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From the exemptions in State aid to the recovery of unlawful aid

Karl SOUKUP
Director
DG Competition

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Outline

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I. Introduction: architecture of State aid control

Architecture of State aid control

- Set out in the Treaty (binding on Member States)
- Exclusive EU competence
- State aid control by the European Commission
- Very limited role of Council / no role of European Parliament
- Wording in the Treaty on the Functioning of the European Union (TFEU) on what is State aid has not changed since 1957, but scope and awareness of State aid control has increased over time
- Violation of state aid rules results in prohibition of measure and (if necessary) recovery of illegal aid ordered by the EU Commission to restore the competitive situation

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The two steps of State aid control

1. Is there State aid? - Notion of State aid
   - Defined by TFEU (Article 107(1)): State aid is in principle prohibited, unless it falls within general or specific exemptions
   - No discretion for the Commission or Member States (objective notion)
   - Interpreted by the European Court of Justice
   - Commission summarizes and provides additional guidance (Notice on the Notion of Aid)
2. Is the State aid allowed? - Compatibility
   - In most cases discretion for the Commission to decide on compatibility: State aid is compatible/allowed when positive effects outweigh the negative effects
   - Commission adopts general rules (Guidelines/Frameworks/etc.)

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Evolving state aid rulebook

- Transparent and publicly available framework explaining how subsidies can be used in an acceptable manner (e.g. guidelines)
- Has been refined over time based on case experience
- State Aid Modernisation (SAM 2014) – further refinements:
  - Transparency
  - Evaluation
  - Common assessment principles
- Flexible, e.g. also allowing response to financial crisis, while safeguarding internal market
- Has proven effective in reducing State aid expenditure and directing it towards horizontal objectives (e.g. environment)

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II. Block Exemptions

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Objectives of Block Exemptions

- State aid is in principle prohibited, but State aid control is not aimed at eliminating all or any State aid, and is rather intended to ensure that aid is allowed only in warranted instances and implemented in the least anti-competitive way
- Objective: protect competition and the European single market from distortions through state subsidies
- Normally, *ex ante* check by the European Commission through a notification
- Member States can notify individual aid or aid schemes (i.e. programmes on the basis of which individual aid can later be granted)
- Block exemptions allow Member States to grant aid without such notification to and approval by the Commission

Objectives of Block Exemptions

- Block exemption covers cases without real competition concerns:
  - Commission develops rules outlining under which conditions aid may be granted (most important GBER and SGEI)
  - Member State checks itself the compatibility with the rules (self-review)
- Through the General Block Exemption Regulation (GBER), and the Service of General Economic Interest (SGEI) rules, the Commission can define ex-ante compatibility criteria for unproblematic categories of State aid or for specific sectors of general interest.
- Only since 2001, based on prior extensive case practice of European Commission

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The General Block Exemption Regulation

- The GBER 2014-2020 is a set of exemptions that can be used to provide effective and compatible State aid
- Today, over 95% of all aid measures are covered by GBER
- Aid under GBER can be provided without prior approval from the Commission
- To use GBER the granting body must publish the measure on the internet and complete an online form which goes to the Commission
- GBER is an exception and its wording therefore needs to be interpreted strictly, and all conditions need to be fulfilled, also according to EU jurisprudence

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The General Block Exemption Regulation

