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The Promotion of Competitive Neutrality by Competition Authorities

Contribution from Lithuania

1. Introduction

1. This Note overviews the legal framework for ensuring competitive neutrality in Lithuania. In particular, it discusses application of competition law to public enterprises as well as powers of the Lithuanian competition authority related to ensuring of equal competitive grounds for public and private economic entities. It also presents experience of the Lithuanian competition authority with a view to creating a level playing field for the competing public and private enterprises. Several advocacy activities are discussed in the Note to show how the respective powers of the Lithuanian Competition Council are implemented in practice.

2. The issue of competitive neutrality proved to be especially prominent in the development of conditions for in-house transactions in Lithuania. On the one hand, exception for in-house contracts is generally recognised under the public procurement law of the European Union. On the other hand, experience of application of this exception in Lithuania showed that it may often restrict competition by impairing competitive neutrality. This tension resulted in rich results both in terms of case-law and legislative activity. Main developments pertaining to in-house contracts in Lithuania are discussed in this Note.

2. Legal framework for ensuring competitive neutrality

3. According to the Lithuanian Constitution, the economy of Lithuania is based on the right of private ownership¹. However, state-owned enterprises play an important role in the Lithuanian economy offering services in some sectors including utilities and infrastructure (energy, transport, waste management, water supply, etc.). Where competition between private and public enterprises is ensured, it can contribute to increasing consumer welfare and providing better products at lower prices. Nonetheless, public enterprises may sometimes benefit from advantages conferred upon them by existing legislative and administrative frameworks, which may have an effect on the quality and prices of the goods and services they provide.

4. The Lithuanian legal framework establishes several safeguards regarding competitive neutrality aiming to ensure that competition between enterprises is not unduly restricted. First of all, the Lithuanian Competition Law prohibits enterprises from performing acts which restrict or may restrict competition, regardless of the character of

¹ Article 46 of the Lithuanian Constitution stipulates that “The economy of Lithuania shall be based on the right of private ownership, freedom of individual economic activity, and economic initiative. <...> The law shall prohibit the monopolisation of production and the market, and shall protect freedom of fair competition.”

their economic activity². This means that competition law applies to all economic entities without distinction as to their legal status or ownership.

5. In addition, in order to maintain competitive neutrality throughout the decision-making processes, Lithuanian public authorities are obliged to ensure freedom of fair competition in carrying out the assigned tasks related to the regulation of economic activities. They are prohibited from adopting legal acts or other decisions which grant privileges to or discriminate against any individual undertakings or their groups and which give or may give rise to differences in the conditions of competition for undertakings competing in a relevant market (except where the different competitive conditions may not be avoided when meeting the requirements of the parliamentary laws)³. The Lithuanian Competition Council is empowered to enforce against decisions of public authorities which restrict competition including when respective decisions of public authorities discriminate between state-owned enterprises and their private competitors, or between several privately-owned enterprises. These enforcement powers contribute to ensuring that competing enterprises would be subject to equivalent competitive conditions, irrespective of their ownership, location or legal form.

6. Furthermore, seeking to ensure that no enterprise, regardless of its ownership or legal form is granted any undue advantage, public authorities initiating new or amending existing legal acts have an obligation to conduct competition impact assessment, if the proposed regulation may impact competition⁴. For example, recognising the competition distortion risks inherent in engagement of state-owned enterprises in economic activities, such competition impact assessment is mandatory before establishing municipal or state-owned economic operators⁵. The Lithuanian Competition Council provides consultations to bodies initiating amendments of legal acts regarding methodology of competition impact assessment.

7. Moreover, Lithuanian competition authority upon request and on its own initiative examines draft legal acts and submits conclusions regarding their impact on competition to the National Parliament and the Cabinet of Ministers. The Lithuanian Competition Council also has the power to submit to the Cabinet of Ministers proposals regarding necessary amendments of laws and other legal acts in force, after identifying unjustified restrictions of competition⁶. Both of these statutory powers may in particular be relied upon in situations where competitive neutrality is endangered by draft legislative acts or legislative acts already in force.

