

State Aid - Frequently Asked Questions

Note: these are intended to help, but they cannot cover all possible situations and you should seek advice from State Aid Branch or equivalent in individual cases.

Basic queries.

Q. What is a State aid?

It is aid from a Member State to business which the Treaty of Rome declares generally incompatible with the common market - with certain possible exceptions. Broadly, it means a Member State's financial aid which favours selected businesses and has the potential to distort competition and affect trade between EU Member States:

Article 87(1) EC states: "Save as otherwise provided in this Treaty, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favoring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market"

Q. What are the governing rules of State aid? Where can I find them?

The principal legislation is Articles 87 to 89 of the EC Treaty as updated. Article 36 ex 42 agriculture; Article 73 – ex 77 transport; Article 86(2) SGEI (Services of General Economic Interest); Articles 4c and 95 ECSC European Coal and Steel Community.

The rules and their interpretation are developed by ECJ case law and Commission secondary legislation – Frameworks, Directives, Communications and Guidelines on how the Treaty articles apply to different *forms* of aid e.g. fiscal measures, and to different *purposes* for which aid is given. Some rules affect particular sectors e.g. there are special rules covering motor vehicles, shipbuilding, steel. Some rules cover aid for "horizontal" objectives *i.e. not sectorally specific*. Examples are aid for R&D, aid for SMEs, aid for training. The sectoral rules take precedence over the horizontal ones – they add restrictions¹.

Q. How do I spot a State aid?

Article 87(1) sets out criteria, all of which must be met for a State aid to be present.

1. The aid favours certain undertakings or the production of certain goods,
2. The aid is provided through State resources,
3. The aid distorts or threatens to distort competition,
4. The aid affects trade between Member States.

¹ For reference, see: **the European Commission's website**
http://www.europa.eu.int/comm/competition/state_aid/legislation/
<http://www.dti.gov.uk/europe/stateaid/index.htm>
www.europa.eu.int/comm/competition/index_en.html

If it is absolutely certain one or more than one of these conditions is not met, you are not dealing with a State aid.

Some basic myths to dispel:

Public funding and State aid are not one and the same, i.e. public funding is not necessarily a State aid. There being public funding is not enough to determine that this funding is a State aid.

The beneficiary can be public or private or a Public Private Partnership (PPP). For a State aid to exist, there has to be a benefit from State resources to an economic entity which is active in an activity traded within the EU. The entity need not itself carry out trade between Member States. The issue is whether the activity it is engaged in is traded between Member States, e.g. insurance; construction; banking. There are few activities which are not traded between Member States these days and which do not affect competition. If the entity does not carry out an economic activity, there is no State aid as far as these rules are concerned.

Q. Why must we comply with the State aid rules? Why bother?

Unauthorised State aid is illegal. These are the consequences for giving such aid:

- aid payments can be suspended
- firms may have to repay the State with interest
- policies may have to be altered
- legislation may need to be amended
- a recipient could be sued by a competitor for damages

The State aid rules work to create fair competition for UK companies in Europe. Application of the rules means that competitors in other EU Member States cannot receive unlawful State subsidies which distort competition.

Q. What is the logic behind the State aid rules?

The basic reason for the existence of the State aid rules is to ensure that aid does not distort competition in the European Union. State aid is one of the few remaining ways in which Member States can hold up liberalisation and protect companies from competition. As sectors become open to competition, the State aid rules start to become more important – this includes areas which have been the subject to State monopoly. Where in years past, sectors were national in nature, they have become cross-border: coal, transport, financial services and broadcasting are examples.

High amounts of aid can of themselves be distortive. That is why the Lisbon Council Conclusions include a commitment to reduce overall levels of aid within the European Community. The rules also exist to stop abuses of aid. For example: Celtic Energy complained under the State aid rules that the massively subsidised German mines were using aid to undercut prices of anthracite on the UK market. The Commission investigated and found the aid had indeed distorted competition and ordered the German companies to repay the DM 20m back to the German State. The German government paid compensation to Celtic.

