recommended that the Department of Treasury and the Department of Finance and Administration institute a process, drawing as appropriate on information obtained from the AVO and other key stakeholders, to determine the extent of the increase in professional indemnity insurance premiums required.

Source: Questionnaire response.

- In **Sweden**, the framework for rate-of-return requirements is based on EU State Aid criteria ("Market investor principle").
- In **Switzerland**, strategic objectives for SOEs are set by the Federal Council and include rate of return/earnings expectations. Although there are no general guidance on rates of return, they are defined according to sector and are benchmarked with international and industry benchmarks, and take into account past performance.

- In the **United Kingdom**, SOEs are expected to earn market consistent rates of return in areas in which they operate commercially (taking into account non-commercial activities) and in accordance with EU State Aid laws (e.g. cost of capital should be at market rates). Where benchmarks for rate of return cannot be made with a private sector equivalent, they are set by the Shareholder Executive or a respective ownership department; such rates are based on commercial principles but take into consideration specific company objectives.

### Box 3.8. Case study: Hungarian Office for Translation and Attestation

The Hungarian Office for Translation and Attestation Ltd. (OFFI Ltd.) is a state owned enterprise, with legal monopoly on authentic translations and translation attestation. OFFI Ltd. has been granted legal monopoly in this field since 1986. Since then, numerous translating agencies have entered the Hungarian market, employing the same translators and proof-readers OFFI Ltd. and which prepare translations of high quality.

According to stakeholders, the only difference between OFFI Ltd. and the other big translation agencies is the state-owned nature of OFFI Ltd. and its legal monopoly. It has been claimed, that OFFI Ltd. – making use of its legal monopoly – charges excessive prices and tries to exclude other translation agencies from the market. Translation agencies lodged a submission to the Constitutional Court, claiming that the legal provisions granting monopoly for OFFI Ltd. were unconstitutional. The Hungarian Competition Authority has also received numerous complaints alleging that OFFI Ltd. abused its dominant position.

Complaints were heard in 1995 and 2007. As the result of the 2007 proceeding, OFFI Ltd. has undertaken commitments to change parts of its general contracting terms.

The latest complaint in 2010 has led the Competition Authority to investigate whether OFFI Ltd. is engaged in excessive pricing and margin squeeze. The case is still pending. According to Hungarian competition law, the Competition Authority may only address legal provisions that distort economic competition, through its competition advocacy activity. Thus, the Competition Authority may investigate the practice of OFFI Ltd. in a proceeding only in case OFFI Ltd. oversteps the scopes of its legal monopoly.

Source: Questionnaire response.

Governments may not require specific rate of return targets for their SOEs, however, they may employ other practices to determine company profit objectives and targets; these practices are described below:

- In **Chile**, while there are no government-wide standards set for rate of return requirements, consistency and comparability of rate of return (as set by the SOE board) is monitored with firms operating in the same industry.
- In **Estonia**, although no rate of return requirements are imposed on SOEs, the *State Assets Act* requires that SOEs generate revenues which ensure “reasonable” profits. Rates of return are compared to similar businesses in the same industry (domestically or internationally).
- In **Finland**, SOEs’ financial performance should be comparable to privately held companies active in the same market. Where SOEs fulfil public interest objectives, prices take into account such objectives, but should general overall profits in the long run.
- In **Iceland**, SOEs are to earn an appropriate return on capital, or the economic advantage to the benefit of the entity must be quantified and counted as compensation (in line with EU and EEA rules on state aid).

- In **Ireland**, rate of return requirements are required in specific sectors, such as the electricity sector. Tariffs take into consideration specific charges and costs associated with maintaining and operating the distribution system. Revenue targets are set every five years and are refined each year to take into consideration equity considerations.
- In **Israel**, although the government does not set rate of return requirements, by law government companies must perform according to similar private sector businesses in the same industry.
- In **New Zealand**, rates of return are not specified by law but SOEs are expected to earn market-consistent rates of return. These rates of return targets take into account the cost of capital and details as to how capital was derived. Other more specific standards may be set out by respective line ministries in “Letters of Expectations” which may for example set out targets for shareholder returns (e.g. to exceed the cost of capital over a five year period).
- In **Spain**, the Ministry of Economic and Finance is entrusted to estimate rate of return requirements of public undertakings. The estimation is to take into account public capital invested in the undertaking, dividends to be paid, financial responsibilities arising from public service obligations and other advantages associated with public ownership.
- In **Turkey**, SOEs are expected to earn commercial rates of return, according to the same practices as that in the private sector.

### 3.4. Accounting for public service obligations

#### *Overview of findings*

Almost all countries compensate undertakings (public or private) which deliver public service obligations alongside their commercial activities. Compensation methods vary depending on the country, the type of public service and the entity delivering such services (respondents mainly reported on SOEs delivering public services as opposed to general government departments). Compensation methods range from direct transfers, capital grants, reimbursements (*ex-post* and *ex-ante*), and budget appropriations, to state aids/subsidies.

Most cited examples of public service obligations (usually in the form of universal service obligations) which benefit from compensation from the public purse appear in the following sectors: post, utilities (telecom, electricity, and gas), health, and transport sectors (passenger bus and rail). In some cases, where essential public services are partly funded through user charges, and where the government may impose tariffs which are below costs (e.g. to ensure equality considerations), any differences in costs may be made up for by compensation. In general, compensation methods and amounts are determined in advance according to sector-specific laws and regulations. The adequacy of compensation is determined by sector regulators (or other public authorities), usually in advance and in accordance with agreed standards in quality and price (Table 3.8).

A few countries report that they generally do not compensate for the delivery of public service obligations (Australia, Israel and New Zealand). In these cases, public service obligations are funded by entirely by user charges for such services, and any costs associated with the delivery of public service obligations are to be incorporated in the company’s cost structure. Operators are to incorporate any public service obligations into tariffs/prices, effectively implying a form of cross-subsidisation – not among activity areas but among customer segments. A number of countries engage in competitive tendering to ensure “value for money” in public service delivery.

**Table 3.8. Compensating for public service obligations**

<b>Compensating for public service obligations – country practices</b>	
<b>Generally, no compensation for public service obligations</b>	Australia, Israel, Korea, New Zealand
<b>Compensation for public service obligations</b>	Austria, Brazil, Chile, Denmark, Finland, Germany, Hungary, Iceland, Ireland, Italy, Poland, Russia, Slovak Republic, Slovenia, Spain, Sweden, Switzerland, Turkey, United Kingdom
<b>Cross subsidisation practices in public service delivery (from profit-making to loss-making activities)</b>	
<b>Cross-subsidisation is permitted</b>	Brazil, Egypt, Russia, Slovenia
<b>Cross-subsidisation is <i>not</i> permitted (in principle)</b>	Austria, Finland, Iceland, Israel, Mexico, Poland, Slovak Republic, Spain
<b>Cross-subsidisation is permitted on a case-by-case basis</b>	Australia, Chile, Czech Republic, Estonia, Hungary, Ireland, Italy, New Zealand, Sweden, Switzerland, Turkey, United Kingdom

Where compensation is provided, in EU and EEA countries, this must be in conformity with EU Rules on State aid and Subsidies. This means that any form of public assistance to an undertaking (public or private) performing services of general economic interest must fulfil a number of criteria in order either *not* to be determined as State aid/subsidy or, if it constitutes State aid, to be declared compatible with the internal market. The compatibility rules aim to ensure that there is no over-compensation or cross-subsidisation of commercial activities. The most important jurisprudence for the qualification of compensation for public service obligations as State aid is the so-called “Altmark criteria” described in Box 3.9.<sup>47</sup>

For what concerns cross-subsidisation practices, most countries either permit or tolerate on a case-by-case basis cross-subsidisation practices from profit-making to loss-making activities to fund public obligations. Most countries make clear that cross-subsidisation practices of an undertaking would not be compatible with competition rules where public funds intended for carrying out essential public services be used to fund commercially-oriented activities. For this reason, a number of countries require that publicly-funded undertakings are required to separate accounts for public service obligations in order to ensure transparency surrounding the use of public funds (see also Table 3.5<sup>48</sup>). In the remainder of responding countries, in principle, cross-subsidisation practices are not permitted – or respondents are not aware of such practices (Austria, Finland, Israel, Mexico, Poland and Spain).

### ***Compensation for public service provision***

In EU (including EEA) member States, compensation used for the operation of services of general economic interest must be compatible with EU rules on state aid, which apply to all EU member states and are applicable to EEA members.<sup>49</sup> In EU States compensation is justified for services of general economic interest (SGEI) provided that no overcompensation is granted and that separate accounts ensure that there is no cross-subsidisation of commercial activities with funds granted to cover a SGEI. Where cross-subsidisation is allowed, it can only be from profit-making activities to finance public service activities ensuring that overcompensation is not provided. The European Court of Justice’s jurisprudence defines 4 “Altmark criteria” that need to be fulfilled in order for a compensation not to qualify as State Aid (Box 3.9). However, if these criteria are not met, compensation is not necessarily prohibited. Compensation is allowed as compatible State Aid if it complies with the conditions of the exemption Decision. If it cannot be exempted, it can be notified to the Commission and can be authorised under the Framework. The compatibility rules for compensation constituting State aid were provided under the 2005 SGEI package (consisting of the

Decision and the Framework) and basically required compliance with the first three “Altmark” criteria to ensure that services of general economic interest are not overcompensated (entrustment with a clearly defined service of general economic interest; objective and transparent pre-defined parameters for calculating the compensation; no overcompensation). On 20 December 2011 the Commission adopted a revised package of SGEI rules. The *Transparency Directive* sets out clear rules as to how undertakings must transparently disclose their cost structure (see Identifying costs above for more details).

Country specific practices for this section are covered as follows (EU Members States’ practices are cited notwithstanding obligations to comply with the EU Transparency Directive):

- In **Australia**, government businesses enterprises are generally not compensated for fulfilling public service obligations, they are expected to price efficiently (taking into consideration any price conditions the government may impose) to fully recover costs. Were compensation to be provided to GBEs for public service provision, this would be publicly disclosed in the government budget. In some cases cross-subsidisation by GBEs within and across services may be allowed.
- In **Austria**, government business providing public services set prices to meet universal service obligations according to sector regulators’ requirements (e.g. postal and gas sectors); sector regulators are also responsible for determining compensation amounts. For the Austrian Post, compensation is provided on the basis on an equalisation fund, financed on a pro-rata basis corresponding to the market share held by the incumbent and other licensed postal operators. A threshold has been set: if net costs of universal service obligations exceed 2% of the annual costs, such costs will be refunded.
- In **Brazil**, public service obligations are compensated if they are “imperative necessities for national security or in the collective interest.” Compensation methods differ according to the sector; in the postal sector, for example, the public operator maintains monopoly rights over more populated and affluent regions in order to compensate for its universal service obligations in remote places.
- In **Chile**, SOEs are compensated for public service obligations (e.g. to finance investments, debt service or infrastructure maintenance) through budget transfers. For some SOEs subsidies are forbidden, whereas for others, subsidies are received to carry out public service objectives under the condition that SOEs are efficiently managing funds and public service delivery.
- In **Germany**, different compensation methods are used depending on the type of public services. In some cases, user charges fund public services, in other cases SOEs may be provided government grants. Specific legal provisions under EU State aid rules, EU Treaty rules (article 102) and national competition law ensure that overcompensation is not provided and that anti-competitive cross-subsidisation practices are prohibited.
- In **Hungary**, the State Aid Monitoring Office ensures that compensation for public service provision is adequate and according to EU rules on State Aid. Specific practices are outlined in Box 3.10. Some state-owned companies are allowed to engage in cross-subsidisation practices, from profit-making to loss-making activities, however such practices must not constitute over compensation.

