María de Molina 41, Madrid, 28006, Spain
E-mail: info@eulawlive.com
Website: http://www.eulawlive.com

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THE FUTURE OF EU STATE AID LAW

CONSOLIDATION AND EXPANSION

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Preface

The goal of this book is to present State aid law and policy with an analysis which does not follow the traditional approach of the now numerous publications in the field. While some chapters necessarily focus on the well-known problematic categories – such as the political economy (Buts and Robins) of State aid control, the nature of the definition of an aid (see De Cecco, Hancher, Cortese), the compatibility assessment (Buendia-Sierra) or the institutional and constitutional aspects and enforcement (Caranta, De Cecco, Cyndecka, Pastor-Merchante), taxation (Szudoczky) and services of general economic interest (Hogan, Jaeger) – other chapters are devoted to new emerging themes that are shaping the area, such as the 'extension' of EU state aid law beyond the territorial constraints of the EU (Rubini, Biondi and Kotsonis, Piernas-López), State aid control in times of recurring crises (Ferri, Kyriazis), impact assessment (Barbu-O'Connor, Derenne, Hofmann, Klotz, Vallindas), State aid and activism in relation to the climate crisis (Kleis-Walravens and Delarue), State aid and gender (Finckenberg-Broman and Broman).

The terms of references given to the various contributors can be summarised as follows: "think outside the box! Provide a fresh assessment of State aid law and policy. Look at the future". As editors, we are extremely pleased to have managed to put together an impressive group of experts and have been encouraged by the authors' willingness to push the boundaries and advance the knowledge in this topical area, going beyond obvious perspectives. State aid is the quintessential laboratory where key paradigms and ideas revolving around the market, public policy and state intervention continue to be re-shaped. The law – in both its skeletal form of the Treaty of Rome provisions and its secondary legislation rich and evolving progeny – has continuously adapted to societal changes and to the evolution of the EU's economic goals, and, increasingly, even beyond the EU. Member States appear to have acquiesced to a transfer of considerable competences to the EU level (largely made possible by a very broad and controversial – construction of the requirements of distortion on competition and effect on trade). This ensures a level playing field with the internal market, but also assists the pursuit of virtuous public policies in view of legitimate horizontal objectives (and, when necessary, allows governments to resist the undue pressure of domestic special interests). It is not far from reality to say that EU State aid is moving from a system of 'subsidy control' to a more complex system of 'subsidy governance' which increasingly raises key constitutional questions that the EU Courts need to address, whether through their review of actions for annulment

Chapter 6

Impact assessment

Ciara Barbu-O'Connor, Jacques Derenne,
Michael Hofmann, Robert Klotz & Dimitris Vallindas

1. Introduction

Since May 2012, the Commission has implemented a major reform of EU State aid rules: the State Aid Modernisation. This allows Member States to quickly implement State aid that fosters investment, economic growth and job creation, leaving the Commission to focus its State aid control on the cases most liable to distort competition. More than 97% of all new State aid measures are now implemented by Member States without the need for prior approval by the Commission. This is mainly the effect of the extension of the General Block Exemption Regulation ('GBER'), although about 40% to 45% of State aid in value are still notified and approved by the Commission (individual aid or aid schemes).[1] As part of the State Aid Modernisation, the Commission has revised a considerable number of State aid rules since 2013.

A number of the State aid rules adopted as part of the State Aid Modernisation were due to expire by the end of 2020. Other State aid rules adopted as part of the Modernisation process have no fixed expiry date. To provide predictability and legal certainty, whilst preparing for a possible future update of the State aid rules adopted as part of the State Aid Modernisation, the Commission took two steps.

First, the Commission prolonged for two years (until end 2022) the validity of those State aid rules, which would otherwise have expired by the end 2020.

Second, on 7 January 2019, the Commission launched in line with the Commission's Better Regulation Guidelines, the evaluation of the rules, which were adopted as part of the

[1] See Commission's press release of 6 October 2021, IP/21/5027.

State aid Modernisation exercise. The evaluation takes the form of a 'fitness check'. It aims to provide a basis for decisions, to be taken by the Commission in the near future, about whether to further prolong or possibly update the existing rules. This ex post evaluation covers the following rules, all of which were adopted as part of the State Aid Modernisation:

- General Block Exemption Regulation ('GBER')
- de minimis Regulation
- Guidelines on regional State aid
- Framework for State aid for research and development and innovation ('RDI')
- Communication on important projects of common European interest ('IPCEI')
- Guidelines on State aid to promote risk finance investments
- Guidelines on State aid to airports and airlines
- Guidelines on State aid for environmental protection and energy
- Guidelines on State aid for rescuing and restructuring

In addition, the Railway Guidelines from 2008 and the Short-term export credit Communication from 2012, which were not revised as part of the State Aid Modernisation, were evaluated in the light of developments in EU law and the Commission's case practice (an external study is being carried out for the Railway Guidelines and the Commission adopted a revised Communication on Short-term export credit insurance on 6 December 2021).

