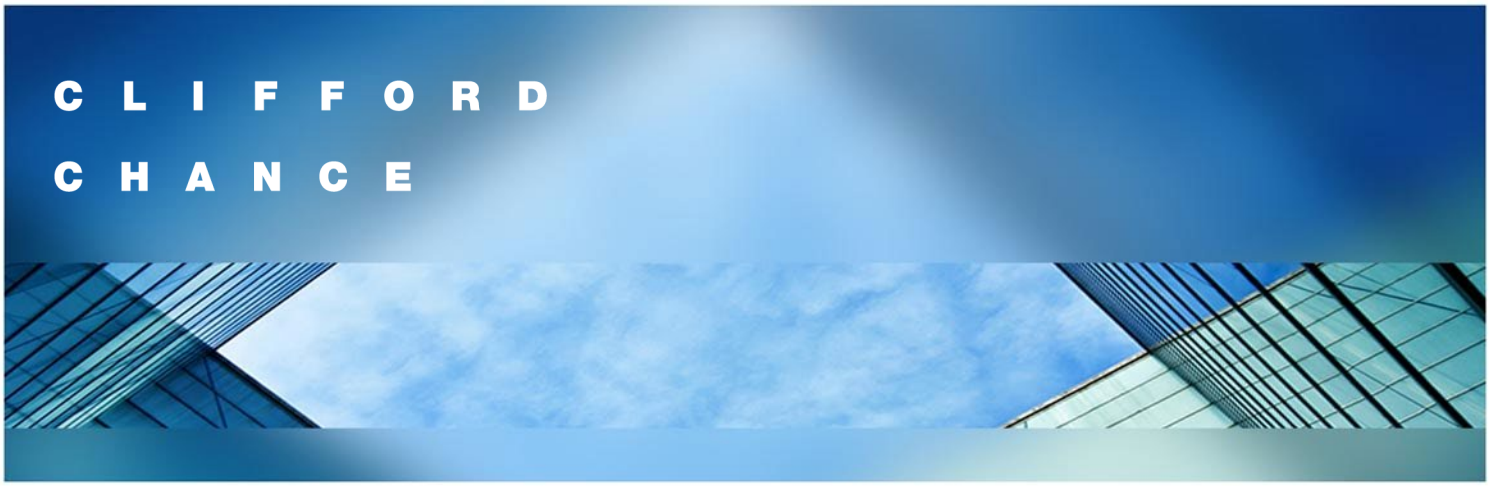

LIGHTS OUT IN THE SUBSIDY CONTROL CHALLENGES TO THE BULB ENERGY TRANSFER

The UK Divisional Court handed down its judgment on 31 March 2023 dismissing subsidy control claims against the UK Government's (**HMG**) transfer of the business of Bulb Energy Limited (**Bulb**) to Octopus Energy Group Limited (**Octopus**). In addition to various public law challenges, the claimants challenged the legality of the subsidies provided by HMG.

The judgment provides useful insight into the framework that the Competition Appeal Tribunal (**CAT**) will likely also adopt for challenges under the new subsidy control regime. In particular, the Court's finding, if adopted by the CAT, that there should be a "light touch" review for subsidy control challenges will amount to a significant barrier that potential claimants may struggle to overcome. The judgment is also an important reminder to claimants to bring challenges promptly.

Key issues

- The claims arose out of HMG's acceptance of Octopus's bid for the business of Bulb, which was put into administration due to serious financial difficulties.
- The claims were brought on various public law and subsidy control grounds. However, they were dismissed in the first instance because the claimants had unduly delayed bringing their claims.
- The Court nonetheless went on to address the merits of the claims and dismissed them.
- The judgment considered a number of the subsidy control grounds in detail, and provided useful guidance on the application of the UK subsidy control regime under the TCA. Much of this will likely be applicable to the new UK subsidy control regime.
- British Gas and E.ON are seeking permission to appeal to the Court of Appeal.