8. Insofar as municipal enterprises are concerned, there are certain limitations to their activities according to the Lithuanian Law on Local Self-Government⁷. Municipalities may decide to engage in new economic activities (through controlled companies) only upon the receipt of a prior consent of the Lithuanian Competition Council and when:

1. a new economic activity is necessary in order to serve the common interest of the local community; and

² Article 2(1) of the Lithuanian Competition Law.

³ Article 4 of the Lithuanian Competition Law.

⁴ Article 4¹(1) of the Lithuanian Competition Law.

⁵ Article 4¹(1)(17),(19),(20) of the Lithuanian Competition Law.

⁶ Article 18(1),(3),(7),(8) of the Lithuanian Competition Law.

⁷ Articles 9¹(1),(2),(4) of the Lithuanian Law on Local Self-Government.

2. taking into consideration their commercial interests, other economic entities would not engage in such activity or would not engage in full which is necessary in order to serve the common interest of the local community; and only
 3. if this will not grant privileges or discriminate individual economic entities or their groups.
9. In order to get a consent of the Lithuanian Competition Council to engage in a new economic activity, the municipality must conduct the competitive tender of selection of a provider of respective goods or services. The competitive procedure must be such that it would reveal whether or not other economic entities who are already operating (or are potential operators) in the market may, taking into account their commercial interests, ensure the provision of needed goods or services. These legal provisions aim at limiting involvement of municipal enterprises in economic activities when private companies are already pursuing them. Indirectly, this legal framework also contributes to the competitive neutrality since involvement of municipal enterprises in economic activity inherently tends to distort the level playing field. However, Lithuanian Law on Local Self-Government also provides for a number of exceptions for this mechanism which reduces its effectiveness in practice.

3. Advocacy of the Lithuanian competition authority aiming at competitive neutrality

10. Some of the activities of the Lithuanian competition authority aiming to create a level playing field for the competing public and private enterprises are overviewed below.
11. Recently, the Lithuanian Competition Council examined a case⁸, in which an applicant claimed an alleged infringement of the competition law due to the restriction of competition imposed by the Palanga City Municipality.
12. The first part of the complaint referred to the alleged conflict of interest, where, on the one hand, the Palanga City Municipality acted as a supervisor of the economic activity pursued by administrators of multi-apartment buildings and, on the other hand, its controlled company *Palangos komunalinis ūkis* was engaged in this economic activity.
13. With regard to the first part of the complaint, the Lithuanian Competition Council found that, in that case, there were no grounds for initiating an investigation into an infringement of the Lithuanian Competition Law. Although there was a risk of restricting competition due to a potential conflict of interest, but the mere risk did not in itself constitute a restriction of competition. In other words, the investigation could not be launched on the basis of a mere potentiality of restriction of competition, without having evidence of the actual restriction of competition.
14. Another part of the complaint referred to the alleged cross-subsidisation between the activities of the municipal enterprise which also received funding from the municipality for city maintenance. The complainant regarded such actions as an instance of actual restriction of competition by Palanga City Municipality. However, the Lithuanian Competition Council also refused to examine these actions because this would not correspond to the priority of activities⁹ established by the Lithuanian competition authority.

⁸ Decision of the Lithuanian Competition Council on refusal to open investigation of actions and decisions of Palanga city municipality entrusting the provision of multi-apartment buildings common use objects' management and maintenance services, 12 January 2021, No. 1S-2 (2021).

⁹ The Lithuanian Competition Council's Resolution No 1S-89 as of 2012-07-02 on the enforcement priority of the Lithuanian Competition Council while implementing the supervision of the Law on

Such decision was based on facts that respective actions of the Palanga City Municipality presumably had had insignificant impact on competition (due to the scale of potential infringement), while investigation of such actions would have required disproportionate resources from the competition agency.