Q. Is State aid illegal?

There is a clear statement of principle under Articles 87 and 88 of the Treaty of Rome that any form of aid, whether provided directly by the State, or indirectly 'through State resources', is incompatible with the Common Market if it distorts or threatens to distort competition within the Community. However, not all State aid is unlawful. The Commission may, as an exception permitted by the Treaty, formally approve aid measures within certain limits (depending on the size, sector and location of the beneficiary). These "limits" are detailed in the frameworks / guidelines / regulations referred to above.

Q. What is the Commission's role?

The Commission has sole competence to decide and review what constitutes a State aid. This means that the Commission has the ultimate say in all State aid matters - subject to limited review by the European Court of Justice. Accordingly, the Commission (DG COMP) has considerable powers to monitor, control, and restrict the forms and levels of aid given by Member States to their industries.

They must decide cases to a timetable set out in a Council regulation agreed unanimously. The Commission has to take a decision within 2 months of a complete notification. However in practice the timetable is longer. Allow at least 6-7 months. The Commission can start a further period of two months by asking for further information if they consider the notification is not "complete" (the further period only starts once the Commission receives the answers). At the end of the final two-month period, the Commission may decide to approve, OR to open a second-stage formal investigation which adds at least another 6 months to the process.

Q. What happens if we break the State aid rules?

Any aid paid unlawfully is subject to recovery with interest from the date granted. Aggrieved competitors may take their complaint about (suspected) illegal State aid directly to the Commission. Aggrieved competitors may also take the recipient of unlawful aid to court in their own Member State to seek damages. The consequences for businesses if funding bodies get the State aid rules wrong can be severe. Member States are obliged to recover illegal aid if ordered to do so by the Commission even if the recovery of aid means that recipient companies go bankrupt,. Companies can also take the government / granting authority to court for damages against illegal aid recovered.

Q. Can we get away with not bothering? Why is it so important to abide by the rules?

Ignoring the rules is not the right approach for critical reasons. **Table 2 below?????** shows the number of non-notified cases in all member states as similar as a proportion of the total – the UK does not have any less than others. However, the UK stands out because to date, almost all our notified aid cases have been approved compared to all other Member States as evidenced in the Table.

The UK has increased its credibility with the Commission and benefit from goodwill when it matters. The Commission shows goodwill often by assessing our cases informally and generally relatively quickly as they know the notifications are detailed, reasonable and thorough.

Moreover, we are in a good position to use cases to develop Commission thinking. For example; the new environmental aid guidelines allow aid for cleaning up contaminated land where the polluter cannot be brought to account. This not only allows for 100% of the costs to be aided but also a profit element on top. That provision is very important and a direct result of effective UK lobbying helped by our excellent track record and corresponding credibility with the Commission.

We must still improve our own house. Yes we have a high approval rate – so far. But too often the State aid issues are only considered at the last moment when a structure has been set and Ministers set on a policy course. State aid consideration needs to be built in right from the start.

Q. What are State Aid Branch's general recommendations on State aid?

Build State aid implications into your initial appraisal. Allow enough time for Commission clearance. Be aware of the risks of implementing unapproved aid. Try to fit any proposals to an existing approved aid or a block exemption. Seek advice early.

DETAILED QUERIES.

Q. What is cumulation?

Ensuring that the relevant aid intensity is not breached when aid received from different sources (*including, in the case of aid for R&D, EC programme funding*) counts towards the same eligible project costs. For example, if an aid beneficiary is receiving State aid from a given public source which constitutes regional investment aid and is also in receipt of another State aid package (from another public source) which constitutes an investment towards the same project, both amounts are added together and need to fit the permitted regional aid intensity.

Q. What do Article 87(3)(a) and Article 87(3)(c) refer to in the SME block exemption regulation?

They refer to national regional aid areas ("Assisted Areas"). These may be more familiar as Tier 1 and Tier 2 areas. Tier 1 = Article 87(3)(a) areas; Tier 2 = Article 87(3)(c) areas. The Article references are to provisions in the EC Treaty which are the legal bases for approving regional aid in specific circumstances.

Q. Are Objective 1 and Objective 2 the same thing as Article 87(3)(a) and Article 87(3)(c)?

For Objective 1: Yes - Objective 1 areas and Tier 1/ Article 87(3)(a) are the same in the UK (note: this is not the case for the transitional Objective 1 areas).