**Box 3.9. Determining when compensation for public service obligations in EU Member States does not constitute State aid according to the “Altmark Criteria” , and is thus not subject to State aid control**

***A compensation for the discharge of public service obligations may or may not entail State aid. The European Court of Justice explained in its judgement Altmark<sup>50</sup> when a compensation does not amount to State aid:***

- First, the recipient undertaking must actually have public service obligations to discharge and the obligations must be clearly defined.
- Second, the parameters on the basis of which the compensation will be calculated must be established in advance in an objective and transparent manner.
- Third, the compensation cannot exceed what is necessary to cover all or part of the costs incurred in the discharge of public service obligations, taking into account the relevant receipts and a reasonable profit for discharging those obligations.
- Fourth, where the undertaking which is to discharge public service obligations is not chosen pursuant to a public procurement procedure which would allow for the selection of the supplier capable of providing those services at the least cost to the community, the level of compensation needed must be determined on the basis of an analysis of the costs which a typical undertaking, well run and adequately equipped, would have incurred in discharging those obligations, taking into account the relevant receipts and a reasonable profit for discharging the obligations.

If a compensation to discharge public service obligations entails State aid (this is very often the case as public sector providers are typically not selected following a tender procedure), it will be subject to scrutiny by the European Commission. The conditions under which a public service compensation constituting State aid can be authorised were clarified in the so-called “2005 SGEI package”<sup>51</sup>. In short, the conditions required correspond to the three first criteria of Altmark. In light of the experience gained since 2005 and the views of the stakeholders, the Commission has revised the “2005 SGEI package” by adopting on 20 December 2011 a new SGEI package.

***Further clarification as to the applicability of rules on State Aid to compensation for the discharge of public service obligations are reflected in the adoption of the new SGEI package in December 2011. The new packages favours the net avoided cost methodology to better estimate the costs associated with the discharge of public service obligations:***

**New SGEI Framework**

The new framework for the assessment of the compatibility of **large** commercial SGEIs uses the net avoided cost methodology as the default rule. Under the net avoided cost methodology, the cost of the public service obligation is calculated as the difference between the net cost for a company of operating an SGEI and the net cost for the same company operating without a public service obligation.

The old framework of 2005, in contrast, was based on a cost allocation methodology, under which costs that are common to the SGEI and other activities of the same provider are allocated based on allocation keys.

The primary reason for introducing a new methodology is to better estimate the economic cost of the public service obligation and to fix the amount of compensation at a level which ensures the best allocation of resources. The new Framework also allows alternative methodologies when the net avoided cost methodology is not feasible or appropriate.

**New SGEI decision**

The new decision applies to public service compensation for **smaller** services and to **social** SGEIs, where no prior notification to the Commission is required. Under the decision, the cost allocation methodology remains the default rule, but public authorities are also free to use the net avoided cost methodology.

Source: Questionnaire response.

- In **Ireland**, public authorities compensate for provision of public service obligations in a number of ways including through user fees (public service broadcasting) and capital grants (public transport). Adequate compensation for public service obligations are defined according to legislation/sector regulations, however in some cases the level of transparency surrounding how public service obligation funding is used could, reportedly, be improved. Some commercial activities may cross-subsidise from commercial activities to public service activities (bus sector).

### Box 3.10. Determining adequate compensation for public service obligations in Hungary

The procedural rules oblige all aid grantors to notify their aid plans *a priori* to State Aid Monitoring Office (SAMO), which is responsible for assessing the compatibility of each aid proposal with relevant EU laws and regulations. SAMO gives guidance and assistance to the aid grantor bodies when they prepare the rules of their aid plan and the notification. The procedure followed by SAMO depends on the characteristics of the notified aid plan. In its preliminary opinion SAMO can recommend modification of the given measure to make it compatible with the EU rules. Indeed, SAMO is allowed/ is empowered to demand additional information in order to obtain a more detailed picture of the planned measure. Aid grantors should co-operate with SAMO at the preparatory stage of their notifications. In cases where the approval of the EU Commission is necessary, if SAMO finds that the rules of an aid measure do not comply with the EU rules, the notification cannot be submitted to the EU Commission unless the Government definitely instructs SAMO to send it to the EU Commission. SAMO will keep the aid grantor informed of any additional questions and decisions of the EU Commission concerning the notified aid plan. SAMO is also responsible for the sub schemes (calls for applications) control.

Apart from the notification, SAMO has other duties, like compiling the annual report on aid. SAMO also formulates the Hungarian position in connection with “appropriate measures” proposed by the EU Commission for the amendment of existing aid schemes, to play a leading role in formulating the national position in the new Community State aid legislation. SAMO also has to keep the aid grantor informed about the recovery or suspension of any aid scheme or individual aid assessed by EU Commission. Not only that/furthermore, SAMO also monitors whether all necessary steps have been taken to execute the decision on recovery or suspension. SAMO regularly publishes discussion of the State aid issues, in the State Aid Law Journal which provides information on Community State aid legislation and related changes, on EU Commission and Court of Justice of the EU decisions and on the assessment of national practices.

SAMO represents a privileged link with the European Commission and aid grantors, and helps in locating the proper tools for realizing/helps to realize the national objectives, in a way which is compatible with current EU State aid laws and regulations.

If the state/municipality intends to compensate a public service provider to fulfil a public service obligation, it should notify their aid plans *a priori* to SAMO (According to Government Decree 37/2011. (III. 22.) and SAMO will decide on a preliminary opinion. According to the regulation, the aid grantor should ensure the avoidance of overcompensation.

In order to avoid overcompensation the aid grantors will have supervisory powers stipulated in the aid contracts. Public service providers should co-operate and facilitate the controlling procedures. Furthermore, they have to prepare a report periodically.

The public service provider, who was compensated for the public service, must account the aid separately. After having fulfilled the public service tasks, the service provider (beneficiary) will have the right for the amount of aid that was *de facto* needed. (Planned budget must be in line with *de facto* spending.) The difference between planned and *de facto* expenditures must be paid back or it will not be paid out. Sometimes it occurred in the past that internal supervisors and auditors helped the aid grantors to examine the expenditures.

In certain cases beneficiaries must submit a report on the fulfillment of the goals defined in the contract and a detailed financial report that should be approved by an external auditor. The auditor issues a declaration for the aid grantor.

There are sector rules for agricultural, fishery, forestry and rural development cases.

Source: Questionnaire response.

- In **Israel**, a large number of government activities incorporate costs for pursuing public service obligations their tariff structures and user fees (postal service, water, electricity); whereas other activities may be funded by the government. Cross-subsidisation practices are not permitted between non-essential and essential services.



- In **Italy**, the government compensates special obligations of public or other bodies entrusted with public service obligations. The amount and terms of compensation are detailed in *Public Service Agreements*, which aim to prevent overcompensation by putting into place cost and subsidy-caps; if costs exceed that which is agreed in the Public Service Agreements, cross-subsidisation is allowed from profit-oriented activities (the exception is the state-owned postal service which fully funds public service obligations through cross-subsidisation).
- In **Mexico**, there are no specific rules concerning compensation of public service obligations; the government ensures that public services are compensated adequately by contracting out service delivery (through PPPs or other competitive tendering processes).
- In **New Zealand**, generally SOEs and other commercial entities do not provide public goods and services along with their commercial activities. If they do, compensation is determined on a negotiated basis (competitive tendering); funding would be provided by the Crown and subject to review by budget appropriations processes according to specific disclosure and reporting requirements. Cross-subsidisation practices are allowed from more to less profitable activities (e.g. postal services).
- In **Poland**, compensation is provided to entities providing public services according to an agreement which does not exceed the amount necessary to cover the costs incurred for fulfilling such obligations; compensation must be used for the provision of such services and is verified through separate accounts (Box 3.11). Cross-subsidisation practices are not allowed.

**Box 3.11. Compensation of Public Service Obligations –  
Example from the public transport sector in Poland**

In the land transport sector, compensation for public service obligations is regulated by the Act of 16 December 2010 on Public Transport.<sup>52</sup> Under that Act, compensation for the provision of public transport services covers revenues lost by the operator (carrier) in respect to the use of concessionary fares (imposed by statutory act or established within the jurisdiction of authority responsible for the organization of public transport) and incurred costs related to the provision of public services. As a rule, the operator is entitled to a so-called reasonable profit. The method of calculating compensation is in each case specifically regulated in the contract for the provision of public services (pursuant to Polish regulations it is called services agreement for public transport). The operator is entitled to compensation if it proves, by presenting relevant documents, that the lost revenue resulting from the use of concessionary fares and the costs incurred in connection thereof, are grounds for incurred losses related to the provision of public transport services. The authority commissioning the provision of services is required to verify documents submitted by the operator. If the operator conducts other business activity in addition to providing services in the field of public transport, it is obliged to keep separate accounts for both areas of activity.

In 2010, the Office of Competition and Consumer Protection conducted a survey among entities supplying the land transport services at central, regional and local levels. The results indicate that the amount of compensation is adequate covering only the costs of providing public services without taking reasonable profit into account.

*Source:* Questionnaire response.



### Box 3.12. Case Study: The News Agency of the Slovak Republic

The News Agency of the Slovak Republic (TASR), a state subsidised organization (contributory agency) of the Ministry of Culture, is entitled to a subsidy from the state budget according to the Act on Budgetary Rules via budget of Ministry of Culture to carry out tasks in the public interest (pursuant to the Act on The News Agency of the Slovak Republic). The main activity of TASR is providing of news services in the public interest, alongside a number of private news agencies which provide news services on a commercial basis.

The Antimonopoly Office of the Slovak Republic received a complaint by the competitor of TASR, a private news agency, which claimed that commercial activities of TASR are financed from state budget, thus, TASR had an unjustified competitive advantage. Pursuant to the Competition Act,<sup>53</sup> competition authorities were to examine whether the Ministry of Culture, as the state administration, was providing support to TASR's commercial activities in a way which advantaged the public undertaking.

The Office found that :

- TASR was indeed carrying out activities in a competitive environment;
- The Ministry of Culture did not define criteria for the use of state budget funds and thus, made it possible for TASR to use public funds for the financing commercial activities ;By its conduct, the Ministry of Culture put the TASR undertaking at an advantage with respect to its competitors;
- The Office decided that TASR must finance commercial news services its own business income as opposed to from state subsidies.

The Office passed two decisions (which were later contested) in this respect and imposed a fine on the Ministry of Culture (200 000 SKK in 2006 and 300 000 SKK in 2007).

The Office is still under discussions with the Ministry of Culture within the advocacy activities on the financing of TASR.

Source: Questionnaire response.

- In the **Slovak Republic**, compensation for public service providers depends on sector regulation (e.g. postal sector, rail, passenger transport, public broadcasting) which determines the level of compensation, how to calculate the costs of compensation and which compensation methods are used (e.g. user chargers, direct or indirect subsidies, compensatory funds). In some cases authorities report that there are no specific controls. In other sectors, compensation is not provided by the government; however certain segments of the market (for example in the network industries) may be reserved for operators providing universal services. In these cases, cross-subsidisation practices are allowed only from profit-oriented areas.
- In **Slovenia**, public service obligations are funded through subsidies or user charges for government services. Compensation is determined according to relevant regulatory authorities. Cross subsidisation practices is allowed from profit to loss-oriented activities.
- In **Spain**, entities (public or private) conducting public service activities must be adequately and transparently compensated for carrying out such activities. Applicable guidance is provided by the Royal Decree 1373/200, including imposing and obligation to maintain separate accounts. Cross-subsidisation practices are not allowed.
- In **Sweden**, public service obligations are financed through tax receipts. The adequacy of compensation is determined according to EU Rules on State Aid in addition to applicable

national and sub-national legislation (e.g. Municipality Act, Public Procurement Act and the Competition Act). Changes to the Competition Act have reduced the scope for cross-subsidisation practices.

