

JUDGMENT OF THE COURT

13 May 2003

(Failure by a Member State to fulfil its obligations – [Articles 49 and 63 TFEU] - Rights attaching to the United Kingdom's Special Share in BAA plc)

In Case C-98/01,

Commission of the European [Union], represented by F. Benyon and M. Patakia, acting as Agents, with an address for service in Luxembourg,

applicant,

v

United Kingdom of Great Britain and Northern Ireland, represented by R. Magrill, acting as Agent, and by D. Wyatt QC and J. Crow, Barrister, with an address for service in Luxembourg,

defendant,

APPLICATION for a declaration that the provisions limiting the possibility of acquiring voting shares in BAA plc as well as the procedure requiring consent to the disposal of the company's assets, to control of its subsidiaries and to winding-up are incompatible with [Articles 49 and 63 TFEU],

THE COURT,

composed of: G.C. Rodríguez Iglesias, President, J.-P. Puissochet, M. Wathelet and R. Schintgen (Presidents of Chambers), C. Gulmann, D.A.O. Edward, A. La Pergola, P. Jann (Rapporteur), V. Skouris, F. Macken, N. Colneric, S. von Bahr and A. Rosas, Judges,

Advocate General: D. Ruiz-Jarabo Colomer,

Registrar: H. von Holstein, Deputy Registrar,

having regard to the Report for the Hearing,

after hearing oral argument from the parties at the hearing on 5 November 2002, at which the Commission was represented by F. Benyon and M. Patakia and the United Kingdom of Great Britain and Northern Ireland by J. E. Collins, acting as Agent, and by D. Wyatt and J. Crow,

after hearing the Opinion of the Advocate General at the sitting on 6 February 2003,
gives the following

Judgment

1.

By application lodged at the Court Registry on 27 February 2001, the Commission of the European [Union] brought an action pursuant to [Article 258 TFEU] against the United Kingdom of Great Britain and Northern Ireland for a declaration that the provisions limiting the possibility of acquiring voting shares in BAA plc (BAA), as well as the procedure requiring consent to the disposal of the company's assets, to control of its subsidiaries and to winding-up, are incompatible with [Articles 49 and 63 TFEU].

Legal background to the proceedings

[Union] law

2.

[Article 63(1) TFEU] is worded as follows:

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

3.

[Article 65(1)(b) TFEU] provides:

“The provisions of [Article 63 TFEU] shall be without prejudice to the right of Member States:

...

(b) to take all requisite measures to prevent infringements of national law and regulations, in particular in the field of taxation and the prudential supervision of financial institutions, or to lay down procedures for the declaration of capital movements for purposes of administrative or statistical information, or to take measures which are justified on grounds of public policy or public security.”

4.

Annex I to Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty [repealed] (OJ 1988 L 178, p. 5) contains a nomenclature of the capital movements referred to in Article 1 of that directive. In particular, it lists the following movements:

“I - Direct investments

1. Establishment and extension of branches or new undertakings belonging solely to the person providing the capital, and the acquisition in full of existing undertakings.

2. Participation in new or existing undertakings with a view to establishing or maintaining lasting economic links.

..."

5.

The explanatory notes appearing at the end of Annex I to Directive 88/361 provide that "direct investments" means:

"Investments of all kinds by natural persons or commercial, industrial or financial undertakings, and which serve to establish or to maintain lasting and direct links between the person providing the capital and the entrepreneur to whom or the undertaking to which the capital is made available in order to carry on an economic activity. This concept must therefore be understood in its widest sense.

..."

As regards those undertakings mentioned under I-2 of the Nomenclature which have the status of companies limited by shares, there is participation in the nature of direct investment where the block of shares held by a natural person or another undertaking or any other holder enables the shareholder, either pursuant to the provisions of national laws relating to companies limited by shares or otherwise, to participate effectively in the management of the company or in its control.

..."

6.

The nomenclature appearing in Annex I to Directive 88/361 also refers to the following movements:

"III - Operations in securities normally dealt in on the capital market

..."

A - Transactions in securities on the capital market

1. Acquisition by non-residents of domestic securities dealt in on a stock exchange

..."

3. Acquisition by non-residents of domestic securities not dealt in on a stock exchange

..."

7.

[Article 345 TFEU] provides:

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

National law

8.

Under the Airports Act 1986 the British Airports Authority, which used to own and operate seven international airports in the United Kingdom, was privatised. Under that Act, the Secretary of State had power to approve with or without modifications the Articles of Association of the company nominated to take over the British Airports Authority's functions. BAA was formed for that purpose in 1987. A One Pound Special Share was created and is held by the Secretary of State for Transport.