The Fitness Check involves internal analyses by the Commission and public consultations as well as, concerning some specific rules, studies prepared by external consultants or targeted consultations of stakeholders. We have carried out five studies in a consortium[2] for the purposes of the Fitness Check regarding regional aid, risk finance, airports and airlines, and environmental protection and energy for which there were two studies conducted. An additional study concerning railways was finalised in November 2022.

Section 2 hereinafter will briefly summarise the findings of each one of the studies conducted in the consortium as part of the Commission's Fitness Check and Section 3 will look at the future of State aid in these fields, referring to the newly adopted texts in 2021.

[2] The consortium is made, in addition to Sheppard Mullin, with several economic consultancies and academic institutions under a multiannual Framework Agreement with the European Commission (E.CA Economics, DIW Berlin, Lear and the University of East Anglia, not each of them contributed to all studies): The external studies commissioned for the Fitness Check are published by the Commission as follows: Retrospective evaluation of the regional aid framework; Evaluation support study on the EU rules on State aid for access to finance for SMEs; Support study for the evaluation of the rules for operating aid under the EU aviation framework; Retrospective evaluation support study on State aid rules for environmental protection and energy; Retrospective evaluation of State aid rules for RDI and the provisions applicable to RDI State aid of the GBER applicable in 2014–2020.

2. Studies carried out for the Commission's Fitness Check

2.1. Guidelines on regional State aid

2.1.1. *Background*

The Retrospective evaluation of the Regional Aid Framework applicable from 2014 to 2020 ('the RAF 2014') was prepared by a consortium composed of DIW, E.CA Economics and Sheppard Mullin. The RAF 2014 comprises the Guidelines on Regional State Aid ('RAG') and the provisions applicable to regional aid in the GBER. The RAF 2014 contains provisions for both investment and operating aid, but the study focused exclusively on the evaluation of investment aid rules.

The objective of this study was to provide the Commission with an independent evidence-based assessment of the implementation of the RAF 2014 and its effects on regional development and competition. In particular, the study evaluated the effectiveness, efficiency, relevance, coherence and added value of the RAF 2014. Overall, the assessment showed that the rules worked well and needed only targeted adjustments.

2.2.2. *Evaluation support study*

Regional aid aims to reduce the development gap between the different regions of the EU. With the help of well-targeted State aid, disadvantaged regions expect to attract additional investment and economic activity. The RAF 2014 establishes the methodology and criteria for the eligibility of regions for regional State aid in the Member States. It also establishes the conditions under which a Member State may grant regional aid without a notification and it defines the criteria that the Commission uses to assess the compatibility of regional investment aid and operating aid measures notified by Member States.

The regional aid maps identify the EU areas that are eligible for State aid under the RAF 2014. 'A' regions are the least developed regions in the EU, with the biggest scope for regional State aid and 'c' regions are less developed regions, with stricter regional aid rules. Regions not included in the maps are non-assisted regions. The desired impact of EU State aid control is to allow aid for regional development while ensuring a level playing field in the internal market and limiting the negative effects on competition and trade to the minimum necessary.

This study covered the first five years of the RAF 2014; the quantitative data on investments was, however, only available for three years (2014, 2015 and 2016). Given this short time period, long-term effects of the rules could not be evaluated. Thus, the study primarily looked at short to mid-term effects of the introduction of the RAF 2014.

(i) Effectiveness of the RAF 2014

The evidence collected in this study confirmed that the availability of regional investment aid in the EU's disadvantaged regions does attract investments to those regions. The relative importance of regional aid as an incentive to attract investment varies depending on the stage in the decision process, the type of investment, enterprise, sector and the eligibility status of the region.

Under the RAF 2014, the most disadvantaged EU regions also spent the highest amount of regional State aid (when measured relative to its GDP), i.e. the higher the average maximum aid intensity of a Member State, the higher the share of regional State aid spent relative to a country's GDP over the period 2014-2017. This indicates that regional aid is well targeted. In addition, descriptive country-level data analysis revealed that the reduction in maximum aid intensities – as introduced by the RAG 2014 – is positively correlated with the change in private investment: the larger the reduction in a country's average maximum aid intensity, the larger the reduction in investment into the country. This provides preliminary suggestive evidence that the changes in aid intensity may affect actual investment flows.

The econometric analysis and the views of aid granting authorities confirmed this by analysing the effects of the two key changes in regional State aid rules introduced by the RAF 2014. Specifically, State aid eligibility of investments by Large Enterprises (LEs) in 'c' areas was restricted and maximum aid intensities in some 'a' and 'c' areas were decreased (and more so for the LEs than SMEs), which impacted the investment rates.

The study also evidenced the importance of regional aid for a company's investment decision making and that the relative importance of State aid depends on the characteristics of the investing company, such as company size and age.

The study found that the effectiveness of the RAG rules may be limited by the fact that the RAG rules were considered not sufficiently clear on several aspects, such as the concepts of maximum aid intensity, relocation and new economic activity.