- In **Switzerland**, compensation is theoretically provided to public entities which are entrusted with public service obligations; compensation is determined through sector specific laws and calculations are assessed by sector regulators (e.g. postal, telecom, transportation and health sectors). However, on national level compensation only takes place in the railway sector by contributions for network infrastructure. At the sub national level, companies may be subsidised for the provision of public services, where user chargers do not cover such costs. Cross-subsidisation practices are allowed, however reportedly it is not possible for authorities to assess whether such practices are being used (e.g. in the case of the postal sector) given that regulators have not identified what costs for universal service obligations are. Cross-subsidies from monopoly to commercial segments are forbidden.
- In **Turkey**, companies which provide public services are compensated according to duty-loss (according to Decree law No. 233 which allows the Treasury to compensate any duty losses to 110% of losses incurred) or capital transfer mechanisms; cross-subsidisation is not a preferred method. Compensation is determined jointly by the concerned line ministry and Treasury based on the SOE's accounts.
- In the **United Kingdom**, compensation for the provision of public services is done based on commercial principles and is usually determined by the authority which commissions the service, however it is reported that assessing the value of such services, given that they may or may not be readily attainable from the market, is complex. In general, value for money is considered by the department awarding the compensation (evaluation criteria is set and there may be competitive tendering). Any compensation that involves State Aid conforms to EU rules and may be audited by the national audit office or the parliament's public accounts committee. Cross-subsidisation practices are permitted if profit-making services fund public service provision.
- In the **United States**, compensation practices vary according to entity and according to its enabling and other relevant legislation. For those entities which perform public service obligations alongside commercial obligations, specific laws exist to ensure that prices for public service are set according to government objectives. Where appropriations are necessary to compensate for services provided at below cost this may be provided by Congress (e.g. U.S. Postal Service); whereas for Power Marketing Administrations, rates are set to ensure cost recovery over a given period of time. These rates are considered by responsible government department and are approved by the regulatory body.

### 3.5. Tax neutrality

#### *Overview of findings*

In a majority of countries public undertakings are subject to the same or similar treatment (tax or regulatory) as private enterprises, especially where public undertakings are conducted as legally incorporated businesses operating at arm's length from the government. In these cases:

- SOEs incorporated under normal company law are for the most part subject to direct taxes in the form of corporate income taxation; and indirect taxes such as value-added taxation (VAT).

- Some exceptions apply to specific categories of SOEs which may be carrying out non-commercial objectives, such as universal service obligations (e.g. in postal sector), and which may exempt from tax on income derived from such obligations in addition to being exempt from paying VAT or charging VAT on these transactions.
- Statutory corporations may be exempt from certain taxes if specified by their statutory laws.

Where some categories of public bodies may be afforded tax advantages through partial or entirely exempt status (direct or indirect taxes or a combination of the two) (Australia, Finland, Russia, Spain, United Kingdom, United States). In these cases:

- undertakings are usually public bodies operating out of general government or at the state/municipal level;
- such undertakings may be subject to some other forms of taxation, depending on the public body and applicable tax laws; and/or
- tax exemptions may be provided as compensation for the provision of services of general economic interest (similar tax exemptions may also apply to similar private/non-profit businesses operating in the same sector).

Finally, a number of countries report that categories of SOEs may be *disadvantaged* due to different tax treatment. This is the case in Chile, Egypt and Israel where, in very specific cases, certain SOEs or public authorities are subject to higher corporate income tax rates (Chile, Egypt) or do not benefit from tax write-offs or refunds (Israel) as would apply to private companies.

**Table 3.9. Tax treatment of public undertakings relative to private undertakings**

Tax treatment of public undertakings		
<b>Equal tax treatment regardless of ownership</b>		Czech Republic, Denmark, Estonia, Germany, Greece, Hungary, Ireland, Italy, Mexico, New Zealand, Slovak Republic, Slovenia, Sweden, Turkey
<b>Similar tax treatment for public and private businesses*</b>		Australia, Austria, Brazil, Chile, Egypt, Iceland, Korea, Lithuania, Poland, Spain, Switzerland
<b>Unequal tax treatment</b>	<b>Advantages**</b>	Australia, Finland, Russia, Spain, United Kingdom, United States
	<b>Disadvantages**</b>	Chile, Egypt, Israel, Poland
*with exceptions		
**depends on status of public body		

Where differences in tax treatment exist, compensatory payments in lieu of taxation are not common practice in most countries. In Australia some form of tax neutrality adjustments are made in order to compensate for differences between public and private business tax treatment. In the United Kingdom, some SOEs are not liable for tax due to their government department status (e.g. Trading Funds); in these cases expectations placed on SOEs are adjusted to reflect this exempt status, for example in setting rates of return.<sup>54</sup> In Finland, income tax exempt state and municipal enterprises are still liable to a municipal and church tax (see below) depending on the type of commercial activity (e.g. if the activity falls outside a given municipality).

### ***Tax treatment of public bodies performing commercial activities***

Concerning tax treatment of public bodies performing commercial activities, most countries subject their SOEs or other public bodies to the same or similar treatment (tax or regulatory) as private companies. This is generally the case for incorporated SOEs; however, some exceptions do apply to

the tax treatment of such SOEs which perform commercial objectives alongside non-commercial objectives (e.g. fulfilling universal service obligations). Difference in tax treatment may be afforded due to the public bodies' legal status; generally if a public body remains integrated with general government such bodies may be exempt from direct and indirect taxes. In only a minority of cases, countries report that specific SOEs or government authorities are subject to tax disadvantages (Chile, Egypt, Israel, and Poland).

For EU and EEA countries, EU Rules on State Aid and the VAT Directive (Article 13) are applicable to the activities of public undertakings. Favourable tax treatment for public businesses, in some cases, is tantamount to State aid. The VAT Directive also considers the treatment of public bodies (Box 3.13). However, a recent EU Green paper points out that the conditions under which public bodies are VAT exempt may need to be clarified [see EU Green Paper on the Future of VAT (2010)].<sup>55</sup> Where country-specific practices are detailed among these countries or other respondents, they are provided below:

- In **Australia**, government businesses are subject to the same or different tax treatment as private sector companies, depending on the legal form and status: entities which are legally separate from the Commonwealth are subject to taxation; whereas Commonwealth entities cannot be taxed by any level government (with the exception of Fringe benefits, and goods and services taxes). Where separate legal entities are subject to taxation, exemptions from taxation may be provided in their enabling (or other) legislation.
- In **Austria, Korea, Lithuania, Poland, Switzerland, and Turkey** generally government bodies are subject to the same tax provisions as private businesses. However, some public companies may be treated favourably in terms of corporate income (Austria, Korea, Lithuania, Poland, and Switzerland) and VAT taxes (Austria); such exemptions are afforded in specific circumstances where public interest objectives are considered such as fulfilling universal service obligations in the postal sector (but also in other cases such as in health, education, or sanitation).
- In **Chile**, public enterprises reportedly pay higher income tax than private companies (40% of profits for statutory corporations). Most public companies are subject to the same VAT rules, but there are a number of exceptions.
- In **Egypt**, both public and private enterprises are subject to the same income and sales tax treatment, with a number of exceptions comprising of public agencies which are tax exempt where importing equipment and machinery (Rail and petroleum authorities). Two public authorities engaged in commercial activities are subject to higher income tax rates (Petroleum and Suez Canal Authorities).
- In **Finland**, tax treatment depends on the status of the public body. For incorporated SOEs, tax treatment (VAT and income tax) is the same as for private companies. However, so-called state and municipal enterprises are exempt from income tax, but are subject to VAT and a fixed tax which is paid in lieu of income tax (municipal enterprises are only subject to the fixed tax on operations outside of the particular municipality).
- In **Greece**, all profit-oriented legal entities are subject to income tax regardless of ownership. Any income tax exemptions that were provided to public or private companies by virtue of general or special provisions have been abolished as of April 2010, with a few exceptions.<sup>56</sup> Local authorities are also subject to income taxes on profits generated from commercial activity.

**Box 3.13. EU Commission VAT Directive –  
Article 13 (Application of VAT on transactions of public authorities)**

**Article 13**

1. States, regional and local government authorities and other bodies governed by public law shall not be regarded as taxable persons in respect of the activities or transactions in which they engage as public authorities, even where they collect dues, fees, contributions or payments in connection with those activities or transactions. However, when they engage in such activities or transactions, they shall be regarded as taxable persons in respect of those activities or transactions where their treatment as non-taxable persons would lead to significant distortions of competition. In any event, bodies governed by public law shall be regarded as taxable persons in respect of the activities listed in Annex I, provided that those activities are not carried out on such a small scale as to be negligible.

2. Member States may regard activities, exempt under Articles 132, 135, 136, 371, 374 to 377, and Article 378(2), Article 379(2), or Articles 380 to 390, engaged in by bodies governed by public law as activities in which those bodies engage as public authorities.

*Source:* EU Commission VAT Directive.

- In **Iceland**, state institutions and all state undertakings are exempted from income and property taxes. However, those involved in commercial activities do not benefit from different tax treatment. If tax exemptions do amount to an advantage, the advantage must be quantified and is considered as part of the compensation provided for discharging public services.
- In **Ireland**, public and private operators face the same/similar tax treatment. Based on decision from the European Court of Justice, since 2009 public bodies in Ireland are subject to charge VAT for all services which are provided in competition with private operators (e.g. in the provision of street parking, waste collection and recycling, recreation and amenities).
- In **Israel**, government companies are subject to the same tax treatment as private companies. In some cases, government companies are not provided tax benefits granted to privately-owned companies.<sup>57</sup>
- In **Poland**, public companies although subject to the same tax treatment as private companies (with a number of exceptions for public interest activities, e.g. hospitals, sanitary services), although companies wholly-owned by the state treasury are subject to an additional 15% tax on profits paid to the state budget; this tax is considered to be a disadvantage for Polish SOEs.
- In **Spain** and the **United Kingdom**, public and private operators are not always subject to the same tax treatment, for example not all public enterprises pay corporate tax<sup>58</sup> (state corporations do, while public trading and public law entities do not). In **Spain**, commercial activities (regardless of ownership) are subject to the VAT.
- In **Sweden**, incorporated SOEs are not treated differently than private companies; however, unincorporated public commercial activities are treated differently.
- In the **United States**, government agencies, government corporations, unincorporated enterprises and some enterprises which may not be directly operated by the government (but considered instrumentalities of States and political subdivisions, or providing an essential

government function) are usually not subject to federal/state income tax. However, a private corporation may be subject to similar exemptions from income tax under specific provisions of the tax code making its activities eligible for tax exemption requirements (e.g. a hospital).

#### **Box 3.14. Case study: Finnish Road Enterprise**

The former Finnish Road Enterprise (FRE) was a state enterprise entrusted, among other things, with maintenance of the Finnish road infrastructure. Private operators in the same field of business alleged, that bankruptcy protection and exceptional tax treatment of the state enterprise constituted state aid, as prohibited by the EU State Aid Rules.

A complaint was placed to the European Commission (by The Confederation of Finnish Construction Industries and Suomen Maanrakentajien Keskusliitto ry). The EU Commission held that:

- bankruptcy protection and exceptional tax treatment of the state enterprise as prohibited state aid (inapplicability of bankruptcy legislation and common Community taxation).
- approved the arrangements relating to the setting up of the Road Enterprise.
- *de facto* opening up to competition of the Finnish road service market was in the common interest.
- the EU Commission did not approve the allegation that FRE had exploited predatory pricing.

The FRE aid measures which were deemed to be prohibited were overturned, and from January 2008 the company was incorporated as a wholly state-owned limited company (Destia Ltd).

