

21 October 2011

REVISION OF STATE AID RULES APPLICABLE TO PUBLIC SERVICES

KEY MESSAGES



- 1** High quality and efficient public services are of fundamental importance for European society, the well-being of its citizens and the competitiveness of European businesses as users of these services.
- 2** Member States need to look critically at their expenditure to ensure a return to sound public finances. EU governments must therefore credibly commit to modernising the public sector by making public spending more connected to economic growth.
- 3** Undistorted competition and transparent application of State aid rules to services of general economic interest (SGEI) are key to avoid protectionism, reinvigorate the Single Market and provide better public services.

WHAT DOES BUSINESSEUROPE AIM FOR?



- Efficient and high quality public services: efficiency criteria need to be introduced in the application of State aid rules to SGEI.
- Effective enforcement of State aid rules: the existing rules must be adapted where necessary to strengthen scrutiny and control. Even large numbers of small subsidies taken together might lead to distortions of competition in the Single Market that can be avoided with effective enforcement.
- More competition: the scope of social services exempted from notification must not be extended to avoid limiting competition in these areas and creating uncertainty for companies.

KEY FACTS AND FIGURES

On average, public services represent 14% of Member States' total spending (2008).

High-quality and efficient public services are key to Europe's competitiveness.



21 October 2011

THE APPLICATION OF STATE AID RULES TO SERVICES OF GENERAL ECONOMIC INTEREST

COMMENTS TO THE COMMISSION DRAFT 2011 SGEI PACKAGE

INTRODUCTION

BUSINESSEUROPE welcomes the new Commission's draft package on State aid rules applicable to services of general economic interest (SGEI) to ensure fair and undistorted competition.

We praise the Commission for providing additional clarity to this complex area, by clarifying key concepts, providing more transparency, simplifying the rules and offering the necessary diversification to better manage different SGEIs.

SPECIFIC COMMENTS TO THE DRAFT TEXTS

1. Commission Communication on the application of EU State aid rules to compensation granted for the provision of SGEI (*clarification of key concepts of the notion of State aid relevant for SGEI*)

Clarification of key concepts

- BUSINESSEUROPE greatly appreciates that many general provisions relating to the concept of State aid have been clarified, such as the concept of undertaking, State resources and effect on trade.
- The clearer differentiation between “economic” and non-economic” activities is useful, in particular in the impossibility of drawing an exhaustive list of such activities. The distinctions made for non-clear cut SGEI areas (e.g. social security, healthcare and education) based on the case-law of the European Courts is helpful for public authorities and will help avoid misapplication of the rules in the future. However, we suggest the Communication should include a reference to the right of the Commission to investigate a “manifest error” in this context and hereby clarify this key concept.
- As stated in point 34, a relatively small amount of aid or the relatively small size of the recipient undertaking does not *a priori* mean that trade between Member States may not be affected. It is crucial to take into account that a large amount of small subsidies, for instance for the provision of local services, taken together can lead to competition distortions in the single market.



- BUSINESSEUROPE strongly supports point 43, aimed at preventing compensation to services that are - or can be - provided by companies operating under market conditions, in a way that is satisfactory and consistent with the public interest (e.g. price and access to the service).

Entrustment

- It is important that obligations, expectations and targets of public services assignment are clearly and precisely defined.
- In this context, BUSINESSEUROPE welcomes points 45 and 46 clarifying the need for an act of entrustment, clearly stating content and duration of the public service obligations, the provider and/or territory concerned, the nature of any exclusive or special rights assigned to the SGEI provider, parameters for calculating compensation and arrangements to avoid overcompensation. This contributes to ensuring a great level of transparency in the entrustment of an SGEI.
- The benchmark of the entrustment act needs to be economically realistic, taking into account i.e. current trends in productivity development of the sector concerned.
- In addition, when Member States grant compensation for these services, they should have an obligation to make their decision publicly available and inform the Commission to ensure further transparency and limit possible distortive effects.