(ii) Efficiency of the RAF 2014

The efficiency of the RAF 2014 was assessed mainly by case studies. The study assessed the balance between the *ex ante* risk of the aid measure to negatively distort competition and affect trade between Member States, and the expected effort required from the stakeholders involved in notifying and assessing a case under the RAG 2014. For 'a' areas, it found that the effort was balanced with the ex ante risk in all notified cases. For 'c' areas it found that the effort was often not balanced.

The case studies provided further insights on the incentive effect and showed that not all investment projects really needed the aid. Out of the 11 (pre-) notified and withdrawn projects, 5 were most likely pursued without State aid thereafter, exemplifying the lack of incentive effect.

The case studies also hinted to some potential room for improvement with respect to clarity under the current rules, concerning e.g. the criteria of paragraph 15 RAG 2014. Additional hints that complexity hinders its application, were found in the survey results. 10% of the surveyed authorities reported that they tried to avoid RAG notifications when feasible. The interviewed experts also stated that, for larger projects for which the State aid amounts are close to the notification thresholds, the project may be restructured in a way to avoid notification. In general, the interviewed experts considered the notification and assessment procedures for regional State aid cases too long and lacking transparency from the perspective of investors.

(iii) Relevance of the RAF 2014

The relevance of the RAF 2014 was assessed by examining whether, and if so to what extent, regional aid has contributed to attracting Foreign Direct Investment ('FDI') to the disadvantaged regions of the EU.

Overall, the descriptive analysis of FDI data did not provide indications of a clear relation between the maximum aid intensity and the share in worldwide FDI inflows. The study further found a weak positive relationship between average maximum aid intensities and FDI flows. However, this correlation appeared to be driven by developed countries that, prior to the RAG 2014, had a low average maximum aid intensity and thus is likely unrelated to regional aid availability.

On the contrary, the expert interviews indicated that regional State aid has played a role in attracting investment to the disadvantaged regions of the EU. However, investment incentives are typically not the key factor in the location decision-making process – they can tip the decision at times when two locations are similar in terms of all other characteristics.[3] These interviews also pointed out that the importance of regional State aid also vary depending on the origin of the investors. Some investors (e.g. American and Canadian companies) often negotiate proactively investment incentives and put regions against each other, while others (e.g. Asian and Australian investors) tend to focus more on the trustworthiness of the relationship with the region (as a business partner) than on the financial package only.

(iv) Coherence of the RAF 2014

One of the objectives of the State Aid Modernisation was to ensure consistency and synergy of State aid policy with other EU policies, in particular with the EU Cohesion Policy. This consistency objective is clearly mentioned in the European structural and investment funds (ESI Funds) provisions and the RAF 2014 and is reflected in the two sets of rules through multiple references to the other set of provisions.

[3] See for example Federico Carril-Caccia & Elena Pavlova, *Foreign direct investment and its drivers: a global and EU perspective*, in Economic Bulletin Articles, European Central Bank, Issue 4/2018; and ESPON 2020 Cooperation Programme reports. Available at: https://www.espon.eu/sites/default/files/attachments/ESPON_2020_Cooperation_Programme_-_SFC_Version-_11-03-15_1.pdf.

The study confirmed the consistency and complementarity between the two sets of rules: the review of legislation showed that the objectives, criteria for application and approval are clearly pre-defined and objective; the analysis of the Scoreboard data showed that, under the RAF 2014, nearly 40% of all cases were co-financed, accounting for 6 billion euros (more than 50% of total aid spent), showing that the ESI Funds provisions and the RAF are very often applied in parallel.

The descriptive analysis and the survey of aid-granting authorities did show some differences between the RAF 2014 and the ESI Funds provisions, in particular in terms of scope of application (geographic and sectoral), definitions of terms and criteria for approval. However, these differences are mainly about some extra burden for the beneficiaries and aid-granting authorities rather than contradictions that would make the two sets of rules irreconcilable.

(v) EU added value of the RAF 2014

The study showed that regional aid rules can bring added value to the Member States and the EU by preventing wasteful subsidy races. Generally, the RAF 2014 reduced regional State aid eligibility and maximum aid intensities compared to the previous regional aid rules and it prohibited State aid from relocating existing investment between Member States. In theory, these measures restricted aid granting authorities in their ability to bid for investments against other EU regions.

2.2. Guidelines on State aid to promote risk finance investments

2.2.1. *Background*

Access to finance is essential for small and medium-sized enterprises to make the most of their growth potential. For this reason, the Risk Finance Guidelines[4] ('RFG') and the relevant provisions in the GBER aim at facilitating access to finance by by small and medium-sized European entreprises ('SMEs') and companies with a medium capitalisation. However, despite their growth opportunities, SMEs may face difficulties in obtaining access to finance, which is caused by the problem of asymmetric information. This means that if the firm has better information about its investment returns than potential investors, external financing may be expensive, if available at all, because of adverse selection and moral hazard problems. This can lead to a situation where SMEs are inefficiently underfunded and unable to fulfil their growth potential, to the detriment of the European economy. In order to tackle such market failures, the revised RFG and the GBER aim to further simplify the existing State aid rules and to make it easier for Member States to give access to finance.