Source: Questionnaire response.

#### **Box 3.15. The tax neutrality system in Australia**

***According to the Australian Competitive Neutrality Guidelines (2004), there are three taxation neutralising systems that may apply to government business activities:***

- making the actual regulatory payment or fulfilling the actual regulatory obligation;
- making an equivalent payment to the Official Public Account; or
- notionally including regulatory payments in the business activity's cost base, and therefore prices, by an amount equivalent to any advantage they accrue by not being subject to similar regulatory arrangements or obligations as their competitors.

Source: Questionnaire response.

#### ***Compensatory payments in lieu of taxation***

Among countries which report difference in tax treatment for public undertakings, compared with similar private undertakings, only a few countries have put into place mechanisms which ensure that difference in tax treatment does not distort competition. These practices have been described below:

- In **Australia**, according to the *Australian Competitive Neutrality Guidelines (2004)* tax neutrality is to be maintained between government businesses and (potential) competitors. In order to ensure tax neutrality there are three tax neutralising systems that may apply to government business activity (Box 3.15).

- In **Finland**, although no tax neutrality adjustments are reported, income-tax exempt state or municipal enterprises are still liable for state/municipal and church taxes.
- In the **United Kingdom**, where an SOE is not liable to pay taxes but is performing activities on a commercial basis, the fact it does not pay tax goes in to the mix of factors when deciding the target rate of return.

### 3.6. Regulatory neutrality

#### *Overview of findings*

The regulatory treatment of public undertakings differs from country to country, and depends on the legal form of the public undertaking and any sector or statutory legislation/regulations which may apply. Generally, most incorporated SOEs are subject to the same regulatory regimes as private enterprises (Table 3.10). However there are a number of exceptions to the equal application of regulations; exceptions are usually found in the case of SOEs performing public interest activities. Regulatory advantages can take the form of exemptions from competition rules which may be laid out in specific provisions of market regulations that apply to sectors where SOEs or former SOE incumbents operate (often in sectors with natural monopoly characteristics, such as in the network industries or in the postal service). In the EU, treaty rules [Article 106 (2) TFEU] set out the conditions under which undertakings (public and private) providing services of general economic interest can be exempted from the application of competition rules.

Some public undertakings are subject to additional regulatory advantages in the form of lower compliance costs, which usually lowers the cost of doing business; whereas other regulatory advantages may be in the form of preferential treatment for public undertakings. Only a few countries report that their SOEs are subject to regulatory disadvantages (Austria, Finland, Mexico and United States;<sup>59</sup>) in these cases disadvantages may be attributed to more stringent requirements where public funds and public service obligations are concerned.

**Table 3.10. Regulatory (dis-)advantages faced by public undertakings**

<b>Regulatory neutrality</b>	
<b>Generally, similar regulatory treatment of public and private sector businesses (incorporated SOEs)</b>	Austria, Chile, Czech Republic, Denmark, Germany, Hungary, Israel, Italy, Korea, New Zealand, Slovak Republic, Spain, Sweden, Switzerland, Turkey, United Kingdom
<b>Different regulatory treatment<sup>60</sup></b>	
<b>Regulatory disadvantages</b>	Austria, Finland, Mexico, United States <sup>61</sup>
<b>Regulatory advantages</b>	Australia, Egypt, Estonia, Finland, Ireland, Lithuania, Russia, Slovenia, Switzerland
<b>Compensatory payments on the basis of regulatory advantages</b>	Australia, Estonia, Slovenia, Switzerland

There are some grey areas for what concerns public businesses which may be operated by departments or agencies which remain integrated with general parts of the government. Indeed, a significant level of controversy surrounding the regulatory advantages associated with public ownership is reflected in case studies reported by surveyed countries. In some cases this controversy arises due to the status of the government businesses; in other cases, controversy arises over specific exemptions (e.g. derogations from competition law, state action defence) afforded to public sector businesses entrusted with special or exclusive rights.

Where regulatory advantages exist for public undertakings, there are few countries which consider compensatory payments on the basis of such advantages. Methods for compensation are not always clear cut, except in the case of Australia which has specific guidelines in this respect.

### ***Regulatory treatment of public undertakings***

In most countries, public sector businesses performing commercial activities are subject to the same regulatory treatment as private sector businesses. In most cases, equal regulatory treatment is afforded to incorporated SOEs, with a number of exceptions as laid out either in sector legislation/market regulation (where natural monopolies are concerned) or in the statutory/enacting legislation concerning the enterprise in question. In the EU there a derogation from competition law can be granted on the basis of Article 106 (2) TFEU. This derogation can be granted to all undertakings regardless of ownership.

Some countries report that state-owned businesses may be afforded outright advantages over their private sector counterparts. In these cases, regulatory advantages can range from lower compliance costs (e.g. exempt or lower costs for permits, registration or licences), to outright exemptions from some laws (e.g. access to roads for truck transport on nights and weekends), or preferential treatment of public sector businesses (e.g. quicker approval of projects, exemptions from competition laws).

In some cases public businesses may be subject to more stringent regulatory requirements than private sector companies (Austria, Finland, Mexico and United States<sup>62</sup>). This may be due to more stringent requirements where the fulfilment of public service obligations is concerned. Where detailed national practices are provided, they are presented below:

- In **Australia**, regulatory advantages may take the form of exemptions from certain obligations to make certain payments or to undertake certain activities or perform activities in a certain manner.
- In **Egypt**, regulatory advantages take the form of market regulations which provide special privileges to SOEs/incumbents operating in specific sectors (e.g. airline, telecommunications, and public utilities). These advantages amount to privileged access to routes (airline), special or exclusive rights to operate networks, or exemptions from competition laws.
- In **Estonia**, regulatory advantages are afforded to SOEs in the form of special or exclusive rights to operate in specific reserved markets (e.g. oil stockpiling, piloting, or air navigation).
- In **EU and EEA Member States**, regulatory advantages (e.g. derogation from competition rules) are generally not permitted (under the TFEU) unless they are required to ensure the performance of services of general economic interest (SGEI). However, this derogation applies to all undertakings (public or private) equally. Furthermore, this derogation only applies insofar as the application of competition rules would *obstruct* the performance of the task of providing SGEI. The rationale and the conditions for derogation are described Box 3.16. As Article 106 (2) provides for an exception, it is interpreted strictly. State Aid rules always apply to SGEI.



**Box 3.16. Restricting competition for the purpose of ensuring the provision of services of general economic interest – The EU approach**

***Specific rules exist in the EU to that allow in exceptional cases to restrict competition only for the purpose of performing Services of General Economic Interest (SGEI):***

- Article 106 (2) TFEU provides a general derogation from the application of the Treaty provisions, and in particular from the competition rules. The derogation applies equally to public and private undertakings provided that the following conditions are met: (i) the undertaking in question must have been entrusted with the operation of a service of general economic interest; (ii) the application of the rules of the Treaty (including those on competition) would obstruct the performance (in law or in fact) of the tasks assigned to this undertaking and (iii) the development of trade is not affected to such an extent as would be contrary to the interests of the Union. As any exception the derogation of Article 106 (2) must be interpreted restrictively.
- The rationale for the derogation is that SGEI are services in the public interest but, for economic reasons, notably their non-lucrative nature, they might not be provided if reliance was placed exclusively on the market forces for their provision. By entrusting the task of performing SGEI to a particular undertaking (or group of undertakings), the State not only assigns responsibility to that undertaking for the provision of the SGEI but also grants it certain economic advantages in order to motivate it to undertake the non-lucrative service. The Court of Justice of the European Union has made it clear that undertakings providing SGEI should be given economically acceptable conditions so that they can perform their tasks in conditions of economic equilibrium.<sup>63</sup> This could justify restrictions of competition from individual undertakings in the economically profitable sectors. If competitors are allowed to cherry-pick the most profitable parts of the system, the provider of the SGEI would not be able to operate in economically acceptable conditions.<sup>64</sup> However, this does not justify the exclusion of competition as regards specific services dissociable from the SGEI, if these could be offered by other undertakings without compromising the economic viability of the SGEI.<sup>65</sup>
- In determining the necessity of the restriction of competition for the purpose of the performance of the SGEI in economic equilibrium, one needs to take into account the economic conditions in which the undertaking operates, in particular the costs which it has to bear and the legislation to which it is subject.<sup>66</sup>

Source: Questionnaire response.

- In **Iceland**, exceptions in the application of competition law are made for two state monopolies of commercial character (in alcohol and tobacco).
- In **Ireland**, preferential regulatory regimes may exist for public service providers operating at the local level. Outright exemptions may be afforded in the form of collection permits, registration processes; preferential treatment may be afforded to public sector operators in terms of quicker timescales to process projects (e.g. waste collection) or refusing to grant new entrants licences where public service companies are already operating (e.g. bus sector).
- In **Korea**, generally commercial activities of SOEs and other public bodies do not benefit from preferential regulatory treatment and are subject to competition laws in the same capacity. However, some companies maintain exclusive rights to carry out services and are provided derogations from competition laws and policies (e.g. electricity transmission and distribution, highway and rail).
- In **Russia**, public businesses may be afforded regulatory advantages in the form of exemptions from general competition rules (e.g. Atomic Energy Corporation and Property

Development Company) and other federal laws which may give undue advantages to economic entities owned by the state.

- In **Spain**, in principle the same regulatory regime is applicable to public enterprises conducting commercial activities and private enterprises. However, public enterprises may not be subject to the disciplines of competition law (antitrust rules) where it is operating by “own means of management” of the public administration

#### Box 3.17. Case Study: Swiss Post

The Swiss Post, a state-owned provider of postal services, was investigated by the Competition Commission to evaluate the effects of special provisions in the company’s regulatory framework which allowed the public operator to preferential access to roads not provided to private logistics service providers. The specific provision allowed the Swiss Post to use heavy weight trucks (> 3.5 t) at night and on Sundays for the transportation of postal goods related to its public service obligation. In addition, the Swiss Post was allowed to fill up to a quarter of its trucks with other goods it was transporting on a commercial basis. According to regulation, private competitors could only use smaller trucks (< 3.5 t) at night and on Sundays; however, they were free to conclude arrangements with the Swiss Post to transport parcels and mail at night.

The Competition Commission came to the conclusion that:

- the provisions afforded by the regulation clearly disturbed competition between the Swiss Post and its competitors;
- private competitors, especially those offering postal services, have a competitive disadvantage compared to the Swiss Post and that possible arrangements with the Swiss Post do not seem to be practical and attractive for those competitors; and,
- competitors may not be able to offer similar services (e. g. the A-Mail >50g) at a comparable price due to higher transportation costs.

The Commission issued a recommendation to the Federal Council to change the problematic provision, by abandoning special privileges of the Swiss Post or to allow competitors to operate under the same conditions. The issue has been addressed by the Federal Council within the context of the revision of Postal Law.

Source: Questionnaire response.

- In **Switzerland**, regulatory advantages for public enterprises may take the form of exemptions from certain laws (e.g. state-owned postal service allowed to transport mail on nights and weekends) to which private sector competitors may be obliged to follow. At the sub-national level, cantonal monopolies operating in specific sectors (e.g. salt or lottery companies) may be afforded regulatory advantages.
- In the **United States**, most government corporations implement public policies or programmes that are distinct from commercial activities of private enterprises. A number of regulatory exemptions may exist in line with these non-commercial activities. Where commercial activities are concerned, exemptions from US anti-trust laws may also apply to federal, State and local governments.<sup>67</sup>

#### *Compensatory payments made on the basis of regulatory advantages*

A compensatory payment made on the basis of regulatory advantages is not common practice in most countries. Only **Australia**, **Estonia**,<sup>68</sup> **Iceland**, **Slovenia**,<sup>69</sup> **Switzerland** report that such practices exist. Where such practices are described they are presented below:

- In **Australia**, according to the *Australian Competitive Neutrality Guidelines* (2004), SOEs which benefit from regulatory advantages are expected to make regulatory neutrality adjustments in order to level the playing field with any potential or actual competition (Box 3.18).

