The importance of EU State Aid and the level playing field

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Introduction

• State aid control is a fundamental safeguard of the EU internal market

• The aim of State aid control is protection of the Single Market against distortions created by Member States (Antitrust targets companies)

• Art. 107(1) TFEU → general prohibition

• However, State aid can be allowed in specific circumstances subject to scrutiny by the Commission

• This is to ensure a level playing field in the single market
  → exclusive competence, subject to control by Union courts only
Contribution to President Juncker's agenda

• Competition policy supports the Commission's overall priorities

• President Juncker's priorities reflected in DG COMP's initiatives: digital single market, energy policy, financial services, industrial policy and the fight against tax evasion

• Focus action on significant competition distortions – 'Big on big and small on small' → cases, sectors and practices that hamper growth
State aid modernisation

- In 2012 the Commission launched a major reform of State aid control (*State aid modernisation* – "SAM")
  - Procedural Regulation
  - Widening of GBER
  - Revision of Guidelines
  - Notion of Aid notice was the last part of SAM → adopted last month

- Aims
  - Fostering growth
  - Big on big, small on small
  - Faster decisions
Making SAM work

Small proportion of aid under the control of the Commission with stricter conditions

Large proportion of aid under the control and responsibility of the Member States (enlarged and simplified GBER)

Avoid shipwrecks
Legal certainty concerns

Assistance to MS
Training actions
FAQ

Monitoring
Evaluation
Transparency

Partnership with MS
First results of SAM

• More than 2,400 schemes and individual cases under new GBER in 2nd half of 2014 and 2015
• GBER cases make up more than 80% of new cases
• Number of GBER measures compared to number of notifications:

  2011  50.94%
  2012  48.49%
    2013  41.37%
    2014  70.14%
    2015  89.44%
Energy sector
Sector inquiry regarding capacity mechanisms

• One of SAM's results: Scope for more ex officio work
• This new procedural tool supports the Commission's overall priorities
• Capacity mechanisms: measures to ensure that adequate capacity to produce electricity is available at all times to avoid black-outs
• Major impact on competition in internal electricity market; no recreation of national borders
• Interim report adopted (April 2016)
• Complements the Energy Union Strategy to create a connected, integrated and secure energy market in Europe
Sector inquiry - What did DG COMP do?

Questionnaires to market participants and public bodies in eleven Member States...

...with a capacity mechanism in place or in the planning.
Sector inquiry - What has DG COMP found?

• Capacity Mechanisms are not always necessary or well-justified
  • Is there really a security of supply issue? Calculation of 'adequacy' is not transparent and not harmonised
  • Reliability is not commonly defined, **objective** standards are rare
  • Most standards are not based on economic analysis (taking into account the value the consumer places on secure supplies)

• Capacity Mechanisms are not always well-designed
  • Most CMs are not open to all types of generation, but rather targeted at a specific group
  • Allocation of contracts happen administratively instead of competitively in half of the CMs
  • Penalties for non-delivery are not always sufficient to ensure reliability
  • Cross-border participation is almost never enabled
Promoting renewable energies

Context

• High share of RES desirable but if outside the market -> distortions
• RES support paid by consumers / taxpayers
• Fragmentation of markets (national measures)

Approach to State aid

Make them a part of the market
• Sell in the market
• No incentives to oversupply (if negative prices)
• Balancing responsibilities

Ensure cost-effective support
• Competitive bidding processes
• Where possible, competition between technologies

Cross-border cooperation
• Start opening up schemes

Renewable support systems constitute State aid

Need for effective State aid control to achieve RES targets whilst preserving the internal market
Approved schemes - operating aid to RES
Energy intensive users:

How to distribute the costs of decarbonisation?

**Aims**
- Common rules to minimise distortions
- Ensure sufficient financing base
- Promote ambitious environmental taxes
- Avoid carbon leakage

**State aid rules**
Partial and targeted reductions from climate/energy policy costs for energy intensive users:
- Charges to support renewable energy
- Environmental taxes, including national carbon taxes
- Indirect EU ETS emission costs
State aid and tax avoidance
How is taxation concerned by State aid control?

- Direct taxation falls within the competence of the Member States
- Exercise of national competences must be consistent with Union law – therefore also fiscal aid fall under state aid control
- The distortive effect of State aid is the same whether a subsidy is in cash, or in the form of lower bills – including tax bills
- More than 1/3 of aid (non-crisis) granted in form of fiscal advantage
- Various Communications provide Guidance
  - 1998 Communication on State aid and direct business taxation
  - 2016 Notion of Aid Communication
State aid and aggressive tax planning

• The financial and economic crisis has drawn again attention to aggressive corporate tax planning practices. Some economic operators have been pushing the limits of aggressive corporate tax planning far.

• Allegations about these instances where the object of public hearings in the US Senate and the UK’s House of Commons. The Commission listened and decided to look deeper into the matter.

• In response to this, a Task Force was set up to look into aggressive corporate tax planning practices, with an emphasis on tax rulings.

