

State aid rules in the coal sector and linked energy sector under the Energy Community Treaty and European Law

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I. Objective

This study presents the EU State aid law requirements with the aim of better understanding the relevant rules of the Energy Community Treaty. The study explains the notion of State aid, the EU rules on the granting of aid in the coal and related energy sectors and reviews the consequences of non-compliance with these rules.

With the information provided, the question of whether a State measure might be State aid can be measured to avoid legal consequences. In addition, the study considers relevant decisions and judgments of EU Institutions and the accompanying case study paper available at bankwatch.org/publications/EnCom-stateaid-cases analyses the possible State aid issues of certain measures that may have been adopted by the Contracting Parties of the Energy Community Treaty in the coal and related energy sectors.

The study draws a number of conclusions regarding the application of EU-compatible State aid rules.

One of the major conclusion of the study is, that ***States not complying with State aid law requirements face serious risks as regards lawsuits both at national and international (European) level.*** Competitors, NGOs and other third parties have become aware that State aid law can be enforced through different means and can easily submit complaints, which can be the basis of further legal proceedings.

With due care and respecting State aid rules *ex ante* these risks can be mitigated. While establishing compliance with State aid rules in a given case one has also to bear in mind that State aid law is not static and the relevant rules have been changed in 2014. Moreover the ever-evolving jurisprudence of the European Courts brings further fine tuning as regards their interpretation.

II. Introduction - State aid rules under the Energy Community Treaty and under EU law

The Energy Community Treaty's objectives are similar to those of the European Union (hereinafter: EU) as regards the energy sector. The Energy Community Treaty even clearly refers to EU law in some of its articles. This is not a coincidence as the European Communities (whose successor is the EU) is one of the Contracting Parties of the Treaty.

The reliance on EU law is most prominent in the field of EU competition law where the European Commission (hereinafter: the Commission) as competition authority dealing with competition law issues outside State aid has traditionally very wide powers and competences conferred to it partly by the Treaty on the Functioning of the European Union (Articles 101, 102 and 106) and partly by Regulation 1/2003 which replaced the original Regulation 17/1962 of the then European Economic Community.

The Energy Community Treaty in its Article 18 considers as *acquis communautaire* the general principles of EU competition law as well as the relevant Articles of the EC-Treaty (which since 2009 has been succeeded by the Treaty on the Functioning of the European Union, hereinafter TFEU). Annex III of the Energy Community Treaty literally repeats most of the competition law provisions of the TFEU, namely Articles 101, 102, 106 and 107.¹ The reliance on EU competition law and more precisely on State aid law results in a situation where the Contracting Parties have the same substantive obligations as the Member States of the EU and have to comply with this set of principles.

1. Principles of State aid procedures are defined in Art 108. The Council of the European Union is moreover empowered in Article 109 of the TFEU to exempt certain aid categories from notification obligation under Art. 108. These two articles are not referred to by the Energy Community Treaty.

As the Energy Community Treaty does not have secondary rules on State aid, it is up to the Contracting Parties to ensure compliance with the State aid acquis, if they want to avoid a breach of their international commitments under the Energy Community Treaty.

Following these cross references this briefing uses the term Member State [of the EU], which is interchangeable with the term Contracting Party of the Energy Community Treaty.

It has to be mentioned that during their negotiations with a view to become members of the EU some of the Contracting Parties have also signed a Stabilization and Association Agreement with the EU and those agreements refer to EU competition and State aid rules and prescribe compliance with them, which implies that national rules on State aid have to be established and enforced.²

The aim of competition rules is to ensure that markets are not distorted by the practices of undertakings or policies of States thereby resulting in situations which harm consumers or the process of rivalry and innovation. State aid law, as part of the European competition law, is intended to contribute to the proper functioning of the internal market. State aid law limits the spending possibilities of the Member States. It does so because resources spent by the State distorts competition in the internal market. ***State aid law creates a level playing field between Member States, prevents a subsidy race and reduces the possibility of wasting public funds, for instance, by maintaining inefficient undertakings on the market.*** State aid law also aims to prevent situations where significant market power is built up with the help of State resources.

The reason behind these requirements is that ***State intervention is not desirable above a specific level³ as it distorts competition. Since, however, State aid may also generate benefits by contributing to a public policy objective, the prohibition of State aid under EU law is not absolute.*** This is why the TFEU empowers the Commission to assess whether the benefits outweigh the costs of distortions and requires Member States to notify their measures to the Commission.

III. The notion of State aid and the most frequent forms of State aid

The notion of State aid as defined in Article 107(1) of the TFEU is an objective legal concept and can only be interpreted by the EU Courts and in some cases by national courts. However this notion is applied also by the Member States' authorities and the European Commission. ***State aid is "[...] 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 [...]"***.

It is now well established in the case law that Art. 107(1) lays down a number of cumulative criteria for State aid to exist: transfer of state resources, conferment of a selective advantage and affectation of trade and distortion of competition. Since these criteria are cumulative, all of them have to be present in order for a State measure to constitute State aid. Even one of them is missing then one cannot consider the measure to be State aid.⁴

2. For more information see Botta M. *State Aid Control in South-East Europe: The Endless Transition in European State Aid Law Quarterly 1, 2013* and Botta M. *Enforcement of State Aid Rules in the Energy Community - Going Beyond Formal Compliance? Oil, Gas and Energy Law 2 (2014)*.

3. According to the case-law, there is no threshold or percentage below which it may be considered that trade between Member States is not affected. The relatively small amount of aid or the relatively small size of the undertaking which receives it does not exclude the possibility that trade between Member States might be affected. In this respect see judgments in case C-142/87 *Belgium v Commission (Tubemeuse)* [ECLI:EU:C:1990:125] paragraph 25; joined cases C-278/92 to C-280/92 *Spain v Commission* [ECLI:EU:C:1994:325], paragraph 20.

4. Case C-280/00 *Altmark Trans* [2003] ECR I-7747. paragraph 87 to 95.

The case law establishes that the content of each criterion is widely interpreted and therefore the notion itself is much broader than a simple subsidy. The case law makes it clear that the assessment of whether a measure constitutes State aid considers only the effects of the measure.⁵ Neither the cause, nor the objective of the State intervention has to be taken into account. However, the aims or objectives of a measures are relevant under the assessment of the compatibility of that measure with the internal market.

The notion of undertaking

State aid is only present where the beneficiary is an undertaking. The jurisprudence defines undertaking “as entities engaged in an economic activity, regardless of their legal status and the way in which they are financed”.⁶ Thus, competition law makes a distinction according to the activity of the entity and not the form, profitability or legal status of the entity under national law. Even non-profit entities may qualify as undertakings. The ownership of an aid recipient undertaking is also irrelevant. Public or mixed entities can also be undertakings.

The classification of an entity as an undertaking is always in respect of a given activity. The same entity may qualify for certain activities as undertaking and for others as a non-undertaking. What matters is whether the activity concerned is economic. The meaning of economic activity is again defined broadly by the courts. Economic activity is the offering goods or services on the market⁷ for remuneration by taking commercial risks. In general if something is provided for a price, it is economic.

Even when the State organises the offering of goods or services “in-house” (by its own departments) it is not enough to preclude the economic character of the activity. Taking the example of coal mining and electricity production, if the State owns a mine and a power plant and uses the coal only to produce electricity to cover the consumption of public institutions, this will not exempt these entities from the scope of State aid law as selling coal and electricity are economic activities.

EU courts have also expanded the notion of undertaking to infrastructure operators, if the infrastructure is used or exploited as an economic activity, namely for consideration. Moreover they also highlighted that the building of the infrastructure cannot be separated from its use.⁸ Therefore State aid rules apply even for State financing of such infrastructure (airport, ports, tollroads).

Since the concept of undertaking is based on an economic approach, different entities controlled by the same entity (e.g. by owing shares or appointing directors) all together are considered to be a single undertaking.⁹ Exceptions are the regulatory and public powers¹⁰ of the State (like issuing passports, air traffic control), activities which are compulsory and based on social solidarity such as compulsory social insurance or pension and activities which are provided by the State to all citizens and funded by taxpayers such as public education or public health.

5. *Case 173/73 Italy v Commission* [1974] ECR 709, paragraph 13.

6. *Joined Cases C-180/98 to C-184/98 Pavlov and Others* [2000] ECR I-6451, paragraph 74.

7. *Case 118/85 Commission v Italy* [1987] ECR 2599, paragraph 7; *Case C-35/96 Commission v Italy* [1998] ECR I-3851, paragraph 36; *Joined Cases C-180/98 to C-184/98 Pavlov and Others* [2000] ECR I-6451, paragraph 75.