**Box 3.18. Regulatory neutrality adjustments – Australia**

***According to the Australian Competitive Neutrality Guidelines (2004), there are three regulatory neutralising adjustments that may apply to government business activities:***

- Notionally include regulatory payments in SOEs' cost base, and therefore prices, by an amount equivalent to any advantage they accrue by not being subject to similar regulatory arrangements or obligations as their competitors;
- Making the actual regulatory payment or fulfilling the actual regulatory obligation, where possible; and/or
- Making an equivalent payment where possible to the Official Public Account.

*Source:* Questionnaire response.

- In **Switzerland**, at the sub-national level, specific cantons may own monopolies in specific sectors (e.g. lottery or salt businesses) which are required to compensate for their privileged market access through providing funds for their local communities (e.g. funds for cultural promotion or other charitable activities).<sup>70</sup>

### **3.7. Debt neutrality and outright subsidies**

#### ***Overview of findings***

Sources of financing for state-owned companies and other public bodies differ from country to country. Where commercial activities are concerned, a majority of countries report that their SOEs (usually incorporated) are financed through the market according to the same terms as comparable private sector businesses. Sources of finance include commercial banks (state-owned or private), capital markets, government-owned credit institutions, as well as dedicated public funds. In some exceptional cases state-owned businesses are not permitted, by law, to obtain financing from the market. In these cases, financing is provided through national funds according to commercial principles, in other words lending is offered at similar rates as comparable private sector companies with at the same level of risk.

If the majority of SOEs obtain financing through market, it does not necessarily follow that they do not obtain unintended advantages due to their ownership. In fact, fifteen countries report that their SOEs benefit from some form of explicit, implicit or perceived guarantees which may afford preferential access to financing. Even where government guarantees are merely perceived by financial markets, it may result in lower interest rates and a preferential access to financing. Explicit guarantees include government backing of debt (e.g. bail outs, or temporary ownership) or other liabilities, which may apply for specific government-owned or controlled companies. Some other countries report that government guarantees of export credit institutions or other types of financial institutions allow for preferential treatment *vis-à-vis* financing from international financial institutions. However, such guarantees apply to both the activities of public and private institutions and thus do not necessarily pose neutrality concerns.

In almost all countries outright subsidies to government enterprises are not the usual practice, except in some countries where government companies are funded from the public budget to fulfil public interest activities (e.g. public service delivery, investment projects or other strategic activities).

Where undue advantages are afforded to government-owned or controlled companies by virtue of their ownership, some governments have put into place frameworks to ensure debt neutrality (Australia, New Zealand, Spain, Switzerland and Turkey). Frameworks vary from country to country, but may include compensatory payments, adjustments of lending rates according to benchmarked rates, and/or disclaimers on loan documentation.

### *Sources of financing for government businesses*

Sources of financing for government businesses differ from country-to-country. In most cases, SOEs (usually incorporated companies) seek financing on the market according to commercial rates, and in principle, according to the same terms as the private sector (for an overview, see Table 3.11). Sources of market financing can range from financing from commercial banks (state-owned or private), capital markets, government-owned credit institutions, or from local funds. In the case of a number of countries, state-owned businesses may not be allowed to borrow from the State for their commercial activities; whereas in others, the country's legislative framework may require SOEs to seek financing from the state (– in the latter cases, generally public funds lend to government-owned businesses at market rates (United Kingdom). Yet in other cases, prior ministerial approval may be required before going to the market for financing (New Zealand). Where state-owned businesses conduct specific activities in the public interest (e.g. public service obligations, invest in infrastructure or carry out other strategic objectives) these are often subsidised through the public purse. In most countries, and especially in EU and EEA countries (where EU Rules on State Aid apply), strict rules apply to the context in which public funds may be used to carry out public interest objectives (e.g. companies must keep separate accounts and may not use such funds to finance their commercial activities).

**Table 3.11. Sources of financing for public undertakings and advantages associated with ownership**

<b>Debt neutrality</b>		
<b>Generally, same treatment of public and private sector businesses (incorporated SOEs) for debt financing</b>		Chile, Czech Republic, Denmark, Germany, Ireland, Israel, Italy, Mexico, Poland, Slovak Republic, Slovenia, Sweden, United Kingdom
<b>Access to debt financing on preferential terms</b>	<b>Implicit or perceived guarantees</b>	Australia, Finland, Iceland, Korea, New Zealand, Switzerland, Turkey
	<b>Explicit guarantees*</b>	Chile, Egypt, Estonia, Israel, Mexico, New Zealand, Russia, Switzerland, United States
	<b>Specifics (export credit; project finance)</b>	Austria, Finland, Poland, Turkey
<b>Provision of subsidies (budget funds) for non-commercial activities</b>		Australia, Chile, Estonia, Germany, Iceland, New Zealand, Russia, Slovak Republic, Switzerland, United States
<b>Debt neutrality adjustments to compensate for the advantages</b>		Australia, Iceland, New Zealand, Spain, Switzerland, Turkey
*This category does not assume that explicit guarantees are provided to every SOE or public body engaged in commercial activity, it refers to case specific examples which have been cited in questionnaire responses (even if cited as exceptional cases)		

Specific country practices, where provided, are described below:

- The **Chilean** constitution prohibits the state or other SOEs to lend to government businesses; SOEs are capitalized through bank lending (private banks) or from financial markets. However, SOEs may receive budget transfers or capital increases if authorised by law, especially to deliver public services.
- In the **Czech Republic**, SOEs and other public bodies do not receive subsidies (direct or indirect); this is regulated by legislation in conformity with EU rules on State Aid.
- In **Egypt**, state-owned banks (and private banks) lend to SOEs. Direct subsidies are not provided.
- In **Estonia**, most SOEs raise funds in the market; however, some SOEs may be financed by the state budget where the SOE operates public service activities, and/or will raise returns for the shareholder.
- In **Finland**, sources of financing for government businesses may originate from a variety of sources at market rates. For municipal enterprises, lending is provided by a municipal credit institution specialised in financing local governments (*Municipality Finance Plc*); this institution is guaranteed by its Shareholders (local government pensions institutions, the state and municipalities), as such it receives funding on favourable terms, which in turn is to be conveyed to its customers (this is in line with the company's objectives).<sup>71</sup>
- In **Hungary**, financing may be provided by state-owned banks according to market rates, and according to EU Rules on State Aid.
- In **Iceland**, State institutions and undertakings benefit from guarantees ranging from unlimited to limited (including exemption from bankruptcy rules).
- In **Israel**, financing for SOEs is raised according to commercial market conditions, via private banks or by issuing bonds (marketable and non-marketable). Financing may be provided by the State where a company's principle objective is to deliver of non-profit public service obligations.
- In **Korea**, public institutions benefit from preferential access to financing (from state-owned or other financial institutions) due to their high credit rating and low risk of bankruptcy (regardless of the actually financial status of the institution). Although subsidies are generally not permitted, state-owned businesses may be reimbursed for losses incurred due to public service obligations.
- In **New Zealand**, for historical and legislative reasons a small number of public bodies (e.g. rail) are not permitted to borrow from the private sector without explicitly permission from the government; in these cases funding is provided rates consistent with commercial rates and cover the full costs of borrowing or prior ministerial approval is required before going to the market for financing.
- In the **Slovak Republic**, budgetary contributions from the central government or municipality may be provided to certain public bodies (budgetary or contributory agencies) conducting public service obligations. Public finances can be used strictly for the performing

of the main function of an agency which is a service in public interest. Any other subsidy to any enterprise must be in accordance with EU Rules on State Aid.

- In **Switzerland**, public companies (especially at the sub-national level) may benefit from subsidised finance to conduct public service obligations, to investment in infrastructure development or where they act according to specific strategic objectives.
- In **Turkey**, state-owned companies and local governments may benefit from guaranteed loans, usually to carry out investment projects. State-owned banks may lend to government businesses according to market rates.
- In the **United Kingdom**, SOEs are generally not allowed to borrow from the open market (to prevent them from benefiting from an implicit government guarantee) and must instead obtain finance from the National Loans Fund (NLF). The NLF must generally ensure that such loans are extended on commercial terms and this usually involves the borrower proving that the terms of the loan are indeed commercial by benchmarking it against the market.
- In the **United States**, most government corporations are self-financed and do not subsist by virtue of subsidised government finance. However, some entities can borrow from the U.S. Treasury should they encounter obligations that cannot be met through their own revenue stream (e.g. contingent liabilities that become actual obligations). In extraordinary circumstances, the government also can acquire temporary ownership of an entity. Other forms of financing include public debt financing.

### *Preferential treatment of SOEs and debt neutrality adjustments*

SOEs and other government businesses often benefit from preferential treatment in terms of access to financing; such advantages are usually in the form explicit, implicit or perceived<sup>72</sup> guarantees. Preferential access to financing for government-owned or controlled companies is often attributed to implicit guarantees, where the lender attributes a lower risk rating due to the implicit perception of government backing. Most countries do not allow outright subsidies of the commercial activities of SOEs and subject their SOEs to the same regulatory framework (e.g. no exemptions from bankruptcy laws) and lending conditions as private sector companies. However, a few exceptions apply where the government may provide outright subsidies to support state-owned businesses. In other cases, subsidised financing may be provided to sustain loss-making SOEs or other government-controlled companies which are too big to fail (e.g. for economic reasons or social reasons such as maintaining jobs).

Where undue advantages are afforded to government-owned or controlled companies by virtue of their ownership, some governments have put into place frameworks to ensure debt neutrality (Australia, New Zealand, Spain, Switzerland, and Turkey). Frameworks vary from country to country.

In the **EU (including EEA) member States**, the European Commission, in charge of State aid control, verifies whether the special status of certain public bodies confers upon them undue advantages with respect to their competitors (e.g. cheaper access to finance, direct or indirect subsidies). Any advantages could result in a decision to have them removed (Box 3.19).

### Box 3.19. Case Study: La Poste

In 2006, the European Commission informed the French authorities of its preliminary finding as to the existence of an unlimited state guarantee which resulted from the legal form of La Poste and which constituted State aid [within the meaning of Article 107(1) TFEU]. European Commission adopted a decision concluding that the French Post Office (La Poste) enjoyed an implicit State guarantee because of its special status as a public body ("Etablissement d'Intérêt Economique et Commercial"). This guarantee conferred an economic advantage over its competitors, which had to operate without such a guarantee, and therefore distorted competition on the postal markets. The EU Commission considered that La Poste's legal entity as governed by public law made :

- it immune from bankruptcy and insolvency procedures;
- applicability to the principle of last-resort state liability for the debts of legal entities governed by public law;
- transfer of the liabilities of an epic that has been wound up to another publicly owned establishment or to the State;
- Direct access to Treasury accounts.

The EU Commission called on France to withdraw the guarantee given, on all its liabilities, to La Poste by virtue of its legal form. French authorities challenged the findings presented by the EU Commission. However, the EU Commission ultimately ruled that the unlimited guarantee given by France to La Poste constituted State aid that is incompatible with the internal market. The Commission concluded that the conversion of La Poste into a public limited company, which took place on 1 March 2010, would remove *de facto* the unlimited guarantee that it enjoyed.

Source: European Commission questionnaire response and *Official Journal L 274, 19/10/2010 P. 0001 – 0053*.

