SPEECH/09/

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State Aids 2008 / 2009

- 12 months of crisis management and reforms

7th Experts' Forum on

New Developments in European State Aid Law 2009

KEYNOTE ADDRESS

Brussels, 14 May 2009

Ladies and Gentlemen,

Let me first thank the organisers for giving me the opportunity to address you at the opening of this Conference. The Estali conferences are an established forum for exchanging views and taking stock of the developments in European State aid policy—and I am sure that we will have highly topical discussions also during the forthcoming two days.

From our perspective, one may say that the last 12 months have seen more developments in State aid policy than the fifty years before:

- We had to position the application of State aid rules within the overall framework set up by the European Union to cope with a world wide financial crisis and a resulting deep economic recession of a hitherto unknown dimension,

- For the first time in fifty years we had to use broadly the concept of a "serious disturbance of the economy", as enshrined in Article 87(3)(b) of the Treaty—up to this period used very rarely, last during the eighties with regard to Greece,

- We had to undertake rapid internal organisational reforms, in order to cope with a situation where aid to institutions of systemic importance required a decision not within months but within weeks and often days,

- At the same time, we had to keep in mind the longer term goals of State aid reform that you are all well acquainted with—the completion of the State Aid Action Plan. We have achieved this goal with the adoption of the Simplification package two weeks ago – the last outstanding measure which stands for a thorough review of our procedures in the field of State aid and vital for our longer term operational efficiency and credibility.

[*State aid control in time of crisis*]

As you all know, the European Commission has adopted in rapid sequence a large number of decisions dealing with aid in the banking sector and more recently in the real economy sector. As our special edition[1] of the State aid score board of last month shows, since October 2008 the Commission has adopted more than fifty State aid decisions in the context of the financial crisis—until March of this year twelve comprehensive guarantee schemes, five major recapitalisation schemes, five framework schemes comprising a combination of these measures and a substantial number of ad-hoc measures concerning certain banks. Taken together the schemes and measures approved sum up to an aid framework of 3 trillion Euros, or 24% of the GDP of the European Union, out of which 2.3 trillion for possible guarantees. Of course, these figures represent the upper level of possible risk shields, rescue and restructuring packages and other measures that Member States have been authorised to undertake—the actual aid element will be substantially lower and it will have to be seen how far banks take up the schemes and guarantees will be drawn.

The Union is now entering a new phase of restructuring and crisis management in the banking sector, as the flurry of State aid decisions

[1] State Aid Scoreboard – Spring 2009 Update, Special edition on State Aid interventions in the current financial and economic crisis, COM(2009) 164, 08.04.2009

recently taken has shown. The cleaning up of the balance sheets and required restructuring will be the dominant topic over the next weeks and months.

Without doubt, we will have intense discussions of the decisions taken and expected developments later during this conference. Therefore, let me limit myself here to some more general comments on our approach and the relationship between the application of State aid rules and general policy measures taken to manage the crisis and re-establish financial stability.

The Commission has addressed the crisis in a broad policy framework, as set forth in the European Recovery Plan submitted to the European Council in November of last year. Given the distribution of roles and competencies concerning fiscal and economic policy management between the European Institutions and the Member States, major measures fall inevitably to Member States. Member States' measures addressing specific banks or other enterprises will generally fall under Article 87 of the Treaty which entrusts the Commission with the task of reviewing Member States action in these fields. The application of State aid rules therefore played a pivotal role in crisis management in the European Union from the start. But the application of State aid rules must be seen in the context of broader regulatory, monetary, and fiscal policies put in place by the Union, the European Central Bank and the Member States to manage the crisis.

It is true that the crisis initially led to calls by some to suspend the application of State aid control, in order to give Member States maximum freedom for crisis management. However, those calls quickly dissipated.

Indeed, some initial cases in both the financial sector and the real economy which were blatantly discriminatory, favouring the domestic sector, led rapidly to the realisation that the application of State aid rules remains vital precisely in a crisis situation—when we have to be careful to get out of the hole, instead of digging deeper into it.

EU State aid rules have helped Member States to find coordinated solutions, have given legal certainty to the measures taken by them and have contributed to maintaining for the future a level playing field.

The Commission has shown that it was able to react to the requirements for saving the EU's banking sector from a melt down without sacrificing sound long term principles. This was particularly demonstrated by the rapid development of the policy framework for application of Article 87(3)(b): State aid for institutions of systemic importance for the whole of the economy "to remedy a serious disturbance of the economy" of Member States.