BACKGROUND TO THE CHALLENGES

In 2021, Bulb ran into serious financial difficulty, and Joint Energy Administrators (**JEAs**) were appointed as administrators. The JEAs conducted a sale process for the Bulb business. At the end of phase 1 of the sale process, in April 2022, two indicative offers were received from British Gas and Scottish Power, whereas E.ON and Octopus made it clear that they would not be bidding.

From mid-April 2022, there were communications between the JEAs (and their advisors) and Octopus to see if it would be willing to re-enter the process and make a bid. Octopus re-entered the process in May 2022 and was ultimately the only party to submit a full bid at the end of the sale process. In its final form, the Octopus bid involved HMG providing certain financial assistance to Bulb and a ringfenced new entity owned by Octopus (**HiveCo**) that amounted to restructuring subsidies (**Subsidies**), as well as other financial assistance to Octopus that HMG decided did not amount to a subsidy.

The JEAs recommended to HMG to accept the Octopus bid. HMG commissioned an independent review of the JEAs' final recommendations, which was supportive, and also received a supporting assessment from the

Accounting Officer to the UK Government, as well a subsidy control assessment (mandated under both the UK-EU Trade and Cooperation Agreement (**TCA**) and the UK Subsidy Control Act 2023 (**SCA**)[1]) that concluded that the terms of the Octopus transaction did not contravene the subsidy control principles, as set out in the TCA. The Octopus transaction signed on 28 October 2022. On 29 October and 7 November 2022, HMG made two decisions to effect the Octopus transaction (**Decisions**).

At a hearing on 11 November 2022, at which the JEAs applied to fix the effective date of the transfer of the Bulb business to Octopus, British Gas asked the court not to fix a date to give it time to bring a public law challenge to the Decisions. British Gas, E.ON, and Scottish Power (**Claimants**) brought their cases on 28 and 29 November 2022. On 30 November, the effective time of the transfer was fixed for 20 December 2022.

On 4 January 2023, the SCA entered into force. However, since the Decisions were made in 2022, the relevant legal framework for the Decisions and, therefore, the challenges, was the TCA.

LIGHTS, CLAIM FORM, ACTION; AND WITHOUT DELAY

Claimants are required to issue their claim forms for judicial review challenges promptly, and in any event not later than 3 months after the grounds to make the claim first arose. Where the Court considers that there has been "*undue delay*" in bringing the application for judicial review, it has the discretion to refuse the application.

The judgment found that the Claimants' claims were issued with undue delay. In particular, the Decisions were taken on 29 October and 7 November 2022, and the Decisions were then publicised within a couple of days. Moreover, as noted above, British Gas applied to be joined to the 11 November 2022 transfer hearing to allow it to bring a public law challenge. The Court found that the Claimants should, therefore, have appreciated that urgency was required at that stage, and delaying issuing their claims until 28 and 29 November 2022 was an undue delay. Indeed, the Court relied on comments made by British Gas's counsel at the 11 November 2022 hearing that reversing the transaction would create "*total chaos*".

Although the Court found that the claims could be dismissed on this basis, it nonetheless went on to consider the substance of the claims.

POWERCUT TO THE PUBLIC LAW CHALLENGES

The Claimants brought a host of public law challenges, which are not considered in detail here. In essence, the bulk of the challenges alleged that the Decisions were misdirected, because the sale process unfairly advantaged Octopus in that the JEAs did not offer the Subsidies to the Claimants that were offered to Octopus. Had the Claimants known about the offer, it is likely that they would have submitted a bid. Moreover, the Claimants argued that HMG acted unlawfully in relying on the JEAs to direct itself that the sales process was fair. The Court dismissed these claims and, in so doing, made various factual findings to the effect that Octopus was not unfairly advantaged, that HMG was reasonably and lawfully entitled to base its Decisions on the advice received from the JEAs, and that HMG was also reasonably entitled to accept the JEAs advice that the sales process was fair.

[1] Further information on the TCA and the SCA can be found here.