Where details are provided, concerning the preferential treatment of government-owned or controlled business, and/or where specific debt neutrality frameworks apply, they are covered by reporting country below:

- In **Australia**, according to the *Australian Competitive Neutrality Guidelines* (2004), government businesses must adjust their cost base, and therefore prices, where they borrow money at preferential rates (e.g. rates which reflects the credit risk of the Australian government as opposed to rates that reflect the credit risk of that type of business activity). Government sector agencies borrowing from public budgets, receive funding with appropriate debt neutrality adjustments already incorporated into the cost of debt. Where government businesses borrow funds from the market, any cost advantages associated with public ownership can be adjusted through a debt neutrality payment to the Office of Public Accounts. Businesses may instead of a payment, make a notional adjustment (and include in its cost base) to neutralise debt.
- In **Chile**, specific SOEs may benefit from government-back guarantees on an exceptional basis. The Chilean government reports that it may be difficult to determine whether markets afford preferential treatment (e.g. to determine the price amount of other aspects of debt) of SOEs due to their public ownership.
- In **Egypt**, SOEs may be provided preferential access to financing in the form of indirect subsidies; this is particularly relevant where SOEs are in financial difficulty or to settle their debts with state-owned banks. Government-owned companies are subject to the provisions of the *State Companies' Law* which provides specific means to dissolve loss-making SOEs;<sup>73</sup>

these provisions may not apply in cases where the government maintains loss-making SOEs for social reasons (e.g. employment).

- In **Estonia**, the *State Budget Act* allows the government to fund SOEs where they may be in financial difficulty (e.g. to solve or prevent a financial crisis that could cause liquidity or solvency difficulties). The same Act allows for state guarantees of state business activities where these activities are linked to the performance of public duties. While credit is provided at market rates, financing may be cheaper if the financiers' risk assessment of the government business so decides (although this is reportedly not impacted by government treatment of SOEs).
- In **Finland**, although subsidised finance is prohibited (on the basis of EU Rules on State Aid), it is reported that SOEs may receive some degree of preferred treatment, and as a result discount on loan margins due to the perception of lenders of implicit backing by the State.
- In **Germany**, SOEs may have preferential access to financing due to a perceived lower risk assessment as derived from its public ownership (this does not preclude private sector companies being afforded financing at the same perceived risk rates).
- In **Iceland**, where guaranteed liabilities (and exemptions from bankruptcy rules) distort or threaten to distort competition, the advantages in accordance with EEA rules on state guarantees be compensated by way of guarantee fees or quantified and calculated as part of a public service obligations (in the case that the entity discharges public services).

#### **Box 3.20. Case Study: Russian federal budget subsidies to state-owned credit institutions**

According to a government decree passed in 2009, federal budget subsidies could be granted to Russian credit organisations to recover decreased income on loans granted to individuals for the purchase of cars (Decree № 244). The credit institutions eligible for subsidies were those with state participation (or their subsidiary banks and credit institutions) with a net worth of over a certain threshold and which provided preferential car loans. Only 8 credit institutions corresponded with the criteria for government subsidies.

According to the Russian competition authorities the decree:

- was economically unfounded;
- provided an undue advantage for banks with state participation; and,
- limited competition in the market of car loans.

The Competition authorities in Russia issued a decree which amended the previous one. The new decree (Decree № 855) extended the subsidies to any credit institution which participated in lending preferential car loans to individuals. According to the data available, more than 90 lending institutions applied for the participation in the programme, which was extended through 2010.

Source: Questionnaire response.

- In **New Zealand**, SOEs may benefit indirectly from their ties to the State as their risk rating is perceived to be lower due to perceived government backing. Loan documentation for the borrowings of SOEs is required to have an explicit disclaimer making clear that the Crown does not guarantee the repayment of debts of its subsidiaries.



- In **Spain**, the *Royal Decree 1373/2009*, stipulates that the extra costs associated with advantages associated with public ownership (e.g. debt, guarantees, safeguards) should be estimated and compensation should be provided to the Treasury taking into account the costs of such advantages.
- In **Switzerland**, where cantonal banks may be backed by government guarantees, it has become common for banks to provide compensation on the basis of such guarantees. In other cases, state-owned entities at the sub-national level may be afforded lower interest rates or access to finance on a preferential basis (due to perceived lower risk). However, such advantages may be difficult to identify and governments are reportedly reluctant to remedy them. The state-owned postal service, although not benefiting from explicit guarantees, pays dividends to the government; such payments may be seen as a “reimbursement” for the advantages associated with its public ownership.
- In **Turkey**, where government-guaranteed loans are provided to SOEs, public institutions and local governments, the government levies a guarantee fee for such loan arrangements.
- In the **United Kingdom**, the National Loans Fund ensures that its loans are extended on commercial terms by requiring the state-owned borrower to prove that the terms of the loan are commercial by benchmarking it against the market. Loans are strictly monitored to ensure that lending is not abused; as such it is illegal if loans are not paid back.

### 3.8. Public procurement

#### *Overview of findings*

In most countries, national public procurement rules have been adopted which incorporate aspects or elements of competitive neutrality and which take into account how state-owned businesses are allowed to participate as bidders. In these cases procurement rules aim to ensure that bidders (public or private) are afforded equal treatment in procurement; that procurement selection criteria and processes are non-discriminatory; that procurement procedures and results are transparent; and that the outcome of managed competitions leads to more efficient use of resources (value for money). Such principles are reflected in WTO Principles and within the EU (according to EU Directives on public procurement). Their implementation can be considered fairly broad. Only two countries report specific exceptions to these principles, where national suppliers are preferred over foreign suppliers (Egypt) or where specific suppliers may be preferred due to their specialised experience (Mexico).

A grey area which emerges from country practices concerns in-house procurement, especially where unincorporated government businesses are concerned. In a number of cases, in-house procurement is not subject to public procurement rules (Egypt, Estonia, Finland, Israel, Mexico, Poland, Spain, Switzerland, Sweden, and Turkey); as such competitive tendering may not be required. Some countries have very specific guidance establishing the situations in which in-house procurement is permitted and when such practices may be exempt from competitive tendering – this is the case in all EU countries if in-house procurement is in conformity with the criteria established by the Teckal judgement (Box 3.21), but also in Korea. Others report that all government bodies are treated the same in procurement processes, regardless of intra-governmental or extra-government supply.

Additional issues may arise, where SOEs run their own procurement and the extent to which national procurement laws apply to their procurement procedures. Where incorporated SOEs are concerned, a number of countries do not apply national procurement law to these enterprises as much

as such laws do not apply to private sector companies. In some cases, voluntary adoption of government procurement procedures is encouraged.

Some countries report disadvantages associated with public procurement procedures for government companies (Austria and Slovak Republic); this was mainly attributed to more complex and lengthy bidding processes as compared with private sector companies.

For the most part, governments do not report cases where controversy may have arisen in a procurement process, the exceptions being Slovenia and Sweden. Although some countries, among which EU member states are included, report that complaints mechanisms exist should such controversy arise.

### ***Public procurement rules that bear on competitive neutrality***

As described above, most countries have adopted national laws which ensure transparency and non-discrimination in the procurement process. In addition to national laws, EU member states are to conform with public procurement legislation enshrined in the EU Commission Directive 2004/18 on contracts for public works, public supply and public service which is the main set of rules on public procurement (Box 3.21). Any infringement of such rules can be brought to the attention of the EU Commission and may be examined by European Court of Justice; action may be taken.<sup>74</sup> Separate rules are set out in Directive 2004/17/EC (Utilities Directive) for water, energy, transport and postal services which extend coverage to private companies operating on the basis of special or exclusive rights where applicable award procedures apply. In general, economic operators are subject to the following principles as applicable in public procurement procedures: equal treatment, non-discrimination, transparency, proportionality and mutual recognition.

#### **Box 3.21. EU Rules on Public Procurement**

##### ***EU Directive on Contracts for Public Works, Public Supply and Public Service – Recital 4***

"Member States should ensure that the participation of a body governed by public law as a tenderer in a procedure for the award of a public contract does not cause any distortion of competition in relation to private tenderers."

##### ***Exceptions to in-house procurement in EU Member States – "Teckal" Judgement***

An exception is provided only for the procurement granted to public sector enterprise by public authority exercising functions of the founding body for the enterprise. In this case, there is no obligation to use public procurement procedures. This exemption, however, has very limited application and can only take place if the following three conditions are met:

- a)** an essential part of the public sector enterprise activity concerns the exercise of public duties in favour of that public authority;
- b)** a public authority exercises control over public sector enterprise equal to the control exercised over its own unincorporated entities, particularly involving the impact on strategic and individual decisions regarding the management of enterprise's matters; and,
- c)** the object of the procurement belongs to the core scope of business of public sector.
- d)** a further criterion, stemming from jurisprudence, necessitates the lack of private participation in the enterprise providing in-house services.

Source: Questionnaire response and ECJ judgements (Cases C-26/03, C-410/04).

Practices and applicability of general procurement rules may differ where in-house procurement practices are concerned. In EU Member States and EEA countries, for example, any contracting authority can be exempted from the scope of EU Public Procurement Directives if certain criteria as set out by the “Teckal judgement” (European Court of Justice) are met; these criteria clarify the notion of exceptions for in-house procurement (Box 3.21). Some EU countries report that a potential problem may arise where intra-governmental provision of services is provided from one part of the government (e.g. a municipal enterprise) to another, as current rules make it possible for authorities to strike direct agreements with these enterprises without going through public tender.

Although preference given to in-house procurement may not be common in practice, a number of countries report that their public businesses may demonstrate preference where in conformance with national rules and practice. Examples of country practices concerning the conditions under which SOEs and other public bodies are allowed to participate as bidders in competitive tendering or as in-house suppliers are provided below:

- In **Australia**, there is a primary obligation on government businesses to comply with the *Commonwealth Procurement Guidelines*. There is a secondary obligation on government businesses that they declare that their tenders are compliant with competitive neutrality principles. This is to ensure that all potential suppliers (public or private) have the same opportunities to compete for government contracts (Box 3.22).

#### **Box 3.22. Ensuring Competitive Neutrality in Managed Competitions – Australia**

The Commonwealth Procurement Guidelines (CPGs) articulate the policy framework and rules which govern agencies procurement activities. Potential suppliers must be treated equitably based on legal, commercial, technical and financial abilities in respect to their ability to provide the product or service. The CPGs do not allow for discrimination on the basis of origin or government ownership. This ensures that all organisations are not disadvantaged on the basis of their organisational structure when agencies are procuring goods and/or services. According to the *Australian Competitive Neutrality Guidelines* (2004), all agencies conducting a tendering process must include a requirement for public sector bidders to declare that their tenders are compliant with competitive neutrality principles. Should a public sector bid be successful, the business activity would need to assess the application of competitive neutrality in accordance with the Guidelines.

- In **Chile**, public procurement rules aim to give equal access and opportunity to all potential providers; such rules apply to the activities general government including non-incorporated government entities. Procurement offers, bids and results are made available to the public (in the majority of cases). Specific guidelines exist concerning the treatment of SOEs in public auctions (e.g. freedom to participate).
- In **Denmark**, beyond generally applicable EU rules on public procurement, importantly, SOEs are generally not permitted to participate in state-binding contracts to avoid risk of indirect state and other neutrality issues.<sup>75</sup>
- In **Egypt**, public tendering must be designed in accordance with the following criteria: publicity, equal chances, equality and free competition. However, public agencies may contract from each other directly without bearing on the provisions of the public procurement law. Furthermore, preferential treatment may exist for domestic firms (this is provided for in the public tenders’ law).
- In **Israel**, the State is subject to mandatory public procurement rules and is required to issue tenders for all procurement transactions, subject to limited exceptions prescribed by

regulations. Government companies and public corporations are also subject to similar public procurement rules. These rules also apply to procurement between the State and government companies. Only in exceptional cases an engagement of a government company by the State may be exempt from the tender requirement for reasons of proven public interest.

