

# State aid 2008-2010: Before and after insolvency

Evert Verwey, secretary to the technical committee of the forthcoming INSOL Europe Annual Congress in Vienna, brings us a taster of the main topic of discussion



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Since 2008 there has been one word which has been repeated over and over in each language across the world: “financial crisis”.

What happened in the last two years? It seems that nobody knows: it has been a contemporary hurricane. It made no difference if we talked about the well-respected European-automotive company, a billion-euro London-based financial institution or even sovereign states; they all needed help. Just as in the 1850s when the railway industry in Arkansas

received state aid, several Member States had to go into rescue business again. Over and over Member States gave (sometimes twice) billions in cash injections to several conglomerates to stimulate the European market and avoid (even more) insolvencies. Opel, Alitalia, RBS, ING, Lloyds, UBS, Commerzbank, Volvo, Volkswagen, HSH Norbank, Northern Rock, Hypo Real Estate. All these respected companies of Europe (and many more) have sought and received state aid. For providing state aid a

Member State has to obtain approval from the European Commission, to be in accordance with the competition laws and the main principles of the European Union (“De Minimis” rule).

In 2007 the state aid granted by Member States was €67.4 billion. In 2008 the amount of state aid added up to the incredible amount of €279.6 billion, representing 2.2% of GDP of the European Union.<sup>1</sup>

Regulation of state aid is an important part of European competition law. This comes from

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the need to maintain a level playing field for all undertakings active in the Single European Market and to avoid Member States getting locked into a contest where they try to outbid each other to attract investments. The European Treaty prohibits any state aid granted by a Member State (or through state resources in any form) which distorts competition by favouring certain firms and trade between Member States. The Commission has the exclusive power to declare state aid compatible with the European Treaty.<sup>2</sup>

The state aid provided by Member States has put many European rules and regulations into the spotlight. What are these rules and implications of state aid?

## Lisbon Treaty

Article 107(1) of the Treaty on the Functioning of the European Union (Lisbon Treaty, hereafter: "TFEU"), provides that *"any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the common market"*.

According to European legislation, in some circumstances government interventions are necessary to preserve a well-functioning and equitable economy and therefore, articles 107(2) and 107(3) TFEU describe some situations in which state aid is allowed. These exceptions need prior authorisation of the European Commission.

The most pertinent of these exceptions are (i) Article 107(3)(a) TFEU covering *"aid to promote the economic development of areas where the standard of living is abnormally low or where there is serious underemployment;"* and (ii) Article 107(3)(c) TFEU referring to *"aid to facilitate the development of certain economic activities or certain economic areas, where such aid does not adversely affect trading conditions contrary to the*

*common interest"*.

As a result of the financial crisis, another exception to the prohibition on state aid has come into focus: Article 107(3)(b) TFEU covers state aid *"to remedy a serious disturbance in the economy of a member state"*. State aid to financial institutions may be justified on this basis.

In the beginning of the crisis, the European Commission was able to tackle individual cases of state aid for European companies under the *"Community Guidelines on State aid for rescuing and restructuring firms in difficulty"* ("R&R Guidelines").<sup>3</sup>

When the crisis spread, and Member States increased the extent of state aid provision, the European Commission thought it would be wise to act rapidly.

To meet this need, on 26 November 2008 the European Commission adopted the *"Temporary Community framework for state aid measures to support access to finance in the current financial and economic crises"* ("Temporary Framework")<sup>4</sup>. The EC recognised that under current conditions there is a need for new temporary aid to guarantee continuity of access to finance and to encourage continued investment. The plan is based on short-term measures to boost demand, save jobs and restore confidence, as well as well-considered investment to improve higher growth and longer term prosperity.

