



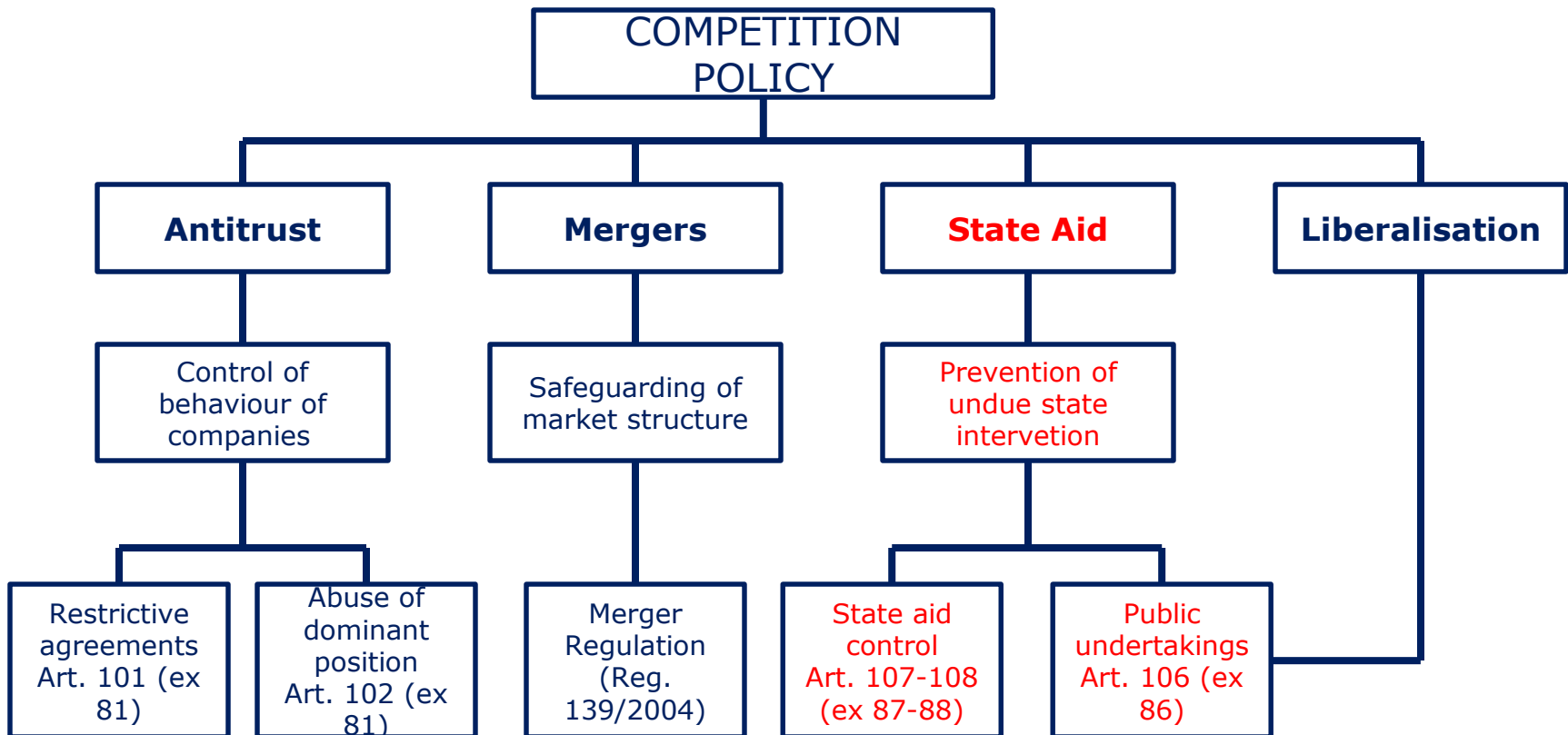
Introduction to State Aid Control: Substance

Overview

- Introduction
- Notion of aid: what is state aid?
- Compatibility: can an aid measure be authorised?
- Brief introduction to secondary legislation and other texts

INTRODUCTION

State Aid and EU Competition Policy



Why Do We Control State Aid?

