

September 28th 2005

AmCham EU response to the Commission's consultation on the State Aid Action Plan

Executive Summary

<u>Subject</u>	<u>Business Perspective</u>	<u>AmCham EU Position</u>
<i>The concept of market failure in state aid policy</i>	This concept might be misused to justify political choices	A thorough economic analysis should accompany the use of the market failure concept
<i>The use of block exemptions</i>	Companies are turned into enforcers of state aid before national jurisdictions	There is no incentives for companies to accept the responsibility for state aid enforcement
<i>Regional aid policy</i>	The draft guidelines on national regional aid for 2007-2013 excludes large companies from regional aid	The criteria for market definition should be refined in order to allow for an improved economic assessment of regional aid for large investment projects
<i>Services of General Interest and public-private partnership</i>	The recent clarifications brought by the Commission on public services compensation are not satisfactory	<ul style="list-style-type: none"> - the idea of a public consultation to define public services obligation needs to be clarified - not the size but the effect of a state measure on the market should be the criterion for assessing aid
<i>Decentralisation of state aid enforcement</i>	The application of state aid rules should be consistent and uniform in all the Member States	The creation of independent national authorities to enforce state aid rules is only possible if overseen by the Commission

INTRODUCTION

The American Chamber of Commerce to the European Union (AmCham EU) is the key organisation in Europe presenting the views of European companies of American parentage. Its member companies are drawn from a broad cross-section of the European business community and typically are present in most Member States of the European Union. As such, it represents some of the earliest and most committed business supporters of the European ideal and, in particular, of the single market concept.

On June 7th 2005, the Commission adopted its Action Plan as consultation document entitled, “Less and better targeted state aid: a roadmap for state aid reform 2005-2009”. The Commission has stated its intention to launch a “comprehensive reform of state aid policy” over the next five years. Noting that it intends to conduct the reform in close cooperation with Member States and stakeholders, the Commission has invited stakeholders to comment. This contribution constitutes the response of AmCham EU to the Action Plan in particular, and the necessity for reform of state aid enforcement policy in general.

On May 25th 2005, in anticipation of the Commission’s Action Plan, AmCham EU released an initial position paper on state aid enforcement. A copy of the position paper is appended hereto and should be considered as an integral part of the AmCham EU response. The paper sets out a series of proposals for a reform of state aid rules around five broad issue areas :

- reflections on the scope of state aid policy;
- predictability and transparency in the application of state aid rules;
- access of concerned undertakings to due process in state aid procedures;
- efficiency of process and
- methodology of economic analysis.

AmCham EU hopes to be involved in the future development of new state aid enforcement policy and regulatory documents by the Commission. The present contribution goes beyond these proposals and addresses specific issues set out in the consultation document. The AmCham EU response is structured around the following issues:

- concept of market failure in state aid analysis;
- use of block exemptions;
- regional aid policy;
- Services of General Economic Interest (SGEI) and Public-Private Partnerships;
- procedural issues and
- decentralisation of state aid enforcement.

I. CONCEPT OF MARKET FAILURE IN STATE AID ANALYSIS

2. AmCham EU welcomes the Commission's intention of introducing more economic analysis in the control of state aid. Such analysis could greatly contribute to a more rational and better control of state aid if used to determine whether, and under which conditions state aid may be approved under Article 87 (3) EC.

The concept of market failure as described in the Action Plan certainly plays an important role in reinforcing a more economic approach to state aid control in the context of Article 87 (3) EC Treaty. But AmCham EU would like to draw the Commission's attention to the limitations and risks of the concept of market failure. Moreover, it is emblematic that the Commission, in its approach, has not chosen to demonstrate how the state aid rules were successful or unsuccessful in dealing with market failure phenomena in the past. AmCham EU has some concern that the new emphasis on the concept of market failure could be misused in practice to justify political choices rather than to identify objective economic grounds for state aid. For example, market power, which the Action Plan identifies as one example of market failure, is not the same thing as a monopoly or the existence of a superdominant player in a market with few or no competitors. Whereas the latter case may be indicative of a market failure the former may well be the market driven outcome of effective competition. Where the most efficient operator in a market achieves a position of market power state aid to its competitors will not correct market failure, but only distort competition. Where market power is the result of state regulation, AmCham EU would advocate that deregulation is much more likely to lead to an economically efficient outcome than state aid.

AmCham EU would call on the Commission to ensure that wherever market failure is cited to justify state aid a thorough economic analysis be carried out to confirm its existence. It is vital to avoid using state aid where regulation or other non-economic factors are at the heart of the identified difficulties and where other measures than state aid would be a more efficient remedy.