[***Adoption of a State aid policy framework in the financial sector***]

The European Union and Member States—as governments worldwide—have taken measures to support financial stability, to act decisively in order to restore confidence in the financial markets and to minimize the risk of a serious credit crunch. The European Council has emphasised the need for coordination of those economic and financial packages of a new dimension – and I refer here back to the figures I have quoted.

It is in this context that the Commission has issued in rapid sequence the three communications setting out a clear framework for the application of State aid rules on the basis of Article 87(3)(b) to the measures undertaken —establishing common principles but also ensuring necessary discipline in assistance to banks. In establishing this policy framework, we have worked in close coordination with the Economic and Financial Committee composed of the Member States and the ECB, and the Commission—another major innovation generated by the crisis.

In the **banking communication of 13 October 2008**[2], the Commission clarified its general approach and justified the use of Article 87(3)(b) as a legal basis against which the compatibility of aid measures will be verified in the crisis situation. We provided guidance on a number of types of State intervention, in particular on State guarantees for bank liabilities which were the most widespread response to the crisis in the first phase, when the re-launching of the inter-bank markets was the main target.

However, it was made clear that there was no blank cheque. The Commission maintained key principles:

– Non-discriminatory access to a national scheme by making sure that eligibility for a support scheme is not based on nationality,

– Limitation in time—support only to be provided as long as necessary to cope with the current turmoil in financial markets. State support has to be reviewed, adjusted or terminated as soon as

[2] Communication from the Commission – The application of State aid rules to measures taken in relation to financial institutions in the context of the current global financial crisis, OJ C 270, 25.10.2008, p. 8 ("the Banking Communication")

improved market conditions so permit—all inherent in the temporary nature of measures based on Art. 87(3) (b),

- State support to be clearly defined and limited in scope to what is necessary to address the acute crisis while excluding unjustified benefits for shareholders of financial institutions at the taxpayer's expense,

- An appropriate contribution of the private sector. This implies that there should be an adequate remuneration for general support schemes and the private sector is to cover at least a significant part of the cost of assistance granted,

- There must be sufficient behavioural rules for beneficiaries that prevent an abuse of State support—no expansion and aggressive market strategies on the back of a State guarantee.

A main target of Commission intervention was to prevent subsidy races between Member States that could undermine financial stability at the EU level, instead of promoting it—such as some measures taken initially in certain Member States.

In a second phase measures for the recapitalization of banks became a key focus, particularly when lending to the real economy started to dry up, as banks began the process of de-leveraging. Guidance on the conditions under which banks' recapitalization by the States would be compatible with the State aid rules was urgently needed. The main principles for the assessment of such measures under State aid rules were set out in the recapitalization **communication[3] of 5 December 2008:**

- The price that beneficiaries had to pay for State funding, depending on the risk profile of the bank, in order to limit the distortive effect to the minimum necessary,

- An exit strategy from reliance on State capital for fundamentally sound banks,

- In-depth restructuring or liquidation for distressed banks, however taking account of the overriding goal of financial stability.

The two communications guided the large number of Commission decisions on schemes and ad-hoc cases concerning guarantees and recapitalisation measures to which I referred. We believe that on the basis of the communications we were able to provide for the necessary coordination between Member States and the necessary coherence of measures, in order to achieve the intended stabilisation effect for the whole of the Union.

The Union’s banking sector is now moving into the third phase towards re-establishing stability and trust required for a return to normal operation of our banking sector—cleaning up of the balance sheets and removal of toxic and other impaired assets which were at the very root of the world-wide crisis in the first place. On 25 February 2009 the Commission

[3] Communication from the Commission – The recapitalisation of financial institutions in the current financial crisis: limitation of aid to the minimum necessary and safeguards against undue distortions of competition, OJ C 10, 15.01.2009 ("the Recapitalisation Communication")

provided **guidance for the treatment of impaired assets**.[4] This third communication addressed the implications of the introduction of asset relief measures (the purchase of such assets or their guarantee against further losses by the Member States). It contains guidelines for the application of the State aid rules to such measures and is based on the principles of transparency and disclosure, adequate burden sharing between the State and the beneficiary, and prudent valuation of assets based on their real economic value.

We must be careful that we move towards re-establishing long term stability. As regards guarantee and recapitalisation schemes, we are in the process of preparing the review announced in the communications, based on the reports to be provided by Member States, in order to assess their effectiveness and need for a prolongation and any necessary changes.