- state aid control = part of competition policy
- some reasons for state aid control:
 - internal market, level playing field
 - role in liberalisation
 - competitive European industry
 - avoid subsidy race
 - element of cohesion

State Aid Rules in the EU Treaty

- Art. 107(1) TFEU: notion of aid and general prohibition
 - *"Any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, insofar as it affects trade between Member States, be incompatible with the internal market".*
- Arts. 107(2-3), 106(2), 93 TFEU: derogations

NOTION OF AID

Notice on the Notion of Aid

- Adopted on 19 May 2016
- Clarify and explain the notion of State aid: easier, more transparent and more consistent application across the Union.
 - Summary of the interpretation of the NoA by **the Union Courts** and the Commission's own case practice.
 - Where Union Courts' case law is not available, guidance is provided in the form of the **Commission's own interpretation**.
- The Notice is the last missing part of the State aid Modernisation process (SAM)

Basic Principles ⁽¹⁾

Art. 107(1) TFEU:

- granted by a Member State or through State resources
- advantage: “favouring”
- selectivity : “certain undertakings or the production of certain goods”
- effect on trade between Member States
- distortion or risk of distortion of competition

Basic Principles ⁽²⁾

- **objective** notion
- measured in relation to its **effects**
- **burden of proof** on Commission



Key Concepts

- undertaking
- state resources
- advantage
- selectivity
- effect on trade
- distortion of competition

State Resources

- *"granted by a Member State or through State resources, in any form whatsoever"* (Art. 107)
- translates into:
 1. is there a **transfer**
 2. of **State resources** and
 3. is this transfer **imputable** to the State?

Transfer– Granting of Aid

- aid is granted as soon as there is a **challengeable act** under national law
- not necessary that aid was actually paid out (or the guarantee triggered), but concrete risk: foregoing state revenue is sufficient
- actual payment important for recovery only

What are State Resources?

- funds under **control** and at disposal of State who have discretion as to their use
 - includes EU structural funds, resources from EIB or EIF or from international financial institutions such as IMF or EBRD
- transferred in **any form whatsoever** (directly and indirectly):
 - **positive transfer:** direct grants, loans, capital participation
 - **foregone revenues:** tax waivers or deferrals, sale of assets below market price (e.g. land sale, privatisations), omission to collect or enforce debt
 - **exposure of State funds:** guarantees (special issue: unlimited guarantees)

Source of the Funds ⁽¹⁾

- money must have been in the State pocket or otherwise controlled by the State
- if money controlled by State, source is irrelevant



- if money paid directly from citizen to undertaking without ever being controlled by State, no state resources (even if e.g. amount set by State): *Preussen Elektra (C-379/98)*



Source of the Funds ⁽²⁾

- note: state control not limited to direct control over money
- example: parafiscal levies/charges
 - compulsory levy from group of specific producers/service providers to finance activities of same group
 - can be state resources if sufficient degree of state control
 - often complex question in practice



Imputability ⁽¹⁾

- what is "the state"?
 - central, regional or local authorities
 - other public or private bodies designated or established by the state
- State resources includes
- what if there are 3 players: state – intermediate body – beneficiary?

Imputability ⁽²⁾

- if intermediate body is publicly owned company, question of who is really taking decision and the degree of intervention of the state
- principle of **neutrality** of public and private ownership (art. 345 of TFEU): cannot just equate publicly owned company with state
- depends on whether decision is **imputable** to the state (*Stardust Marine, C-482/99*)
- Not imputable if mandatory under EU law

Advantage

- *"favouring certain undertakings or the production of certain goods"* (Art. 107)
- various definitions, e.g.:
 1. A state measure is capable of favouring an undertaking if it produces an economic advantage that the company would not have obtained under normal market conditions, or prevents it from getting worse.
 2. A transfer of resources to the company or relief from charges (e.g. tax advantages or reduction of social security contributions) which a company normally has to bear, whereby the financial advantage is for free or without adequate remuneration.

Advantage

- **Only the effects** of the measure on the undertaking are relevant and not the cause or objective of the State intervention (thus even if the advantage is compulsory for the undertaking)
- To assess the existence of an advantage the financial situation of an undertaking, in its own legal and factual contest, following the measure should be compared with its financial situation if the measure had not been taken.
- However only **the foreseeable effects** and not the actual effects are relevant to establish the presence of an advantage: reference has to be made when the SA is granted (the time that the right to receive it is conferred)

Test Tool MEOP ⁽¹⁾

- **Market Economy Operator Principle (MEOP):** no advantage if state behaves like "normal" player on market
- reasoning:
 - state has right to act on market like any other market player (principle of neutrality)
 - if state behaved like a private player, alleged beneficiary did not obtain anything outside "normal market conditions"
- key question: what would commercial operator do?