9.

BAA's Articles of Association, adopted on 7 July 1987, describe the Special Share in greater detail.

10.

In that regard, Article 10 of BAA's Articles of Association, headed "the Special Share", provides:

"(1) The Special Share may be transferred only to one of Her Majesty's Secretaries of State, another Minister of the Crown or any other person acting on behalf of the Crown.

(2) Notwithstanding any provision in these articles to the contrary, each of the following matters shall be deemed to be a variation of the rights attaching to the Special Share and shall accordingly be effective only with the consent in writing of the Special Shareholder:

(a) the amendment, or removal, or alteration of the effect of, all or any of the following articles:

(i) article 1, to the extent of the definitions of "holder", "the Special Share", "the Special Shareholder" and "Stock Exchange Nominee";

(ii) this article;

(iii) article 39;

(iv) article 40;

(b) the Company ceasing (for whatever reason) to have the right to exercise or to control the exercise of over half the voting rights exercisable on all resolutions considered at a general meeting of any subsidiary owning a Designated Airport or any agreement being entered into with a view to the Company so ceasing;

(c) any proposal being made for the voluntary winding up or dissolution of the Company or of any subsidiary owning a Designated Airport other than a voluntary winding up or dissolution of a subsidiary which forms part of a scheme of reconstruction or amalgamation under which the said Designated Airport is disposed of in such a manner as results in the airport operator being the Company or another subsidiary;

(d) the Company or any subsidiary disposing or entering into an agreement with a view to its disposing of a Designated Airport or any part thereof in such a manner as would result in neither the company nor any subsidiary being the airport operator of such Airport.

(3) For the purposes of this article:

(a) the expression "Designated Airport" means an airport which is for the time being designated for the purposes of section 40 of the Airports Act 1986;

(b) the expression “dispose of” shall include sell, transfer, surrender, mortgage, charge, create any estate or interest in or right over, part with possession of or control over and dispose of in any other way;

(c) the expression “airport operator” shall have the meaning ascribed to it by section 82(1) of the Airports Act 1986.

(4) The directors of the Company will exercise all powers of control exercisable by the Company in relation to its subsidiaries so as to secure (so far as by such exercise they can secure) that no subsidiary shall take any action which (either alone or when taken together with any other action) would involve a variation of any of the rights attached to the Special Share.

(5) The Special Shareholder shall be entitled to receive notice of, and to attend and speak at, any general meeting or any meeting of any class of shareholders of the Company, but the Special Share shall carry no right to vote nor any other rights at any such meeting.

(6) In a distribution of capital in a winding up of the Company, the Special Shareholder shall be entitled to repayment of the capital paid up on the Special Share in priority to any repayment of capital to any other member. The Special Share shall confer no other right to participate in the capital or profits of the Company.

(7) The Special Shareholder may, subject to the provisions of the Act, require the Company to redeem the Special Share at par at any time by serving written notice upon the Company and delivering the relevant share certificate.”

11.

Article 40(1) of BAA's Articles of Association provides:

“The purpose of this article is to prevent any person (other than a Permitted Person) being, or being deemed or appearing to the directors to be, interested in shares of the Company which carry (or may in accordance with their terms in certain circumstances carry) the right to more than 15% of the votes which could be cast on any resolution at any general meeting of the Company (whether or not the votes could be cast in relation to all resolutions at all general meetings).”

12.

Paragraphs (2) and (3) of Article 40 describe in detail the procedures for implementing the rule laid down by paragraph (1).

Pre-litigation procedure

13.

By letter of 3 February 1999 the Commission informed the United Kingdom Government that the special powers conferred on it by BAA's Articles of Association might infringe the [FEU] Treaty provisions on free movement of capital and freedom of establishment. The Commission granted the government a two-month period in which to submit its observations.

14.

The United Kingdom Government did not reply to the letter of formal notice.

15.

The Commission therefore sent the United Kingdom a reasoned opinion on 6 August 1999 requiring it to comply therewith within two months.

16.

The United Kingdom Government responded to the reasoned opinion on 5 November 1999. In that letter it defended the view that Member States have the right to define, within the framework of national company law, the essential characteristics of shares in private companies, which are available on the market, and that use of that right does not impede access to the market in those shares.

17.

The Commission was unconvinced by that reply and decided to bring the present action before the Court of Justice.

Pleas and arguments of the parties

18.

In its application the Commission refers, first, to its Communication of 19 July 1997 on certain legal aspects concerning intra-EU investment (97/C 220/06) (OJ 1997 C 220, p. 15; "the 1997 Communication"). It observes that in the Communication it publicised its view on the interpretation of the Treaty provisions concerning the free movement of capital and freedom of establishment in relation to measures taken by a Member State in the course of privatisation of a public undertaking.