[4] Commission Communication of 22 January 2014 on the Guidelines on State aid to promote risk finance investments, *OJ 2014 C 19/4*.

2.2.2. *Evaluation support study*

In June 2020, the Directorate General for Competition ('DG COMP') of the Commission published an Evaluation support study on the EU rules on State aid for access to finance for SMEs.[5] The study relied on: (i) a comprehensive literature review; (ii) interviews with selected stakeholders, i.e. beneficiaries that received support under SME access to finance measures, financial intermediaries involved in risk finance measures, and European and national associations representing SMEs as well as investors active in the SME finance market and, (iii) five relevant case studies of national schemes implemented through the GBER or the RFG.

The results of the study confirmed that, overall, the State aid rules for risk finance implemented in 2014 worked well and contributed to addressing the market failure identified. Nevertheless, the fitness check evaluation has also shown the need for further simplification and clarification of the application of the rules to facilitate the deployment of State aid schemes in support of risk finance. The evaluation focused in particular on the relevance, the effects and the awareness of the State aid rules regarding access to risk finance.

As regards the relevance of the rules, stakeholders showed a general satisfaction with the RFG and the GBER, which were broadly found to be still relevant and well designed to address the identified market failure. However, the study also showed some criticism, wich emerged from interviews with stakeholders and from case studies. For instance, some stakeholders criticised the rule according to which SMEs are eligible for funding under the GBER only if they have been operating in any market for less than seven years following their first commercial sale, whereas past this threshold the RFG apply. In addition, the rule was criticised according to which SMEs are eligible for aid if they require an initial risk finance investment which, based on a business plan prepared in view of entering a new product or geographical market, is higher than 50 % of their average annual turnover in the preceding years.

Regarding the quantitative restrictions, i.e. the investments' limits and thresholds set by the GBER, some interviewed stakeholders expressed concerns that under the GBER the total amount of risk finance cannot exceed 15 million euro. Overall, however, the study suggested that the 15 million euros threshold is suitable for most cases. Moreover, some stakeholders had concerns about the requirement in the GBER that a private investor always participates in the investment (though with varying thresholds). Some of the stakeholders have pointed out that in those regions where financial markets are not strongly developed and for companies in the start-up stage (e.g. Poland, Romania, and Greece), finding a private investor may be particularly challenging.

As regards the effectiveness of the rules, the evidence collected throughout the study suggested that the RFG and the GBER may have been effective, and that their possible negative effects were limited. According to stakeholders, the positive contribution of the RFG and

[5] Avialable at: https://op.europa.eu/en/publication-detail/-/publication/597b6844-a932-11ea-bb7a-01aa75ed71a1/language-en

the GBER in remedying the identified market failure has been driven by three characteristics as compared to the previous framework. First, the rules are less strict than the previous ones (e.g. the private participation rates have been lowered). Second, they are more flexible, as they encompass many risk finance instruments. Third, certain limits have been broadened, especially the one on the total size of the investments.

There are several reasons why the rules might have negative effects, although the conducted interviews suggested that such negative effects are limited. One reason might be that aided access to finance may have discouraged financial intermediaries from making appropriate profit-driven financial decisions. Moreover, funding supplied thanks to the rules may have substituted for funding that would have been supplied privately anyway. In addition, the rules may have generated harmful effects on competition, as a company that receives State support inevitably gains an advantage over its competitors that do not, and this will generally distort competition in the relevant market where that company operates.

As regards the awareness and the clarity of the rules, the majority of financial intermediaries interviewed for the study stated that they were generally aware of the rules in the RFG and the GBER. In some cases financial intermediaries expressed a higher degree of awareness about the specific national schemes they were involved with or applied for. Beneficiaries were generally unaware of the rules, and the case studies showed that they may not know the schemes directly, because they typically approach funds to search for financing and they do not necessarily know that they are supported by a State aid programme.

2.3. Guidelines on State aid to airports and airlines

2.3.1. *Background*

Under the Aviation Guidelines,[6] the Commission considers that airports should normally bear their operating costs. Nevertheless, regional airports with annual passenger traffic of up to 3 million, due to their contribution to the connectivity of citizens and regional development, can receive operating aid only for a transitional period of ten years that will end on 3 April 2024. This measure is meant to enable small airports to adjust to the phasing out of operating aid following industry changes since the liberalisation of air transport in 1997.

In the Aviation Guidelines, the Commission recognises that there is great variability in airports' profitability prospects depending on the airports' size in terms of annual passenger traffic, due to the increasing economies of scale that characterise the industry. Larger size is associated with decreasing financial needs of airports. The Commission identifies five groups of airports based on the annual passenger traffic ('classes'): Class 1: 0-200,000; Class 2: 200,001-700,000; Class 3: 700,001-1 million; Class 4: 1,000,001-3,000,000; and Class 5: above 3 million.

[6] Commission Communication of 4 April 2014, on the Guidelines on State aid to airports and airlines, *OJ C 99*, pp. 3–34.