8. *Joined Cases T-443/08 and T-455/08 Freistaat Sachsen, Flughafen Leipzig/Halle et al v Commission* [2011] ECR II-1311, in particular paragraphs 93 and 94, upheld on appeal, see *Case C-288/11 P Mitteldeutsche Flughafen AG and Flughafen Leipzig-Halle GmbH v Commission* [2012]

9. *Case C-480/09 P AceaElectrabel Produzione SpA v Commission* [2010] ECR I-13355 paragraphs 47 to 55.

10. *Case 118/85 Commission v Italy* [1987] ECR 2599, paragraphs 7 and 8.

State resources and imputability - State origin

State aid can only be granted directly or indirectly from State resources. In addition, the decision to grant aid must also be attributed to the State (imputability).¹¹ State resources are interpreted likewise broadly. All levels of the State administration are covered¹² and measures which have a negative impact¹³ or incorporate certain risk on the budget (tax exemptions, tax deferrals, guarantees) are considered as State resources.

As regards imputability, ***the decision to grant aid must be taken by the state or imposed by the state. This is of particular relevance when the aid is granted by a private or public entity not forming part of the government. In these cases the focus is on the control exercised by the State on the aid-granting entity.***¹⁴

If the spending of the sources is set by the State in legal norms, the conditions are defined by the State or the decision maker is dependent on the State (i.e. it cannot disregard the orders of the state, the State has veto, or its consent has to be obtained) then imputability is presumed.

The existence of imputability was a crucial point of the State aid assessment for measures in the electricity sector as Member States often design the financing from payments by consumers. Moreover, if private sources came under the control of the State they became State resources (e.g. special funds collected from the payments of consumers).

This is though not the case, if the State just redistributes certain sources directly between economic operators without gaining control over them. The often cited Preussen Elektra judgment¹⁵ dealt with this situation in the electricity sector. The German law imposed an obligation on private electricity suppliers to purchase electricity produced from renewable energy sources at fixed minimum prices (above the market price).

Since the national law did not set up any compensation mechanism or fund to cover the losses originating from this obligation on the electricity suppliers the measure did not entail the direct or indirect transfer of State resources to undertakings which produce that type of electricity. Therefore it did not constitute State aid.

The concept of advantage

Advantage in State aid law is any economic benefit which an undertaking would not have obtained under normal market conditions, that is without the intervention of the State!¹⁶ The simulation of market conditions and their effects is often a complex part of the State aid assessment and needs case by case assessment of the facts.

11. *Case C-482/99 France v Commission (Stardust) [2002] ECR I-4397, paragraph 24.*

12. *Case T-358/94 Air France v Commission [1996] ECR II-2109, paragraph 56.*

13. *Case C-83/98 P France v Ladbroke Racing Ltd and Commission [2000] ECR I-3271, paragraphs 48 to 51.*

14. *Case C-206/06 Essent Netwerk Noord [2008] ECR I-5497, paragraph 70;*

15. *Case C-379/98 PreussenElektra [2001] ECR I-2099.*

16. *Case C-39/94 SFEI and Others [1996] ECR I-3547, paragraph 60; Case C-342/96 Spain v Commission [1999] ECR I-2459, paragraph 41.*

During this assessment one has to compare the economic situation of the undertaking concerned with and without the measure and has to determine whether a market player would have provided similar benefits to the recipient or not.¹⁷

If after this analysis it turns out that a market player would not have offered the same benefits, the measure confers an advantage to the recipient. As it will be explained later, *the advantage can practically appear in any form, and any relief of financial burdens or operating cost is also advantage*. Advantage is also present if a measure compensates charges of a different nature that are unconnected with that measure. Since only the effect of the State intervention is relevant in some cases the advantage is transferred or channelled from the direct recipient to other entities who become indirect beneficiaries of the aid.¹⁸

Selectivity

State aid has to “favour certain undertakings or the production of certain goods”. It follows that general measures having equal effect on all undertakings are not considered selective, and hence they are not State aid. On the contrary, measures which provide advantage only to a limited number of undertakings are selective (e.g. tax reduction for small undertakings).¹⁹

Selectivity is often the key point of the State aid assessment in case of tax measures. This can happen either de jure when a measure clearly limits its scope to a defined group of undertakings²⁰ or de facto, when the measure is in theory open for every operator on the market, but certain conditions linked to it preclude some of them in practice (e.g. tax exemption can only be used after large amounts of investment).²¹

In the case law there is a three-step test of selectivity of tax measures. First the normal or general tax rule has to be established. This is the reference system. Second, it is examined whether the measure in question deviates from the reference system, and if yes, whether it puts the undertakings concerned in a more advantageous position than under the reference system.

Third, if the measure confers a selective advantage then it is necessary to ask whether there might be any objective justification for this derogation, which is based on the internal logic of the reference system such as not levying a profit tax on revenue which is not profit. Under this three-step test, undertakings in a comparable legal and factual situation have to be treated in the same way.²² Tax differentiation between undertakings in a non-comparable situation is therefore allowed.

17. *Case 173/73, Italy v Commission [1974] ECR 709, paragraph 13.*

18. *Case 30/59 De Gezamenlijke Steenkolenmijnen in Limburg, case C-403/10 Mediaset SpA v Commission [2011] ECR I-117, paragraphs 73 to 77.*

19. *Case C-143/99 Adria-Wien Pipeline [2001] ECR I-8365, paragraph 48.*

20. *Case C-75/97 Belgium v. Commission.*

21. *Joined Cases C-106/09 P and C-107/09 P Commission and Spain v Government of Gibraltar and United Kingdom*

22. *Case C-143/99 Adria-Wien Pipeline paragraph 41.*

Distortion of competition and effect on trade

In practice these two conditions are considered together as the case law deems them to be linked.²³ Contrary to other branches of competition law State aid rules do not require a detailed assessment of the effects of the aid and a more simplified approach is followed. In the majority of the cases the fulfilment of these conditions is assumed or is very easy to prove.

The jurisprudence supposes that if selective advantage is given to an undertaking operating on a liberalized market, then competition is or can be distorted and the condition is fulfilled.²⁴ Since the condition under Article 107(1) of the TFEU is very broad (“distorts or threatens to distort”) there is no need to prove that the beneficiary is actually better off. Nor is it necessary to compare the beneficiary to competitors.

The same is true for the analysis of the effect on trade, since in the internal market undertakings can freely export or import their goods and services and any advantage might influence their position compared to undertakings in other Member States.²⁵

This holds even for cases where the recipient is not involved in cross-border trade.²⁶ The case law states that with the advantage the recipient can compete from a stronger position. Only in a very small number of cases does the Commission accept that the activities concerned have a truly local character and that the measure is not liable to affect intra-EU trade.

How does the presence and amount of advantage depend on the form of the aid?

The answer to this question always needs a case by case assessment. State aid rules cover all aid irrespective of form. However, the specific method used to determine the amount of aid, if any, varies depending on the form of the aid. Therefore a brief review of the different requirements related to specific forms is needed to have a deeper understanding of the application the notion of State aid in practice.

Equity measures

Article 345 of the TFEU declares that the EU is neutral as regards the property ownership in the Member States. From this it follows that ***Member States can make investments as private investors. State aid rules however limit this freedom by declaring investments [e.g. loans and equity] as State aid, if under similar conditions and circumstances no market investor would have made such an investment.***

This is the market economy investor principle (MEIP) developed in the jurisprudence. If the MEIP is not met the beneficiary undertaking receives finance at more favourable terms and therefore an advantage.²⁷ To prove the existence of more favourable terms it is necessary to consider the risks assumed by the investor, under the same information, and compare it to the expected return or profit.

23. *Joined Cases T-298/07, T-312/97. Alzetta Mauro [2000] ECR II-2325, paragraph 81.*

24. *Case 730/79 Phillip Morris [1980] ECR 267, paragraph 11.*

25. *Case T-288/07 Friulia Venezia Giulia, [2001] ECR II-1619, paragraph 41.*

26. *Case C-172/03 Heiser [2005] ECR I-1627.*

27. *About the application of the MEIP see Commission 2013/126/EU Official Journal L 85/1. 23.3.2013.*

Loans

Loans provided by the State or State owned banks or financial institutions are considered to include State aid when the debtor could not have received the loan at the market at all, or only at a higher interest.

In the first case the whole amount of the loan is State aid. In the second only the difference between the interest rate charged and the corresponding market rate is the amount of State aid.

The market rate can be established by comparing the pricing of similar (amount, period, collaterals) loans for similar undertakings. As this may in practice be very complex, the Commission has created a proxy for the market interest rate. This is the so-called reference rate.²⁸

The reference rate consists of a base rate applicable for the given Member State and a risk premium that reflects the credit rating of the borrower and the quality of the collateral it can offer. The base rate is equal to long-term interbank rates, and is calculated by the Commission for each Member State.