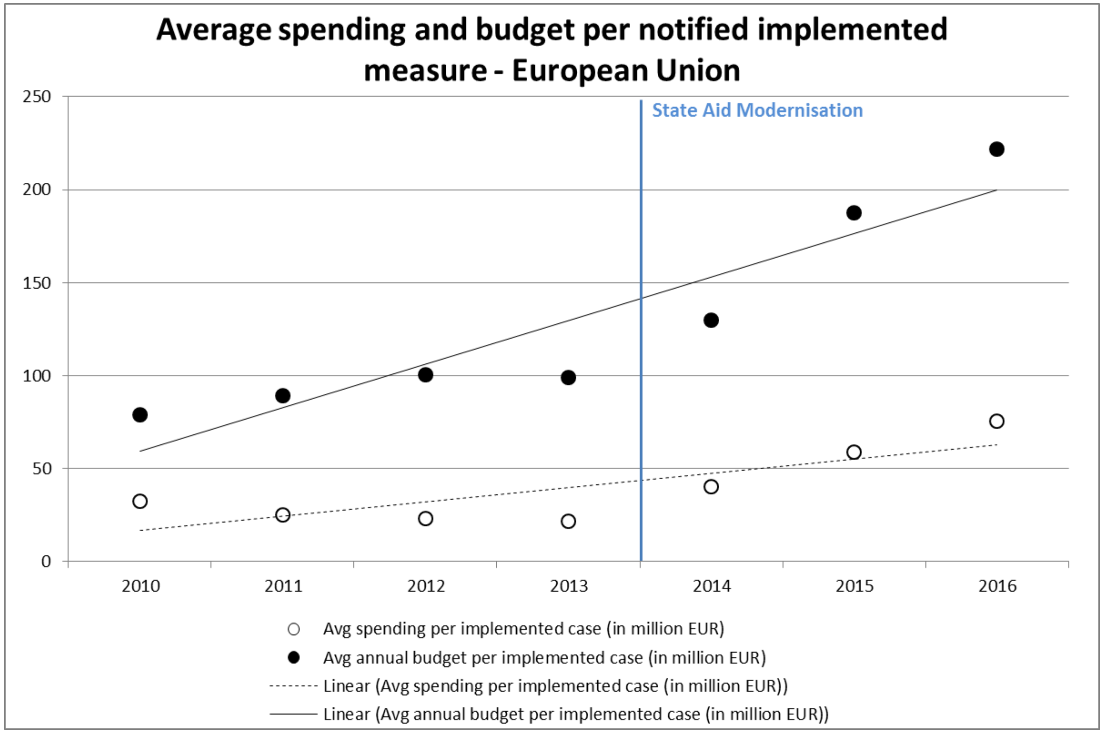
- Examples of categories of State aids which are exempted if the conditions set in GBER are met:
  - Aid for small and medium-sized enterprises (SME)
  - Research and Development aid
  - Training aid
  - Aid for broadband infrastructures
  - Aid to regional airports
  - Aid to maritime and inland ports
  - Risk finance aid
  - Aid connected to energy and environment
  - Regional development aid
  - Aid for natural disasters

GBER uptake

- Almost 6,000 schemes and individual cases registered under new GBER by end 2017
  - More than 95% of new aid measures have been implemented under the GBER in 2016
  - Commission can concentrate on bigger, notified cases

European Union (registered)							
	2011	2012	2013	2014	2015	2016	2017
Total number of notifications	395	450	590	349	257	236	233
Share of GBER	51%	48%	41%	70%	89%	89%	87%

GBER uptake



- Notified measures cover bigger budgets/amounts (more than double compared to pre-SAM)
  - Commission can concentrate on bigger cases
- Results vary between different areas (share of implemented measures under GBER):
  - For example, 97% under GBER for training, 89% for research and development, 87% for employment and SMEs, 72% for environmental protection and energy, 60% for risk capital, 0% for rescue and restructuring

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Services of General Economic Interest

- Services of general interest are services that public authorities of the EU member countries classify as being of general interest and, therefore, subject to specific public service obligations
- They can be provided either by the state or by the private sector

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Services of General Economic Interest

- Compensation for discharging SGEI is not state aid because there is no advantage if specific criteria set by EU jurisprudence 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 must be established in advance in objective and transparent manner
  3. No overcompensation (the compensation can cover all or part of costs plus reasonable profit)
  4. Tender procedures have to be organised or there must be a comparison with the costs of typical well run undertaking

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Services of General Economic Interest

- Legal Framework for SGEI:
  - SGEI Communication - Clarification of the notion of State aid relevant for SGEI
  - SGEI De minimis Regulation - Compensation is no aid if it amounts to not more than € 500.000 over 3 fiscal years
  - SGEI Decision - Aid below € 15 million/year is compatible and exempted from notification, but the entrustment is max. 10 years:
    - Specific rules for hospitals, social housing and other social services
    - Specific benchmarks for airports (< 200.000 passengers), air and maritime links to islands (< 300.000 passengers), ports < 300.000 passengers
  - SGEI Framework - Compatibility criteria for aid requiring notification to the Commission