SPOTLIGHT ON THE SUBSIDY CONTROL CHALLENGES

In addition to the public law challenges, the Claimants brought a further host of subsidy control challenges. All the challenges were dismissed.

Light touch standard of review

A key question for the new subsidy control regime is whether, in line with the intention of the regime to be quick and flexible, courts should adopt only a "light touch" review. In this case, the Claimants argued that the Subsidy Control Principles[2] themselves adopt a proportionality test, which is usually a more intense form of review (compared to the more usual rationality test).

The Court accepted that the language of the Subsidy Control Principles meant that the principle of proportionality applies. However, the Court also held that the proportionality test is a flexible one, and that its application will depend on context. In the context of subsidy control, it held that standard is one of "*a relatively "light touch" standard of review*".

Open, non-discriminatory, and competitive process – neither necessary nor (sometimes) sufficient

As part of the Decisions, HMG decided that the sales process was open, non-discriminatory, and competitive and that, therefore, the transaction was on "commercial market operator" (**CMO**) terms.[3] This led HMG to reach two conclusions. First, that the financial assistance to Octopus was not a subsidy (i.e. because it was CMO compliant and, hence, did not confer an economic advantage to Octopus). Second, that the Subsidies (i.e. to Bulb and HiveCo) were the minimum necessary, because it was clear that none of the bidders would transact without some form of subsidy, and the competitive process led to the minimum subsidy.

The Claimants challenged HMG's claim that the sales process was open, non-discriminatory, and competitive, arguing therefore that HMG had no basis to claim that the CMO principle could be relied on.

The Court dismissed this for similar reasons that it dismissed the public law challenges; HMG was reasonably entitled to conclude that the sales process was open, non-discriminatory, and competitive, and that, in any event, HMG also relied on other evidence from the JEAs and the investment bankers, including counterfactual and benchmarking analyses. Of particular note, the Court held that, in the circumstances, HMG was entitled to not advertise to bidders that it would contemplate bids that were contingent on significant financial support by HMG. Similarly, the Court found that there was no unfairness in HMG not disclosing to all bidders information provided to one bidder. Accordingly, it was reasonably open to HMG to conclude that the bid that emerged from the sales process was a fair reflection of the value which the market placed on Bulb's business in the prevailing circumstances. In so doing, the Court largely referred to analogous EU State aid law and UK statutory guidance under the SCA (**Statutory Guidance**), which states that pursuing an open, non-discriminatory, and competitive process is not necessary to evidence compliance with the CMO principles – but can be an important source of evidence – and that, moreover, such evidence may also not be sufficient in itself where only one bid is made.

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[2] The principles against which public authorities are required to self-assess whether their subsidies are compatible.
[3] The analogous term under EU State aid law is the market economy operator principle, or MEOP.

Objectives can be reviewed in the round

One of the Subsidies was a protection to HiveCo against the consequences of a change in the regulatory regime. The Claimants argued that HMG did not specifically identify how this measure served a legitimate subsidy objective. The Court dismissed this argument, noting that zooming in on one specific aspect of the Subsidies package "*seeks artificially to isolate part of what was an integrated transaction*". Rather, it was open to HMG to look at the Subsidies in the round and to conclude that the Octopus bid was the most proportionate of the available options to meet the objective it identified.

The vice of unlimited guarantees

The TCA (and the SCA) prohibits "*subsidies in the form of a guarantee of debts or liabilities of an economic actor without any limitation as to the amount of those debts and liabilities or the duration of that guarantee*". Some of the Claimants argued that the Subsidies package breached this prohibition, since it included an agreement under which HMG would provide HiveCo sufficient funding to cover the wholesale cost of energy until 31 March 2023, with (among other concessions) any repayment by HiveCo limited to a price cap.

The Court dismissed this argument on two principal bases. First, it doubted whether the concept of unlimited guarantees extend to the types of agreement in question, which ultimately amounted to an exchange of cashflows, since such agreements economically are more akin to a hedge or a swap. Second, the Court considered that one of the perceived "*vices*" of unlimited guarantees is that their extent cannot be properly measured at the point at which they are granted. However, the Claimants did not seek to prove that "*the realistic degree of residual uncertainty was such as to preclude a reasonable valuation of the* [the relevant Subsidy] *at the date of entry*."