For Objective 2: caution! The Objective 2 map is larger than the Assisted Area (State aid) map, therefore some Objective 2 areas will not also be in Tier 2/Article 87(3)(c) areas. If State aid is involved in a project involving Objective 2 funding, it is the Assisted Area map that takes precedence over the Structural Funds map.

Q. Do the bonuses in the training aid block exemption regulation mean you can give 90% in certain cases?

Yes. General training for disadvantaged workers employed by SMEs in a Tier 1 / Article 87(3)(a)/ Objective 1 area.

Q. Can a firm have SME aid or Regional aid or Training aid *with de minimis* aid at the same time without raising cumulation issues?

Yes. "De minimis" is volume-based and stands separate from all other types of aid. It should be seen as a last resort for small amounts of aid which cannot be provided any other way (because it would otherwise be prohibited). De minimis (DM) only cumulates with itself, i.e. with other sources of de minimis aid. The limit on cumulated de minimis aid is €100,000 over a rolling three-year period from all sources e.g. DM aid £10,000 from a local authority plus DM aid £15,000 from an RDA spread over three years is OK and can be given in parallel to State aid which complies with State aid rules, e.g. under an approved State aid or under the SME block exemption.

But there are some exclusions from de minimis aid: it cannot be given to agriculture; transport; or for exports. De minimis also comes with burdensome monitoring and cumulation rules which are not optional extras but must be complied with to ensure legality of the aid. Officials should not pay de minimis aid unless they have first complied with the cumulation rules and have a monitoring system in place.

Q. Can a firm have Regional and Training and SME State Aid at the same time?

Yes, provided that the aid is for different projects with distinct sets of eligible costs.

Q. Who is responsible for abiding by the de minimis threshold?

The provider of the aid. If you are providing de minimis aid you must first ascertain that the amount will not exceed the €100,000 limit over a three-year period when added to any other de minimis aid the intended recipient has already received from all sources during that period. You must ask the firm concerned to provide you with information in writing about any other de minimis aid received during that period.

Q. How are Structural Fund (SF) managers to go about ensuring compliance?

The first issue is to identify whether the SF itself is being used like a State aid within the meaning of Article 87(1). If yes, the issue is to identify which are the relevant aid rules - Regional aid? Training aid? R&D? - and hence what the State aid ceiling and other conditions are. Another issue is to ascertain whether there is any other public

funding going towards the same project costs. If so, the manager has to ascertain whether that other public funding is notified and approved aid or block exemption aid. If not, the whole project will either have to be notified and approved before it can be used with the SF money for a State aid purpose, or comply with the terms of one of the block exemptions.

If once the other (non-SF) public money is approved aid, the next step comes into play. This is to ensure that all the public money plus the SF contribution is within the relevant State aid ceiling (usually the regional aid ceiling as the aid will be assistance towards an initial investment) and meets any other relevant State aid conditions (such as special rules to certain industries, e.g. motor vehicles).

If there is other UK funding (to match the structural fund financing) which is non-approved aid, and spending of that particular fund can't be avoided by replacing it with another pot of public funds which is approved, it would be most efficient to notify this as an aid scheme or check to see that it complies with a block exemption rather than notify an ad hoc aid (i.e. an individual aid to one company).

The advantage of notifying a scheme is that once approved, you don't have to keep notifying every use of it. If an aid scheme is notified, the SF manager will not have to work out before notifying, the precise amount which could be allocated to a particular project. Once the scheme were approved however, the SF manager would be required to apply the cumulation rule to every project.

If an ad hoc aid were notified, then it would be pragmatic for the SF manager to have ensured that the amount did not, when cumulated with the other aid including SF, exceed the relevant State aid ceiling for that particular project. In other words, there is no point in getting approval for £z if we can only pay £x.

Q Is a notified/approved aid one which falls outside the agreed exemptions / ceilings?

No. On the contrary. Notified and approved State aid must respect the aid ceilings - otherwise the approval lapses, and indeed it wouldn't be approved in the first place.