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Monitoring

- Monitoring is the regular, ex-post, sample control of block-exempted and approved schemes by the EU Commission
- Due to the increased responsibility of Member States with block exemptions there is the need of appropriate mechanisms at national level to ensure compliance
- The national legal basis of each State aid scheme has to cover all relevant conditions for the exemption for the correct implementation of state aid schemes in practice
- Member States are required to keep files demonstrating compliance with State aid rules, in view of the transparency principle
- If irregularities found, corrective action requested

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III. The role of the EU Commission and of the national authorities in the enforcement and recovery of State aids

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Illegal and incompatible aid

- Aid granted without prior notification is illegal (except under block exemptions)
  - Procedures before national courts can be initiated on the basis of illegality of the aid
  - National courts can:
    - Order recovery of the illegal aid and/or of the illegality interest
    - Award damages or interim relief
- The Commission may consider the aid incompatible with substantive EU State aid rules
  - The Commission must order the Member State to recover the illegal and incompatible aid

Purpose of recovery

- The purpose of recovery is to re-establish the situation that existed on the market prior to the granting of the aid
- Recovery is not a penalty, but the logical consequence of finding aid illegal and incompatible
- The aid must be recovered by the Member State together with recovery interests
- Recovery is governed by national law (procedural autonomy), provided this allows for immediate and effective recovery
  - Immediate: the procedure must take place without delay
  - Effective: the procedure must lead to actual recovery
- National rules preventing effective and immediate execution need to be left unapplied

Role of national courts in enforcing State aid rules

- National courts have an active role in:
  - Enforcing the direct effect of the 'Standstill clause' (Article 108(3) TFEU) by:
    - Preventing payment of unlawful aid
    - Seeking recovery of unlawful aid/interest
    - Granting compensation for damages
  - Ensuring immediate and effective execution of Commission's recovery decisions, when called to:
    - May not suspend the execution of the recovery decision on grounds linked to the validity of the Commission decision
    - Suspend the enforcement of national orders for payment of the illegal aid
    - Oversee insolvency proceedings of beneficiaries of incompatible State aid

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IV. Case studies on enforcement and recovery

Example: Regional aid

- The applicable EU Regional Aid Guidelines for 2014-2020 allow the granting of aid for investment projects in less developed regions if – on balance – their positive impact on regional development (and thus cohesion in the EU) outweighs the distortion of competition brought about by the aid
- When approving an aid measure under the Guidelines, the Commission has to be convinced that the following conditions are respected:
  - The aid must have a real "incentive effect", in other words, it must effectively encourage the beneficiary to invest in a specific region
  - The aid must be kept to the minimum necessary to attract the investment to the disadvantaged region
  - The aid must not have undue negative effects, such as the creation of excess capacity in a declining market
  - The aid must not exceed the regional aid ceiling applicable to the region in question

Example: Regional aid

- Conditions (continued):
  - The aid must not directly cause the relocation of existing or closed down activities from elsewhere in the EU to the aided establishment
  - The aid must not divert investment away from another region in the EU which has the same, or lower, level of economic development than the region where the aided investment takes place
- For example, in recent years, the Commission has assessed a series of projects in the automotive sector in order to verify that this balancing test is met and that the aid is necessary and proportionate for implementing the investment.
- Two case studies are here mentioned:

  1) Jaguar Land Rover Slovakia (2018)

  2) BMW Leipzig (2014)

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Case study on regional aid: Jaguar Land Rover

- Decision:
  - By decision of 4 October 2018, the EU Commission has concluded that Slovakia's €125 million investment aid to Jaguar Land Rover is in line with EU State aid regional rules
  - This amount represents the maximum aid that can be granted for such a project under the Commission's Regional Aid Guidelines
  - The compatible aid will contribute to the development of the region of Nitra (Slovakia), without unduly distorting competition in the single market

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Jaguar Land Rover - Slovakia

- Background:
  - Jaguar Land Rover is a large car manufacturing company owned by Tata Motors Limited India
  - Jaguar Land Rover is investing €1.4 billion to build a car manufacturing facility in the region of Nitra (Slovakia), an area eligible for regional aid under EU State aid rules (Art. 107 (3) a) TFEU)
  - The plant is due to have a production capacity of 150,000 cars per year and expected to create about 3,000 direct jobs
  - Slovakia notified the Commission of its plans to grant €125 million of public support for the project