15. Despite its refusal to open the investigation concerning the alleged infringement of competition law, the Lithuanian Competition Council noted that the Lithuanian legislation in force did not impose an obligation on the municipalities to monitor, how their controlled companies ensure separation of different activities and distribution of revenues from the provision of public services entrusted by the municipalities and services provided on competitive markets. The absence of such rules poses a serious risk of a restriction of competition. Municipal enterprises may benefit from the municipality's resources allocated to the provision of public services using them for the provision of commercial services. Thereby, municipal enterprises are enabled to operate on the market on more favourable terms than other economic operators.

16. Consequently, the Lithuanian Competition Council submitted a proposal to the Lithuanian Cabinet of Ministers on the amendment of local self-government laws. It suggested to improve the governance of municipal enterprises by requiring a separation of accounting for the provision of public services entrusted by the municipality and for the provision of commercial services. Such change would make the accounting of municipal enterprises more transparent and contribute to ensuring effective competition in markets where both state-owned enterprises and private companies compete. Following this proposal of the Lithuanian competition authority, the Ministry of Economy replied that requirements to separate activities of municipal companies are generally enacted in law. However, recommendations for methodology of such separation were amended on the basis of the proposal of the Lithuanian Competition Council, with a view to making the legal framework clearer and more effective¹⁰.

17. While pursuing pro-competitive advocacy, the Lithuanian Competition Council has recently issued its opinion concerning rules governing activities of tourism information centres¹¹. First of all, the Lithuanian competition authority pointed out that tourism information centres engage in economic activities and hence are subject to principle of competitive neutrality. Possible economic activities of tourism information centres consisted in services related to travelling and tourism, including intermediating between tourists and providers of accommodation and transportation services. National laws entrust municipalities with a responsibility of creating conditions for the development of tourism, promoting such activities¹² and entitle them to establish tourism information centres¹³. However, tourism information centres may be established not only by municipalities but also privately by other legal persons, whenever requirements for the tourism information centres are met.

Competition, point 1: "Establish that the Competition Council's Enforcement Priority is to conduct investigations or otherwise intervene in the functioning of the market, only if such intervention could significantly contribute to the effective protection of competition and ensure the highest possible benefits to consumers".

¹⁰ Resolution of the Minister of Economy No. 4-1036, as of 29 September 2021.

¹¹ The Lithuanian Competition Council's letter No. (2.11MR-45)-1041, as of 16 July 2021.

¹² Article 6(38) of the Lithuanian Law on Local Self-Government.

¹³ Article 40(1)(4) of the Lithuanian Law on Tourism.

18. The Lithuanian Competition Council considered that participation of municipalities in economic activities through their tourism information centres may cause the risk of breaching provisions of Lithuanian Competition Law prohibiting anti-competitive actions of public authorities, because of possible:

1. conflict of interest arising from the municipality's participation in the tourism services market, which it regulates;
2. non-transparency of financing the municipality's commercial activity;
3. ineffectiveness, where municipal tourism information centres may be granted more favourable conditions to operate in the market or protected against more efficient private competitors;
4. unlawful state aid.

19. In this context, although national laws allow establishing municipal tourism information centres by municipalities, this right must be exercised without prejudice to the Lithuanian Competition Law. Decision to establish the municipal tourism information centre should be adopted after an assessment, whether its services are necessary in order to serve the common interest and other economic entities would not engage in such an activity, taking into consideration their commercial interests¹⁴. Moreover, the activities of existing municipal tourism information centre should not be privileged compared to similar activities of other tourism information centres or other tourist services providers.

20. In summary, while the Lithuanian laws allow establishing tourism information centres by both municipalities and private entities, in accordance with the principle of competitive neutrality which is embedded within the Lithuanian legal framework, it is essential to ensure that municipalities would set up their tourism information centres only after assessing the merits of their establishment, and that they would not adopt decisions which favour municipal entities against other economic operators. Following this letter of the Lithuanian Competition Council, the Lithuanian Ministry of the Economy and Innovation drafted amendments to the Law on Tourism which narrow down the scope of activities of tourism information centres. These amendments would limit the services provided by tourism information centres to only informational ones which, allegedly, could be non-economic. Thus, the risk of impairing competitive neutrality by benefiting tourism information centres would be minimised if respective amendments of the law were enacted.