Another way to think of it is this: Why do we bother to notify aid and await Commission approval? It is so that we, and the firms concerned can have confidence that the aid we pay is legal. Approval is not unconditional. It will only stick if the aid provided meets the terms of the approval, which in turn will reflect the terms of the relevant aid guidelines where these exist. State aid guidelines always make clear that the ceilings apply to all the State aid given to that particular set of eligible costs. NOTE: This does not include de minimis aid which is not counted towards approved or block exemption State aid ceilings. De minimis aid only counts towards the de minimis ceiling.

The block exemption regulations cover forms of State aid which are exempt from prior notification – so long as the conditions are met. The aid must comply with all the terms of the regulation, which will include aid ceilings (the SMEs, training and employment block exemption regulations threshold). The regulations do not exempt very large sums –these require Commission approval. You have to provide

summary information on the aid provided under block exemption terms and maintain records.

De minimis aid is a volume ceiling, i.e. a total amount, rather than a percentage ceiling of project costs. You have to ensure compliance with the ceiling and maintain records, but do not have to provide the summary information required for the block exemptions.

An approved aid is State aid and must be cumulated with State aid from any other source including Structural Funds used for the same purpose (but not with de minimis aid).

Q. PPPs (Public Private Partnerships / Joint Ventures) Is there State aid where the public sector gets back something of the same value as that which the private partner or beneficiary gains?

There still could be State aid. The difficulty is in proving how a given undertaking has not received a State aid by virtue of the public sector intervention in the first place. This can most often be circumvented by going to open tender in choosing private partners for a project where benefits will be shared between the public and the private participants. Technically, because you go to open tender in selecting the private partners you get around the "distortion of competition" criterion of Article 87(1) in that all interested parties had a chance to bid for it.

Q. How do Public Private Joint Ventures steer clear from State aid concerns? How can one ensure that JVs/PPPs do not raise State aid problems?

This is by no means easy, and such initiatives should be cleared with State Aid Branch. By market testing and placing OJEC (Official Journal of the European Community) notices you are certainly heading along the right lines.

Here are some general introductory points to assist in steering clear of state aid when considering Joint Ventures:

1. Market Failure

The first is establishing that there is market failure. The project should, for example, concentrate only on property that is not attracting a private developer because it is not financially viable to buy and develop the site in question without public intervention. This should eliminate any state aid concerns that the partnership is potentially competing against such private developers.

2. Selecting a private partner(s)

In creating a Joint Venture Limited company, the public body should competitively select their private partners. This should be done through rigorous advertising, which outlines the criteria that need to be met by the partner(s). The purpose of this is to prevent selectivity towards particular partner(s), which could in turn improve their competitiveness in the market place. By the same reasoning, it might be sensible to have only a three / four year contract with the

selected partner(s) and then undergo another open tender. This should minimise the potential to distort competition in favour of the initial partner(s) as the project grows. This open tendering exercise might also provide a better guide as to how much public money needs to be made available to make the project happen.

3. Generated income

Another state aid implication is how the proceeds from projects are split. This includes the revenue created whilst projects are ongoing as well as the way profits/assets are divided upon expiry of a scheme. A Joint Venture is generally considered to be free of state aid if the public and private contributions to the project are symmetrical in what each gets out of the project. For example, if the ratio of funds channelled in is 75% public and 25% private, this ratio should be respected in receipts. This would mean that the private partner(s) should receive only 25% of the proceeds. By the same token, just as all profits should be shared between public and private, so should all risks, again in proportion to their contribution to the venture.

4. Getting started

A final point to draw out involves the timing of the public and private funds being made available to the Joint Venture. In order to remain free from State aid, the public funds should not be made available to the Joint Venture before the private funds. It is recommended that each contribution is synchronised although there is nothing to stop the private money preceding the public.

In summary: There is no aid where all investors in a JV/PPP share risks and rewards on exactly the same terms, i.e. as there is no benefit, there is therefore no State aid. By contrast there is State aid where the public partner subordinates its return, enabling a commercial return to the private investors. The government participation is State aid. *How about the aid issue to beneficiaries of a PPP/JV Fund's investments?* There will be no State aid if the fund in question invests on exactly the same terms as other funds and there is no aid to beneficiaries of the funds. This is the case for our UK High Tech Fund which was approved. The State aid rules are agnostic about the legal status of an undertaking. They only affect PPPs where the participation of the public partner provides a benefit to the private partner and/or the PPP as an entity provides a benefit to others.