19.

In the Commission's submission, the provisions of Article 40 of BAA's Articles of Association limiting the possibility of acquiring voting shares in BAA as well as the procedure requiring consent to disposal of the company's assets, to the control of subsidiaries and to the company's winding-up (Article 10 of the Articles of Association) do not comply with the conditions set out in the 1997 Communication and accordingly are in breach of [Articles 49 and 63 TFEU].

20.

The national provisions at issue, although they apply without distinction, could create obstacles to the right of establishment of nationals of other Member States as well as to the free movement of capital within the [Union], since they may hinder, or render less attractive, the exercise of those freedoms. As regards the free movement of capital, account should be taken of Annex I to Directive 88/361 which refers, first, to portfolio investment, that is to say, acquiring shares without seeking to influence the way in which the company is managed, and, second, direct investment, a characteristic of which is the fact that the shareholding owned by a person enables him to participate effectively in the management of the company or in its control.

21.

Although it is true that the Member States may, by reason of exceptions provided for by the Treaty, impose restrictions on those freedoms in certain circumstances linked to the exercise of official authority, to public policy, to public security and to public health, the exceptions must be restrictively interpreted and their scope cannot be determined unilaterally by the Member States. Furthermore, they must pass the proportionality test, be in conformity with the principle of legal certainty and must not be implemented for purely economic ends (see Case C-19/92 *Kraus* [1993] ECR I-1663 and Case C-55/94 *Gebhard* [1995] ECR I-4165).

22.

Article 40 of BAA's Articles of Association is clearly incompatible with the Treaty provisions. The United Kingdom Government has not even argued that there is any general interest so far as it is concerned: nor has it relied on special circumstances to justify such a measure.

23.

Similarly, Article 10(2) of BAA's Articles of Association, which makes a number of important decisions concerning the company's activities conditional upon obtaining consent from the Special Shareholder, confers on the United Kingdom a wholly discretionary power, the exact scope of which is not defined. That power restricts the ability (which is none the less an integral part of direct investment) of other shareholders to participate in the management of the company. Consequently, it hinders, or renders less attractive, the exercise of the freedoms concerned.

24.

In relation to the argument put forward by the United Kingdom Government in its reply to the reasoned opinion, namely that the application of private company-law mechanisms is *prima facie* not covered by the requirements of the Treaty, the Commission claims that, although the measures concerned are permitted by national company law, they do not arise from the normal operation of that law but have been adopted by the Member State through an Act of Parliament and must therefore be examined as actions of the State.

25.

In its defence, the United Kingdom Government contends that the rights conferred on the Special Shareholder by Articles 10 and 40 of BAA's Articles of Association do not amount to restrictions on the Treaty freedoms. The Commission's action is therefore unfounded and should be dismissed.

26.

The government explains that under national company law in force in the United Kingdom different classes of shares may exist and that the rights attached to them may be different, both in relation to sharing in the company's profits and to its management. The Special Share concerned merely falls within one of those classes. In particular, shares without voting rights are commonly found in certain companies.

27.

The measures at issue are quite compatible with [Union] law, since they apply to all Member State nationals without discrimination on grounds of nationality and do not restrict access to the market. No justification for those measures is therefore called for.

28.

The Commission is wrong to defend the proposition that any measure which hinders, or renders less attractive, the exercise of the fundamental freedoms must be justified from the point of view of the requirements of the principle of proportionality when those requirements apply only to measures restricting access to the market. In the context of the free movement of goods, an over-extensive application of the Court's case-law was corrected by the judgment in Joined Cases C-267/91 and C-268/91 *Keck and Mithouard* [1993] ECR I-6097. The consequence of the Commission's argument in this case would be that all the difficulties which led to that judgment would be replicated in the context of freedom of establishment and free movement of capital.

29.

In this case, neither the rules of private law which determine the characteristics of shares available on the market, nor those which entitle special shareholders to participate in the decisions of the company, or which require the consent of the special shareholders before certain decisions can be taken, amount to restrictions on access to the market.

30.

The rights which the Special Shareholder may exercise under Article 10 of BAA's Articles of Association do not interfere with either the right of establishment or the free movement of capital, since companies are not obliged to sell assets and, until the assets are placed on the market, there can be no breach of the fundamental freedoms of persons who might wish to acquire them. There are obstacles to those freedoms only where a particular person is obliged to obtain approval in order to acquire assets put on the market, which is not the case here.

31.