21. Examples provided in this section of the Note illustrate the practical implementation of legal safeguards in Lithuania aiming at establishment of the level playing field between public and private enterprises. Still, competitive neutrality should be seen as a constant goal which requires continuous attention and commitment on the part of the Lithuanian Competition Council and other Lithuanian public authorities.

4. Competitive neutrality and in-house transactions with state-controlled enterprises

22. In Lithuanian experience, one of the serious risks in terms of competitive neutrality is an exception from the public procurement rules allowing direct purchase from the state-owned enterprises under certain conditions (in-house exception).

¹⁴ See Article 9¹ of the Lithuanian Law on Local Self-Government which is discussed in Paragraphs 8 and 9 of this Note.

23. European Union public procurement rules (which are mirrored in Lithuanian national law) provide for an exception allowing direct purchase from the legal person where:

1. the contracting authority exercises a control over that legal person which is similar to the control which it exercises over its own departments;
2. more than 80% of the activities of that legal person are carried out in the performance of tasks entrusted to it by the controlling contracting authority or by other legal persons controlled by the latter; and
3. there is no direct private capital participation in that legal person¹⁵.

24. From the perspective of competitive neutrality, application of the in-house exception without additional safeguards may result in a distortion of competition in relation to private economic operators, insofar as it places a public provider of services in a position of advantage vis-à-vis its competitors. Therefore, the Lithuanian Competition Council argued that provisions of Lithuanian Competition Law prohibiting anti-competitive decisions of public authorities are applicable to in-house transactions and limit the possibilities to conclude them. The Lithuanian Competition Council decided in several cases¹⁶ and the Lithuanian Supreme Administrative Court confirmed¹⁷ that notwithstanding the in-house exception, public authorities must respect Article 4 of the Lithuanian Competition Law which prohibits direct award of contracts as distorting competition, even when conditions of the in-house exception are satisfied.

25. Such interpretation of the laws, when in-house transactions had been subject not only to in-house conditions based on EU law but also to requirements of the Lithuanian Competition Law, was questioned by the Supreme Court of Lithuania which referred the case to the Court of Justice of the European Union requesting the preliminary ruling¹⁸.

26. The Court of Justice of the European Union ruled in the case C-285/18 *Irgita* that it is open to a Member State to impose on a contracting authority additional conditions for conclusion of in-house contracts which are not laid down in EU rules on public procurement. The EU Court held that the conditions applicable to in-house transactions must be made known by means of precise and clear rules of the substantive law governing public procurement which must be sufficiently accessible, precise and predictable in their application to avoid any risk of arbitrariness¹⁹.

27. In line with this preliminary ruling of the Court of Justice of the European Union, currently all the conditions for conclusion of in-house contracts are provided for by the

¹⁵ Article 12 of the Directive 2014/24/EU of the European Parliament and of the Council of 26 February 2014 on public procurement and repealing Directive 2004/18/EC (OJ 2014 L 94, 65), see also Article 10(1) of the Lithuanian Law on Public Procurement.

¹⁶ Decision of the Lithuanian Competition Council on decisions of Kaišiadorys district municipality regarding waste management services, 26 June 2014, No. 2S-6/2014; decision of the Lithuanian Competition Council on decisions of Kaunas city municipality regarding cemetery maintenance services, 2 May 2016, No. 2S-4/2016.

¹⁷ Judgement of the Supreme Administrative Court of Lithuania, 29 March 2016, No. A-347-552/2016; Judgement of the Supreme Administrative Court of Lithuania, 26 January 2018, No. eA-1475-556/2018.

¹⁸ Decision of the Supreme Court of Lithuania of 13 June 2018 in case No. e3K-3-120-469/2018.

¹⁹ Court of Justice of the EU, Case C-285/18 *Irgita*, paragraphs 49 and 57.

Lithuanian Law on Public Procurement²⁰. In addition to the above-mentioned conditions²¹ for in-house contracts which are established in EU law, there are two sets of alternative additional requirements in Lithuanian national law.