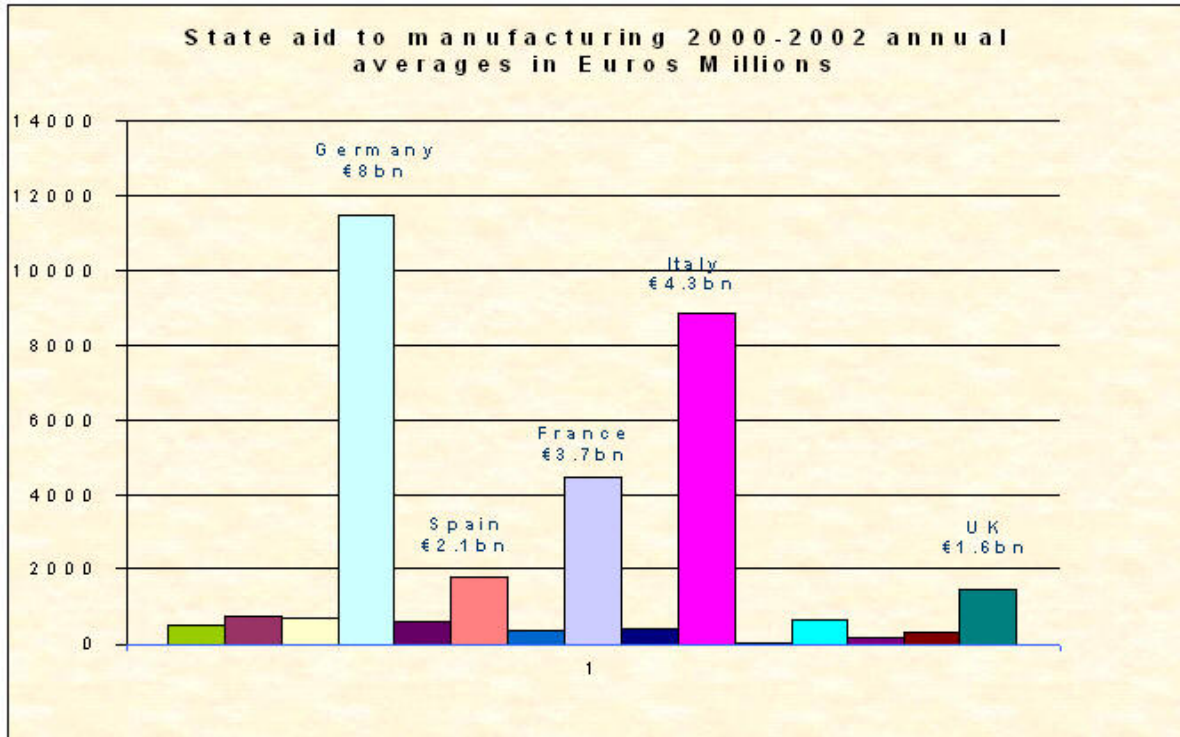
Q. Is funding to universities treated as aid?

Not normally: the funding of universities to provide teaching to students is not deemed State aid. Neither the Universities nor the students (individuals) are considered to be "undertakings". However, where Universities enter into collaboration with firms, there may be State aid present. This will be the case where the firms concerned are getting some benefit which they have not paid the full commercial price for. This needs critical analysis as there may be an element of "payment in kind" e.g. free or cheap use of University laboratories by the firms in return for the University(ies) sharing the fruits of the resultant end product at less than full cost. In this case the aid is to the firms, not the university. Any aid will need to be notified and approved.

There will be no State aid e.g. where the firms pay a commercial fee for the use of University facilities or where the results of the collaboration are made available to all-comers (so the firms concerned do not get a selective benefit).

Q. How does the UK compare with other Member States (EU-15) in amounts of aid it gives?

The chart below which shows the aid given by the 10 Member States to their respective manufacturing industries in 2000 – 2002.



End

DTI
State Aid Branch
Consumer & Competition Policy Directorate

January 2005