The rules under the Aviation Guidelines link the maximum intensity of operating aid permitted during the transitional period to the number of airport passengers. Smaller airports could benefit from higher aid intensity than larger airports. In 2017, the Commission extended the scope of the GBER to operating aid granted to airports below 200,000 annual passenger traffic.

2.3.2. *Evaluation support study*

The Support study for the evaluation of the rules for operating aid under the EU aviation framework looked at three questions: (i) whether regional airports can contribute to regional development; (ii) whether the transitional period of 2014 to 2024 for the phasing out of operating aid is adequate to enable airports become self-sustainable; and (iii) whether the categorisation of airports to establish the need for operating aid is suitable, and whether the aid intensity thresholds are fit for purpose. The Study relies on a review of the relevant literature to assess regional airports' contribution to regional development, as well as statistical, cluster and econometric analysis using data at the airport level on past and expected financial performance and on annual passenger traffic.

(i) Do regional airports contribute to regional development?

The analysis examined the airports' economics and potential determining factors of profitability in particular air traffic size, ownership structure, proximity to other airports and other transport infrastructure, as well as economic incentives to attract airlines and the dependence on low-cost carriers ('LCCs'). The evidence confirms the positive link between size and technical and economic efficiency even though it does not suggest that there exists a minimum size for airports to break even. Regional airports often face limited demand, and there will inevitably be airports – although run efficiently – that do not generate enough business to cover their operating costs. Air traffic has a positive impact on regional development specifically for service industries in terms of employment, GDP and trade. It is however apparent that smaller regional airports need some form of long term public support to survive. The question is therefore whether such support can be justified by the positive economic impact these airports bring to their respective regions.

(ii) Is the transitional period of 2014 to 2024 for the phasing out of operating aid adequate?

All airports above 700,000 passengers (classes 3, 4 and 5) should be able to fully cover their operating costs by 2024. Both when looking at sample data and at Eurostat data for all EU airports, classes 3, 4 and 5 display a larger growth potential than smaller classes. The data also suggests that these airports tend to rapidly scale up above their class-specific boundaries. This overall suggests that the duration of the transitional period is likely to be adequate for airports above 700,000 passengers. The majority (69%) of airports belonging to class 2 will be able to achieve equilibrium by 2024. In addition, those expected to not be in equilibrium

by 2024 exhibit an improving trend. These results suggest that the transitional period is adequate for the majority of airports in class 2 to reach equilibrium and that, on average, they are moving towards equilibrium. The results for airports belonging to class 1 are different: first of all, only 37.5% will be able to achieve the equilibrium; secondly, they mostly show declining operating funding gap ('OFG') trends. The evidence shows that none of the class 1 airports that have received operating aid are expected to reach financial equilibrium in 2024.

(iii) Are the categorisation of airports and the aid intensity thresholds fit for purpose?

This evaluation is based on passenger traffic and implies several interrelated questions: whether the number of passengers is a relevant factor to establish the need of operating aid; whether it is sufficient; and whether the current thresholds are appropriate and, if not, which categorisation should be adopted. The analysis shows that passengers are certainly important for an airport's profitability. Moreover, the positive correlation between airport's traffic and its profitability is stronger the larger the airport in terms of passengers. However, there seems to be quite some heterogeneity within and across classes. There are other factors which may have an impact on the definition of the need for aid including the share of LCCs passengers, the ratio of incentives paid to airlines per passenger and the attractiveness of the airports' location. Focusing on differences within classes, since most of class 1 airports never manage to be profitable, the number of passengers seems to be a sufficient indicator of profitability up to 200,000 passengers. Looking at differences within class 2, other factors than passengers (especially the share of LCCs passengers), explain why some airports in class 2 manage to be profitable while others do not. Most of the airports in classes 3 and 4 were already profitable over the period 2015-2018; thus, given this evidence, passengers may be sufficient to forecast their funding needs. Finally, very large airports (above 3 million passengers per year) are always profitable. Hence, the number of passengers seems to be enough to identify theneed for operating aid. On the appropriateness of the original categorisation of airports adopted in 2014 for the purposes of defining aid intensities, the Study shows that the finer five-class categorisation (Class 1: 0-200,000; Class 2: 200,001-700,000; Class 3: 700,001-1 million; Class 4: 1,000,001-3 million; and Class 5: above 3 million) might have been a better predictor of an airport's ability to cover its operating costs, and there may be room for further improvement.

2.4. Guidelines on State aid for environmental protection and energy I

2.4.1. *Background*

The Guidelines on State aid for environmental protection and energy ('EEAG')[7] enable Member States to support projects for environmental protection as well as measures to ensure

[7] Commission Communication on Guidelines of State aid for environmental protection and energy 2014-2020, *OJ 2014 C 200/1.*

energy generation adequacy. The EEAG aim at helping Member States meet their ambitious EU energy and climate targets. With its revision of the EEAG, the Commission wants to enlarge the scope of the EEAG to new areas and to all technologies that can deliver the Green Deal. The revision also aims at facilitating the phasing out of subsidies for fossil fuels, in particular those that are most polluting. In this regard, the Commission has conducted an evaluation of the current EEAG as part of the State aid Fitness Check.