Guarantees

Guarantees and similar financial instruments reduce the risks associated with loans and result in lower interest rates charged by lenders.²⁹ **If the State provides a guarantee without charging a premium that reflects the risk it assumes, it grants State aid.** The Commission has issued a notice on State guarantees and has set the conditions under which guarantees do not constitute State aid.³⁰

These are the following: the debtor cannot be in financial difficulty, the amount of the guarantee must be limited in terms of amount and time, the guarantee can cover only 80% of the debt and interest payments, and a market price (premium) has to be paid for the guarantee. In its communication on State guarantees the Commission has also set safe harbour rates for SMEs depending on their riskiness. These rates are considered as not conferring advantage to the borrower.

Privatization and sale of land

Privatization of State owned undertakings can confer advantage both to the buyer and to the entity sold. There is no advantage only if the States sells to the highest bidder.³¹ **If the State puts resources into an ailing public undertaking to save it until it is sold, then the State confers to it an advantage.** If the State imposes conditions concerning the sold undertaking after the sale, then the State does not act as a private vendor.

Sale of public land is free of State aid when the land goes to the highest bidder. If the sale is not effected through an auction, then the land has to be valued by independent experts and sold at a market price. In both the case of privatisation and the sale of land through an auction, the procedure has to be open, transparent and non-discriminatory.

28. *New Communication from the Commission on the revision of the method for setting the reference and discount rates Official Journal C 14/6, 19.1.2008.*

29. *Case T-154/10 France v. Commission.*

30. *Commission Notice on the application of Articles 87 and 88 of the EC Treaty to State aid in the form of guarantees Official Journal C 155/10. 20.06.2008.*

31. *Joined cases C-214/12 P, C-215/12 P and C-223/12 P Bank Burgenland.*

Long-term power purchase agreements

Before the first EU Directive on the electricity sector introduced the rules on liberalization the electricity supply was covered by long term contracts between the producers and the wholesale buyers. In most cases, the contracts were signed by State-owned entities on the buyer side. With liberalization these contracts were not 'market conform' any more since the fixed prices in the contracts deviated from the prices determined by spot and forward electricity markets. Less efficient producers could sell electricity only in peak demand periods when prices were higher. The most recent Commission investigations examined the Polish and the Hungarian systems right after the accession of these countries to the EU.

The Commission's assessment of the power purchasing agreements [PPAs] was based on the principle that the State, in all its purchasing of goods and services on the market, must not pay a price that exceeds the market rate. Therefore, when the State, possibly through the State-owned electricity distributor, enters into long-term PPAs with electricity generating companies it must ensure that the price it pays corresponds to the value of the electricity it purchases.

Recent case law indicates how such agreements can be free of state.³² ***At minimum a power purchasing agreement should not eliminate the commercial risk that should normally be borne by the generators of electricity such as the risk from fluctuations in fuel prices or the risk from the operation of plants. In addition, the State should try to diversify, to the extent possible, its sources of supply*** and should not rely exclusively on one or some generators. Lastly, any benefits from fixing long-term prices should be reciprocal. Not only should the supplier be guaranteed a stable price, but the purchaser should also be given discounts when costs decline.

Case study: Hungarian PPA

Hungary notified to the Commission its PPAs which were concluded between some power plants and the Hungarian electricity wholesaler MVM. The contracts' duration were pretty long (15-25 years) and the pricing conditions ensured a good return for the owners of the power plants (8% return on equity). Some of the contracts were linked to the privatisation of the old power plants and the buyers refurbished them. Their investment and operating costs were supposed to be covered from revenues under the PPA.

All of the contracts were signed with "take or pay" conditions, which obliged MVM to buy the capacities determined previously. MVM could not change the pricing formula unilaterally and in case it was not able to sell the energy on the market at least at the price paid, the State compensated its losses from a fund made up of payments by consumers. This compensation methodology was notified to the Commission in early 2004. The Commission however, instead of focusing on the compensation mechanism, asked questions about the link between MVM and the power plants including the conditions of the PPAs. Then the Commission opened a formal investigation procedure since it had doubts regarding the compatibility of the PPAs with State aid law. The power plants defended their acquired rights, and so did Hungary. The procedure was closed after almost three years with the Commission concluding that the PPAs were not market compliant.

As electricity cannot be stored in large quantities for long periods, a liberalised electricity market is characterised by much shorter contractual relations (spot market, daily contracts) and PPAs were covering 60-80% of the market, practically barring liberalisation from becoming effective. Moreover the pricing agreed in the PPAs was set in a way that the power plants could reach a very high return without any risk for a long period of time due to the take or pay condition. The Commission did not find the PPAs compatible with any of the State aid rules applicable at that time. The Commission could not find the contracts to constitute aid existing before accession ("existing aid") whose recovery cannot be asked as the exact exposure on the State was not known at the time of accession.

As the contracts were not suspended at the time of the accession they constituted incompatible and unlawful aid and the Commission was bound to order recovery of the advantage earned under the PPAs as well as to stop the PPAs.

32. See T-182/09, *Budapesti Erőmű v Commission and related Commission Decision 2009/609/EU*.

The latter was done by an Act of Parliament at the end of 2008 and the Commission required Hungary to carry out calculations and simulations from the day of accession until termination on an hourly basis about the revenues earned by the power plants and compare them with the revenues earned under the PPAs. The difference had to be recovered by the government from the power plants with interest (as to the involvement of stranded costs compensation in the recovery calculations see this section below).

The Commission's procedure and its outcome lead to far reaching consequences in the Hungarian electricity market. Moreover the power plants appealed at the General Court against the Commission's decision. The General Court dismissed all of the applications and found the Commission's decision correct. Some of the power plants even started arbitration proceedings against Hungary for terminating the PPAs and not paying fair compensation for the losses.

The Commission allowed the payment of only compensation for the so-called stranded costs (see in section IV below), which was obviously far less than revenues under the PPAs claimed by the power plants. In a nutshell, if long term PPAs concluded by State-owned entities and electricity producers contain pricing formulas, which lead to an outcome higher than the market price, or they have take-or-pay clauses, they are not considered to be market-based contracts.

IV. The most relevant rules for the compatibility of aid granted to the coal sector and linked energy sector

In relation to these two sectors substantive State aid rules can be divided into two categories: 1) allowing certain types of aid and 2) banning certain types of aid. Indeed, the Commission has recently revised most of the State aid *acquis* (State Aid Modernization, SAM), including that which concerns the two sectors.

Under the new State aid framework we have to differentiate between aid subject to ex ante notification to the Commission and 'block exempted aid' which Member States can implement without notification and are only required to send ex post just summary information.

Although the general rule under Article 108(3) is that Member States have to notify aid ex ante, the State Aid Modernization has broadened significantly the possibilities of Member States to grant block-exempted aid. With this change the Commission wants to avoid unnecessary notifications for which there is a long standing practice as regards the compatibility criteria.

With respect to aid that is not block-exempted and therefore has to be notified, the Commission assess its compatibility on the basis of the so-called "common assessment principles". These principles are the following:

- a) Contribution to well-defined objective of common objective: the aid should not be advantageous only for the beneficiary but for the wider community as well.
- b) Need for State intervention, existence of market failure: the State can grant aid only if the market in itself does not deliver the desired outcome.
- c) Appropriate policy instrument: other State measures would not lead to the desired outcome.
- d) Incentive effect: the aid has to change the beneficiary's behaviour compared to the scenario without aid.
- e) Proportionality of the aid: the aid should not exceed the minimum required to bring about the desired effect.
- f) Avoidance of undue negative effects on competition and trade: the measure has to be established in a way that negative effects (e.g. crowding out other operators, creating market power or entry barriers, maintaining inefficient firms) are limited.
- g) Transparency of aid: the relevant information about the aid (e.g. beneficiary, amount) has to be published on a website for all decisions after 1 July 2016.

Member States have to provide in the notification documentation sufficient evidence to demonstrate how all of the above principles are respected. If the Commission deems that the notification is incomplete it sends written questions to the Member State and takes the final decision only after all necessary information is at its disposal.

Closure aid for the coal sector

There is an explicit Council Decision (787/2010/EU) adopted in 2010, which allows aid to coal mining but in a very restricted manner. This is because there is overcapacity in this sector and coal is not a clean source of energy. By contrast, Council Regulation (1407/2002/EC) which is no longer in force allowed aid for operating losses. ***The Decision allows operating aid to be granted as an exceptional tool for inefficient coal mines only if their irreversible and definitive closure has been decided and aid is limited to the exceptional costs of the closure.*** The Decision defines the eligible costs strictly. The annual amount of the closure aid must be reduced significantly in comparison to the previous year. The eligible costs for closure aid and exceptional costs can be found in Annex I of this study.

An undertaking receiving aid under the Decision cannot receive any further State aid in respect of these costs. Aid under the Decision can only be granted if notified to and approved by the Commission. The notification has to contain:

- a) identification of the coal production units;
- b) the real or estimated production costs for each coal production unit per coal year;
- c) estimated coal production, per coal year, of coal production units forming the subject of a closure plan;
- d) the estimated amount of closure aid per coal year.