MEOP ⁽²⁾

- different applications of test:
 - **M**arket **E**conomy **I**nvestor **P**rinciple (MEIP)
 - state as creditor
 - state as vendor
- not relevant:
 - revenues related to state prerogatives (tax revenues, savings on unemployment benefits)
 - positive externalities related to public policy remit (regional development, industrial / employment policy)
 - philanthropic, social considerations



MEOP ⁽³⁾

- test can be difficult in practice:
 - what are normal market conditions, how to calculate correct return, what is correct benchmark?
 - complex financing structures (e.g. infrastructure investment cases, PPP-arrangements...)
 - no hindsight!
- ⇒ check if CET should be involved

Services of General Economic Interest (SGEI)

- compensation for discharging SGEI not state aid (no advantage) if 4 *Altmark* criteria (C-280/00 of 2003) are met:
 1. beneficiary must actually have public service obligations to discharge, and obligations must be clearly defined by an entrustment act
 2. parameters for compensation: established in advance in objective and transparent manner
 3. no overcompensation (all or part of costs + reasonable profit)
 4. tender or comparison with costs of typical well run undertaking, with adequate means



Services of General Economic Interest (SGEI)

SGEI Communication -Clarification of the notion of State Aid relevant for SGEI

SGEI de minimis Regulation -Compensation which is no aid: € 500.000 over 3 fiscal years

SGEI Decision - Compatible aid exempted from notification

SGEI framework -Compatibility criteria for aid requiring notification



Services of General Economic Interest (SGEI)

The SGEI Decision

- Compatible aid exempted from notification for compensation below € 15 millions/year
- Entrustment max 10 years
- Hospitals, social housing & other social services
- Airports < 200.000 passengers
- Air and maritime links to islands < 300.000 passengers
- Ports < 300.000 passengers

Selectivity

- "favouring **certain** undertakings or the production of certain goods" (Art. 107)
- test: is the measure **selective** in comparison to a **system of reference**?
- not selective: **general measures** (apply to all companies in all sectors of a MS, no discretionary power)
 - rate of corporate tax
 - progressive tax systems
- but watch out for *de facto* selectivity!



Material Selectivity

- ***de jure*** selectivity: selectivity derives from the "law"; measures reserved to certain undertakings
- ***de facto selectivity***: although formally measure seems general, structure of measure is such that it "*significantly favours a particular group of undertakings*" (C-106/09P *Gibraltar*)
- selectivity based on discretion

Material Selectivity

- 3-step test:
 - identification of **correct reference system**
 - **derogation**: does measure differentiate between economic operators who, in light of objective of system, are in comparable factual and legal situation
 - **justification** by nature or general scheme of system



Material Selectivity

- Paint Graphos (C-78/08):

"In order to classify a domestic tax measure as 'selective', it is necessary to begin by identifying and examining the common or 'normal' regime applicable in the Member State concerned. It is in relation to this common or 'normal' tax regime that it is necessary, secondly, to assess and determine whether any advantage granted by the tax measure at issue may be selective by demonstrating that the measure derogates from that common regime inasmuch as it differentiates between economic operators who, in light of the objective assigned to the tax system of the Member State concerned, are in a comparable factual and legal situation."



Material Selectivity

- identification of reference system for fiscal measures:
 - rules that generally apply, on basis of objective criteria, to all undertakings falling within its scope as defined by objective (e.g. general corporate income tax system, VAT system, anti-abuse rules, etc.)
- derogation:
 - differentiation between undertakings such as "to favour certain undertakings or the production of certain goods"

Material Selectivity

Derogation as regards an individual aid measure:

The Union Courts clarified in *MOL (C-15/14P)* that in the case of an individual aid measure, as opposed to a scheme, *"the identification of the economic advantage is, in principle, sufficient to support the presumption that it is selective"*



Material Selectivity

- justification by nature or general scheme of reference system: examples
 - cooperatives which distribute all profits to members are not taxed themselves as cooperatives - justified provided that tax is levied on individual members
 - profit in country A not taxed provided it is taxed in country B - justified by need to avoid double taxation



Regional Selectivity

- *Azores* (C-88/03): when infra-state body is sufficiently autonomous from MS, selective character of its decisions must be assessed with respect to factual and legal situation within its territory rather than within MS
- criteria:
 - institutional autonomy
 - procedural autonomy
 - financial responsibility