2.4.2. *Evaluation support study*

In June 2020, the Commission published a Retrospective evaluation support study on the EEAG.[8] The overall objective of the study was to support the Commission with an evidence-based review of the implementation of the EEAG and the provisions applicable to aid for environmental protection and energy of the GBER. The study provided input for assessing whether the EEAG and the relevant GBER provisions are fit for purpose taking into account the general State aid modernisation objectives, the European Green Deal objectives, and the specific objectives of the legal framework and the current and future challenges. The topics covered in the study are related to the effectiveness, efficiency and relevance of the State aid rules.

On the effectiveness of the rules, the study, among others, provided information on Renewable Energy Sources (RES) schemes in order to understand their particular features and the evolution of prices. This included the need to understand the effectiveness of bidding processes and the impact, or not, of bidding processes being open to multiple technologies. Averaging across the sampled schemes, a consistent picture did not emerge as to whether average prices were lower in multi-technology than single-technology auctions.

The performance of capacity mechanisms has been assessed by comparing various auction outcomes and scheme designs. It appeared, for instance, that Greece, Poland, and Ireland had higher capacity prices than France or the UK. Moreover it was found that, e.g., in Germany fast interruptible load auctions almost always cleared at price caps in 2017 and 2018 and that in 2019 prices fell below the price caps by no more than 4%.

With regard to efficiency, the study provided, among others, information on the impact of reductions of RES levies and other comparable levies for energy intensive users ('EIU'), as well as on levies paid by different consumer groups and on the relevance of the grandfathering rule. It was assessed, among others, whether the introduction of levy rebates for EIU led to increases of levies for other users. The data allowed the identification of three broad groups. First, there are three countries with a pattern consistent with a lasting redistribution effect. Second, there are countries with a pattern consistent with a short-lived redistribution effect that vanishes over time. And third, there are countries where no effect on rates for non-rebated customers could be observed.

[8] Available at: https://op.europa.eu/en/publication-detail/-/publication/d3289dd8-a930-11ea-bb7a-01aa75ed71a1

As regards the relevance, the study provided input regarding subsidy-free renewable energy projects in the EEA. Subsidy-free renewable energy projects were defined as those where the project receives zero public funding, irrespective of any movements in energy market prices. The total volume of announced subsidy-free renewable energy projects currently in Europe is approximately 18 GW. However, a significant part of the 18 GW volume comes from projects that are only at the planning stage and there is no guarantee that they will actually be built. Companies may have secured only enough finance to get a project through the planning process, rather than to build it. In the subsidy-free environment, lenders may be tentative to invest when the earning potential of the project is left to the wholesale electricity market.

Moreover, publicly accessible or dedicated alternative fuel infrastructure projects were analysed with a particular focus on the financing of the projects. It appeared that all schemes analysed, except one, were carried out based on a tender or a call for applications. The projects concerned the purchase of electric or natural gas buses and/or related charging and re-fuelling infrastructure. Moreover, the study has shown that the electric charging stations for cars and cruise ships were generally publicly accessible, whereas the electric infrastructure projects for buses were dedicated or semi-dedicated to public transport operators.

2.5. Guidelines on State aid for environmental protection and energy II

2.5.1. *Background*

As explained above, the EEAG enable Member States to support projects for environmental protection and energy generation adequacy. This second study on the EEAG looked at three specific issues: (i) transparency, tendering and broadening; (ii) operating aid versus investment aid; and (iii) EIUs.

2.5.2. *Findings of the study*

Firstly, on transparency, tendering and broadening, the study reveals that large investments needed for a transition to a low-carbon economy warrant the consideration of a potential revision of the rules ensuring that State aid schemes for environmental protection and industrial decarbonisation are cost-effective and do not unduly distort competition. Against this background, the Study examined whether and how the transparency of environmental protection costs of decarbonisation aid schemes should be increased by quantifying both the benefits to environmental protection and their costs. The study further addressed whether tendering requirements in aid schemes should be extended. Finally, whether environmental protection schemes can be broadened to different sectors and technologies which could advance the same environmental protection objective to a similar extent, rather than being sector- or technology-specific was assessed.

Member States increasingly rely or plan to rely on the €/tCO2 criterion to allocate the support for renewable energy and decarbonisation schemes or to assess their effectiveness. This suggests that there are benefits in moving away from approaches that select the measures to be aided based on the cost per unit of energy output which ignore any environmental costs and benefits. The cost-effectiveness metric should facilitate a better evaluation of the contribution to the targeted environmental objective and the proportionality of the aid; in addition, it should help identify measures which have an unusually high costs and merit further scrutiny or stricter compatibility conditions.

Furthermore, auction design can have an impact on participation, competition, and in turn, bidding behaviour. The main design elements that can influence the outcomes of the auctions are pricing rules (pay-as-bid or uniform price), formats (static, dynamic or hybrid), and scoring rules (based only on price or on multiple factors). There is also a debate on whether auctions should be technology-neutral – i.e. open to all available technologies which would compete under a common budget – or technology-specific. Although technology-neutral auctions can lead to cost minimisation they may also lock out the most expensive technologies and generate windfall profits for the least expensive ones. It appears that technology-specific auctions may foster technology diversity and enhance security of supply.