- In **Korea**, specific rules exist for public corporations and quasi governmental institutions' contracting and in general contracting law. These rules stipulate that public procurement contracts should be awarded on a competitive basis. However, a wide set of exceptional circumstances do allow for restricted or no competition in public contracts (e.g. in the case of natural disaster or for reasons of business confidence, size of contract, negotiated contracts, specific qualification requirements, etc.).
- In **New Zealand**, public procurement rules are consistent with competitive neutrality, as such they do not accord preferential access to or treatment of SOEs or other public entities; rather selection criteria places emphasis on value for money.
- In **Sweden**, beyond generally applicable EU rules on public procurement the national procurement act ensures that the participation of public bodies in tenders does not distort competition in relation to private tenders. However, procurement rules do not apply in the case of in-house procurement. Procurement rules contain specific provisions to exclude abnormally low tenders, where they are the result of competitive advantages that are wholly or partly funded by the government (these are said to apply generally to all EU Members States as stipulated in EU Directives concerning public procurement).
- In **Switzerland**, procurement provisions ensure the basic principles of transparency and non-discrimination (WTO). Public procurement rules do not apply to intra-government provision.
- In **Turkey**, public procurement enshrines transparency and non-discrimination; however the public procurement law has exceptions which apply to intra-government provision in specific cases as described by Article 3 of the Law.
- In the **United Kingdom**, beyond generally applicable EU rules on public procurement competitive neutrality in the procurement process has been considered by a number of government reports; these reports underline the role of competition and consumer tools to remedy any distortions that may arise in managed competitions.<sup>76</sup>

Additional issues may arise concerning how SOEs run their own procurement processes, the extent to which they involve other parts of the public sector as suppliers, and whether national public procurement laws apply. Specific country practices are reported below:<sup>77</sup>

- In **Austria** and the **Slovak Republic**, procurement rules only apply to the activities of some SOEs which are required to advertise bids for procurement; however it is reported that such requirements put SOEs at a disadvantage *vis-à-vis* competitors due to long and complex procedures which deter potential bidders from providing competitive bids.<sup>78</sup>
- In **New Zealand** they are not obligatory for SOEs and other Crown entities which operate on a commercial basis (although they are encouraged to follow these guidelines).
- In **Chile** how public auctions initiated by the SOE are to be carried out (e.g. equal treatment of participants, publicity of auctions). While incorporated SOEs are not subject to the government's public procurement rules.

### ***Incumbency advantages and compensation on the basis of such advantages***

In almost all countries no such advantages have been reported on by respondents. It is clear that in some cases controversy may arise, as Australia and at the level of the EU (and within EU countries), specific mechanisms have been set-up to receive complaints in cases of non-neutrality. For EU Member States, Directive 2007/66/EC sets out review procedures with regard to improving the effectiveness in awarding public contracts.

#### **Box 3.23. Case Study: Dala-Mitt rescue services in Sweden**

The local federation Räddningstjänsten Dala-Mitt (Dala-Mitt Rescue Services), is jointly owned by the Borlänge, Falun, Säter and Gagnef municipality (joining in 2011). Its main activity is to provide emergency response services to the Swedish Civil Contingencies Agency (MSB), a government agency. According to the procurement criteria as set out in the competitive tendering process, access to specialised training facilities is necessary in order to run the training courses. Specialised facilities authorised for such use are in public ownership, usually held at the municipally-owned training grounds held outside of Borlänge.

On three consecutive tendering processes, a private competitor (Niscayah) was refused access to the specialised training facilities outside of Borlänge. A complaint was submitted to the Swedish competition authority.

In this case, the competition authorities consider that:

- Refusal of access is a breach of the Competition Act as it distorts and impedes, by object or effect, the occurrence and development of effective competition in tendering for emergency response operation training for part-time fire-fighters in the area of mid-Sweden.
- Given that all specialised training facilities are in public ownership, refusing a private company access to key infrastructure makes it very difficult for other companies to compete in the market.

The competition authority has petitioned that Dala-Mitt Rescue Services may be prohibited through an injunction from refusing Niscayah AB access to training facilities at Bysjön training area for the purpose of providing emergency response operation training activities. The case is pending with the Stockholm City Court.

Source: Questionnaire response.

Where specific advantages arising out of public ownership as have been reported are presented below:

- In **Slovenia**, a complaint was received by the Ministry of Finance from a private laundry service provider concerning the equality of treatment among tenders in public procurement was breached. The claimant claimed that a public institution had commission laundry services from another public institution without going through a tendering contract. At the time of writing this report, the complaint remains unresolved.
- In **Sweden**, a branch of government called *Statistics Sweden* was alleged to offer lower prices when competing for contracts due to the advantages conferred by its status as an administration agency under central government. Other allegations have been made by private sector competitors concerning the level of competition for contracts which are awarded to subsidiaries of public enterprises, in the absence of procurement processes (Box 3.23).

## Notes

1. A recent study which attempted this task can be found as follows: OECD (2011), “The size and composition of the SOE sector in OECD countries”, *OECD Corporate Governance Working Papers*, No. 5, [www.oecd.org/daf/corporateaffairs/wp](http://www.oecd.org/daf/corporateaffairs/wp). The OECD Indicators of Product Market Regulation indicate the presence or absence of state-owned or state-controlled firms according to ISIC industry classifications, [www.oecd.org/eco/pmr](http://www.oecd.org/eco/pmr).
2. Although Finland seems to be moving towards full incorporation of its public enterprises according to the recent reform of the State Enterprises’ law and the draft amendment to the Local Government Act which is currently being considered.
3. It should be noted further that according to question 5, unincorporated business activity is reviewed by sector ministries, which seems to contrast with the answer provided in this question.
4. Hungarian law stipulates that unincorporated bodies cannot perform commercial activities. SOEs may operate as “business associations” but the same rules apply to other market participants as reflected in the 2006 reform of the Business Associations Act.
5. As far as respondents are aware.
6. Israel reports that no data is available on these types of public bodies. Japan, Korea, Lithuania, and Sweden do not report on such entities.
7. However, given the scope of the questionnaire answers are limited to “traditional” SOEs the responses from Chile do not go into detail about such activity and their competitive positions. National Health Supply Agency is *CENABAST*.
8. As a general rule, in Estonia economic and business activities are performed in the form incorporated companies (e.g. limited liability companies or foundations), other cases are reportedly rare exceptions to the rule.
9. Currently a parliamentary bill proposing an amendment of the Local Government Act is under way; it aims to reform the way municipal enterprises and agencies operate commercial to improve compatibility with EU regulations.
10. Entities falling within the scope of the Law 30/2007 on Public Sector Procurement, but to which only certain provisions are applied, such as public agencies or Social Security mutual insurance companies.
11. This table does not provide an exhaustive overview of country-specific experiences with structural separation; it merely attempts to demonstrate commonalities among various national experiences.
12. By way of example please refer to Part 3 of the Commonwealth National Competition Policy Annual Report 1997-98 found at:  
<http://www.treasury.gov.au/documents/176/HTML/docshell.asp?URL=structural.asp>.
13. Countries which did not report on such practices are excluded from the analysis in this section.
14. In the Czech Republic authorities review continued government stake and commercial objectives of both incorporated and unincorporated activities of government via sector ministries.
15. In Estonia, SOE oversight ministries report, on an annual basis, the need for continued government stake in SOEs under their administration.

16. In Germany, the Ministry of Finance and sector ministries conduct biennial reviews of SOE activities in which continued government stake is evaluated.
17. Although Switzerland reports that there is period review, it also reports that such processes are not institutionalised.
18. In Egypt, there is no legislation requiring such periodic review. However, review of government stake has been considered in the context of privatisation and liberalisation programmes taking place during the 2004-09 period; such reviews were stopped due to “political and labour pressures”.
19. Chile reports that such types of reviews (although not systematic) have led the government to sell its stake in companies in which it has been involved.
20. The Ministry of Finance in Ireland established a Review Group on State Assets and Liabilities in 2010.
21. In Mexico, laws provide means to review government stake in government business activity. Such reviews are generally conducted if there are specific contextual, political or strategic considerations.
22. On occasion the Crown considers the nature, composition and structure of its commercial activities.
23. Denmark reports that such a review may take place in the context of a competition investigation.
24. This Operational Efficiency Review looked at all government assets and the future strategy for each of such assets.
25. The Transparency Directive foresees certain threshold below which there is no obligation to separate accounts (see Box 6).
26. Country which report transparency and disclosure practices but do not provide details on such practices are the following: Brazil, Czech Republic, Ireland, Italy, Lithuania, Poland.
27. In Egypt the federal executive may also be involved.
28. Estonian SOEs also make board remuneration practices available to the public.
29. A number of countries do not report on this: Austria (n/a), Brazil, Germany (n/a), Greece, and Japan. All EU member states are to comply with the Transparency Directive which requires accounting separation for companies falling under the Directive.
30. For non-profit and HSHC companies.
31. Only for entities receiving Crown funding.
32. Not applicable for most SOEs.
33. But monitored.
34. Public service obligations are defined as follows: the organisation would not elect to do on a commercial basis, or that it would only do it commercial at higher prices; and the government does not, or would not require other organisations in the public or private sectors to undertake or fund.
35. EU Member States are bound to report the attribution of liabilities according to the EU Transparency Directive.

36. In accordance with Report of Contingent Liabilities for the State.
37. Attribution of liabilities is required by law, but no further information is provided concerning the standards that are enforced.
38. According to legislation (unspecified).
39. According to the questionnaire this practice is rare.
40. A number of countries do not report on these issues or consider them non-applicable: Austria, Brazil, Denmark, Germany, Greece, Hungary, Japan, Lithuania, and the Slovak Republic.
41. As a matter of principle, the risks should be borne by those best placed to manage them. The Australian Government should generally not accept risks which another party is better placed to manage.
42. Some liabilities are of such a magnitude that the government is required to step in and assume some of the risk (Royal Mail or nuclear liabilities).
43. [http://www.whitehouse.gov/sites/default/files/omb/circulars/a136/a136\\_revised\\_2011.pdf](http://www.whitehouse.gov/sites/default/files/omb/circulars/a136/a136_revised_2011.pdf)
44. <http://www.fasab.gov/pdffiles/sffas-5.pdf>. Government businesses may have to report liabilities differently depending on specific legislation pertaining to that enterprise. For example the US Postal Service must prefund all its pension liabilities under the Postal Accountability and Enhancement Act.
45. Most SOEs are non-profit enterprises.
46. Similarly, as seen in the following sections, some countries depart from other aspects of competitive neutrality (e.g. in the form of tax concessions or soft loan) in an attempt to compensate SOEs for public service obligations.
47. If these criteria are not met, compensation is not necessarily prohibited. Compensation is allowed as compatible State Aid if it complies with the conditions of the exemption decision. If it cannot be exempted, it can still be notified to the Commission and can be authorised. The new EU Decision and Framework on SGEI contains requirements regarding the Entrustment Act, the calculation of the compensation, control, etc. The Framework also explains a preferred methodology to calculate compensation (net avoided cost method) and provisions to determine “reasonable profit” where relevant.
48. All EU Member States are obligated to comply with the Transparency Directive which requires accounting separation.
49. <http://www.eftasurv.int>
50. Case C-280/00, Altmark Trans, 2003, ECR I-7747.
51. Commission decision of 28 November 2005 on the application of Article 86(2) of the EC Treaty to State aid in the form of public service compensation granted to certain undertakings entrusted with the operation of services of general economic interest (OJ L 312, 29.11.2005, p. 67) and Community Framework for State aid in the form of public service compensation (OJ C 297, 29.11.2005, p. 4).
52. Journal of Laws of 2011 No. 5, item 13.
53. Infringement under specific provision in the Competition Act: “State administration authorities during the performance of state administration, local self-administration authorities during the performance of self-administration and transferred performance of state administration, and special interest bodies during the



transferred performance of state administration must not provide evident support giving advantage to certain undertakings or otherwise restrict competition”.