As regards the forthcoming assessment of restructuring where required by the communications, important decisions have been taken during the last days. Let me just mention the Commerzbank decision[5] of last week and the decision on WestLB[6] two days ago, as well as the opening of in-depth investigations on a number of other important financial institutions. We are working on how the restructuring practice under State Aid rules should be adjusted to the overriding goal of financial stability without jeopardizing the proven principles of rescue and restructuring as set down in previous guidelines and cases—long term viability which must include

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[4] Communication from the Commission on the Treatment of Impaired assets in the Community Banking Sector, OJ C 72, 26.03.2009 ("the Impaired Assets Communication")
[5] Commission press release, IP/09/711, 07.05.2009, State aid: Commission approves recapitalisation of Commerzbank
[6] Commission press release, IP/09/741, State aid: Commission approves aid package for German bank WestLB

submitting the plans of the banks concerned to the appropriate stress test; fair burden sharing; no undue distortion of competition.

[**Measures for the real economy**]

The financial crisis has had a direct impact on the EU's real economy. Banks are deleveraging and becoming more risk averse. Companies are experiencing difficulties with access to credit. A serious downturn is affecting the wider economy. As a consequence the Union and the Member States have put major economic stimulus programmes in place, additional to the monetary measures decided by the ECB and other Central Banks.

Under the very specific circumstances of this deep crisis, Member States need the necessary flexibility to put into immediate effect economic stimulus policies that allow a countercyclical effect. Again, the Commission decided to use Article 87(3)(b) as the instrument to provide for temporary measures to this effect, as far as the economic stimulus measures fall under State aid rules. Far from being a straitjacket impeding effective economic stimulus action by Member States, we believe that Article 87(3)(b) provides the necessary flexibility to the application of State aid rules needed at Member States' level in the current crisis, in parallel and within the framework of the European Recovery Plan established at the Union level.

The Temporary Framework[7] for State aid measures to support access to finance in the current financial and economic crisis, adopted in December on the basis of Article 87(3)(b) serves that very purpose.

The temporary aid measures pursue three main objectives:

- To immediately unblock bank lending and thereby help providing for continuity in companies' access to finance;

- To ensure that aid reaches recipients in the most rapid and effective way;

- To link to the maximum to the long term investment goals of the Union, such as the development of green products.

As most here will know, under the Temporary Framework Member States may grant, under certain conditions and until the end of 2010:

- €500,000 per company for the next two years. This aid can be cumulated with *de minimis*, but within the limit of €500,000 for the period 2008-2010,

- State guarantees for loans at a reduced premium,

- Aid in the form of subsidised interest rates, which will be calculated on the basis of the central bank overnight rate, instead of the one

[7] Temporary Community framework for State aid measures to support access to finance in the current financial and economic crisis ("the Temporary Framework"), OJ C 16, 22.01.2009, p.1. The consolidated version, integrating the amendments adopted by the Commission on 25.02.2009 is published in OJ C 83, 07.04.2009, p.1

year inter-bank offered rate , plus a premium[8]

- subsidised loans for the production of green products,

- extended risk capital aid,

- extended facilities for aid in the export credit insurance market.

These new facilities have been taken up massively by Member States. The special March edition of the State aid score board on the financial and economic crisis testifies to this.

Measures under the Temporary Framework target relief for the difficulties due to the financial crisis and its spill over into the real economy. They are not intended to remedy pre-existing structural issues. Therefore, while the measures in the Temporary Framework are also available to the car sector, like all other sectors, it should be stressed that the Temporary Framework does not apply to companies whose problems pre-date the current crisis. To that effect, a cut-off date was introduced in the Temporary Framework, i.e. the Framework can only be applied to firms not in difficulty on 1 July 2008. For firms already in difficulty by that date, the rescue and restructuring guidelines remain the most adequate tool to restore long-term viability. Again I believe that an interesting debate is ahead at this conference.

[8] equal to the difference between the average one year interbank rate and the average of the central bank overnight rate over the period from 1 January 2007 to 30 June 2008 plus the credit risk premium corresponding to the risk profile of the recipient, as stipulated by the Commission Communication on the revision of the method for setting the reference and discount rates.

[Case practice & return to market conditions]

At this stage it is very difficult to predict when we can conclude that the serious disturbance of the economy will have ended.