Selectivity: Tax rulings

- Tax rulings can create legal certainty and predictability but have to respect State aid rules
- Does the tax ruling just apply the ordinary tax rules or does it misapply the tax rules, resulting in a lower amount of tax?
Selective advantage
- **Tax ruling on transfer prices for intra-group transactions:** selective advantage if it does not respect arm's length principle because standalone company would be taxed on accounting profits (reflecting prices determined on the market)
- Principle requires that transfer pricing must result in a reliable approximation of a market-based outcome

Undertaking and economic activity

- every entity engaged in an economic activity, regardless of the legal status of the entity and the way in which it is financed (*Höfner*, C-41/90)
- economic activity: offering goods and services in the market (*Pavlov*, C-180/98 to C-184/98)
- not economic activity: regulatory tasks, supervisory tasks, activities based on solidarity, basic functions of the State (state education, customs, air safety, treatment of prisoners ...)
- NOA includes specific guidance for social security, health care and education

Undertaking

- focus on nature of activity, not set-up of entity
 - Public undertakings, part of administration, not-for-profit organisation, charitable organisation
- Whether market exists depends on organisation by authority
 - Differences between MS
 - Developments over time

Undertaking and economic activity - reflection

A State subsidises a publicly-owned airport to cover expenses related to security and police functions and to implement fire-protection measures.

Examples

Non-economic: exercise of public powers

- Activity forms part of the essential functions of State or closely connected to those activities
- Examples: army or police, air navigation safety and control, etc.

Social security schemes:

- Schemes based on solidarity vs. economic schemes
- Affiliation compulsory?
- Scheme is non-profit?
- Benefits independent of contributions?
- Etc.

Examples

Education

- Payments by parents/pupils only cover fraction of costs or all costs?
- Competing private organisations?

Healthcare


- Public hospitals as integral part of solidarity-based national health system; directly funded from social security contributions / State; free of charge for affiliates
- Hospitals providing services against remuneration (by patients or their insurance); certain degree of competition between hospitals

Examples

Culture and heritage conservation

- Covers a vast array of purposes and activities (both inside and outside State aid control)
- Non-economic: free of charge or entrance fee covers only fraction of the costs
- Economic: predominantly financed by fees or other commercial means
- Non-economic: activities objectively non-substitutable
- Economic: benefitting exclusively certain undertakings rather than the general public

Distortion of competition & effect on trade

- Criteria Inextricably linked
- Easily met
 - Even if the recipient is not directly involved in cross-border trade
 - Even if the recipient exports all or most of its production outside the Union
 - Fulfilled if product or service subject to trade between Member States
- No need to define the market or to investigate in detail the impact of the measure **BUT**
 -  Effect on trade cannot be merely hypothetical or presumed

Some case law

- "...it is not impossible that a public subsidy granted to an undertaking which provides only local or regional transport services and does not provide any transport services outside its State of origin may none the less have an effect on trade between Member States..."
- "...there is no threshold or percentage below which it may be considered that trade between Member States is not affected. The relatively small amount of aid or the relatively small size of the undertaking which receives it does not as such exclude the possibility that trade between Member States might be affected..."

Altmark (C-280/00)

- "...since it is not inconceivable ... that medical practitioners specialising in dentistry, such as Mr. Heiser, might be in competition with their colleagues established in another Member State, [... an effect on trade ...] must be considered to be fulfilled"

Heiser (C-172/03)

De Minimis

- Regulation No 1407/2013: de minimis aid **not aid** within meaning of Article 107(1) TFEU
- assumption: amount so low that it cannot affect cross-border competition
- €200,000 over 3 years
- €500,000 for SGEI (Regulation No 360/2012)
- exceptions: transport (€100,000), primary agriculture production (€7,500), fisheries (€30,000); export, coal, companies in difficulties not eligible
- transparent aid only

Legal monopoly

Distortion of competition is excluded if

- Service is subject to a legal monopoly (in compliance with EU law)
- No competition on and for the market
- Service is not in competition with similar (liberalised) services
- If service provider is active in another market that is open to competition, cross-subsidiation has to be excluded

(cumulative conditions!)

Local services

Long decision-making practice (e.g. Leisure Pool Dorsten, 2001), confirmed in NOA

- No presumption: depends on facts = evidence available
- Local commercial radius: will beneficiary attract customers from other Member States?
 - ✓ "Local" more likely for services than goods
 - ✓ Less likely when beneficiary is part of national network
- (Potential) impact on investments and establishment must be foreseeable (evidence of exchanges in the relevant sector) + more than marginal.