54. Where SOEs are performing an economic activity in a market, state aid rules apply which generally means that preferential tax treatment is not permitted.
55. [http://ec.europa.eu/taxation\\_customs/common/consultations/tax/2010\\_11\\_future\\_vat\\_en.htm](http://ec.europa.eu/taxation_customs/common/consultations/tax/2010_11_future_vat_en.htm).
56. These include Bank of Greece, Public Debt Management Authority, New Economy Development Fund, and Workforce Employment Authority.
57. The rationale being that tax benefits to public companies would merely represent a transfer from “one pocket of the state to another”. This policy was reportedly confirmed by a Supreme Court decision.
58. State corporations in Spain and limited liability SOEs in the UK pay corporate taxes the same as the private sector. Whereas, public trading funds in the UK and Spain and public law entities in Spain are not subject to taxes.
59. For what concerns the United States Postal Service for non-competitive products and operations stemming from universal service or other obligations.
60. This table does not provide an exhaustive overview of country-specific experiences differences in regulatory treatment; it merely attempts to demonstrate commonalities as reported among various national experiences.
61. See FN 104.
62. See FN 104.
63. C-320/09 Corbeau [1993] ECR I- 2568-2569, para 15-18.
64. Ibid.
65. Ibid, para 19
66. Case C-393/92 Almelo, para. 49.
67. For State and local governments this exemption falls under the *State Action Doctrine* which in some circumstances allows for “anticompetitive restraints imposed by the States as an act of government” (*Parker v. Brown*, 1943). The *Local Government Antitrust Act of 1984* further prohibits antitrust damages against local governments and other governmental units established by State law.
68. Estonia responds that SOEs are making compensatory payments on the basis of regulatory advantages afforded to SOE which are provided regulatory exemptions to conduct public interest objectives. However, details on the modes/methods of compensatory payments are not provided.
69. Slovenia responds that compensatory payments are made on the basis of regulatory advantages afforded to the state-owned SID Bank, a development bank. However no details are provided on the nature of these regulatory advantages nor of the methods/modes of compensation.
70. Dependent on context this may be functionally equivalent to the corporate philanthropy demanded of SOEs in some emerging economies as part of their corporate social responsibility obligations.

71. *Municipality Finance Plc* operates under the oversight of the Financial Supervisory Authority. Finnish banks have called attention to this competitive neutrality issue on several occasions.
72. Perceived guarantees occur for example where a State has no intention of supporting an enterprise, but markets assume that it is so systemically or macro-economically important that it cannot be allowed to fail.
73. This law does not prevent SOEs from being subject to bankruptcy rules; however, it has reportedly been the preferred means to dissolve SOEs.
74. PP Directives 2004/17 on utilities, 2004/18 on “classical” procurement and 2007/66 on remedies shall be transposed into national legislation and infringement procedures may start on the basis of the breach of any of the three directives.
75. One exception is the bidding for concession contracts on the railway network, which are regularly won by the incumbent state-owned railway operator.
76. For instance, OFT report on “Assessing the impact of public sector procurement on competition” (2004), and the OFT report on “Commissioning and Competition in the Public sector” (2011).
77. In EU member states the applicability of EU rules may go beyond “public undertaking” to include “bodies governed by public law” (as applicable in Directives 2004/17/EC and 2004/18/EC, respectively). The EC reports that all utilities’ companies operating in EU Member States are to comply with the EC public. All utilities companies operating in EU Member States are to comply with the EU public procurement directives unless they are exempt under Article 30 of 2004/17/EC.
78. The example from Austria should take into account that public procurement exemption for its Postal Service is with regard to parcels and electricity aspects of its business.

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## ANNEX

### QUESTIONNAIRE

#### **PART A: Competitive neutrality framework**

1. Have the authorities in your country expressed commitment to address aspects or elements of competitive neutrality in the presence of government-controlled businesses?<sup>1</sup> In which laws, regulations, or guidance documents does this appear?<sup>2</sup>
2. Do the aspects or elements of competitive neutrality apply only to “traditional” SOEs, or also to other public bodies, including non-incorporated government activities (at the national or sub-national level)?
3. Which bodies are responsible for oversight, investigation and enforcement of competitive neutrality? In cases of non-compliance which types of remedies are taken (e.g. financial penalties, sanctions)?

#### **Part B: Disciplines bearing on competitive neutrality**

##### *Streamlining operational form of government business*

1. Please list the organisational forms of publically-owned corporate entities that participate in commercial activities (e.g. statutory corporations, limited liability companies). Do these differ at central and sub-national levels of government?
2. In addition to the entities listed above, are there public bodies operating in the commercial market as entirely unincorporated entities (e.g. departments of government)? If yes, please describe their organisational form and the goods/services being offered.
3. Insofar as commercial activities are being delivered by government entities, to what extent have they been structurally separated<sup>3</sup> from their public service activities?

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<sup>1</sup> In this questionnaire government activities that can be constituted as “business” are not limited to the entities traditionally referred to as SOEs. Commercial undertakings at the sub-national levels of government as well as from within the general government must also be considered. For example, they may be state or municipal agencies, state or municipal enterprises, and state-owned or municipally-owned (statutory) corporations.

<sup>2</sup> There may be various kinds of legislative responses to competitive neutrality including reforming the competition law, reform of other regulatory laws shaping the general economic environment, de- or re-regulation of industry-specific laws, or enactment of a particular competitive neutrality law. There may be a policy response to competitive neutrality problems *without* legislative reforms including changing ownership policies or private industry-specific by-laws.

<sup>3</sup> Structural separation implies division of a formerly integrated entity into competitive and non-competitive parts. There are different types of separation ranging from accounting, functional or corporate

4. In the above cited example(s), the government has decided not to structurally separate commercial from non-commercial activities, owing to the following reasons:

*Please tick one or more of the below that apply and provide a brief justification.*

- ☐ To maintain public service obligations (please describe) \_\_\_\_\_
  - ☐ To pursue industrial policy objectives (please describe) \_\_\_\_\_
  - ☐ To protect fiscal revenue (please describe) \_\_\_\_\_
  - ☐ To protect political or strategic interests (please describe) \_\_\_\_\_
  - ☐ On efficiency grounds (e.g. economies of scale reaped from joint provision of commercial and non-commercial activities) (please describe) \_\_\_\_\_
  - ☐ Costs outweigh the benefits (please describe) \_\_\_\_\_
  - ☐ Infeasible (e.g. intertwined production processes or dependence of the same physical or human capital) (please describe) \_\_\_\_\_
  - ☐ Other (please describe) \_\_\_\_\_
5. Is there a periodic review of the need for continued government stake/control in incorporated or unincorporated business activity? If so, is there a regular review of the relevance of commercial objectives?

#### ***Identifying the costs of any given function***

6. Please describe transparency and disclosure practices and requirements of incorporated *and* unincorporated business activity operating at the central *and* sub-national levels of government (including from within general government). In particular, are state-controlled companies subject to disclose financial and non-financial information related to the company's accounts (e.g. financial assistance including guarantees). Is this made available to the public (e.g. through annual reports)? Are business activities subject to internal or external audit procedures?
7. Do public bodies performing commercial activities separate their accounts to demonstrate how their budget and cost structure is divided between purely commercial and public interest objectives (e.g. accounting separately for public service obligations)?
8. How do you handle the attribution of liabilities (including contingent liabilities) in public bodies pursuing both purely commercial and public interest objectives? Are there standards or guidelines to ensure reporting of liabilities?
9. Specifically, where public bodies perform commercial activities, how do you deal with public sector pension liabilities? Are they reflected in the SOEs/public body's balance sheets?

#### ***Achieving a commercial rate of return***

10. Are there any rate of return requirements imposed on goods and services offered on a commercial basis by SOEs and other public bodies? How are these defined (i.e. for example does government business pay a market-consistent rate of return that is comparable with what is earned by the majority of firms within the same industry)?

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separation, to ownership separation, club ownership, and separation of ownership from control. Type of separation may depend on the nature of the company and sector/industry.

11. Please provide an overview of regulated markets where government-owned businesses are operating, including how they co-exist with private competition.

### ***Public service obligations***

12. Please describe how the authorities compensate for the provision of public service obligations. Are there means to avoid over compensation for the provision of public services?
13. Is there legislation or regulation to ensure adequate and transparent compensation? Does sector regulation (e.g. financial, infrastructure) impose additional requirements in this respect?
14. Are government-controlled commercial entities allowed to compensate for public service provision by cross subsidising from more profit-oriented activities? If so, how is adequacy of the compensation assessed?

### ***Tax neutrality***

15. Do public and private operators face different tax treatment on commercial activities as a result of their ownership structure? If yes, please describe how (i.e. differences in corporate tax treatment or VAT rules). Specifically, are unincorporated government businesses, public statutory corporations, or commercial activities operating from within government treated differently in this respect?
16. For those entities that face different tax treatment, is there a system of compensatory payments in lieu of taxation?

### ***Regulatory neutrality***

17. Are there examples of public owned enterprises and other public bodies conducting commercial activities benefitting from a preferential regulatory regime? This might include lenient regulatory treatment of entities owned distinctly by the state, including financial institutions or locally-owned enterprises (e.g. vis-à-vis zoning regulations, licences, property rights, and building permit regulations). This might also include exemption from the application of general rules on competition.
18. If so are compensatory payments made on the basis of these regulatory advantages?

### ***Debt neutrality***

19. Do SOEs and other public bodies, including non-incorporated government activities conducting commercial activities, benefit from subsidised finance? Are they receiving financing from state-owned banks or other SOEs? Is there any form of regulatory control on such direct and indirect subsidies for state owned enterprises? What are criteria which inform the regulatory review of such subsidies?
20. Do they have cheaper access to finance in the market place due to their special situation (i.e. due to government backed guarantees, exemption from bankruptcy rules or other preferential treatment)? If yes, is the government seeking to remedy these advantages (i.e.

levies to compensate for cheaper access to finance, reimbursements for difference between theoretical and actual funding costs)?

### ***Public procurement***

21. Please describe rules for public procurement bearing on competitive neutrality. Do they apply equally to intra-government provision by non-incorporated entities?
22. Have remaining incumbency advantages been alleged (e.g. by private sector competitors)? If so, please describe. Have there been any attempts to compensate on the basis of these advantages?

### **Part C: Case Studies**

The Secretariat would appreciate country examples of concrete cases where controversy has arisen concerning the competitive neutrality of the activities of either SOEs, enterprises owned by sub-national levels of government, or unincorporated public sector business activities. For each example, you are invited to use the following template.

<b>CASE STUDY TEMPLATE</b>	
Please describe the institutions/businesses involved.	
What was the overall nature of the controversy?	
In your view, which one of the following six competitive-neutrality related points were involved in the contestation?	<input type="checkbox"/> Low rate of return requirements for the public business <input type="checkbox"/> Incorrect compensation for public service obligations <input type="checkbox"/> Discriminatory tax treatment <input type="checkbox"/> Regulatory differences <input type="checkbox"/> Unequal access to finance or different funding costs <input type="checkbox"/> Public procurement practices <input type="checkbox"/> Other (please describe)
Through which mechanism was the controversy addressed (e.g. complaints office, competition authority)?	
What were the main outcomes of the investigations/complaints handling?	
In the case of departures from competitive neutrality, were any remedial steps taken (prohibitions, warnings, financial compensation)?	



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