Jaguar Land Rover - Slovakia

- The investigation:
  - The Commission's investigation opened in May 2017 confirmed that, when analysing in 2015 where to build the new car plant, Jaguar Land Rover considered several locations both Europe and outside
  - The Commission's investigation established that without the investment aid, the project would not have been carried out in the disadvantaged region of Nitra in Slovakia
  - The Commission's investigation also showed that the aid was limited to the minimum necessary to trigger the decision by Jaguar Land Rover to carry out the investment in Slovakia, as it compensated the company for the financial disadvantages incurred for carrying out the project in Nitra

Case study on regional aid: BMW

- Decision:
  - On 9 July 2014 the European Commission adopted a decision on aid Germany intended to grant to the car manufacturer BMW in order to attract a major investment project
  - The Commission found that only part of the planned aid was necessary to carry out the project and has therefore authorised only €17 million out of the €45 million planned by Germany
- Background:
  - The project concerned the production of an electric passenger car, expected to create 800 new jobs
  - The Commission found that of the total of €45 million that Germany originally planned to grant, only €17 million was actually necessary to bring the investment to Leipzig and approved the project only to that extent

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BMW - Germany

- Investigation:
  - This aid had to be notified to the Commission by Germany, because aid for large investment projects exceeding certain amounts have to be notified individually
  - The Commission verified whether the criteria of the Regional Aid Guidelines were met; in particular, it verified the incentive effect (i.e. whether the aid actually changes the behaviour of the company, instead of subsidising projects it would have carried out anyway) and the proportionality of the aid, as well as its contribution to the development of the disadvantaged region
  - Through the investigation, it reached the conclusion that the amount of aid was not the minimum to achieve this change and that only €17 million out of the €45 million planned by Germany were necessary

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Case study on fiscal State aid

- Why is taxation concerned by State aid?
  - Direct taxation falls within the competence of the Member States
  - Exercise of national competences must be consistent with Union law
  - The central element in fiscal aid is existence of a selective advantage, this implies that the taxpayer or a group of taxpayers is treated better than others in a comparable factual and legal situation
  - Profits made by firms should be taxed in the jurisdiction where the firm operates according to the general rules and rates that apply in that jurisdiction
  - For companies belonging to a group the arm's length principle is important to ensure they are treated in the same way as stand-alone companies

Case study: Apple

- Decision:
  - By decision of 30 August 2016, the Commission required Ireland to recover a selective tax advantage granted to Apple by way of tax rulings amounting to €13 billion plus interests
  - Ireland and Apple have appealed the decision before the EU General Court
  - The Commission decided on 4 October 2017 to refer Ireland to the European Court of Justice for failing to implement the decision in accordance with Article 108(2) of the TFEU because at that time Ireland had taken only preparatory steps but had not recovered any of the illegal aid
  - On 6 September 2018, Ireland completed the recovery of the illegal state aid worth more than €14 billion into an escrow fund

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Case study: Apple

- Background:
  - The case is about the allocation of profit within two Irish Apple companies: ASI and AOE, i.e. between the head offices and the branches
  - Both companies are incorporated in Ireland but not tax resident there, Ireland can therefore only tax the profits of the Irish branches of ASI and AOE
  - ASI and AOE hold the rights to use the Apple IP under a cost sharing agreement with Apple, Inc.
  - Two tax rulings (from 1991 and 2007) endorse a profit allocation whereby most of the profits are allocated to the head offices, while only very little profit was allocated to the Irish branches

Case study: Apple

- Investigation:
  - The Commission's investigation revealed that the head offices had no employees, no premises and virtually no business activities
  - The revenues by ASI and AOE were mainly sales revenue from the manufacture and distribution of Apple products
  - The branches had the operational capacity to generate such revenues but not the head offices
  - The Commission therefore found that the profit allocation as approved in the rulings had no factual or economic justification

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III. Conclusions

Conclusions on state aid enforcement and recovery

- Enforcement needs to be based on clear and transparent rules with objective criteria to be effective - it has to be:
  - Open, transparent and evidence-based rule making
  - Need to regularly adapt rules to new circumstances to steer state aid towards common objectives and appropriate mechanisms
  - Carried out by independent enforcement authority
  - Based on detailed economic assessment
  - Focus on preventing undue distortions of competition
  - Subject to control by independent judiciary
- Recovery has to be immediate and effective with the objective to re-establish the situation that existed on the market prior to the granting of the aid

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Thank you!

Questions?