Market testing and efficiency

- BUSINESSEUROPE strongly supports the introduction of efficiency criteria in the application of state aid rules to SGEI. The fourth criterion of the *Altmark* ruling clearly specifies that efficiency is one of the parameters that have to be taken into account to evaluate whether the SGEI compensation is compatible with State aid rules.
- Therefore, based on the Court's interpretation of EU law provided by this ruling, the Commission has not only the power to introduce efficiency criteria in the application of State aid rules to SGEI, but also has an obligation to do so.
- Increased market testing to assess optimal efficiency and quality in the provision of public services is crucial. This further promotes the use of public tenders or – in cases when it is not economically efficient – would at least ensure that there are realistic possibilities to evaluate whether the compensation granted to the SGEI provider does not amount to State aid.
- Therefore we support point 55, stating that in sectors where there is no provider comparable to the provider entrusted with the SGEI operation, a comparison may be made with providers situated in other Member States, or if necessary in other sectors. As the 4th criterion of the *Altmark* ruling stipulates, compensation offered must either be the result of a public procurement procedure or the result of a benchmarking exercise with a typical, well-run company (point 56).
- We also strongly support point 57 that the best way for public authorities to meet the fourth *Altmark* condition is to conduct a transparent, open and non-discriminatory tender in line with the applicable rules (e.g. on public procurement

and services concessions), insofar as the tender allows for the selection of the tenderer capable of presenting the most economic advantageous offer for the community.

- We support the definition of reasonable profit proposed in point 70 as the rate of return on capital that would be required by a typical company considering whether or not to provide the SGEI, taking into account the level of risk.

This should not however be the default method. Member States should be able to rely on other profit level indicators to determine the reasonable profit, such as accounting measures (e.g. average return on equity (ROE), return on capital employed (ROCE), return on assets (ROA) or return on sales (ROS)). This is stated in the Decision (recital 19) and should also be referred to in point 70 of the Communication.

The level of risk depends on the sector concerned, the type of service and the characteristics of the compensation mechanism. This rate should be determined where possible by reference to the rate of return on capital that is achieved on similar types of public service contracts under competitive conditions (e.g. contracts awarded under a tender).

2. Commission Regulation on the application of Articles 107 and 108 TFEU to de minimis aid granted to SGEI providers (*compensation deemed no-aid*)

De minimis thresholds

- Article 1 (2) of the draft de minimis Regulation holds that it only applies to aid granted by local authorities representing a population of less than 10000 inhabitants. The average size of municipalities differs greatly between the Member States. Whereas the average municipality size in the UK is around 137.000 inhabitants, while in Germany the average is around 5.600 inhabitants.¹

BUSINESSEUROPE considers that this threshold is not relevant and should be deleted.

As mentioned, a large number of small subsidies, for instance for the provision of local services in bordering municipalities by the same service provider, taken together can still lead to competition distortions. In addition, the great diversity of the size of municipalities in the different Member States makes this threshold uneven and hard to apply in practice, even more so as municipalities constantly grow or shrink, possibly around the given threshold.

- According to Article 2 (2), Member States' measures can only benefit from the Regulation if (i) the total amount of aid granted to an undertaking providing SGEI does not exceed EUR 150000 per fiscal year, and (ii) if this undertaking has an average annual turnover before tax, all activities included, of less than EUR 5 million during the two financial years preceding that in which the aid was granted.

¹ Website of Local Government Denmark: <http://www.kl.dk/Kommunalpolitik1/Artikler/65026/2009/11/Hvor-mange-indbyggere-har-de-danske-kommuner-i-gennemsnit/> (figures from 2009).

BUSINESSEUROPE welcomes these thresholds as it clearly clarifies what compensation for the provision of SGEI should be deemed not to affect trade between Member States and/or not to distort competition, and therefore should not be considered as State aid, hence therefore not be notified. This will relieve burdens both in terms of control from the Commission as well as administrative relief for public authorities. Yet, at the same time BUSINESSEUROPE considers the thresholds sufficiently low not to include possible amounts of aid to distort competition.

- In this regard, BUSINESSEUROPE welcomes Recital 10, stating that it should not be possible for State aid measures exceeding the de minimis ceiling to be broken down into a number of smaller parts in order to bring such parts within the scope of this Regulation.