The Commission has approved the measures in favour of banks so far under the condition that aid beneficiaries are to demonstrate the ability to operate on the market in the long term without State support. At the same time, and in follow up to the de Larosière report and the discussions in the global context, the Commission is tabling substantial reforms of the regulatory framework of the financial markets which should facilitate return to market conditions. Both State aid control and regulatory reform should allow attaining the overall objective: stabilisation of the financial system and return to market conditions—and return to market conditions should re-establish normal working of credit markets and provision of funding to the real economy.

As regards the Temporary Framework for State aid measures for the real economy, Member States have to provide information on the measures put in place as well as data which should allow the Commission to conclude whether the Framework needs to be kept in place beyond 31 December 2010 and/or whether other adjustments will be needed.

[Organisational and administrative reforms in State aid control]

The financial and economic crisis has been a stress test for the management of European State aid control. Overall I believe that our system has performed well. In reaction to the crisis reaction, we have been able to set up within days special fast track decision procedures for handling banking cases and later the measures tabled under the Temporary Framework—without falling into the trap of rubber stamping. I believe we have maintained a high level of solid analysis and reasoning. We were helped in this by the prior re-organisation of State aid operations within DGCompetition along sectoral lines and the rapid setting up of a special Task Force in our State aid organisation for handling the financial crisis cases.

With the adoption of the State Aid Simplification Package on 29th April we are now carrying over this experience into general State aid management practice: we need streamlined procedures but we also need the necessary rigour of analysis and we need cooperation by Member States and Third Parties in the assessment process.

The Simplification package was the missing link in the implementation of the State Aid Action Plan initiated at the start of this Commission's mandate. After its publication in the Official Journal, it is now expected to enter into force by 1 September. The package is composed of the Best Practices Code and the Notice on Simplified Procedure.

[Best Practices Code]

The Best Practices Code[9] provides guidance on the day-to-day conduct of State aid proceedings at each step of the investigation.

One of the main novelties introduced by the Code is that **Pre-notifications** are systematized for all cases, but in particular for cases where there are particular novelties or specific features.

Moreover, in cases which are particularly novel, technically complex or otherwise sensitive, or which have to be examined as a matter of absolute

[9] Notice from the Commission – Best Practices Code on the conduct of Stat aid control proceedings, adopted on 29.04.09, http://ec.europa.eu/competition/state_aid/reform/reform.html

urgency, the Commission services will offer ***Mutually Agreed Planning*** to the notifying Member State. This instrument, requiring intense cooperation, will enhance predictability of the likely duration of a State aid investigation.

To reach its objectives, the Code proposes to enhance discipline and ensure a **more rigorous enforcement of the existing procedural rules**. For instance, during the preliminary examination, the Commission will use more often the possibility to deem a notification withdrawn if the Member States does not provide all the information necessary to assess a case. During the formal investigation, the Commission will strictly apply the deadlines for the Member States and the third parties to reply.

Finally, in response to a strong demand from Member States and other stakeholders, the Best Practices Code proposes a staged and **predictable procedure for dealing with complaints**. As a matter of transparency, the Code notably foresees that the Commission services will use their best endeavours to inform the complainant of the priority status of its submission and the planned follow-up, within two months from the date of receipt of the complaint.

[Simplified Procedure]

The Simplified Procedure[10] aims at tackling straightforward cases within an accelerated timeframe of **one month** after the notification. This should obviously improve the predictability of the procedure.

The Notice aims at substantially expanding the scope of the rather scarce amount of cases currently treated under the existing simplified procedure foreseen in the Implementing Regulation. The existing simplified

[10] Notice from the Commission on a simplified procedure for treatment of certain types of State aid, adopted on 29.04.09, http://ec.europa.eu/competition/state_aid/reform/reform.html

procedure has a limited scope of application as it concerns only certain alterations to existing aid.

The categories of cases in principle suitable for the Simplified Procedure include those falling squarely within the 'standard assessment' sections of existing frameworks and guidelines (like Research & Development & Innovation, Risk capital) or firmly in line with constant Commission decision-making practice, for example certain aids for SMEs, environmental aid and rescue and restructuring aid.

To ensure more efficient exchange of information between the Member States and the Commission, the Simplified Procedure introduces systematic **pre-notification contacts**. I would like to stress the fact that the pre-notification contacts are crucial to enable the adoption of the decision within the accelerated timeframe of twenty working days after the notification of the measure.