Before resorting to state aid, it should be verified whether other less distortive measures could remedy the market failure. State aid should be designed so that it effectively solves any market failure, by creating incentives as well as being proportionate.

II. USE OF BLOCK EXEMPTIONS

AmCham EU welcomes the Commission's intention to establish one state aid block exemption in order to simplify and consolidate applicable rules. Using one legal instrument, could facilitate future extensions of the block exemption concept (it appears from the State Aid Action Plan that the Commission intends to seek block exemption powers for such additional areas as risk capital, culture and cinema).

This said, AmCham EU is concerned about the risk that such a general block exemption instrument, as contemplated by the Commission, could transfer part of the onus of state aid monitoring and enforcement to companies, which could be obliged to go before national Courts to challenge the applicability of the general block exemption to a given measure. This concern derives from the Commission's view expressed at point n° 59 of the Action Plan, according to which the general block exemption would have a "negative effect" by which national Courts would apply the block exemption criteria to rule on the compatibility of the aid. National judges would exercise those powers only where companies brought disputes

before them. The question is thus to what extent will companies have the financial appetite and see it as a business priority to engage in long procedural battles before national Courts. Many companies are, in fact, litigation-averse and may not wish to accept responsibility for state aid enforcement in national jurisdictions.

III. REGIONAL AID POLICY

AmCham EU supports the Commission's initiative to better focus regional aid. We note that to this end the current draft of the Guidelines on National Regional Aid for 2007-2013 (the Draft Guidelines) provides that regional aid should be used sparingly and proportionately and should be concentrated on the most disadvantaged regions of the European Union. In addition, the advantages of the aid in terms of the development of a less-favoured region must outweigh the resulting distortions of competition.

However, AmCham EU would challenge the Commission's approach to regional aid to large companies and large investments. The Action Plan assumes a "necessity to use investment aid to large firms sparingly in order to preserve its effectiveness in promoting overall, long-term competitiveness through a reduction of regional disparities" (point n° 42). The Draft Guidelines also appear biased against regional aid for large companies. This bias is not objectively justified. To the extent that state aid is desirable in support of innovation, it should be extended to all companies, whatever their size. Where need for regional aid has been established based on objective criteria, AmCham EU submits all businesses, whether small or large, must overcome the same additional cost to profitably invest and contribute to economic development. Whether the aid involved unduly distorts competition is another matter, but this should not lead to automatic exclusion of aid to large companies or large investment projects. Indeed, AmCham EU does not believe that state aid in support of innovation should be limited to SMEs.

AmCham EU notes that the current Draft Guidelines increase Member States flexibility to target very localised regional disparities. AmCham EU agrees with the Commission that Member States, which wish to make use of this possibility, must demonstrate that the areas in question are "relatively more in need of economic development than other areas in that region". However, AmCham EU strongly opposes the Commission's approach to allow aid only to SMEs in such areas and with the statement that "the Commission will not approve aid for investments by large companies in these areas, or aids for investments with eligible expenses exceeding €25 million." AmCham EU submits that this approach is not economically sensible. Once a Member State has demonstrated that a localised region is more in need of economic development, the additional costs for business to invest in such a region are the same for all companies. AmCham EU believes that the Commission should not and cannot legally rely on a perceived "potential for distortion of competition resulting from the spill-over effect into the more prosperous surrounding regions" to exclude large companies (regardless of the volume of their investment) and investments with eligible expenses exceeding €25 million from regional state aid for very localised regional disparities.

In addition, AmCham EU regrets that so far the Commission has refrained from seizing the opportunity to introducing a more economic approach to the assessment of the compatibility of regional aid for large investment projects with the common market. The current Draft Guidelines incorporate the 2002 Multisectoral Framework on Regional Aid for Large Investment Projects, but maintain the existing eligibility criteria (maximum of 25% market share or creation of up to 5% of market capacity in terms of apparent consumption) without

refining the criteria for market definition. AmCham EU calls on the Commission to reconsider its position and amend the Draft Guidelines line with its overall policy for better state aid by requiring a more economic market definition and assessment of regional aid for large investment projects.

Finally, at various points, the Commission refers to the “common interest” in state aid enforcement. The Commission could usefully refer to this concept in order to broaden its analysis of regional aid. In the dichotomy R&D/innovation aid vs. regional aid, it is regional aid, which seems to be considered less crucial from an economic point of view. However, it should be recalled that funding for general investment in production sites is often required to attract investors to certain regions, who would otherwise prefer to invest in countries outside the EU (such as Asia, etc). To strengthen its competitiveness globally, the EU has to maintain its attractiveness, in particular in capital-intensive production industries. Often regional aid appears, on the basis of the foregoing analysis, to correspond to the common interest in these situations. This does not necessarily entail a distortion of competition between Member States. Many projects do not significantly affect intra-Community competition, both between potential site locations for the investment and on the markets on which the new plant will be active (i.e. where those markets are global). In worldwide location competition, why limit aid to the least-developed regions only?