• Tax rulings endorsed artificial and complex methods, not reflecting economic reality.
What is it about: Transfer pricing

Reference is the arm's length principle

- **UNCONTROLLED TRANSACTION**
  - Group 1
  - Enterprise 1
  - Enterprise 2

- **MARKET PRICE**

- **CONTROLLED TRANSACTION**
  - Group 1
  - Low taxation country
  - Enterprise 1
  - Enterprise 2
  - No taxation country

- **TRANSFER PRICING**
  - Incentive to overprice products/services bought from low taxation country
First final decisions

- First Final decisions were adopted on 21 October 2015 regarding the Netherlands on Starbucks and Luxembourg on Fiat
- Both decisions are negative decisions with recovery
  - Recovery amounts are estimated at EUR 20-30 million per company
- Commission has used for the first time the new market investigation tools
- These decisions are assessed against the national tax system finding a violation of arm's length principle
National law as reference system

• To establish whether a tax measure raises State aid concerns, the Commission continues to examine whether it gives a selective advantage to one or several economic operators over others
• To that end, we compare the tax treatment of the companies that benefit from them to the ordinary tax treatment reserved to companies in comparable circumstances under national law
• The ordinary corporate-tax law in each Member State is thus the very reference against which we assess whether the tax treatment in individual cases departed from national law or practice
• The Commission is however not in the business of second-guessing the work of national tax authorities with regard to every single tax ruling. The Commission has subjected to deeper scrutiny only those rulings where taxation did not reflect actual economic reality
Financial services
Selected key requirements under the Crisis Communications

- Exceptional legal basis (Art. 107(3)(b) TFEU) and detailed rules explained in seven Commission legal texts.

- Financial stability as overarching objective while ensuring that State aid and distortions of competition are kept to the minimum.

- The exit of less efficient firms is a normal process in a market economy. The most distortive type of aid is aid which artificially keeps afloat non-viable companies.

- The compatibility assessment of restructuring aid aims to minimise those problems and distortions of competition.
Compatibility of restructuring aid

To be compatible with the internal market, the restructuring plan of a financial institution has to comply with three pillars:

- **Viability**
  - Return to long term viability in the longer term without State aid
  - Only healthy banks can finance real growth of the economy

- **Burden sharing**
  - Minimisation of the cost for the State/
    maximising own contribution
  - Mitigation of moral hazard

- **Competition**
  - Proportionate remedies reflecting:
    - Market characteristics
    - Relative/absolute size of the aid

If viability cannot be restored → liquidation plan
State aid control acted as the "de facto" resolution framework at EU level since 2008

• Under the exceptional legal basis (art. 107(3)b of the Treaty) and detailed rules explained in seven Commission communications ...

• ... from 2007 to 2015, DG Competition has worked on 117 banks in 22 Member States

• Out of € 45 trillion of assets in European banks
  • € 12 trillion assets in restructuring cases
  • € 1 trillion assets in liquidation cases

~30% of European banking sector under State aid control
~2% resolved
Large parts of EU banking sector subject to State aid conditionality

€ 4.9 trillion of aid approved by the Commission (39% EU GDP), thereof € 1.7 trillion used at peak (13.5% EU GDP)
The New World (post-BRRD/SRM)

• Is it really new?

  New rules, new players BUT State aid control will remain a central element of the Banking Union

• The paradigm change from bail-out to bail-in is a key element of the Banking Union.

• State aid / Fund aid will continue to be possible, but only as a last resort.

• State aid control remains a central element of the Banking Union, applies alongside the Bank Recovery and Resolution Directive (BRRD) and guarantees equality of treatment and level playing field between Banking Union ins & outs.
State aid: a trigger for resolution under BRRD

• From 1 January 2015, under BRRD any State aid will imply that an institution is *failing or likely to fail*.

• State aid can only be granted in resolution, unless it is one of the three exceptions of Article 32.4.(d):
  - a State guarantee to emergency liquidity assistance (ELA) provided by central banks
  - a State guarantee of newly issued liabilities
  - precautionary recapitalisations (can only be used to cover capital shortfalls arising under an *adverse scenario of a stress test*)
Key challenges

- In order to prevent resolution, Member States might use sophisticated intervention instruments (e.g. Special Purpose Vehicles, capital instruments, derivatives, funding guarantees)...

- ... in order to invoke the Market Economy Operator Principle, avoid imputability to the State, avoid selectivity or claim early intervention.

- The Commission's task is to preserve equality of treatment and level playing field – if a measure is State aid, the bank has to go in resolution; only if a measure is not State aid, it can go ahead.

- Otherwise, the whole resolution system and the Banking Union will be undermined.
State aid control going forward

• Deepen relationship with MS

• *Ex post* control and information (monitoring, evaluation, transparency)
  ○ Linked to MS role: if MS take more ownership, Commission can scale down

• More emphasis on significant *ex officio* work
Thank you