Examples of local services

- Sports/leisure: swimming pool, marinas, outdoors sports centre, community golf clubs
- Health care: emergency or « standard » medical services
- Culture: only largest have the potential to affect trade because of particular features
- Small ports and airports, ski lifts



State Aid Modernisation (SAM) ⁽¹⁾

- objectives:
 - foster growth in a strengthened, dynamic and competitive internal market
 - focusing enforcement on cases with the biggest impact on internal market
 - streamlined rules and faster decisions



State Aid Modernisation (SAM)⁽²⁾

- revision of most rules and guidelines (completed)
- harmonisation of compatibility assessment: common principles
- significant extension of categories of aid that do not need to be notified (GBER)
- Communication on Notion of Aid: adopted in May 2016

Infrastructure

- **Until 2000:** Construction and operation of infrastructure (e.g. airport) is general measure of public policy
- **Aéroports de Paris (2000):** operation of an airport = economic activity
- **Leipzig/Halle (2011):** All public funding of infrastructure (including its construction) that is meant to be commercially exploited subject to State aid rules
- Financing granted before 2000: not subject to State aid rules (legitimate expectations)

Infrastructure

- Need for specific clarifications; requested by Member States and many stakeholders
- Very high practical relevance
- Legal uncertainty in the wake of Leipzig/Halle

Infrastructure - economic activity

- Economic exploitation = economic activity (Leipzig/Halle)
- No economic exploitation = no economic activity
 - Exercise of public powers (public remit = police, military, customs,...)
 - Not used for offering goods/services on a market (roads for free public use)

Mixed use:

- General principle: separation of costs and revenues
- Concept of ancillarity (up to **20%** of overall capacity p.a.)
- "customary amenities" (restaurants/shops/...): normally no effect on trade between MS

Infrastructure - distortion of competition/effect on trade

- Local cases (Commission's "no effect on trade" decision-making practice)
- Conditions excluding any effect on trade/distortion of competition as regards construction of infrastructure (cumulative criteria):
 - **Infrastructures do not face direct competition** from other infrastructures of the same kind or other infrastructures of a different kind offering services with a significant degree of substitutability, or with such services directly (*likely for comprehensive network infrastructures that are natural monopolies*)
 - **Private financing insignificant** in sector concerned on Member State level
 - **Not dedicated infrastructure**

Infrastructure – Sectoral guidance

- *State aid control typically applies to the construction of infrastructure in the following sectors:*

Airports, Ports, Broadband, Energy

- *State aid control typically does not apply to the construction of infrastructures in the following sectors:*

Railway, Roads/Bridges/Tunnels, Canals/Inland Waterways, Water Supply and Wastewater Networks

- Available for free: no economic activity
- Against fee (toll): *construction* typically fulfills conditions for no effect on competition/trade (as opposed to operation)

Infrastructure - operators and users

3 levels for infrastructures

If operators or users of an infrastructure built with public financing **pay a market price**, they do not receive any 'indirect' State aid (no advantage passed on to them).

Clarification that:

- Competitive tender excludes aid to the operator
- Incremental cost coverage (if no other methodologies are possible) excludes aid to users (approach from Aviation Guidelines)

Last Words (on the Notion of Aid)

- remember: objective notion of aid
- existence of aid \neq prohibition
- purpose of aid, low impact etc. taken into account in compatibility assessment
- conclusion on existence of aid can be left open in exceptional cases only

COMPATIBILITY

Legal Bases ⁽¹⁾

- Art. 107(2): automatic compatibility
- Art. 107(3): margin of discretion to define criteria
 - frameworks and guidelines
 - General Block Exemption Regulation
- Art. 106(2): SGEI
- Art. 108(2): unanimous Council decision



Legal Bases ⁽²⁾

- Art. 107(2) TFEU: *"shall be compatible"*
 - (a) aid having a social character, granted to individual consumers, without discrimination related to the origin of the products concerned
 - (b) aid to make good the damage caused by natural disasters or exceptional occurrences
 - (c) aid granted to compensate for disadvantages caused by the division of Germany [obsolete]

Legal bases ⁽³⁾

- Art. 107(3) TFEU: *"may be considered"*
 - (a) economic development of most disadvantaged regions of Community
 - (b) important common European project or serious disturbance in the economy of a Member State
 - (c) development of certain economic activities or certain economic areas
 - (d) culture and heritage conservation
 - (e) other categories as may be specified by a decision of the Council

Legal Bases ⁽⁴⁾

- Art. 106(2) TFEU: services of general economic interest
 - Undertakings entrusted with the operation of SGEI or having the character of a revenue-producing monopoly shall be subject to the rules contained in the Treaties, in particular the rules on competition, in so far as the application of such rules does not obstruct the performance, in law or in fact, of the particular tasks assigned to them. The development of trade must not be affected to such an extent as would be contrary to the interests of the Union.