Moreover, in order to increase **transparency**, the Simplified Procedure Notice provides for the publication of a **summary of the notification** on the website of the Commission (DG Competition) before the adoption of the decision to enable interested third parties to send their comments. This transparency measure echoing other Commission initiatives, should help us taking decisions closer to the economic reality, without hampering quick decision-making.

[Longer term goals of State Aid reform]

The State Aid Action Plan—now completed with the adoption of the Simplification Package—was a vast exercise of streamlining, simplification and modernisation of the complex rules of State aid control in the European Union. It proposed to enlarge the category of measures which do not need to be notified in advance to the Commission but will be subject to ex post monitoring and to accelerate the decision-making process while enhancing cooperation with the Member States—without however sacrificing the necessary rigour needed for the implementation of Article 87 and 88 of the Treaty.

The Commission has been streamlining procedures across the board with:

(a) the de minimis Regulation of 2006, exempting small subsidies from the obligation to notify for clearance by the Commission (doubling the ceiling to €200,000),

(b) the General Block Exemption Regulation of last year consolidating and enlarging the scope of the measures that do not need to be notified to the Commission in advance,

(c) A thorough review of the major guidelines and aligning them on the major Community goals of common interest—cohesion and regional development, R&D&I, environment and climate change. In all these areas new guidelines and/or frameworks were issued, with special emphasis on the promotion of SMEs,

(d) continuous practice of including "safe harbours" in the Guidelines,

(e) introducing sound economic reasoning into the compatibility assessment under Article 87(3),

(f) And last but not least, the Simplification Package for State aid procedures, now adopted.

We have made remarkable progress. Last year, out of a total of more than 1000 schemes and ad-hoc measures falling under the application of State aid rules, 60% were dealt with under the block exemptions by the Member States and only 40% had to be notified to the Commission for assessment, inverting the ratio of some 45% / 55% three years before. Decentralisation works. In 2008 already, nearly 200 measures were dealt with under the new General Block Exemption.

But let me emphasise one new development which I consider as one of the most important in the longer term: the growing role private enforcement could take in the State aid field—as in other fields of Community competition policy. The new role given by the Commission to private enforcement in the field of State Aids with the adoption of the Notice on the enforcement of State aid rules by national courts[11] has the potential to lead to a watershed in the development of State aid control. I refer here to the discussion of this topic later during this conference. Let me just make one comment. We need the court system and the scrutiny introduced in State aid use by complaints of Third Parties before national courts to come to a more balanced development in the implementation of State aid rules in the Union. It is the legal profession and the courts that should become a main force in the enforcement of the rules. Once this happens State aid enforcement will fundamentally change. A more active role of the national courts will give the judiciary its full role in the State aid field—additional to the strong role that the Court of First Instance and the European Court

[11] Commission Notice on the enforcement of State aid by national courts, OJ C 085, 09.04.2009, p.1

of Justice have always had in this area. With the new enforcement notice the Commission is offering a launch pad for this process.

[Concluding remarks]

We will see other important developments in the application of State aid rules during the coming months. The public consultation on a revised draft for a new Communication on State funding of public service broadcasting has just closed. We hope that the work on this new communication can now be completed soon and a new communication adopted by the Commission.

As announced by Commissioner Kroes, in a related field, DG COMP is currently working on draft Guidelines explaining how the Commission applies EU State aid rules in relation to broadband financing. The draft Guidelines will not only codify our existing practice for traditional broadband but will also address public financing of very high speed, so-called "next generation access networks". Its objective is to provide a clear and predictable framework for the application of State aid rules in this important sector.

This ongoing work emphasises the close alignment of work on State aids with the basic goals of the Union. Besides its objectives in climate change, the introduction of universally accessible advanced broadband networks is another major objective of the Union—based on the major success of the Union’s telecommunications policies during the last two decades. As is well known, the Commission has introduced a € 1 billion line for broadband deployment in the European Recovery Plan.

Ladies and Gentlemen,

The financial and economic crisis has propelled State aids to the top of the agenda of the Commission. The handling of the crisis situation is a basic test for the validity and the reasoning of the application of European State Aid rules. It tests the basic rationale, our ability to communicate and our ability for reform. Let me conclude therefore with a quote from Commissioner Kroes: "State aid reforms since 2005 have ensured the system is fit to meet the tests of this crisis; … Now is not the time to dismantle the State aid system or give up the benefits of European integration and cooperation." Let me end on this quote.

Thank you for your attention.