IV. SERVICES OF GENERAL ECONOMIC INTEREST AND PUBLIC-PRIVATE PARTNERSHIPS

In its Action Plan, the Commission refers to services of general economic interest as a key component of the European welfare state and essential for ensuring territorial and social cohesion. The Commission further announces the adoption of legal texts that would provide more guidance on the subject. This guidance has now been given through the publication of (i) a draft Commission decision on the application of Article 86(2) EC to State aid in the form of public service obligation; (ii) a Framework Paper describing when public service compensation which constitutes state aid and does fall outside the scope of the draft decision can be found compatible with the EC Treaty and (iii) a draft Commission directive amending Directive 80/723/EEC on the transparency of financial relations between Member States and public undertakings.

Clarification of the conditions under which the European Court of Justice (ECJ) has considered public service compensation as not constituting state aid is certainly welcome. It is questionable, however, to what extent the Commission’s texts have provided the necessary clarification. According to the text of the draft Decision, it will apply only to those measures that (i) do not comply with the *Altmark* criteria; (2) fulfill all the conditions for Article 87(1) EC to apply and (3) granted to undertakings of specific size in terms of turnover. AmCham EU makes the following observations:

- the Commission correctly states that, according to the ECJ’s case-law and in line with the subsidiarity principle, it is the Member States’ task to define the activities that qualify as a public service. The Commission’s Framework Paper suggests that Member States should widely consult with users in defining a public service obligation. AmCham EU would appreciate if the Commission could clarify what type of questions would need to be directed at users and to what extent views of other stakeholders, such as private competitors, would be solicited;

- the thresholds provided for by the draft Decision exempt smaller public service companies from the application of the state aid rules. In previous position papers, AmCham EU has always opposed a distinction between small and large companies in the assessment of state aid rules. Both operate on the same competitive playing field. Not size but the effect of a state measure on the market should be the criterion for assessing aid. It is unclear why the Commission departs from its overall intention, expressed in the Action Plan, to direct aid towards horizontal objectives whereby any company, irrespective of size, could benefit and
- the Framework Paper provides guidance for those measures that do not comply with the *Altmark* criteria, fulfill all the state aid conditions under Article 87(1) EC, and do not qualify under the draft Decision. It is unclear, however, to what extent this guidance differs from the criteria laid down by the ECJ in its *Altmark* judgment on the constitution state aid. AmCham EU would appreciate if the Commission could clarify in what respect the compatibility criteria in the Framework Paper differ from those laid down in *Altmark* and, therefore, what would be the difference in finding a specific measure not to be state aid under *Altmark* as against finding it compatible aid under the Framework Paper.

V. PROCEDURAL ISSUES

AmCham EU encourages the Commission to pursue its various goals, as stated in the Action Plan; to use its enforcement resources in a proportionate manner, to render state aid control “more predictable and user friendly (...) to increase transparency and advocacy about state aid policy to allow undertakings, the academic world, competition specialists, consumers and the broader public to get involved (...), with more effective procedures, better enforcement, higher predictability and enhanced transparency” (points n° 17 and 18 of the Action Plan).

However, AmCham EU is not convinced that the Commission is on the right track in seeking concrete means to achieve those goals. AmCham EU is somewhat sceptical about the feasibility of a system which would involve the empowerment of “independent authorities” in the Member States to “facilitate the task of the Commission” (point n° 51 of the Action Plan), and the creation of a “network of state aid authorities or contact points” to facilitate the flow of enforcement information (point n° 53 of the Action Plan). Given the poor track record of many Member States in recovery of illegal aid, how would the creation of an independent authority change the picture? Would it be possible to guarantee that national authorities were truly independent, meaning that they could be trusted to enforce state aid rules against their Member State? Would the creation of an additional state aid bureaucracy at national level really enable the Commission to attain its stated objectives? How would the Commission ensure that such national authorities have the required experience, in all 25 Member States, to ensure uniform application in this very complex area of law? Indeed, in the view of AmCham EU, any involvement of a Member State authority in the enforcement of the state aid rules (albeit an independent authority) is inconceivable without some system of Commission oversight. One example is in the field of antitrust enforcement under Regulation No. 1/2003, which enables the Commission to take over a case where it disagrees with the approach of a national competition authority. (see Section VI below).