Environmental impacts and the efforts to mitigate the negative effects have also to be shown.

Member States granting aid under the Decision are also subject to a regular reporting obligation to the Commission. Since the adoption of the Council Decision (December 2010) the Commission has dealt with a handful of notifications concerning aid for the closure of coal mines in different Member States, the most recent of which was taken in early February 2015.

In all cases the mines received operating aid under the previous rules which were incorporated in Council Regulation 1407/2002/EC. However under the new Council Decision, Member States have to decide either to stop providing aid to uncompetitive coal mines or to set a closure plan and grant aid just for the costs until the closure and for the closure itself (see above).

Case study 1: Coal mines in Poland

Poland notified its plan in May 2011 and the Commission adopted a positive decision in November 2011 (decision in case SA.33013). The measure concerned hard-coal mines which were closed already before 1 January 2007. The costs covered were those of the closure including environmental remediation and some social payments for the miners under collective labour agreements, court judgments or settlements. The total budget of the scheme for 2011-2015 was around EUR 603 million. Part of the aid was granted as a waiver from social security contributions and environmental fees and penalties.

Surprisingly the Commission did not object to this, although in other cases it required full compliance with environmental rules. Cumulation with other types of aid was excluded. After establishing that the measure constituted State aid, the Commission compared the eligible costs of the scheme with the costs detailed in the Council Decision. The value of the land after the remediation was to be deducted from those costs. The Commission found the scheme compatible with the Council decision but reminded the Polish authorities about their regular notification and monitoring obligations.

Case study 2: Coal mines in Romania

In Romania there was only one hard-coal mining company with several production units. The Romanian authorities made an assessment on the viability without State aid for each production unit although the public debts of the company (EUR 1200 million) were not taken into account. The authorities confirmed that any aid granted to handle the public debts would be subject to a different notification.

Based on those calculations, three units had to be closed (one in 2015, two in 2017) and the notified measure covered only aid to those three units.

The Romanian authorities notified a detailed breakdown of costs and the aid tranches per year in every category allowed under the Council Decision (closure, rehabilitation, worker support, and also the activities which would mitigate the environmental impacts). The total amount of the plan was EUR 269 million. The Commission found the measure to constitute State aid and declared that the costs covered complied with the Council Decision, although it reminded the Romanian authorities that annual corrections have to be made based on the real costs incurred. The Commission also highlighted that the aid would not lead to distortions on the coal market and that it was decreasing in every year as well as that it was lower than the amount granted under the previous Council Regulation. After reiterating that the exceptional costs covered did not result from the non-compliance with environmental regulations and the ban of cumulation with other types of aid, the Commission approved the financing of the closure plan (decision in case SA.33033).

Case study 3: Coal mines in Hungary

The Hungarian notification (decision in case SA.33861) concerned the closure of a lignite mine (Márkushegy) whose coal was used by a power plant to provide heat and electricity for the city of Oroszlány. The mine and the power plant formed a single economic unit. The production was envisaged to be stopped in 2015, however the closing process would last until 2017.

The budget of the measure was EUR 140 million. Here again the costs categories followed the logic of the Council Decision and emphasis was put on environmental compliance. The possibility was mentioned that the power plant might be replaced by a biomass plant. The nature of the Commission assessment was similar to the previous ones. During the notification it had to be ensured that the costs of the mine and the power plant were separated and a simulation was made about the revenue of the mine by giving the coal to the power plant and creating revenues only at the side of the power plant for the use of electricity and heat.

Case study 4: Coal mines in the Czech Republic

The Commission issued on 12 February 2015 a press release that it had approved closure aid under the Council Decision for the Paskov hard-coal mine (decision in case SA.39570) whose restructuring was several times unsuccessful in the past. The decision is not published yet.

According to the press release the closure costs were covered and “[T]he proposed Czech measure will contribute to funding one-off severance payments to workers who have lost or will lose their jobs due to the closure, as well as to provide special bonuses to workers who have been exposed to occupational health risks working in the mine.”

Regional aid

Regional aid is meant to address regional disparities within the EU thereby strengthening cohesion. Regional aid rules allow subsidies for investments and new jobs in regions which are less developed in terms of GDP/capita than 75% of the EU average and to a lesser extent to regions which are less developed in relation to the national average.

In the case of regional aid the new rules can be separated as regards the regional aid guidelines requiring the aid to be notified and the relevant provisions of the general block exemption regulation [Regulation 651/2014, the general block exemption regulation, hereinafter: the GBER].

Regional aid can only be granted to initial investment. Simple replacement investment is excluded from its scope. Compared to the rules applicable in 2007-2013, the current regional aid rules allow aid for coal mines subject to notification, but exclude the granting of regional aid in the energy sector (see below).

Therefore theoretically and legally it is possible to grant regional aid to coal mines. However, the requirements of the common assessment principles set by the regional aid guidelines 2014-2020³³ are fairly burdensome, especially when looking at individual aid to a single beneficiary.

33. *Guidelines on regional State aid for 2014-2020 Official Journal C 209/1 23.7.2013.*

In order to grant regional aid to develop or open a coal mine, the granting authority has to prove that the aid is part of a coherent regional strategy and that it can have a positive impact on the economy. The costs of the project have to be established, and both tangible and intangible investments or gross wage costs over two years are eligible. In addition, the relevant environmental requirements have to be complied with. The beneficiary has to contribute at least 25% of the project costs with its own resources without aid, which makes it difficult for purely State-owned entities to receive regional aid.

The investment has to be maintained for 5 years [3 years for SMEs], and the beneficiary has to show with internal documents that the aid is necessary to make the project sufficiently profitable (scenario I) or that the aid is only compensating the disadvantages of the underdeveloped region and additional cost in comparison to the same project being carried out without the aid in a more developed region (scenario II). This comparison is called counterfactual analysis. The aid intensity cannot be higher than the regional aid map (see Tables 2 and 3) set by the Commission and/or the amount cannot exceed the funding gap of the project. Projects with eligible costs exceeding EUR 50 million are subject to stricter requirements. Taking into account the level of proof under scenario I and II and the overall situation of the coal mining sector in Europe ***it is very difficult to grant regional aid for a new mine or for the extension of an existing one.*** Regional aid cannot be compatible with the internal market:

- if it creates additional capacity on a declining market,
- if it contributes to the maintenance of inefficient market structure,
- if it weakens competitors, maintains or create market power, discourages new entrants, or
- if it contributes to the loss of activity elsewhere in the EU.

Combining these requirements with scenario I and II, it is nearly impossible to comply with all the elements. Both coal consumption and EU demand are declining, a significant number of undertakings in the sector are not profitable and because of the location constraints (need of coal) it is difficult to prove that there was a credible alternative location in a more developed region.

Energy and environmental aid

The State Aid Modernization had a significant impact on the State aid rules concerning environmental measures. First, here again the use of block exempted aid is much simpler than aid under the relevant guidelines. Second, the new environmental aid rules also cover the energy sector. The new guidelines setting the compatibility criteria for notifiable aid are called energy and environmental aid guidelines³⁴ (EEAG).

Third, due to the development of the jurisprudence as regards aid for infrastructure projects (e.g. the Leipzig-Halle judgments) and to the need for a unified internal market for energy, the new State aid rules set conditions for infrastructure financing. Here we have to mention that a special Commission notice has been adopted for financing important projects of common European interest (IPCEI), which might be relevant for cross-border energy infrastructure and storage capacities serving several Member States.

The basic approach in the field of environmental aid is that ***State aid can only be granted for projects (costs) which go beyond EU environmental standards or in the absence of such standards go beyond national requirements. Otherwise the aid would not have incentive effects as the undertakings would have to abide by the legally required standards in any event.*** Additionally, eligible costs are established after a comparison to those of a non-environmentally friendly project and only the additional costs are eligible after deducting any operational benefits (energy saving, cheaper maintenance costs).

From this it follows that in certain cases the eligible costs are only a small fraction of the total costs of the project. Bonuses (+20/+10%) for SMEs are in general applicable resulting in higher aid intensities. As a detailed presentation of all environmental and energy aid types would go beyond the scope of the this study only the most relevant points are presented here.

34. *Guidelines on State aid for environmental protection and energy Official Journal C200/1 28.6.2014.*

The block exemption regulation contains simplified rules for environmental aid and energy aid projects.³⁵

- The possibility is open for Member States to grant aid to undertakings which go beyond environmental standard or carry out energy efficiency investments.
- Aid can also be granted to investments in highly-efficient cogeneration units, district heating and cooling.
- The regulation allows investment aid in new installations producing electricity from renewable sources and also operating aid in the form of feed-in premiums topping up market price but not substituting it (feed-in tariff) for such electricity. The latter can only be granted after an open bidding procedure between potential producers with some additional conditions. For small scale producers (<500kW) the conditions are more relaxed.
- The regulation also allows environmental tax benefits. The beneficiary has to pay the minimum level of taxes in case they are harmonized at EU level (Directive 2003/96/EC).
- Moreover, aid can be granted for the investment costs of energy infrastructure (excluding electricity and gas storage and the oil sector) if after the deduction of profits there is a funding gap in the project.