Transparency

- BUSINESSEUROPE also welcomes Article 5 stating that for the purposes of transparency, equal treatment and effective monitoring, this Regulation should apply only to de minimis aid which is transparent. Transparent aid is aid for which it is possible to calculate precisely the gross grant equivalent ex ante without a need to undertake a risk assessment.

3. Commission Decision on the application of Article 106 (2) TFEU to public service compensation granted to certain SGEI providers (*compatible aid exempted from notification*)

Social services exempted from notification

- The draft Commission Decision provides a broader definition of block exemptions from notification than the 2005 SGEI Package. Article 1 (c) specifies that these services exempted from notification are SGEIs meeting essential social needs as regards health care, childcare, access to the labour market, social housing and the care and social inclusion of vulnerable groups. This list is not sufficiently clear and includes areas that can already be provided by private operators in the market, without the need to provide compensation by the Member State.
- Extending the scope of exempted services by widening its definition creates a higher degree of uncertainty for companies and might limit competition in areas where private operators can provide the SGEI as well.

The envisaged relief of administrative burden does not justify extending the scope of measures exempted from notification. BUSINESSEUROPE is worried that a trend towards less control by the Commission could open the door to an increase in distortive measures put forward by Member States.

- In this context, BUSINESSEUROPE recommends that public authorities, before taking a decision on the way to provide these services, should test the market every time it is economically sensible to do so. This would ensure that efficient



options that can be provided by the market are duly considered when deciding on the provision of SGEIs in the area of social services such as health care, childcare, access to the labour market, social housing or the care and social inclusion of vulnerable groups.

- Likewise, when Member States grant compensation for these services, they should make their decision publicly available and inform the Commission to ensure further transparency and limit possible distortive effects.

Thresholds

- The current threshold of 30 million Euros is already very high and allows Member States not to notify most of their SGEI operations, assuming that those operations comply with the Decision's conditions.
- BUSINESSEUROPE therefore strongly supports lowering the thresholds to 15 million Euro be able to increase field scrutiny and control, therefore being better able to avoid any possible distortions of competition (Article 1 a).
- We also welcome the deletion of the reference to the recipient's average annual turnover before tax, all activities included, of less than 100 million Euros during the two financial years, as mentioned in the 2005 Decision.
- However, the Commission should have strengthened reporting obligations for Member States as to the level of aid that is granted for all those cases that fall under the scope of the draft 2011 Decision.
- Without questioning the rationale of this exemption, BUSINESSEUROPE believes that the Commission should strengthen reporting obligations for Member States in this regard. This analysis should be made known to the public and to operators active in the provision of SGEI.

Compensation

- Referring to Article 4 (6), BUSINESSEUROPE proposes that before setting a level of reasonable profit for the provision of SGEIs not connected with a substantial commercial or contractual risk, the Commission should investigate whether the level currently proposed (reasonable profit not to exceed the relevant swap rate plus a premium of 100 basis points) is appropriate or should be raised.

4. Commission Communication on the EU Framework for State aid in the form of public service compensation (*compatibility criteria for large commercial SGEI*)

Transparency

- BUSINESSEUROPE strongly supports point 14 that Member States should show that they have given proper consideration to the public service needs supported by way of a public consultation or other appropriate instruments to take the interests of users and providers into account.
- We agree with point 32 that the Member State shall provide the Commission with evidence that the projected profit does not exceed what would be required by a typical company considering whether or not to provide the service, for instance by providing references to returns achieved on similar types of contracts awarded under competitive conditions.
- Transparency is key in ensuring more open competition and better enforcement of State aid rules and to avoiding distortions of competition in the Single Market.

Therefore, BUSINESSEUROPE fully supports point 18 on compliance with the Transparency Directive and in particular point 52 on publishing requirements. Under this Framework public authorities should publish information on the results of public consultation, the content and duration of public services obligations, the undertaking and/or territory concerned and the amounts of aid granted to the undertaking on a yearly basis.

Compliance with relevant EU single market legislation

- BUSINESSEUROPE welcomes point 19 which underlines that aid will only be considered compatible where the responsible authority assigning the provision of the service has complied or commits to comply with the applicable EU rules (e.g. on public procurement and services concessions).
- We strongly support point 20 on equal treatment and non-discrimination between undertakings (private or public).