AmCham EU welcomes best practice guidelines on state aid procedure. More rapid and more efficient notification procedures are critical. The duration of the notification process is often a

serious hurdle for the realisation of a project due to business constraints. One issue remains: why choose guidelines to ensure procedural objectives rather than a regulation?

The Commission will have to address various practical issues in connection with its proposals which are not dealt with in the Action Plan. The Commission advocates greater transparency without proposing how to ensure that business secrets and other confidential information of beneficiary undertakings are not disclosed. It further advocates decentralisation and delegation of specific tasks in state aid enforcement. Such proposal should be accompanied by measures to ensure that the state aid rules are applied in a consistent and uniform manner (see Section VI below).

Finally the Commission advocates greater private enforcement of the state aid rules before national Courts pursuant to direct applicability of Article 88(3) EC. However, we are concerned that examples of successful private enforcement are rare due to a number of factors, including provision of evidence.

VI. DECENTRALISATION OF STATE AID ENFORCEMENT

In addressing the issue of procedural reform, the Commission states that better governance is a shared responsibility with Member States on whom the successful implementation of the rules and procedures depends. It intends to examine whether independent Member State authorities could help the Commission with enforcement (detection and provisional recovery of illegal aid, execution of recovery decisions).

Whatever the means, the Commission will have to ensure that state aid rules are applied in a consistent and uniform manner throughout the Member States; that regulators are truly independent, show no specific bias, and are not competing with each other or duplicating tasks. Authorities should have substantive knowledge of the area in which they are exercising their judgment. To this end AmCham EU urges that Community funds be made available for training local officials.

Member States are already under an obligation to recover aid which is declared illegal yet it is questionable whether an independent authority in a Member State which has a bad record on compliance with recovery orders, can be reasonably trusted to be more successful.

Commissioner Kroes has expressed the view that less and better state aid can only be reached by agreement with the Member States and by involving Member State policy-makers in the formulation of overall policy so that they have a common understanding of the Commission's objectives.

To this end she announced in July 2005 that she wished to set up a State Aid Network with counterparts in the Member States, which would facilitate co-operation in the day-to-day treatment of state aid cases; allow the Commission to provide guidance on the application of the rules, help granting authorities to design state aid-compatible measures and serve as a forum for policy discussions with policy-makers.

Subject to its reservations on uniform application of the state aid rules, AmCham EU would welcome such a network as a means of enhancing awareness of state aid objectives at state level. Indeed, if organised correctly such network could facilitate the objective of consistency in the application of the rules. AmCham EU also considers that increased transparency in

procedures and notifications will be even more necessary if authorities across the Member States are members of a cooperation network with the Commission in state aid control.

AmCham EU recognises that the Commission has limited resources to ensure state aid enforcement. Despite its reservations to the idea of decentralisation of state aid enforcement, AmCham EU accepts that such decentralisation and delegation of specific tasks in state aid enforcement may be necessary to free resources and enable the Commission to focus on more important state aid cases. However as previously stated, AmCham EU remains somewhat sceptical about the need to create state aid bureaucracies at Member State level in order to attain the stated objectives. There is an obvious risk of inconsistent enforcement by national Courts (qualitative inconsistency can already be seen in the various Article 88 (3) EC direct effect judgments of national Courts in the past).

Decentralisation also raises issues of private enforcement. As a general rule, AmCham EU members tend to be adverse to any system for the enforcement of state aid rules, which would rely heavily on private litigation. State aid rules are addressed to and must be complied with by Member States. So, at best private litigation can play only a supporting role in terms of increasing the risk for recipients that aid received will be investigated, found illegal and ultimately have to be repaid with interest. In any event, private litigation has hitherto not been an effective means of enforcing state aid rules (there are various hurdles, including the obtaining of evidence) and it is not clear how and why that could change in the future.

CONCLUSION

The reform of State aid enforcement policy is a tremendously difficult challenge. AmCham EU recognises that State aid law, a full and complex area of competition law, is a particularly delicate area for some of the Member States. For some time now, it has been apparent that the current enforcement policy was not fully meeting its objectives. AmCham EU believes that a radical reassessment of the system is necessary to take into account current realities. The above discussion is intended to contribute in a direct and sincere way to the Commission's reflections on the best way to ensure that the right means are used to reach the goals set out in the Action Plan.

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The American Chamber of Commerce to the European Union (AmCham EU) is the voice of companies of American parentage committed to Europe towards the institutions and governments of the European Union. It aims to ensure an optimum business and investment climate in Europe. AmCham EU facilitates the resolution of EU – US issues that impact business and plays a role in creating better understanding of EU and US positions on business matters. Total US investment in Europe amounts to \$850 billion, and currently supports over 3.5 million jobs.

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Enclosure Position Paper of May 25th 2005