The United Kingdom Government explains that the rights of the Special Shareholder under Article 10 of BAA's Articles of Association, which require the government's prior written consent to the taking of certain decisions by the company, are wholly in accordance with the normal rules of company law in force in the United Kingdom, which allow the issue of different classes of shares. It is irrelevant whether those rules are "usual" or not. BAA's Articles of Association do not constitute national legislation and cannot be equated to it. Member States are entitled to engage in economic activities on the same basis as private market operators, within the framework of contracts governed by private law. In the absence of harmonisation of the rules of national company law, [Union] law cannot impose on a company which issues shares the obligation to place the control of that company on the market, or to attach to its shares the whole range of rights which all actual and potential investors might wish to see attached to them.

32. The same analysis is valid for Article 40 of BAA's Articles of Association. The purpose of that provision is to define the characteristics of shares put on the market, under the applicable company law, and not to make acquisition of a shareholding by a particular investor subject to approval, thereby restricting access to the market in those shares.

33. In its reply, the Commission argues that there cannot be any doubt that the measures at issue restrict access to the market for investors from other Member States and render the exercise of the freedoms concerned less attractive. Since the powers concerned are exercised by the United Kingdom *qua* State, it is irrelevant that they are exercised by means of national company law.

34. The principles laid down by the Court in *Keek and Mithouard* cannot apply to the present case. That judgment concerned a particular case of national selling arrangements in the context of the free movement of goods. Even if those principles could be applied to the free movement of capital and freedom of establishment - something the Court has already refused to do in several judgments such as those in Case C-384/93 *Alpine Investments* [1995] ECR I-1141, paragraphs 36 to 38, and Case C-415/93 *Bosman* [1995] ECR I-4921, paragraph 103, - what is at issue here is not the manner in which shares may be acquired or dealt with, but the actual acquisition of shares and thus the negation of a fundamental aspect of the freedoms concerned, and a real restriction on their exercise.

35. In its rejoinder, the United Kingdom Government stresses the fact that the Special Share with which this action is concerned forms part of the rules deriving from national company law and that the measures in question do not therefore require justification. If the Special Share were open to challenge, so would be every class of share whose voting rights could be described, in one way or another, as being more extensive than those of another class of shares. The Commission's argument would mean that holders of ordinary shares could rely on the Treaty in order to renegotiate the rights attached to the shares that they had bought.

36. At the hearing the United Kingdom Government again insisted that the system of prior approval does not affect the independence of BAA's day-to-day management and that it relates to eventualities which are too uncertain and too indirect to amount to a restriction on the freedoms laid down by the Treaty.

37. At the hearing the Commission indicated that it concurred with the findings made by the Court in its judgments in comparable cases delivered after commencement of this action, namely the judgments of 4 June 2002 in Case C-367/98 *Commission v Portugal* [2002] ECR I-4731, Case C-483/99 *Commission v France* [2002] ECR I-4781; and Case C-503/99 *Commission v Belgium* [2002] ECR I-4809. The Court held in those judgments that systems of prior approval such as that at issue here are incompatible with the free movement of capital.

Findings of the Court

[Article 63 TFEU]

38. It must be recalled at the outset that [Article 63(1) TFEU] gives effect to free movement of capital between Member States and between Member States and third countries. To that end it provides, within the framework of the provisions of the chapter headed "Capital and payments", that all restrictions on the movement of capital between Member States and between Member States and third countries are prohibited.

39. Although the Treaty does not define the terms "movements of capital" and "payments", it is settled case-law that Directive 88/361, together with the nomenclature annexed to it, may

be used for the purposes of defining what constitutes a capital movement (Case C-222/97 *Trummer and Mayer* [1999] ECR I-1661, paragraphs 20 and 21).

40.

Points I and III in the nomenclature set out in Annex I to Directive 88/361, and the explanatory notes appearing in that annex, indicate that direct investment in the form of participation in an undertaking by means of a shareholding or the acquisition of securities on the capital market constitute capital movements for the purposes of [Article 63 TFEU]. The explanatory notes state that direct investment is characterised, in particular, by the possibility of participating effectively in the management of a company or in its control.

41.

In the light of those considerations it is appropriate to examine, first, whether the rules which, pursuant to Article 40 of BAA's Articles of Association, prevent any person (other than a Permitted Person) from acquiring or being interested in BAA shares carrying the right to more than 15% of the votes is a restriction on the movement of capital between Member States. Second, it is appropriate to consider whether the fact that the national authorities' prior approval is required for the decisions referred to in Article 10(2) of the Articles of Association, including the company's voluntary winding-up, amendment of the provisions of the Articles relating to the rights attaching to the Special Share, disposal of one of the company's airports or surrender of the right to exercise over half the voting rights in a subsidiary owning an airport, also amounts to a restriction on the movement of capital between Member States.