Secondly, the Study also assessed the effects of awarding State aid either as investment aid or operating aid. This can help the Commission discern whether compatibility rules for investment and operating aid should be aligned. Overall, in the field of support for environmentally friendly energy production, operating aid is often more effective at securing investment than investment aid. Both types of aid contribute to the economic feasibility of the environmental protection measures, however, they do so in different ways, suggesting both may still have an important role within the State aid toolkit.However, in practice, operating aid seems more frequently awarded, while investment aid, under the existing rules can fail to cover the increased costs of investment. Solutions have already been found for appropriately incentivising energy investments, with some new energy investments having aid levels bid down to zero, suggesting that State aid for certain categories of energy investment may be increasingly unnecessary as the market alone may accommodate necessary investments due to decreasing investment costs and increasing demand for renewable energy.

Finally, regarding EIUs, the Study looked at whether the economic parameters currently used by the EEAG to determine the eligibility of sectors for exemptions from decarbonisation levies for EIUs are the most relevant parameters for the risk of relocation from an economic perspective, and the extent to which the profitability of EIUs is affected by different levels of Renewable Energy Sources ('RES') and Combined Heat Power ('CHP') levies on electricity for a sample of 10 sectors. Measures of electro-intensity and trade intensity were found to be relevant for the risk of relocation of firms. Regarding electro-intensity, the Study finds that the most energy-intensive firms are negatively affected by increases in energy prices (including levies) on various levels: production, productivity, employment, probability of exit, exports

and imports. The different effects on energy-intensive and non-energy-intensive firms support the relevance of electro-intensity as an important criterion in the EEAG. Regarding trade intensity, the study also confirms its relevance as a criterion to distinguish between sectors of high and low risk of relocation due to changes in levy levels.

3. Conclusion and Outlook

On 30 October 2020, the Commission published a Staff Working Document summarising the results of the retrospective evaluation of EU State aid rules.[9] While State aid rules are broadly fit for purpose, some individual rules will need to be adapted or updated, notably to reflect the recent European Green Deal and digital strategies.

3.1. Regional aid

On 19 April 2021, the Commission adopted revised EU Guidelines on regional State aid.[10] They were the first set of State aid rules that are revised following the announcement of the European Green Deal and the European Industrial and Digital Strategies.

The revised regional aid guidelines entered into force on 1 January 2022. They include a number of targeted adjustments to simplify and reflect experience gained from the application of the previous rules, as well as to reflect new policy priorities related to the European Green Deal and the European Industrial and Digital Strategies, such as:

- Increased overall regional aid coverage to 48% of the EU population (previously 47%) and updated list of assisted 'a'-areas and predefined 'c'-areas based on the latest available Eurostat statistics on GDP (2016-2018) and unemployment (2017-2019).
- Increased maximum aid intensities to support the European Green Deal and Digital Strategy objectives by enabling additional incentives for investments in the disadvantaged areas of the EU. In addition, the Guidelines include several aid intensity bonuses: (i) for outermost regions, (ii) for border areas, (iii) for Just Transition Areas in the most disadvantaged areas, and (iv) for areas experiencing a population loss.
- Validity of regional aid maps for the period 2022-2027, with a mid-term review envisaged for 2023 based on updated statistics reflecting the recent economic developments and enabling regions to bounce back from the crisis.
- A general simplification of the structure of the Guidelines, a clarification of some of the definitions and terminology, and some targeted changes in light of the European Green Deal and the EU's Industrial and Digital Strategies. For example, the sectorial scope of the Guidelines was updated, as well as the criteria used for balancing the positive impact of the aid against its negative effect on competition and trade.

  This assessment may now also take account of other positive and negative effects, such as a substantial contribution to the green and digital transition or some related negative externalities.

3.2. Risk Finance

On 21 May 2021, the Commission published its revisions of the RFG and launched a public consultation for interested parties to comment on these proposals. The Study suggested that the RFG are overall fit for purpose. However, specific areas have been identified where improvements could be made to increase efficiency in application by Member States and beneficiaries without jeopardising the goal to protect the level playing field and minimise potential market distortions. The Commission proposed revisions to the current rules with a focus on the need to further simplify and clarify the application of the rules and suggests reordering the provisions to increase readability and ease of application. Moreover, the revised RFG intend to clarify certain concepts and level of evidence needed to demonstrate the existence of a specific market failure or other relevant obstacles in accessing finance and intend to streamline existing formulations and align definitions to increase consistency with the GBER.

Finally, the Commission also wanted to streamline the structure of the RFG. This consists, in particular, in the consolidation under one single section of the requirements for the ex ante assessment that the notifying Member State needs to submit to the Commission in order to demonstrate why the aid measure is necessary, appropriate and proportionate; these requirements were included in different sections. Access to finance should also be seen as an enabler in light of the investments required for the Green Deal, Industrial Strategy and the digital transformation.