Restructuring plans – credibility and significance

Under the TCA, aside for SMEs, restructuring subsidies require the economic actor or its owners, creditors, or new investors to contribute significant funds to the cost of restructuring. The Claimants argued that Octopus, as the "new investor", has not made such a contribution, and in any event less than the "*minimum 50% of the total cost of the restructuring*" (save in "*exceptional circumstances*") cited in the Statutory Guidance under the SCA.

The Court rejected this argument. It noted that the subsidy control assessment expressly considered the amount of Octopus's contribution and concluded it was sufficient in the prevailing circumstances. The exact amount of the contribution is redacted, but it appears to have been less than the usual 50% threshold cited above. The Court also relied on the Octopus bid being the only one to emerge from a lengthy sales process.

Other challenges

The Claimants' subsidy control challenges also included a further litany of alleged failures by HMG, which were all dismissed. These included that HMG took account of irrelevant considerations, failed to have regard to relevant considerations, and failed to make adequate enquiries including as to the effects of the transaction on competition; the Subsidies had not been granted for permissible objectives; and that HMG erred in classifying the Subsidies as responding to a national or global economic emergency.

These challenges largely failed on factual grounds (e.g. HMG did not take account of irrelevant considerations). The Court also placed considerable weight on HMG's subsidy control assessment, which considered many of the issues that later were subject to the challenges. The Court found that the conclusions in the subsidy control assessment should be afforded weight and that HMG "*was entitled to accept and act on that assessment*."

COMMENT

Given that much of the Courts' findings relied on State aid law that the CAT will likely also have regard to, general subsidy control principles, and the Statutory Guidance for the SCA, the judgment provides useful insight into the framework that the CAT will likely adopt for challenges under the SCA regime. In particular, the Court's finding, if adopted by the CAT, that the standard of review against which to judge subsidy control challenges is a "light touch" review will amount to a significant barrier that potential claimants may struggle to overcome. Other points from the judgment that are likely to be relevant to the SCA are as follows:

- **The CMO principle in competitive sale and tender processes**: The judgment provides helpful guidance on the relevance of open, non-discriminatory, and competitive processes to the application of the CMO principle. The CMO principle is one that public authorities often seek to rely on when considering whether subsidies exist, and whether any subsidies are limited to the minimum level necessary. Moreover, the judgment suggests that, where a UK public authority does not advertise the possibility of subsidies, bidders that would not be interested in a transaction absent subsidies should proactively detail in their bids the subsidies that they would require.
- **The scope of unlimited guarantees:** The judgment also provides a permissive approach to the interpretation of unlimited guarantees and restructuring subsidies, and it will remain to be seen whether public authorities seek to take advantage of this permissive approach.
- **Contemporaneous documentary evidence of the assessment on which decisions are based will remain of key importance**: The judgment is a helpful reminder to public authorities that UK courts may be reluctant to second guess decisions where those decisions are made on the basis of appropriately scoped assessments, even if the courts may themselves have reached a different view. Recording the assessments contemporaneously will therefore be key for public authorities when granting subsidies that third parties may later seek to challenge.
- **Bring challenges promptly**: Finally, the judgment is also a reminder to potential claimants to bring their challenges promptly. Although the time limits under the SCA are different to those under the TCA (under the SCA, the starting point is that challenges must be bought within one month from the relevant date of the decision to grant a subsidy), the SCA gives the CAT discretion to refuse to grant any relief if the CAT considers that there has been undue delay in bringing the challenge. It remains to be seen whether the CAT will take the same strict approach that the Court took in the present case. However, claimants may not wish to test this point.

British Gas and E.ON have since stated that they are seeking permission to appeal the judgment to the Court of Appeal. These challenges will flicker on.

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