42.

The United Kingdom Government argues that the rules in question apply without distinction on grounds of nationality. There is thus no discrimination as regards nationals of other Member States. Consequently, those rules do not amount to a restriction on the free movement of capital.

43.

That argument cannot be accepted. It is clear from paragraphs 44 and 40 of the judgments in *Commission v Portugal* and *Commission v France* respectively that the prohibition laid down in [Article 63 TFEU] goes beyond the mere elimination of unequal treatment, on grounds of nationality, as between operators on the financial markets.

44.

Rules which limit the acquisition of shareholdings in the way that Article 40 of BAA's Articles of Association does, or which restrict in some other way the scope for participating effectively in the management of a company or in its control, as is the case of the system of prior approval provided for in Article 10(2) of the Articles, constitute a restriction on the free movement of capital.

45.

In particular, the United Kingdom Government's argument that the measures at issue do not restrict access to the market within the meaning of *Keck and Mithouard* cannot be accepted. The measures at issue are not comparable to the rules concerning selling arrangements which were found in that judgment not to fall within the scope of [Article 34 TFEU].

46.

According to that judgment, the application to products from other Member States of national provisions restricting or prohibiting, within the Member State of importation, certain selling arrangements is not such as to hinder trade between Member States so long as, first, those provisions apply to all relevant traders operating within the national territory and, second, they affect in the same manner, in law and in fact, the marketing of domestic products and of those from other Member States. The reason is that the application of such provisions is not such as to prevent access by the latter products to the market of the Member State of importation or to impede such access more than it impedes access by domestic products (*Alpine Investments*, paragraph 37).

47.

In this instance, although the relevant restrictions on investment operations apply without distinction to both residents and non-residents, it must none the less be held that they affect the position of a person acquiring a shareholding as such and are thus liable to deter investors

from other Member States from making such investments and, consequently, affect access to the market (see, also, the judgment of today's date in Case C-463/00 *Commission v Spain* [2003] ECR I-4579, paragraph 61).

48.

The United Kingdom Government's argument that what is concerned here is solely the application of private company-law mechanisms cannot be accepted. The restrictions at issue do not arise as the result of the normal operation of company law. BAA's Articles of Association were to be approved by the Secretary of State pursuant to the Airports Act 1986 and that was what actually occurred. In those circumstances, the Member State acted in this instance in its capacity as a public authority.

49.

Consequently, the rules at issue constitute a restriction on the movement of capital for the purposes of [Article 63 TFEU]. Since the United Kingdom Government expressly stated that it did not wish to rely on any justification based on possible overriding requirements relating to the general interest, there is no need to examine whether the rules can be justified on that basis.

50.

It must therefore be held that, by maintaining in force the provisions limiting the possibility of acquiring voting shares in BAA as well as the procedure requiring consent to the disposal of the company's assets, to control of its subsidiaries and to winding-up, the United Kingdom has failed to fulfil its obligations under [Article 63 TFEU].

[Article 49 TFEU]

51.

The Commission is also seeking a declaration that there has been an infringement of [Article 49 TFEU], namely freedom of establishment in so far as it relates to undertakings.

52.

In that regard, it is appropriate to point out that in so far as the rules in question entail restrictions on freedom of establishment, such restrictions are a direct consequence of the obstacles to the free movement of capital considered above, to which they are inextricably linked. Consequently, since an infringement of [Article 63 TFEU] has been established, there is no need for a separate examination of the measures at issue in the light of the Treaty rules concerning freedom of establishment.

Costs

53.

Under Article 69(2) of the Rules of Procedure the unsuccessful party is to be ordered to pay the costs if they have been applied for in the successful party's pleadings. Since the Commission sought an order for costs against the United Kingdom and the latter has been unsuccessful, it must be ordered to pay the costs.

On those grounds,

THE COURT,

hereby:

1. Declares that, by maintaining in force the provisions limiting the possibility of acquiring voting shares in BAA plc as well as the procedure requiring consent

to the disposal of the company's assets, to control of its subsidiaries and to winding-up, the United Kingdom of Great Britain and Northern Ireland has failed to fulfil its obligations under [Article 63 TFEU];

2. **Orders the United Kingdom of Great Britain and Northern Ireland to pay the costs.**

Rodríguez Iglesias

Puissochet

Wathelet

Schintgen

Gulmann

Edward

La Pergola

Jann

Skouris

Macken

Colneric

von Bahr

Rosas

Delivered in open court in Luxembourg on 13 May 2003.

R. Grass

G.C. Rodríguez Iglesias

Registrar

President