28. According to the first alternative, the Lithuanian Law on Public Procurement stipulates that in-house transactions may be awarded subject to the condition that the continuity, good quality and availability of services cannot be ensured if they are purchased through public procurement procedures²².

29. According to the second alternative which can be relied upon only by municipalities²³, a municipality may conclude an in-house transaction with regard to:

1. water, heat supply, wastewater and waste management, passenger transport, territorial and street maintenance, catering services, social or healthcare services, or
2. the provision of public services where it requires the management and use of immovable property of municipality or municipal enterprise and no other economic entity is able to provide such services on its own premises, or
3. the Lithuanian Competition Council's consent was received for the establishment of a new legal person or entrusting the provision of public services engaging in an economic activity to the existing legal person managed by the municipality²⁴.

30. Consequently, the contracting authority intending to rely on an in-house exception will have to ensure that conditions set in Lithuanian Law on Public Procurement are satisfied. However, even within this reviewed framework of in-house transactions in Lithuania, there is room for enforcement of provisions of the Lithuanian Competition Law prohibiting anti-competitive actions by public authorities. This is exemplified by the recent case of the Lithuanian competition authority against Palanga City Municipality which is discussed below.

31. The Lithuanian Competition Council found in its recent decision²⁵ that the Palanga City Municipality exceeded the scope of the in-house exception and restricted competition by entrusting the company *Palangos komunalinis ūkis* with provision of territorial management and maintenance services.

32. First of all, the Lithuanian Competition Council pointed out that part of the services procured by the Palanga City Municipality from the company *Palangos komunalinis ūkis* via in-house transaction satisfied the requirements of the Public Procurement Law. To this extent, no violation was found. However, the Lithuanian Competition Council also held

²⁰ However, one of the conditions for in-house contracts is actually stipulated in Article 9(2) of the Lithuanian Law on Local Self-Government but this provision is explicitly referred to in Article 10(2)(2) of the Lithuanian Law on Public Procurement.

²¹ See Paragraph 23 of this Note.

²² Article 10(2) of the Lithuanian Law on Public Procurement.

²³ Article 9(2) of the Lithuanian Law on Local Self-Government, as referred to in Article 10(2)(2) of the Lithuanian Law on Public Procurement.

²⁴ As required by the Article 9¹ of the Lithuanian Law on Local Self-Government, this provision is discussed in Paragraphs 8 and 9 of this Note.

²⁵ Decision of the Lithuanian Competition Council on decisions of Palanga City Municipality entrusting *Palangos komunalinis ūkis* the provision of Palanga city territorial management and maintenance services, 13 July 2021, No. 1S-75 (2021).

that the Palanga City Municipality acquired from *Palangos komunalinis ūkis* several categories of services²⁶ which did not fall under the category of services which were permitted as an object of the in-house transaction. The Lithuanian Competition Council specified that in-house transactions, as an exception, must be applied narrowly only to the extent which is allowed by the Lithuanian Law on Public Procurement. Therefore, the respective actions by the Palanga City Municipality restricted competition as they favoured its controlled entity and defended it from competition.

33. The Lithuanian Competition Council concluded that Palanga City Municipality infringed the Lithuanian Competition Law and ordered to pay a fine of EUR 33 750. The Lithuanian competition authority also ordered to put an end to the infringement and organise a competitive procedure to select the provider of respective works and services, should they still be needed. This decision of the Lithuanian competition authority has been challenged and is now²⁷ pending in courts.

34. Despite numerous changes concerning approach as to the legality of in-house transactions, the development of this field may be not over yet. Currently, there is a pending case²⁸ before the Lithuanian Constitutional Court regarding the constitutionality of one of the conditions of legality of in-house contracts²⁹.

²⁶ I.e. building administration and engineering systems maintenance services; buildings and civil engineering works, localization, reconstruction, repair, demolition and other works; building design services.

²⁷ As of 29 October 2021.

²⁸ Case of the Lithuanian Constitutional Court No. 3/2021, initiated on the basis of the request of Panevėžys Regional Court as of 21 December 2020.

²⁹ This condition is discussed in Paragraph 29 of this Note.