The Commission adopted the revised Risk Finance Guidelines on 6 December 2021. They apply from 1 January 2022.[11]

3.3. Aviation aid

Whilst air passenger transport can stimulate local economies and have important effects on overall connectivity of a given region, the Study indicates that aid to airports might not always be the most efficient use of public resources to promote regional development. This will need to be taken into account in the amendment of the Aviation Guidelines which the Commission is considering in the near future.

[9] Commission Staff Working Document of 30 October 2020 on the Fitness Check of the 2012 State aid modernisation package, railways guidelines and short-term export credit insurance, SWD(2020) 257 final.

[10] Commission Guidelines on regional State aid, *OJ C 153, 29.4.2021*, pp. 1–46.

[11] Guidelines on State aid to promote risk finance investments, *OJ C 508, 16.12.2021*, pp. 1–36.

One of the most important developments since this Study was conducted is the Covid-19 outbreak. The full impact of the COVID-19 outbreak is not yet known. However, it is becoming clear that the aviation sector is one of the most heavily affected sectors. While the impact of the Covid-19 pandemic had not been assessed in the Study, the conclusions of the study should be deemed to still be valid when the sector goes back to its pre-Covid levels. Nevertheless, any possible revision of the Aviation Guidelines will need to take account of the changes in the aviation sector created by the COVID-19 pandemic therefore some specific rules may need to be reshaped once the long-term impact of the crisis is known.

3.4. From EEAG to CEEAG

The assessment suggests that the EEAG and corresponding GBER rules have generally delivered on their objectives. They already explicitly support the Union's environmental and sustainable energy policy objectives while at the same time ensure an effective and efficient State aid control. However, some limitations and problems have become visible. There are indications that the scope of the guidelines might have been too restricted and that the current guidelines are too tightly focused on specific aid categories and technologies. They are thus not sufficiently future-proof to cater for recent and expected technological and market developments and novel aid designs.

There are some indications that the compatibility rules on environmental protection are not entirely suited to face the climate neutrality challenge, in particular the rules to ensure necessity of aid, proportionality and limitation of distortions. Thus, in June 2021, the Commission published for consultation the draft revised EEAG. The Commission proposed a number of changes to the current rules. Due to the increased importance of climate protection, the revised guidelines were re-named the Climate, Energy and Environmental State aid Guidelines ('CEEAG'). The Commission broadened the scope of the CEEAG to enable support in new areas such as clean mobility, energy efficiency in buildings, circularity and biodiversity. Moreover, the CEEAG apply to all technologies that can deliver the Green Deal and the revised rules would generally allow for aid amounts covering up to 100% of the funding gap and to introduce new aid instruments, such as Carbon Contracts for Difference.In addition, the Commission increased flexibility and streamlined the existing rules by introducing a simplified assessment of cross-cutting measures under a single section of the CEEAG.

Finally, the Commission also aligned and ensured coherence with the relevant EU legislation and policies in the environmental and energy fields. This includes, for instance, phasing out subsidies for fossil fuels, in particular those that are most polluting. Measures involving new investments in natural gas are covered by the CEEAG, only insofar as it is demonstrated that the investments are compatible with the Union's 2030 and 2050 climate targets. The Commission adopted the new CEEAG on 27 January 2022. The new guidelines apply from that date.[12]

[12] Guidelines on State aid for climate, environmental protection and energy 2022, *OJ C 80, 18.2.2022*, pp. 1-89.

Chapter 7

State aid conditionality and misuse of aid

Malgorzata Cyndecka

1. Introductory remarks

Pursuant to Article 107(1) TFEU, aid that distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods in so far as it affects trade between Member States is incompatible with the internal market, and thus prohibited. Yet, the Treaty provides for several exceptions from that prohibition. Aid may be declared compatible with the internal market if it fulfils the conditions set out it Articles 106(2), 107(2) or (3) TFEU. Moreover, some types of aid are automatically exempted from the notification obligation and the subsequent compatibility assessment if they meet the requirements set out in the General Block Exemption Regulation ('GBER').[1] While Article 107(2) TFEU includes a list of categories of aid that is automatically exempted from the prohibition of Article 107(1) TFEU, aid falling within the scope of Articles 106(2) or 107(3) TFEU is subject to the compatibility assessment.[2]

Such assessment is an exclusive competence of the Commission under Article 108 TFEU. In essence, the Commission may declare a given aid measure to be compatible with the internal market if its granting is necessary for achieving an objective or objectives of common

[1] In case of some sectors, the Treaty provides for more specific regulations. For example, Article 93 TFEU provides for an additional derogation with respect to transport. For more details on the application of State aid law in the transport sector, see Tibor Scharf, 'Transport', in Leigh Hancher, Tom Ottervanger and Piet Jan Slot, *EU State Aids*, Sweet & Maxwell, 2021, pp. 705 – 749.

[2] Commission Regulation (EU) No 651/2014 of 17 June 2014 declaring certain categories of aid compatible with the internal market in application of Articles 107 and 108 of the Treaty, OJL 187, 26.6.2014, pp. *1–78, with amendments.*