It is important to highlight that any aid under the GBER has to comply with the general rules on incentive effect, transparency, cumulation, publication etc. The EEAG cover also projects not mentioned in the GBER or above the notification thresholds set therein. The EEAG are based on the common assessment principles explained previously and are deemed to cover projects outside the scope of the GBER. Besides the types of aid listed under the GBER, the EEAG allow aid for carbon capture and storage (CCS) projects, operating aid for energy intensive users, and have more detailed rules on environmental tax exemptions and wider applicability for energy infrastructures, and generation adequacy (continuous supply of electricity) and tradable permits (emission trading systems).

Case study: Conversion of a coal power plant in the UK

The complexity of applying State aid requirements to energy and environmental projects is also highlighted by the fact that the Commission opened a formal investigation procedure (see details in section IV) on 19 February 2015 concerning a plan of the UK government to support the conversion of the Lynemouth black coal-fuelled power plant to biomass (wood pellet) fuelled plant.³⁶

The focus of the investigation is on the proportionality of aid and whether aid is necessary to achieve environmental objectives. The Commission is also assessing whether the positive effects of the aid outweigh the distortive effect on the market. The capacity of the plant would be 420 MW and the form of the aid would be the “contract for difference”, which is the standard solution in the UK to promote the use of low carbon energy sources. Under the contract for difference electricity sold on the market below the strike price can be supplemented by a top-up to reach the previously set strike price.

There is no guarantee from the State's side to buy the electricity, only to pay the top-up if it is sold on the market. A high amount of wood pellets would be transported to the power plant from USA and Canada. This is one of the reasons, besides the level of the strike price, why the Commission has started the formal investigation procedure.

The Commission is double checking the calculations made by the UK authorities and also their reliability as well as the profitability of the project since these have a significant impact on the level of the aid. The considerable amount (1.5 million tonnes / year) of wood pellets to be transported is a cause for concern as regards distortion of the global wood pellet market and negative environmental impacts.

35. Articles 36-49. of the GBER.

36. The text of the decision (SA.38762) is available at:
http://ec.europa.eu/competition/state_aid/cases/255986/255986_1634646_59_2.pdf.

Compensation for stranded costs in the electricity sector

With liberalizing the electricity sector across the EU the Commission has recognized that the behaviour of the market players will significantly change. Their capacity cannot be further absorbed by long term power purchase contracts and their future revenues, including profits, would be much more uncertain.

Competition on the other hand would put pressure on the market players to operate more efficiently and this could lead to a drop of energy prices. These changes in the electricity market may lead to a situation where the costs of investments made by energy producers in the past could not be recouped under the conditions of the liberalized market. However, the Commission wanted to ensure a smooth transition to genuine competition and not to jeopardize the viability of electricity undertakings.

Consequently, it adopted a notice³⁷ on the possibility to grant compensation in line with State aid rules for the investments made or committed but not depreciated before the liberalization (date of entry into force of the first electricity directive). These investments are the so-called “stranded costs”. Compensation can only be granted if the Commission approves the calculations, and Member States have to provide annual reports on the amounts paid and ex post calculations. Undertakings receiving compensation for stranded costs cannot benefit from rescue and restructuring aid.

In the calculation of the costs any internal revenues of the undertaking, even coming from producing units not touched by the stranded costs have to be deducted (consolidated approach). The notice has been applied only by a few Member States: Italy, the Netherlands, Greece, Portugal, Belgium, Poland and lastly by Hungary. The Member States used several times this compensation to offset the effects of terminating long term power purchase agreements.

Case study: The Hungarian stranded costs compensation scheme

After long discussions with the Commission about the compatibility of the Hungarian system of long term power purchase agreements (PPAs) Hungary notified its stranded costs compensation scheme to the Commission. It was a somewhat special measure as the intention was to grant compensation only to power plants which had to pay back unlawful and incompatible aid originating from the PPAs.

Hungary did not proceed with the recovery procedure for PPAs until the Commission cleared the compensation scheme (decision in case N691/2009). Three power plants were subject to the recovery order based on the PPAs and calculations were only made for those power plants.

In all three cases the amount of stranded costs was higher than the amount that had to be recovered. In order not to infringe the recovery obligations the Hungarian authorities monitor the future cash-flows (based on the forecast dispatch, demand and price assumptions) of the three plants and compare these with the forecasts submitted with the notification until the original expiry of the PPAs.

If a plant earns higher revenues and profits as forecast by the energy regulator they are deducted from their pool of stranded costs. Should this method lead to negative stranded costs the recovery obligation comes into play again and the plant has to pay. The difficulty of the case was on the one hand to carry out calculations both for the recovery and for the stranded costs at the same time (to avoid recovery in practice as much as possible) and to do this in a relative short timeframe.

Independent experts were involved in the calculations who had the necessary modelling software. Procuring these experts also led to some delay in the procedure. In the end the Commission considered the scheme as compliant with the stranded costs notice.

37. *Commission Communication relating to the methodology for analysing State aid linked to stranded costs Adopted by the Commission on 26.07.2001 not published in the Official Journal.*

Compensation provided for the provision of services of general economic interest

Under Article 106(2) TFEU Member States are entitled to support the provision of services of general economic interest (SGEI). SGEIs are services which have special characteristics as compared to other services on the market. SGEIs are considered to be essential to some or all groups in society and for this reason they are expected to be supplied universally at affordable prices, high level of quality, etc.

The State is justified to intervene when SGEIs are not satisfactorily provided by the market under acceptable conditions in terms of price, quality, continuity or universality. The Member States have a wide margin of discretion in defining SGEIs and the terms under which they should be provided. The Commission has only competence to check manifest errors.

However, the discretion of the Member States is limited when EU law regulates a sector and defines the SGEI in that specific sector (like in the electricity sector). SGEI providers have to be obliged by an act of the State to offer their services under predefined conditions.

The landmark Altmark judgment in 2003 has established that under certain, very strict, conditions State compensation for the extra costs of SGEIs does not constitute State aid. The four cumulative conditions are the following:

- The recipient undertaking must have public service obligations imposed on it and the obligations must be clearly defined;
- The parameters for calculating the compensation must be objective, transparent and established in advance;
- The compensation cannot exceed what is necessary to cover all or part of the costs incurred in the discharge of the public service obligations, taking into account the relevant receipts and a reasonable profit;
- Where the undertaking which is to discharge public service obligations is not chosen pursuant to a public procurement procedure which would allow for the selection of the tenderer capable of providing those services at the least cost to the community, the level of compensation needed must be determined on the basis of an analysis of the costs of a typical well-run company.

In the past ten years only a handful of Commission decisions or court judgments confirmed compliance with all of the above four conditions. ***In the majority of the non-compliant cases the Member State did not select the provider in an open tender allowing real competition***, or they did not specify ex ante parameters of compensation, while the second part of the fourth condition proved really difficult to apply in practice.

The Commission elaborated in 2005 and then in 2012 rules on how to grant compensation that is compliant with Article 106(2) TFEU. Without going into details, these rules do not request Member States to prove that the fourth condition of Altmark is satisfied. The SGEI rules require compliance only with the first three Altmark criteria but they also impose on Member States the obligation to comply with relevant public procurement procedures. The compatibility assessment does not search for the least cost but tries to prevent overcompensation without requiring the highest efficiency level possible. Bigger amounts of compensation are subject to more detailed scrutiny than smaller ones.

As regards the electricity sector, Article 15(4) of the current Directive 2009/72/EC stipulates that “A Member State may, for reasons of security of supply, direct that priority be given to the dispatch of generating installations using indigenous primary energy fuel sources, to an extent not exceeding, in any calendar year, 15% of the overall primary energy necessary to produce the electricity consumed in the Member State concerned.”

Similar provisions were found in previous EU directives for the electricity market. Member States have obliged certain operators to produce electricity from peat, lignite or coal. However, even if some operators are entrusted with SGEI obligation as defined by EU law, State aid law and compliance with other provisions of the TFEU cannot be disregarded.

Case study: Electricity produced from coal in Slovenia

In its decision 2007/580/EC, the Commission examined the financing of the Trbovlje power plant which was obliged to use 15% of its fuel from domestic resources (brown coal which was the only fossil fuel in Slovenia) to produce electricity and meet the security of supply requirements.

The plant produced heat as well as electricity. Since Slovenia considered its payments to be compensation for SGEI, the Commission applied the four conditions of the Altmark judgment to establish whether there was State aid or not.