Compensation

- Point 43 leaves to Member States to decide whether companies' profits related to the infrastructure necessary to provide the assigned SGEI may be allocated to the financing of the SGEI. We believe additional clarification is needed in this regard. In particular, if the objective of this provision is to avoid cross-subsidisation, we do not believe this choice should be left to member States.
- It is important that Member States carry out checks, or arrange for checks to be made at the end of the entrustment and, in any case, at intervals of maximum 3 years (point 46).



- With specific regard to overcompensation, the draft (points 44-47) is unclear on the possibility for Member States to use a refund / clawback mechanism, i.e. an adjustment of the contractual payments at the end of the financial year. In this context, BUSINESSEUROPE believes that the distortive effects of overcompensation cannot be remedied just by, e.g. using dividends as claw-back mechanism. In cases where the state owns the company providing the SGEI, the acceptance of dividends as claw-back mechanism provides a mixing-up of the role of the state as investor and as customer, and could be detrimental to fair and equal competition.

Efficiency

- Under the rules of the current 2005 SGEI Package, the compensation to public service providers can cover all the costs incurred plus a reasonable profit, regardless of how efficient the provider is. This conflicts with the growing need to make better use of public money and making SGEI provision more efficient and cost-effective.
- Therefore, BUSINESSEUROPE fully supports points 36 to 43 of the Communication requiring Member States to introduce efficiency incentives when assigning the provision of a SGEI. In addition, we fully agree that efficiency gains should not reduce the quality of the service provided.

We believe it is correct that Member States are obliged to give greater consideration to optimising cost-effectiveness in the provision of SGEI, while having high flexibility in their design.

More efficient spending of public money will have a positive impact on trade between Member States and will increase competition as it will incentivise public authorities to use public tenders to deliver high quality SGEIs at the best price. It is only fair that efficiency gains can be retained as “additional reasonable profit” when undertakings perform better than the level set by the public authority in the entrustment act.

- There is a need to clarify the last sentence of point 38, as it is not clear what “rewards” linked to productive efficiency gains refers to.
- It is positive that Member States should show that they have given proper consideration to the public service needs supported by way of a public consultation or other appropriate instruments to take the interests of users and providers into account (points 14 and 52).

Application of the framework

- Point 57 needs clarification regarding the fact that if a Member State does not expressly agree with the appropriate measures proposed by the Commission, the Commission not only will take it that the Member States does not agree, but also that as a consequence a formal investigation on the compatibility of the SGEI aid concerned will be opened.

ADDITIONAL GENERAL COMMENTS

Transparency

Ensuring a great level of transparency, equal treatment and effective monitoring in the application of the SGEI Package is critical to its effectiveness. Compensation for the delivery of SGEI should only be granted when the entrustment act is fully transparent. Transparent aid is aid for which it is possible to calculate precisely the gross grant equivalent in advance without a need to undertake risk assessment.

Effective enforcement

It is important that well-established general state aid principles are reflected in the new SGEI Package. This is particularly the case for the “Deggendorf principle”. The Court judgment on the Deggendorf case established that the Commission can order a Member State to suspend the payment of new aid to a beneficiary that has not yet reimbursed unlawful aid previously received.

BUSINESSEUROPE therefore suggests explicit reference to the Deggendorf principle in the draft Package. In this context, we recall that the Commission notice "Towards an effective implementation of Commission decisions ordering Member States to recover unlawful and incompatible State aid" (2007/C 272/05) states that the Commission intends to integrate the Deggendorf principle into all new State aid rules.

Transitional arrangements

BUSINESSEUROPE recommends further clarification regarding the transitional arrangements between the 2005 SGEI Package and the 2011 SGEI Package. It is unclear whether Member States need to modify existing contracts in accordance with the new SGEI Package (for instance on the removal of references to the possibility to carry forward an overcompensation of up to 10% to the next year - point 21 in the 2005 Community framework). Clarification is also needed as to whether non-compliance with the new SGEI Package will in all cases lead to a negative Commission decision ordering the Member State to recover unlawful State aid.

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