In particular, it enables Member States to grant, under certain conditions:

- aid of up to €500,000 per company for the next two years;
- state guarantees for loans at a reduced premium;
- subsidised loans, in particular for the production of green products (meeting environmental protection standards early or going beyond such standards); and
- the Temporary Framework relaxed the restrictions for state aid to promote risk capital investments. (risk capital aid up to €2.5 million per enterprise per year (instead of €1.5m) in cases where at least 30%

(instead of 50%) of the investment cost comes from private investors).

Cash grant, state guarantees and loans based on the Temporary Framework may only be granted to companies that were not "in difficulty" on July 1, 2008. The Temporary Framework expires on 31 December 2010.

This Temporary Frameworks is not as strict as the R&R Guidelines. Under the R&R Guidelines the European Commission will normally demand compensatory measures in return for the provision of state aid to avoid unfair competitive advantage. These measures may include divestments of assets, reductions in production capacity or a decrease in market presence.

To avoid any misunderstanding the European Commission stressed that:

*"during a financial and/or economic crisis, state aid control is all the more necessary because there can be greater temptation for Member States to grant aid that would risk putting out of business companies in other Member States, thereby making the crisis worse. State aid control also avoids subsidy races, which would tend to penalise smaller Member States which lack the deep pockets of larger Member States"* (MEMO/08/795

Brussels, 17th December 2008)

Besides, the European Commission may order member states to recover unlawful state aid. This is important to note and investigate in respect of a subsequent insolvency.

## What if...

What if a company which received state aid files for insolvency, and the Member State which gave state aid is instructed to recover this because it was given unlawfully?

Article 108 TFEU gives the European Commission the ability to order the recovery or repayment of unlawful state aid. The recovery of unlawful state aid shall be effected without delay and in accordance with the procedures under the national law of the Member State concerned,

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provided that they allow the immediate and effective execution of the European Commission's recovery decision.

A number of issues have been raised at Member State level as to the relationship between the recovery of state aid and (national) insolvency laws. The issues arising in insolvency proceedings are preferential treatment of recovery claims and participation in a restructuring plan. In Italy and Spain, payment claims by the government are usually treated as preferential claims in insolvency proceedings. In those countries, where the claim is based on administrative law, it would appear that preferential treatment is also available for state aid recovery claims.

In Germany some court decisions have clarified that state aid recovery claims are not subordinate even in situations where a claim by a private party would have been subordinate

(capital injection or grant of a loan by a shareholder). Restructuring plans in insolvency proceedings are a relatively new phenomenon in Europe. The question of whether the state can waive part of a claim for repayment of aid in such a restructuring plan in order to secure the continued existence of the insolvent business remains to be answered.

### After state aid

It is surprising to note that in the recent past some recipients of state aid have announced their objections to competition demands made by the European Commission. ING Groep NV ("ING") announced that it will file an appeal with the General Court of the European Union contesting the way the European Commission has calculated the amount of state aid ING has received. In December 2009, ING and the Dutch government had agreed to reduce the repayment

premium owed by ING upon its repurchase of the first €5 billion tranche of Core Tier 1 securities from the Dutch government, resulting in a penalty payment of €500 million instead of €2 billion. ING plans to contest the Commission's view that the €1.5 billion reduction is additional state aid.

Recently Greece received aid from the fellow Member States of the European Union after acceptance of a €700 billion bailout plan constructed by those same Member States. It seems that Member States will give each other state aid to prevent a further recession in the European Market.

Update – Special Edition on State Aid Interventions in the Current Financial and Economic Crises, page 6.  
[http://ec.europa.eu/competition/state\\_aid/studies\\_reports/archive/scoreboard\\_arch.html](http://ec.europa.eu/competition/state_aid/studies_reports/archive/scoreboard_arch.html).

4. This Temporary Framework has been amended since then a couple of times.

### Footnotes

1. European Commission, State Aid Scoreboard, Report on State aid granted by the EU Member States – Autumn 2009 Update, page 4.
2. "State Aid Action Plan – frequently asked questions".
3. European Commission, State Aid Scoreboard, Report on State aid granted by the EU Member States, Spring 2009

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