Assessment of a Measure

1. under secondary legislation
2. directly on the basis of the Treaty:
 - only if measure not covered by existing secondary legislation



Basic Principles of Compatibility

- general goal: positive effects of aid should outweigh negative effects
- pre-SAM: balancing test
- post-SAM: common principles
- used for assessment directly under the Treaty
- incorporated directly into secondary legislation

Common Principles

1. contribution to well-defined objective of common interest
2. need for state intervention
3. appropriateness of state aid as policy instrument
4. existence of incentive effect
5. proportionality of the aid amount (aid limited to minimum necessary)
6. avoidance of undue negative effects on competition and trade
7. transparency



Objective of Common Interest

- depends on Guidelines concerned
 - Regional Aid: reduce developmental gap between regions
 - R&D&I: promotion of R&D&I
 - Aviation (aid to airports): increase mobility of Union citizens and connectivity of regions by establishing access points for intra-Union flights, combat air traffic congestion at major Union hub airports or facilitate regional development



Need for State Intervention

- general principle: target aid to bring about material improvement which market cannot deliver
- efficiency and equity considerations
- specific qualifications in guidelines:
 - Aviation: no market failure for large airports
 - Risk Finance: *ex ante* assessment of funding gap required

Appropriateness

- aid must be appropriate policy instrument
- selection of least distortive tool
- potential alternatives:
 - other policy instruments (e.g. regulation)
 - other forms of aid (e.g. grant vs loan / repayable advance)

Incentive Effect

- aid must induce recipient to change behaviour in line with common objective
- need to ensure that, in absence of aid, same objective would not have been reached
- counterfactual analysis : what would company do with and without aid?
- application for aid must precede work
- different degrees of factual evidence required



Proportionality

- aid must be proportionate = limited to minimum
- limits expressed as caps on aid amount and/or aid intensity
- aid amount: e.g. net extra cost to achieve objective
- aid intensity: proportion of eligible costs



Negative Effects

- aid must avoid undue negative effects on competition and trade
- positive effects must outweigh negative effects
- depends on relevant product and geographical markets



Transparency

- regional or national website (by July 2016)
- full text of aid measures
- details of beneficiaries
- individual aid awards above certain sizes

BRIEF INTRODUCTION TO SECONDARY LEGISLATION AND OTHER TEXTS

Texts Clarifying the Notion of Aid

- Specific texts:
 - Guarantee Notice
 - Reference Rates, Recovery Rates
 - *De Minimis* Regulation
- **Communication on Notion of Aid: May 2016**

Texts Concerning Compatibility

- **GBER (General Block Exemption Regulation):**
 - regional aid; SMEs; access to finance for SMEs; research and development and innovation; training; aid disadvantaged workers and workers with disabilities; environmental protection; natural disasters; transport for residents in remote regions; broadband infrastructure; culture and heritage conservation; sport and multifunctional recreational infrastructures; local infrastructures
- standard measures considered not very harmful → deemed to be compatible
- do not need to be notified to the Commission

Texts for Specific Sectors

- examples:
 - broadband
 - public service broadcasting
 - air transport
 - other forms of transport

Horizontal Rules

- examples:
 - rescue and restructuring (R&R)
 - environmental protection and energy (EEAG)
 - regional aid (RAG)
 - research, development and innovation (R&D&I)
 - risk capital

SGEI Rules

- current package in force since 1 February 2012:
 - **Communication:** on the notion of aid in SGEI cases
 - **Decision:** exempts specific SGEI cases from notification
 - **Framework:** guides the assessment of large compensation amounts granted to operators outside the scope of the Decision
 - **De minimis Regulation** (adopted April 2012): €500,000 over 3 years

SMEs in Secondary Legislation

- SMEs generally get more advantageous and/or simpler treatment than big companies
- most secondary legal bases contain specific provisions for SMEs
- definition of "SME": Commission Recommendation of 6 May 2003 (= Annex I GBER) + case law

Last Words

- always start with existence of aid
- compatibility:
common principles = same key questions
for all cases

but application depends on sector / measure
concerned