As regards the first condition, the assessment was positive because the plant was under obligation to use brown coal to produce energy. On the second condition, the Commission stated that the compensation was granted through a fixed purchase price and the price-fixing followed a transparent methodology with a list of eligible costs, which covered only the plant's generation costs.

The second criterion was also fulfilled. In relation to the third condition, the Commission concluded that the purchase price did not cover more than the cost of generating the expected amount of electricity. It did not include any profit element.

The Commission therefore considered that this was in line with the third condition. During the analysis of the fourth condition it was clear that the power plant was not selected through an open and competitive procedure, but it was shown that this was the cheapest solution for the community. It was proven that only two power plants were capable of complying with the obligation to produce 15% of the national electricity demand from domestic energy sources (one of them was Trbovlje).

The other plant was however producing at full capacity which would require investment to comply with the obligation set by the national authorities based on the Directive. In order to exclude overlaps, support to Trbovlje covered only the share of the 15 % which could not be covered by the other (Šoštanj) plant. Since there was no other real alternative and the financing did not include any profit, the Commission accepted this solution as the one with the least cost for the community and hence in line with the fourth condition of the Altmark judgment.

The Commission also noted that building any new capacity would lead to high investment costs to be covered by the State and in case of public procurement the bidder would have requested a reasonable profit in order to generate a return on the investment.

This all would lead to a higher amount of compensation than to finance the existing Trbovlje plant. Surprisingly the Commission did not demand proof that Trbovlje was a typical, well-run undertaking but argued that nothing indicated that this was not the case. Then the Commission compared the costs of using biomass (renewable but probably indigenous energy source) and concluded that brown coal was the cheapest solution to comply with the 15% rule. This was probably the lightest successful Altmark assessment ever made by the Commission.

Case study: Electricity produced from coal in Spain

The General Court dealt with the issue of granting State aid for the provision of electricity under the 15% rule set by the electricity directive recently (Case T-57/11, *Castellnou Energía v Commission*). In 2010 the Commission considered the Spanish measure of granting preferential dispatch and compensation to ten electricity producers using domestic hard coal up to 15% of the domestic demand as compatible aid under Article 106(2) TFEU (decision in case N178/2010).

Based on this mechanism, which was set for a definitive period of four years, every day, the outcome of the clearing of the day-ahead electricity market was modified to the extent necessary to ensure that the above-mentioned coal-fired power plants could place on that market pre-defined volumes of electricity generated out of indigenous coal. This meant that those producers were granted stable demand for their product at a preferential price. Spain argued that the measure enhanced security of supply by creating backup for electricity generated from renewable energy sources that were highly variable due to weather conditions.

Spain also mentioned that the Spanish electricity system was not well connected to other major European systems, so security of supply was needed.

The capacity payment mechanism was financed through a levy imposed by national law on electricity retail suppliers as well as direct consumers and was managed by an entity entrusted by the Spanish TSO. Payments to the generators were also made by order of the TSO under a very complex mechanism.

After confirming the presence of an SGEI and the compliance with the 15% threshold, the Commission did not follow the logic of the Slovenian decision, as it considered the fourth Altmark criterion was not met, given that some of the costs of the power plants were based on historic values, but not on values associated with the hypothetical well-run operator. Spain did not question this statement of the Commission.

After having established that the other elements of Article 107(1) were also met, the Commission analysed the compatibility of the aid based on its framework for State aid in the form of public service compensation in force at the time of the decision and found it compatible as the costs taken into account were well-founded and overcompensation was excluded. Since several third parties submitted complaints during the procedure and the Commission assessed the compatibility with other EU law provisions as well, namely the compliance with the State aid rules for the coal sector in force at that time.

The Commission separated the legal basis for the Coal Regulation 1407/2002/EC (Article 107(3)(e) TFEU) and the SGEI framework (Article 106(2) TFEU), and stated that one did not limit the scope of the other. The Commission dismissed the complaints that the measure was indirectly granting advantage to coal mines by creating artificial demand for coal.

The Commission also dismissed the complaints that the measure was favouring only Spanish companies and thereby infringing the free movement of goods and the freedom of establishment. Third parties also raised the issue of environmental protection, arguing that the measure is in breach of climate change obligations undertaken by Spain and the EU. The Commission argued that the possible higher emission coming from the higher use of coal would be subject to the CO₂ trading mechanism, which was from a quantitative point of view a capped system. Therefore the measure did not compromise the Spanish or EU CO₂ emission target.

This Commission decision was appealed to the General Court by Castelnou Energía, an electricity producer using natural gas. The applicant questioned mainly two issues in the Commission decision. First, it questioned the SGEI character of buying and using domestic coal and also whether it really contributed to the security of supply as well as the insufficient assessment from the Commission's side.³⁸

Here the GC accepted the Commission's approach and found it sufficient to rely on the provisions of the Directive. The possible interruption of coal supply or supply of any other fuel was not dealt with in detail either in the Commission decision or in the GC's judgment.

The GC even said that the Commission went further than requested by the Directive by assessing the compatibility of the measure under Article 106(2). The GC dismissed the plea of the applicant in this regard. Second, as regards the infringement of other EU law provisions, especially the rules on environmental protection, the GC confirmed that if the aim of the measure is not environmental protection the Commission is not bound to take environmental rules into account during the compatibility assessment.

Nor can the Commission use its powers concerning the compatibility of a State aid measure in order to determine whether the measure infringes other parts of EU law. Nonetheless, the Commission cannot declare compatible a measure when it is inseparably linked to such infringement. One of the parties joining the case mentioned that the measure infringed the polluter-pays principle of EU law (Article 191(2) TFEU), but the GC dismissed this argument as well by pointing out that after 2013 the CO₂ quotas were not free of charge for the polluters, namely for the power generators. The GC also underlined that even if a measure has negative environmental effects this did not necessarily harm the internal market and the four freedoms.

38. *Case T-57/11 Castelnou Energía v Commission*.

Rescue and restructuring aid

State aid rules allow Member States to rescue and restructure undertakings in financial difficulties only if the aid is granted in line with the relevant guidelines.³⁹ Since there is a special Council decision for the rules on closure aid (see section IV) to coal mines these horizontal guidelines are not applicable to the coal sector. Nevertheless they can be applied in the energy sector. ***The guidelines allow rescue aid only as a temporary help in the form of loan or guarantee at market rate for 6 months until the future of the undertaking is decided.*** If the undertaking or its assets are not bought by third parties in the meantime, the beneficiary should either be wound up or restructuring aid can be granted after the Commission has individually assessed the measure.

This assessment focuses on the issue whether the viability of the undertaking can be restored in the medium term and how much State aid is needed for this purpose. Compatible restructuring aid requires private investors to move first and the State can only be the last resort to finance. Moreover the beneficiary should finance a significant part (25-50%) of the restructuring costs, and a detailed restructuring plan has to be submitted to the Commission identifying the causes of financial difficulty and solutions.

The plan must be realistic, robust and based on current market data as well as forecasts. The form of the restructuring aid has to be adapted to the liquidity and capital needs of the beneficiary. The aid has to be limited to the minimum necessary to achieve viability. The recipient also has offer “compensatory measures” to offset the distortion caused by the aid. Such measures normally take the form of divestment or constraints on commercial behaviour.

De minimis aid

Article 107(1) TFEU defines State aid as having an effect or possible effect on competition and on trade between Member States. The Commission has defined a small amount of aid that has a negligible effect on competition and trade.⁴⁰ Such de minimis aid is consequently not State aid in the sense of Article 107(1). The current rules define the de minimis aid threshold to be EUR 200,000 per undertaking per three fiscal years (see Table 4).

De minimis aid may also be granted to undertakings in the coal sector and also to undertakings in financial difficulty. This threshold applies irrespective of the form of the de minimis aid or the objective pursued. The grant equivalent, namely the amount of advantage conferred to the beneficiary has to be calculated before granting the aid. It has to be expressed in present values if the disbursement is made in different calendar years.

It has to be stressed that the ceiling is applied to every single undertaking. From this it follows that legal entities which through votes, nomination of the directors or other means of control form a single undertaking, then the ceiling is not multiplied by the number of legal entities but remains EUR 200,000. For example, if a coal mining company has 60% of the shares of a company operating a power plant then the mining company exercises dominant influence on the power plant and they form together one undertaking. Hence they have one common de minimis threshold.

Although de minimis aid is not State aid in the sense of Article 107(1) TFEU, it cannot be used to circumvent the ceilings and aid intensities which are laid down in other State aid rules. This means that de minimis aid funding costs which are eligible to receive aid under other rules can be granted only up to the ceiling defined in those other State aid rules. For example, if the undertaking receives regional aid up to the maximum aid intensity allowed, it cannot obtain de minimis aid linked to the same costs (e.g. an investment loan below market rate to finance the same investment).

39. *Guidelines on State aid for rescuing and restructuring non-financial undertakings in difficulty, Official Journal C 249/1, 31.07.2014.*

40. *See Regulation 1407/2013/EU, Official Journal L 352/1 24.12.2013.*

V. Legal consequences of not complying with State aid rules

State aid law defines two different breaches of law, which have different legal consequences. (See Table 1): i) Aid that is put into effect before it is notified in accordance with Article 108(3) TFEU is unlawful. As already mentioned earlier, Member States can also comply with procedural requirements by granting aid that does not need to be notified such as de minimis aid or aid based on the GBER.

[It is important to point out that the *Energy Community Treaty currently does not refer to Article 108 TFEU, therefore, on procedural issues the Contracting parties have to follow other ECT rules or national rules.*] ii) Aid that does not comply with the compatibility requirements set mainly by the Commission is incompatible with the internal market.

Unlawfulness or illegality: Non-notified aid

It is the responsibility of Member States to duly notify their aid measures in advance and wait until the Commission adopts a positive decision declaring them compatible (standstill clause). This requires that the competent State bodies should be aware of State aid rules and their application.

The notification procedure is between the Member States and the Commission. Third parties, even the beneficiary, are not directly involved in the procedure and their rights are very limited. For instance access to the documentation of the notification can only be granted when the procedure is closed and business secrets are redacted first.

The procedure starts after the official notification from the Member State and the Commission has two months to take a decision or ask questions. After asking and receiving answers the two-month period starts again. In this first phase of the procedure the Commission can declare that the measure contains no State aid, or that the aid is compatible or, if it has doubts as regards any element of the notification, it can start the formal investigation; i.e. phase two.

In phase two, third parties (beneficiary, competitors, professional associations, other Member States) are invited to inform the Commission about their position and the Member State can later reflect on the information which is submitted. After having heard all of the opinions, the Commission takes its final decision. On average a phase one procedure lasts 5-6 months and the formal investigation takes 12-18 months.

The Commission does not deal with the question of unlawfulness. It has to decide about the compatibility of the aid without taking into account whether it was granted unlawfully.

However, unlawful aid can be subject to proceedings before national courts and competitors of the recipients can ask national judges to take necessary measures to protect their rights. Legally the basis of this protection is Article 108(3) TFEU. This provision is directly applicable in the EU Member States, hence individuals can refer to it in legal proceedings.

National judges are required to protect the rights of individuals against the State who violated EU law by granting aid not previously authorised by the Commission. National judges are obliged to take all necessary measures to redress the illegality of aid. They may order the suspension of the measure or order the beneficiary to repay the aid plus interest for as long as the aid has not been approved by the Commission.

National judges can also order measures to protect third-party rights in line with national law, such as ordering the beneficiary to pay damages to competitors or order the aid granting authority to pay damages to competitors.

National judges can cancel contracts granting illegal aid, in particular where, in the absence of less onerous procedural measures, that cancellation is such as to lead to or facilitate the restoration of the competitive situation which existed before that aid was provided.

Incompatibility with the internal market

Incompatibility is established solely by the Commission. Even the EU courts have a limited review of the Commission's complex economic assessment of compatibility. The legal consequence of incompatibility is that the measure cannot be put into effect. If, however, the Member State has already granted the aid, then the Commission is obliged to order its recovery with compound interest⁴¹ as this eliminates the undue advantage and the market distortion.

The EU jurisprudence emphasises that recovery is not a sanction but the logical consequence of the incompatibility of the aid.⁴² Recovery has to return the beneficiary to its situation before receiving the aid (in integrum restitutio). Bankruptcy and liquidation procedures are no obstacle to recovery. Quite the opposite, ***Member States are required to use all possibilities under national law to enforce recovery. If the State fails to participate actively in such proceedings it is considered as an infringement of EU law.***

Appeal against a Commission decision has no suspension effect. Moreover, national judges in national recovery proceedings are in general not in a position to question the validity of the Commission decision ordering recovery, but they can ask for a preliminary ruling from the CJEU, if the interpretation of the EU law is not straightforward (Article 267 TFEU). The recovery has to be executed by the Member State in accordance with its national law. It should be however effective.

The Commission generally gives Member States two months to prepare and show the measures to be taken to recover the aid and an additional two months to recover it in full with interest, which is calculated on a daily basis. ***National law or procedures, which do not allow effective and immediate recovery have to be set aside even by national courts because of the primacy of EU law over national law.***

Member States and beneficiaries have very few possibilities to argue against recovery.

- They can first argue that the aid was granted more than ten years ago as this is the general limitation period in State aid law.
- They can argue that the aid is existing aid and as such is not subject to recovery obligation. Existing aid is either aid that is already approved by the Commission or put into effect before membership of the EU.
- They can argue that the recovery is against the principles of EU law. This is the case when an EU institution has acted in a way that the beneficiary legitimately believed that the measure was not State aid or was compatible aid. This defence invokes "legitimate expectations". Acts of national institutions cannot establish legitimate expectations.
- They can argue that it is absolutely impossible to recover the aid. This is only accepted when the beneficiary has ceased its activities and left the market (wound up) or when there are no records of the aid so indeed it is not possible to identify the beneficiaries or the amounts they received.

Non-compliance with State aid rules and the Energy Community Treaty

Since the Energy Community Treaty refers to and includes the EU State aid law and given the fact that the Contracting Parties are not yet members of the EU, it is not the EU law, but their own internal legal system which makes State aid law enforceable. This can happen at two levels. The first level is the compliance mechanism set in the international treaty itself like dispute settlement, conciliation procedures, etc. The second level can be any implementing rule in the national legal order.

The Energy Community Treaty as an international treaty, as well as the Stabilization and Association Agreement, is at the top of the hierarchy of legal norms in the national legal order.

41. Based on Article 14 of Council Regulation 659/1999/EC on laying down detailed rules for the application of Article 108 of the Treaty on the Functioning of the European Union of the EC Treaty.

42. Case C-183/91, *Commission v Greece*, [1993] ECR I-3131, paragraph 16.

For this reason, in case of infringement of the rules set in these treaties national judges should take into account the provisions of such treaties as well as national implementing norms. It follows that the legal consequences applied by national judges are drawn from national legal norms.

In the absence of national implementing norms the national legal order has to provide some kind of constitutional remedy like application to the constitutional court to establish the validity of a legal base containing a State aid measure in the light of a ratified international treaty.

As regards the incompatibility with substantive State aid requirements on a purely national legal basis the national judge should use the tools available as foreseen in the national implementing State aid rules, competition Act or unjustified enrichment provisions of the civil code.

On an informal basis the European Commission can take into account the willingness of a candidate country to comply and enforce State aid rules as a precondition to close the competition chapter during the accession negotiations or even to start them. The Commission can also consider the compliance with State aid law as a precondition to agree on the allocation or disbursement of pre-accession funds or any other advantages like free trade agreement, duty preferences, preferential visa disbursement, etc.

Overall, the rules of the Energy Community Treaty differ fundamentally from EU rules in three respects. First, there is no obligation on Contracting Parties to notify aid before they implement it. Article 18 of the Energy Community Treaty refers to Article 87 EC, now 107 TFEU, but not to Article 88 EC, now 108 TFEU. Second, there is no institution which is identified as responsible for receiving notifications or assessing the existence of aid or its compatibility.

There is, however, a dispute resolution mechanism under Articles 90-92. Third, it is likely to be exceedingly difficult to eliminate an incompatible aid measure. This is because, a breach of Article 18 has to be brought to the attention of the Ministerial Council which then has to decide on the basis of a simple majority [Article 91].

But then any “serious and persistent breach” can only be decided by the Ministerial Council on the basis of unanimity [Article 92]. Such requirements create significant obstacles to the enforcement of the prohibition of incompatible State aid by the Contracting Parties.

There is of course also the possibility that compliance can be achieved indirectly through private enforcement as it often happens in relation to breaches of anti-trust rules on cartels and dominant market players. Competitors would have to initiate proceedings before domestic courts of the Contracting Parties. Presumably national courts should have power to enforce the provisions of the Energy Community Treaty as it has been transposed in national law.

But even this possibility differs significantly from EU practice. Unlike national courts within EU Member States, whose powers are limited only to establishing whether a public measure contains State aid, a national court in a Contracting Party would first have to establish the existence of State aid and then consider its compatibility with the provisions of Article 107(2) or (3).

This Article is mentioned in both Article 18 and Annex III of the Energy Community Treaty. Assessment of the compatibility of aid often depends on subjective judgment including economic analysis and at this stage it is simply unknown how a national court would deal with that.

VI. Conclusions

The purpose of this study is to present the main elements of the EU State aid system, the State aid rules which are relevant to the coal and linked energy sectors and consider briefly the existence of State aid in the current energy policies of the Contracting Parties of the Energy Community Treaty.

Any State measure aiming to facilitate the financial situation of undertakings in the coal and energy sectors can potentially involve State aid. Such aid must then be made compatible with the rules concerning exemption of aid.

These rules favour aid that is granted to viable projects, which contribute to economic growth and innovation as well as the fight against climate change. Therefore the solutions in compliance with EU State aid law are rather limited in relation to the coal and energy sectors as the sector-specific State aid rules allow only certain targeted interventions like aid to closure of mines.

Furthermore, horizontal rules (like the EEAG or the GBER) demand complex calculations to limit the aid to the minimum possible amount even if it is necessary to achieve objectives of common interest like the protection of environment. There is also the possibility to provide aid to undertakings which are entrusted to provide SGEI in the electricity sector in line with the Electricity Directive.

In general, it is difficult to prove that the State acts in line with the Market Economy Operator Principle and no advantage is granted through equity, loans or guarantees especially if the beneficiary undertaking faces financial problems.

Ensuring compliance with the rules on State aid exemption is crucial as legal consequences are far-reaching and incompatible aid can be proscribed for a period of ten years. Compliance is in the interest of both the State and the beneficiary. ***In case incompatible aid is granted, Member States are under strict obligation to recover it from the beneficiaries, which causes inevitable financial loss for them, sometimes resulting in liquidation. The obligation to recover incompatible aid is also applicable to State aid granted before the accession of a country to the EU.***⁴³

With respect to the Contracting Parties of the Energy Community Treaty, incompatible aid may even lead to proceedings before national courts which have to apply the relevant State aid provisions of the Energy Community Treaty as such provisions are incorporated in national law. The question of applying State aid soft law [i.e. guidelines] as developed by the Commission in a country which is not a member of the EU is, though, open.

For those countries which have signed a Stabilization and Association Agreement with the EU the obligation is present and the enforcement is more predictable at national level as well as the bargaining power of the European Commission is stronger to enforce the right application of State aid rules. For these reasons ***it is advisable to carefully assess the compliance with State aid rules before any public measure is adopted for the purpose of granting public funding or facilitating private financing of coal and energy projects.***

43. Case C-262/11. *Kremikovtzi* paragraph 71.

Annex I: Eligible costs for the closure of coal mines under Council Decision 2010/787/EU

1. Costs incurred and cost provisions made only by undertakings which have closed or are closing coal production units

The following cost categories exclusively, and only if they result from the closure of coal production units:

- (a) the cost of paying social welfare benefits resulting from the pensioning-off of workers before they reach statutory retirement age;
- (b) other exceptional expenditure on workers who have lost or who lose their jobs;
- (c) the payment of pensions and allowances outside the statutory system to workers who have lost or who lose their jobs and to workers entitled to such payments before the closure;
- (d) the cost covered by the undertakings for the readaptation of workers in order to help them find new jobs outside the coal industry, especially training costs;
- (e) the supply of free coal to workers who have lost or who lose their jobs and to workers entitled to such supply before the closure, or the monetary equivalent;
- (f) residual costs resulting from administrative, legal or tax provisions which are specific to the coal industry;
- (g) additional underground safety work resulting from the closure of coal production units;
- (h) mining damage, provided that it has been caused by the coal production units which have been closed or which are being closed;
- (i) all duly justified costs related to the rehabilitation of former coal mining sites, including:
The increase in the value of the land shall be deducted from the eligible costs for the cost categories referred to in points (g), (h), (i) and (m).

2. Costs incurred and cost provisions made by several undertakings the following cost categories exclusively:

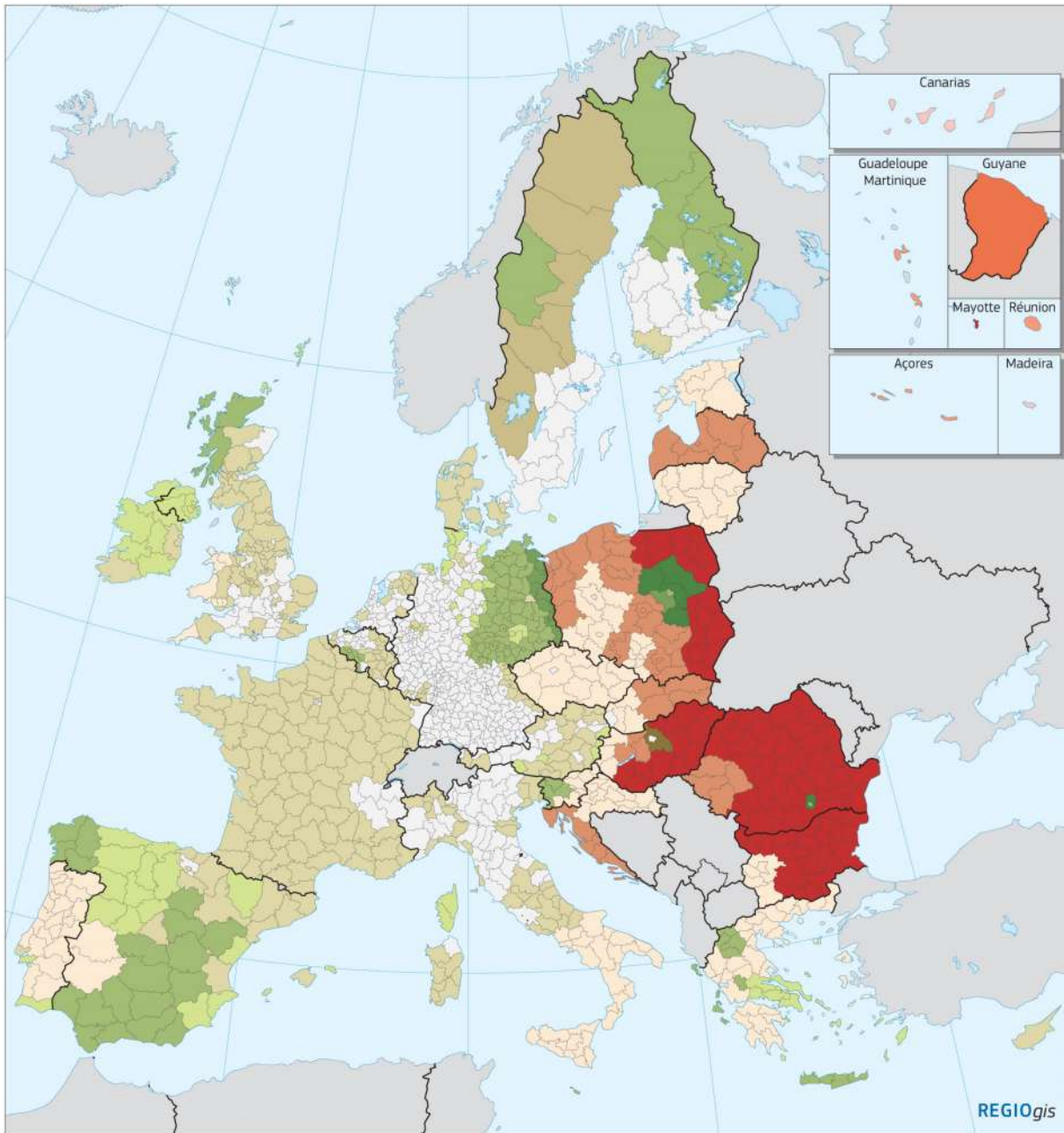
- (a) increase in contributions, outside the statutory system, to cover social security costs as a result of the drop, following closure of coal production units, in the number of contributors;
- (b) expenditure, resulting from the closure of coal production units, on the supply of water and the removal of waste water;
- (c) increase in contributions to bodies responsible for supplying water and removing waste water, provided that this increase is the result of a reduction, following the closure of coal production units, in the coal production subject to levy.

Table 1: Legal consequences of the different breaches of State aid law

Lawfulness	Compatibility	Consequence
Notified	Compatible	COM approval
Notified	Non-compatible	Prohibition, cannot be put into effect
Non-notified	Compatible	COM approval, but based on an action national court can take measures due to the unlawfulness
Non-notified	Incompatible	Unlawful & Recovery

Tables 2 and 3: Aid intensities under the regional aid map and the current regional aid map of the EU

	Large undertaking	Medium undertaking	Small undertaking
a) regions, GDP below 45%	50	60	70
a) regions, GDP between 45% and 60%	35	45	55
a) regions, GDP between 60% and 75%	25	35	45
Ex a) regions, below 90% until 2018	15	25	35
c) regions	10	20	30



Regional state aid, 2014-2017

Eligible regions and maximum aid intensity

Art 107.3.a	Art 107.3.a Outermost regions	Art 107.3.c total	Art 107.3.c partial	Other regions
25%	35%	10%	10%	Grey
35%	45%	15%	15%	
50%	55%	20%	35%	
70%		35%		

Source: DG COMP



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Table 4: The application of the EUR 200,000/3 years rolling de minimis thresholds

